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China Law Deskbook Monthly: News & Views from Beijing

The following are a few new laws, regulations, and policy trends that I find of interest this month:

- *New immigration law penalizing employers of foreigners that illegally enter, live or work in China*
- *NDRC effectively puts a stop to the Qualified Foreign Limited Partner (QFLP) programs in China*
- *MOF issues government procurement rules that emphasize the buy-China policy*
- *MOF issues new rules requiring the videotaping of government contract review deliberations in bid to bring more transparency and fairness to the process*
- *New labor regulations to protect expat Chinese employees dispatched overseas*
- *State Council adopts new regulations protecting female workers against sexual harassment in the workplace and extends maternity leave benefits*
- *MLR penalties on developers that fail to build in one year after acquisition of property*
- *MOF regulations on foreign accounting firms requiring local control*
- *SPC's judicial interpretation on insider trading and improper disclosure of commercial secrets*
- *Corruption Watch: SARFT rules to control media bribery and jailing of Wukan village leadership for corruption*

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On June 30, 2012, the National People's Congress Standing Committee adopted a ***new immigration law*** that provides for severe penalties against foreigners who illegally enter, live or work in China. Employers are now subject to monetary fines of RMB 10,000 (US\$1,574) for every foreigner they illegally employ up to a maximum of RMB 100,000. Any monetary gain resulting from such employment is also subject to confiscation. Foreigners are required to obtain valid identification documents when working in China, and that foreigners may not be employed without valid work permits (employment certificates). The law also encourages Chinese citizens to spy on and report information regarding foreigners who are suspected of illegally living or working in China. The number of foreigners employed in

China increased from 74,000 in 2000 to 220,000 by the end of 2011, with many working as employees of foreign companies, teachers or representatives of foreign organizations. *This is one of the first sets of rules that impose the obligation on the employers to ensure that their employees have proper visas and work permits. It will be interesting to see if the Public Security Bureau goes after the domestic and foreign companies equally. It will also be interesting to see how the PSB treats workers with pending applications, and especially renewal applications given the bureaucratic headache and time involved to obtain work permits. For NGOs and businesses that operate in a grey area or under the radar screen, it's left for observation whether there will be any wiggle room. And the NPC's encouragement of Chinese citizens to spy on their foreign neighbors is repugnant at best. But this is China!*

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On April 23, 2012, the National Development and Reform Commission (NDRC) released a notice in response to the Shanghai government's request for clarification of the status of its **Qualified Foreign Limited Partner (QFLP) program**. Under Shanghai's QFLP program, foreign investors through RMB Funds can secure favorable treatment provided that no more than 5 percent of the fund's total capital originated offshore. The NDRC ruled that the fund's general partner was backed by foreign capital and thus the investment is required to follow regulations in the *Catalogue for the Guidance of Industries of Foreign Investment*. A contribution of even an insignificant amount of foreign-sourced capital would make the fund "foreign." Under the NDRC's notice, a foreign-sourced RMB fund is "foreign" and subject to investment restrictions set forth in the Catalogue that restrict investments in certain sectors, such as media, education, telecommunications, Internet, and technology. *The NDRC's approach appears to be inconsistent with the position of the Ministry of Commerce, which has publicly stated that foreign invested PE firms should only be treated as "foreign investors" when a foreign limited partner is involved. In Blackstone's RMB fund, all of the limited partners are Chinese investors. MOFCOM is currently drafting regulations to clarify the issues which could shed some light on how foreign PE firms' Chinese entities should be treated when they invest in Chinese companies.*

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On May 8, 2012, the Ministry of Finance issued a notice designed to improve the management of **government procurement** and specifically favors the acquisition of **made-in-china products** over foreign produced goods. Government agencies are prohibited from purchasing imported products if there are equivalent products manufactured in China. The MOF requires that central government departments support the purchase of energy-saving and environmentally-friendly products and to purchase only copyrighted (and not pirated) software. The MOF notice requires that government departments that import a significant amount of foreign goods are required to establish an in-house review mechanism. The MOF notice follows a circular in 2010 which requires the purchase of domestic products. *This rule reinforces the government's policy to buy-local and places foreign companies at a disadvantage over domestic competitors. The only real exemption is if an equivalent product is not produced in China. However, there is no guidance on how to determine whether "equivalent" goods are commercially available in the domestic marketplace.*

