The Market Access Negative List Approach is Unveiled in China

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In brief

In September 2015, the government central leading team for the comprehensive market access reform adopted the opinion on the implementation of the market access negative list regime (“Opinion”). Following the adoption of the Opinion, the State Council officially released Guofa [2015] No. 55 in October 2015 clarifying the general principle, the primary missions and the supportive measures for implementing the market access negative list regime. On March 2, 2016, National Development and Reform Commission (NDRC) and Ministry of Commerce (MOC) jointly released the first draft of Market Access Negative List (trial version) (referred to as “Draft Negative List”). The Draft Negative List specifies the prohibited access and limited access industries, fields, and business in China. The Draft Negative List is pilot-run in Tianjin, Shanghai, Fujian, and Guangdong effective from the end of 2015.

In this issue of China Tax and Business News Flash, we share the government’s direction in the reform of the market access system in China, our observations on the Draft Negative List and its influences on investments and operations in China.

In detail

The direction of the China’s market access system reform

The market access system is currently reformed in accordance to the “Decision of the Central Committee of the Communist Party of China on Some Major Issues Concerning Comprehensively Deepening the Reform” 3. The major change of the market access system is to shift from a “positive list” approach to a “negative list” approach. Under the “negative list” approach, two negative lists are published, one is the market access negative list and the other one is the foreign investment negative list. The market access negative list stipulates the measures in investments applicable to all investors, both domestic and foreign investors. The foreign investment negative list regulates investments by foreign investors into China. The Draft Negative List recently released by the NDRC is the market access negative list. The foreign investment negative list refers to the “Special Management Measures for Foreign Investment Access” which is currently implemented in Free Trade Zones (FTZ Negative List) 4.

Under the market access negative list approach, the State Council lists out industries, sectors and businesses which are prohibited to be accessed and those which are allowed to have limit access. Under this approach, all investors, both domestic and foreign investors, can invest and operate in any industries, sectors and businesses other than those stated in the list on equal footing.

In addition, ensuring the market access negative list can be successfully implemented and the relevant risks can be monitored, measures are introduced. These measures include: 1) streamlining the pre-approval system and ensuring the procedures are clearly simple, easy to understand and transparent; 2) establishing a mechanism focusing on the monitoring during and after investment; 3) establishing a credit rating system for businesses with penal and reward mechanisms; 4) creating a public information platform for the credit rating of businesses, including making their annual reports publicly available, naming good practices and businesses that contravene the rules. These measures can guide businesses to be self-disciplined in their investments and to encourage businesses to take proper decisions in their investments though their compliance costs will be increased.
Observation on Draft Negative List

Key content of Draft Negative List

Draft Negative List contains a total of 328 items, 96 prohibited items and 232 items with limited access. Both domestic and foreign entities are not allowed to invest in the 96 prohibited items and the relevant authorities will not assess, approve, and process any applications in these items. Entities can invest in the 232 limited access items but subject to meeting the conditions stipulated and approval by the relevant authorities.

The prohibited and limited access items in Draft Negative List cover businesses in the primary, secondary and service industry sectors. The prohibited items concentrate on water conservation, environmental, public facilities management and businesses which are overproduced or technologically out-dated. Examples include petrochemical, coal, electricity, steel, non-ferrous metal, medical and technologically lagged machinery industries. The scope of limited access items is broader. These items correspond to lists provided by various departments of the State Council, the “Catalogue Guiding Industry Structure Adjustments”, the “Investment Catalogue required Government Approval”, those stated in the law and administrative regulations and those stated in the State Council Decisions. However, the NDRC mentioned in press conference that Draft Negative List is not a list simply consolidates all the current restricted items, it streamlines and revises the existing items according to the current business practices and developments. Besides, the Draft Negative List also takes into consideration of the need of upgrading industry structure and the principle of lowering barrier for innovation and start-up. Hence items such as new technology, new product, new type of operation, new business model are not included in Draft Negative List.

The implementation

The Opinion specifies that market access negative list approach will be implemented on a trial basis in some regions from the end of 2015 to December 31, 2017 first. The implementation will be extended to the entire country in 2018. The regions selected for the trial implementation of the Draft Negative List are Tianjin, Shanghai, Fujian, and Guangdong. The main reason for choosing these regions is that the foreign investment negative list and relevant monitoring mechanism are currently in place in the free trade zones in these regions. It will be smoother to implement the Draft Negative List by leveraging on existing mechanisms and practices. At the time of writing, it is uncertain whether the Draft Negative List will be adopted in other regions after the trial implementation in these four cities.

As there will be modifications in limited access items due to administrative reasons or in accordance to existing/new regulations, the Draft Negative List is not the final draft and will be adjusted during the trial implementation.

