

Amended Regulations Could Open Telecoms Sector

Amendments to China's *Regulations for the Administration of Foreign-invested Telecommunications Enterprises* came into effect in September 2008. The amendments lower capitalisation thresholds for the operation of basic services and make applications simpler. But it is not clear if the new rules will encourage more foreign investment in the telecoms sector. By Fraser Mendel and Shan Liu of Morrison & Foerster. For full translation see page 92.

The State Council of the PRC recently issued amendments to regulations covering the administration of Foreign-invested Telecommunications Enterprises (FITEs). While it is perceived that the regulations were amended in response to pressure to open China's telecommunications sector to foreign investment, at this time it is not clear if the amendments will actually have that effect.

A key change made by these amendments is reducing the minimum registered capital requirement for foreign investors engaging in basic telecommunications services. Under the PRC, *Telecommunication Regulations*, telecommunication business is divided into basic services and value-added services. Basic services are services providing public network infrastructure, public data transmission and basic voice communication, while value-added services are telecommunication and information services that use public network infrastructure. The amendments only address capital investment requirements for basic services, and do not affect such requirements for value-added services.

The *Regulations for the Administration of Foreign-invested Telecommunications Enterprises* (FITE Regulations) were first promulgated on December 11 2001 and went into effect on January 1 2002. The FITE Regulations stipulate that FITEs must be established as Sino-foreign equity joint ventures – wholly foreign-owned FITEs are not permitted. FITEs can undertake either basic or value-added telecommunications services.

The amended FITE Regulations no longer require a submission of a feasibility study report for approval.

Depending on the nature of its operations and the geographic scope of its services, the minimum capitalization for a FITE could vary from Rmb1 million (US\$146,300) to Rmb2 billion. The minimum registered capital required for a FITE licensed to provide national or inter-provincial basic services was Rmb2 billion. The minimum registered capital for a FITE to provide services within a province was Rmb200 million.

The FITE Regulations established a lengthy application

process requiring approvals from several government ministries. An applicant was required to obtain initial approval from the telecommunications administrative department before proceeding to the foreign investment authorities for investment approval. Approval from the National Development and Reform Commission (NDRC) is required for certain telecommunications projects.

The amended FITE Regulations (*State Council, Decisions on Amending the Regulations for the Administration of Foreign-invested Telecommunications Enterprises*) were issued and came into effect on September 10 2008. They lower the capitalisation thresholds for FITEs to operate basic services, simplify the application process, and update references to the various government ministries to reflect recent government restructurings.

These amendments are discussed in detail below:

- **Lower registered capital requirements for FITEs providing basic services:** Article 5 was amended to lower the minimum registered capital requirement for a FITE offering national/inter-provincial basic telecommunications business from Rmb2 billion to Rmb1 billion. The minimum registered capital requirement for a FITE providing basic services within a province was lowered from Rmb200 million to Rmb100 million.
 - **Simplified application process for FITEs:** The FITE application package no longer requires a feasibility study report. Previously this had been the most time-consuming aspect of the application since it required detailed information including an investor's corporate and business background, business model, FITE business scope and structure, market information, profit forecast, fee schedule, and business plans and strategies. The amended FITE Regulations no longer require a submission of a feasibility study report for approval.
- Another required document, the "project proposal", has been changed to "project application report". However, this is not a substantial change because a project application report covers the same content as a project proposal: name and basics of the joint venture parties, total investment, registered capital, investment ratios of the parties, and types of services and term of operation of the FITE.

- **Various housekeeping updates to names of government departments:** Since the FITE Regulations were promulgated in 2001, the Chinese government has undergone several structural reforms. Relevant changes include: the Ministry of Foreign Trade and Economic Cooperation (MOFTEC) was renamed the Ministry of Commerce (MOC) in 2003; the State Council's planning authority was restructured as the NDRC in 2003; and the Ministry of Information Industry (MII) was changed to the Ministry of Industry and Information Technology (MIIT) in 2008. The amendments update the FITE Regulations to reflect the applicable new government department names. NDRC approval for certain FITE projects has been changed to "examination and consent". This change appears intended to highlight that MIIT plays the key role in granting approvals to FITE applications as well as issuing licences for all telecommunications services providers.
- MIIT's examination and consent are no longer needed for overseas listings by domestic telecommunications enterprises: The amendments deleted Article 23 from the FITE Regulations, which had required an approval from MIIT for overseas listings by domestic telecommunications enterprises.

The amendments to the FITE Regulations raise the possibility of increased opportunity for foreign investors entering China's basic telecommunications services market. While the lower registered capital requirement and simplified application requirements could encourage foreign investment in China's basic telecommunications sector, ultimately it will require a loosening of the government's approval requirements to encourage new foreign investment.

The amended FITE Regulations signal potential movement by the government in expanding the ability for foreign telecommunications companies to operate in China.

Following promulgation of the original FITE Regulations, there has been markedly limited investment by foreign telecommunications operators in the Chinese basic services market, which has been monopolised by the major Chinese telecommunications carriers. Various reasons have been cited for this lack of foreign investment. From a technical perspective, such reasons include the reluctance of foreign companies to commence a very lengthy application process involving the commitment of large amounts of registered capital with the end result being only a minority equity interest. In addition, there has also been a perception that the PRC regulatory authorities had imposed a moratorium on approving applications for foreign investment in the sector.

The previous registered capital threshold for a foreign investment was considered a significant obstacle for foreign operators

to enter into the market. This was partially due to the requirement under the *PRC Company Law* and *PRC Sino-Foreign Equity Joint Venture Law* that registered capital be contributed within a certain time limit after the joint venture was established. Combined with the PRC's restrictive foreign exchange control policies, contributing such a large amount registered capital could be seen as a significant burden.

The timing of the application process has also been considered an important factor discouraging foreign investment. While the FITE Regulations provided for a best case scenario of a six-month application process, a realistic evaluation was that nine months would be the fastest and could easily take twice that long. Many viewed this long application process as introducing significant additional risk into an already highly competitive market environment.

Ultimately, of course, the key obstacle is the foreign shareholding restrictions for a FITE, which are set forth in the *Catalogue for the Guidance of Foreign Investment Industries*, revised by the NDRC and MOC in 2007: foreign shareholding cannot exceed 49% in a FITE engaging in basic telecommunications services (excluding, for this purpose, wireless paging) and 50% in a FITE engaging in value-added services (including wireless paging, for this purpose, which is otherwise categorised as a basic telecommunications service). Limited to a minority position in a FITE, foreign operators would be committing to a major investment in a FITE, yet be unable to exercise control. This has discouraged foreign interest from setting up a FITE.

Finally, the perception among foreign investors was that while the FITE Regulations theoretically permitted foreign investment in the sector, the government was focused on restructuring the domestic telecommunications market following the 1995–1999 period. The government's crackdown on foreign investment in CCF models at the end of the 1990s accompanied a new policy emphasis on building up major national telecommunications operators who could compete effectively with international telecommunication companies. Until the government has determined that the domestic telecommunications companies are robust enough to compete, it will be challenging for a foreign investor to provide basic services in China.

The amended FITE Regulations signal potential movement by the government towards expanding the ability for foreign telecommunications companies to operate in China. However, lowering the registered capital requirement and streamlining the approval procedures are really only cosmetic changes as long as the maximum percentage of foreign investment shareholding in a FITE remains unchanged. This has been, and still will be, the major concern for foreign investors evaluating whether to establish a FITE in the basic telecommunications business.

Nevertheless, amending the FITE Regulations does signal a potential opening of the Chinese telecommunications market and a change of attitude towards foreign investment among Chinese policy makers.