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Also in **government procurement**, on June 11, 2012, the Ministry of Finance issued a notice that requires that deliberations on government contracts by central and provincial-level authorities must now be videotaped in an effort to make the process more transparent,

fair, and effective. The MOF also requires that the review committee members surrender their personal cellular phones during bid reviews. The new regulation is the first to enhance the bid evaluation process since the Government Procurement Law was promulgated in 2002. *The public bidding process is not transparent and every year dozens of scandals involving conflicts of interest, fraud and bribery are reported. However, this seems like an extreme measure that the MOF must require that members of the tender review committees surrender their personal cell phones and that their deliberations be recorded by videotape. These new rules are more of an admission that corruption in the procurement process is systemic, pervasive, and cannot be easily corrected. Corruption aside, the MOF has promised to restructure government procurement mechanisms in accordance with the WTO's Government Procurement Agreement (GPA) rules, which China agreed to join although the process has been slow. In the interim, most foreign companies are either restricted or barred from access to the market opportunities of government procurement, which has increased substantially from RMB 100 billion in 2002 to RMB 1.13 trillion (US\$179 billion) in 2011.*

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Effective August 1, 2012, a new set of ***labor regulations has been adopted to protect the rights of expatriate Chinese workers*** sent overseas and targets the practices of Chinese labor bureaus engaged in hiring citizens for foreign postings. Under the new regulations, expatriate Chinese labor service enterprises will each be required to set up a special bank account containing no less than RMB 3 million (US\$476,000) in order to cover service fees, wages, compensation for losses and emergency expenses when Expatriate Chinese labor service enterprises or their employer-clientele fail to pay the expat employees. The regulations further provide that labor bureaus are not allowed to charge any service fees or ask for deposits or financial guarantees from workers under contract, and are required to purchase personal accident insurance for its retained workers. Expatriate labor bureaus also are required to send administrative staff members to accompany large groups of expat workers (100 or more) to assist in managing their affairs. The regulations make it illegal for labor bureaus to contract with workers for gambling, prostitution, or other illegal industry sectors. *These rules are designed to correct a major headache for the Chinese and foreign governments that are forced to step in and protect Chinese expat workers dispatched overseas by Chinese companies that fail to pay the salaries of their workers and oftentimes strand their workers in far-flung work sites around the globe. By requiring the labor bureaus to post guarantee funds, the workers (and the governments) can be assured that they will be paid for their services and returned to China at the conclusion of their overseas assignments.*

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The State Council adopted new ***labor regulations designed to protect female workers***. Effective April 28, 2012, employers are required to extend maternity leave from 90 to 98 days and to provide medical leave for woman that have miscarriages (i.e., 15 days for a miscarriage within the first four months and up to 42 days leave for a miscarriage that occurs after the fourth month of pregnancy). Employers may not lower the wages or dismiss a female worker as a result of pregnancy, childbirth or breast-feeding, and employers are required to reduce the workload or arrange other tasks for workers if they are unable to handle their original work due to pregnancy. Employers are prohibited from extending the work hours or from requiring a pregnant woman in her seven to ninth months of pregnancy from working a night shift. The regulation requires that employers allow women with infants less than one year old an hour a day for breast-feeding. Employers are subject to monetary fines ranging from RMB 1,000 to 300,000 (\$160 to \$47,600) for violations and depending upon the circumstances, and those employers who seriously violate the rules could have their

business license suspended. *China generally has well-written and progressive labor laws protecting woman in the workplace. But, as with most laws in China, implementation is a work in progress. Until the government grants employees effective remedies through the courts, or adopts a system that allows the trade unions to operate independently from the political process, the full protection and recognition of worker rights is left for observation.*