In the future when the final nationwide market access negative list is released, governments of provinces/municipals are allowed to propose the regional modification to the nation-wide market access negative list based on factors such as difference in the regional developments, comparative advantage of industries in the region, and impact on the environment of the region. Once the proposed modifications are approved by the State Council, the list that is applicable to a particular region will be different from the nation-wide market access negative list though the differences will not be substantial.

The takeaway

Accelerating modernization of the market access system, establishing fair and transparent market principle, and reforming market monitoring mechanism and enterprise credit rating system are important in the comprehensive market access reform. The Draft Negative List is the first step for the comprehensive market access reform heading this right direction. Although the Draft Negative List merely contains 300+ items, each industry or business is listed in detail. For example, one of the limited access items is establishing schools, specific education institutions and related businesses. The Draft Negative List clearly specifies that this item includes establishing preschool education, higher education, Chinese-foreign joint education, technical and vocation education. Therefore, when an enterprise is considering investment in a specific industry, it should examine the details of relevant item to see whether they are in the prohibited list or in the limited access list. If it is in the latter, the detailed descriptions and the conditions to be met.

Other than the Draft Negative List, specific negative lists also exist for different categories of investors, such as investors from Hong Kong and Macau who can take advantage of CEPA or investments in specific regions, such as FTZ. However, investment into China which is allowed under the CEPA or the FTZ Negative List are still required to comply with requirements in the Draft Negative List. In other words, the businesses that are not prohibited or limited in FTZ Negative List and CEPA may be prohibited or limited in the Draft Negative List. Therefore, an enterprise should consider overall regulations, not just the Draft Negative List, in its investment decision into China.

Neither the Draft Negative List nor its press conference clarifies whether it will affect the existing investments. Hence, we suggest an enterprise that has investment in any item specified in the Draft Negative List to contact the in-charge authorities to clarify its situation, particular if the investment may be considered as a prohibited item in the Draft Negative List. If the existing investment is a limited access item, it may be required to obtain approval or to modify its existing business operations to meet the relevant conditions before it continues to operate.

The adoption of “negative list” approach in the market access system apparently makes it easy for enterprises to invest in businesses that are neither prohibited nor limited access. On the other hand, the approach will strengthen the post-investment supervision and enable sharing and publication of information. Compliance cost and risk will be increased for enterprises as once an enterprise is found to be not meeting the conditions in limited access items, as its production, investment and distribution will be interrupted. Not only those enterprises in the pilot regions will be affected, enterprises in the non-pilot regions will sooner or later will be affected. In order to implement the “negative list” approach nation-wide finally, we believe local governments will gradually improve their market monitoring mechanism and enterprise credit rating system. Enterprises should prepare themselves for these upcoming changes. For example, they should establish good reputation/creditability and maintain adequate and appropriate information.
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for their operations. Our China tax and business advisory team will keep a close eye on the reform and development of comprehensive market access reform in China and share our insights timely.

Endnote

1. 《Opinions of the State Council on the implementation of the negative list regime for the implementation of market access》 (Guofa[2015] No. 55) please see more in official link: http://www.gov.cn/zhengce/content/2015-10/19/content_10247.htm

2. 《Notice of NDRC and Ministry of Commerce on issuance of draft market access negative list (Trial)》 (Fagaijingti [2016] No. 442) please see more in official link: http://www.sdpc.gov.cn/zcfg/zcfgb/201604/t20160411_797874.html

3. 《Decision of the Central Committee of the Communist Party of China on Some Major Issues Concerning Comprehensively Deepening the Reform》 please see more in official link: http://www.china.org.cn/chinese/2014-01/17/content_31226494.htm

4. The specific management measures for foreign market access in free trade zone, please see more in official link: http://www.gov.cn/zhengce/content/2015-04/20/content_9627.htm

5. The content of NDRC’s response for Draft Negative List in the press conference, please see more in official link: http://www.sdpc.gov.cn/gzdt/201604/t20160408_797743.html

6. CEPA is the abbreviation of “Mainland and Hong Kong Closer Economic Partnership Arrangement” and “Mainland and Hong Kong Closer Economic Partnership Arrangement”
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Let’s talk

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PwC’s China Business & Investment Advisory Team specializes in China regulatory advisory and implementation work, ranging from market entry solutions, structure set-up, foreign exchange solutions, to restructuring solutions, e.g., equity transfer, merger and liquidation, etc. The team maintains close dialogues with various Chinese approval and registration authorities as well as industry bureaus at central and local levels. It also has extensive involvement and experience in advising clients on business cases from both the regulatory and practical perspectives.

In the context of this News Flash, China, Mainland China or the PRC refers to the People’s Republic of China but excludes Hong Kong Special Administrative Region, Macao Special Administrative Region and Taiwan Region.

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