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Effective on July 1, 2012, the Ministry of Land Resources issued a set of revised regulations that **impose penalties on property developers who fail to commence construction on land within one year of the purchase.** The penalty amount that may be levied is up to 20 percent of the sale price. The regulations provide that a developer can apply for an extension of the one-year deadline in extenuating circumstances, including in situations where local governments fail to transfer the property in a timely fashion, if there is a change in land use policies, if local residents dispute the planned construction, or if the project is delayed based upon national security issues or if archaeological interests take priority over development of the property. The regulations also provide that local governments are required to rescind land use rights certificates without compensation if the subject property remains idle for two years. *This rule is designed to guard against speculative land purchases that drive up the cost of real property. Only developers with the assets and means to develop property will be allowed to buy property. One downside of this rule is that foreign companies that purchase land for factories or facilities will be required to move quickly to commence construction or they too could be sanctioned for delays in construction.*

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The Ministry of Finance issued new regulations on May 10, 2012, that requires **foreign accounting firms** to limit the number of foreign-certified partners in China to no more than 40 percent. In five years (2017), the threshold will be decreased to 20 percent and all senior partners are required to be Chinese nationals. It is estimated that only about 30 percent of the partners in large foreign accounting firms are locally certified. *The rule change takes place at a time when the auditing sector has been bogged down by accounting scandals involving several U.S.-listed Chinese companies. Some observers suspect that this rule is designed to allow the PRC government to better control the auditing sector, and thus control the flow of potentially bad news that might be generated by international auditing firms.*

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The Supreme People's Court issued a **judicial interpretation** on May 22, 2012, which is designed to provide the lower courts with new guidelines in criminal cases that involve **insider trading and improper disclosure of commercial secrets.** The judicial interpretation provides greater clarity on those persons defined as “insiders” – namely, people possessing insider information – and the activities that constitute insider trading. In the past five years, China has only prosecuted 22 insider trading cases (of which 11 cases were handled in 2011), and it is anticipated that more cases will be initiated with the adoption of this judicial interpretation. *Recent cases of insider trading have involved huge insider transactions. In 2010, a court in Beijing imposed a 14-year prison sentence on Huang Guangyu, the major shareholder of Beijing Centergate Technologies, which is listed on the Shenzhen Stock Exchange. Huang had asked others to buy the company's stocks before statements of major transactions and corporate restructuring*

were issued. Huang acquired more than 140 million shares valued at RMB 1.8 billion (\$286 million) and realized profits of nearly RMB 400 million in three such insider transactions.

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Corruption Watch:

- On June 13, 2012, China's top media regulator, the State Administration of Radio, Film and Television (SARFT), issued a notice and commenced a crackdown from June 15 to September 15 against unethical practices in the media including the receipt of cash for interviews and media coverage. SARFT is reinforcing a pre-existing ban on bribery and extortion, and media professionals will be required to produce press credentials during interviews. Media operations are also required to conduct internal compliance reviews. *Media bribery is rampant in China and goes hand-in-hand with other forms of censorship and media manipulation. In 2008, hundreds of journalists engaged in a collective cover-up after a mine explosion killed 35 people and caused RMB 19.24 million in damages. An investigation found that local officials paid RMB 2.6 million in bribes to multiple media outlets.*
- On April 20, 2012, the Communist Party's Lufeng Discipline Inspection Commission of Guangdong Province detained the former Wukan party committee chief and seven village committee members for embezzling government funds, illegal land seizures, and election fraud. In September 2011, villagers in Wukan staged protests to draw attention to rigged elections and illegal land grabs by the officials. The village party secretary and village director both held official posts for 40 years, and are suspected of using public funds to purchase personal luxury items such as automobiles. The officials have been placed under *shuanggui* an extra-judicial form of detention used by the Communist Party disciplinary system. *In a very interesting twist, Wukan protest leader Lin Zulian was elected as chairman of the village committee by the CCP on March 3, 2012. The CCP's new tactic of appeasement is that if you can't beat 'em, get them to join ya!*

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