Baker McKenzie FenXun.
奋迅·贝克麦坚时

Guide to Legal and Regulatory Practice in Guangdong-Hong Kong-Macao Greater Bay Area (“GBA”)

Baker McKenzie FenXun
A Leading China and International Law Joint Platform

2024 Edition

Foreword

The Guangdong-Hong Kong-Macau Greater Bay Area ("**GBA**") remains one of China's most ambitious and high profile initiatives to date, promoting the integration of nine Mainland cities and two Special Administrative Regions to create a Bay Area to rival a global economic, innovation and technology hub. The "Guide to Legal and Regulatory Practice in Guangdong-Hong Kong-Macao Greater Bay Area ("**GBA**")" is designed to provide in-depth insights and practical guidance for business professionals and legal practitioners. In this guide, we will explore how to effectively address legal and compliance challenges and seize opportunities in this region where diverse legal systems intersect, promoting sustainable development of enterprises. With an in-depth analysis of the unique legal environment and the latest policy developments in GBA, this guide will help readers build a solid legal foundation to navigate their businesses forward.

The regulatory compliance policies are continuously evolving alongside the ongoing development of GBA. Policy changes may involve new regulation, the revision or update existing laws, and to strengthen cross-border cooperation. For example, more facilitation measures and preferential policies may be introduced to facilitate the flow of people, capital and information within GBA. At the same time, along with the change of the international business environment, GBA may strengthen the dock with the international legal standard, to attract more foreign investment. To help you navigate the relevant GBA legislations and policies, our lawyers and partners have put together this publication, which focuses on key issues pertaining to doing business in this area. The publication delves into key practice areas, including **Bankruptcy & Restructuring**, **Capital Markets**, **Compliance**, **Cross-border Investment & M&A**, **Data Protection**, **Dispute Resolution**, **Employment**, **Financial Opening and Innovation**, **Intellectual Property**, **Real Estate and Infrastructure**, **REITs**, **Tax**, aim to provide domestic and international clients with our interpretation of the relevant legislation and policies of GBA in the above related areas, introduction to relevant market practices, analysis of selected typical cases and share our practical insights.

Baker McKenzie FenXun (FTZ) Joint Operation Office, as the first China (Shanghai) Free Trade Zone Joint Operation, delivers a truly integrated service covering international and PRC law that none of our competitors can presently match. With over 50 years' experience in advising on doing business across the Greater China region, we combine a valuable insight into China's legal, commercial and political landscapes. In response to the national development strategy, we are committed to providing clients with multi-field and comprehensive legal services in the GBA. We are supported by Baker McKenzie's network of more than 6,500 lawyers in 74 locations across 45 countries and regions. You will get first-hand, in-depth knowledge of the local laws and customs of countries across the globe – all in one integrated firm. As such, we bring to matters an instinctively global perspective combined with deep market knowledge and insights.

Tracy Wut
Managing Partner, China Offices
Baker McKenzie

Table of content

Financial Opening and Innovation	01	Opportunities and Challenges for Green Finance in the Greater Bay Area	4
Cross-border Investment & M&A	02	Practice of and Reflection on State-Owned Enterprises' Mixed Ownership Reform in the Context of Cross-Border M&A Transactions	15
Capital Markets	03	Going Public in Hong Kong SAR for Companies within the Greater Bay Area	25
REITs	04	Introduction to Hong Kong and China REITs	33
Real Estate and Infrastructure	05	Overview of Green Building Legal Regime on the Mainland Side of the Guangdong Greater Bay Area	39
Wealth Management	06	Observations on private wealth management practice in GBA	47
Compliance	07	Focus on the Greater Bay Area: Enterprises "Going Global" with Compliance at the Forefront	53
Data Protection	08	New rules on cross-border transfers of personal information in the Greater Bay Area	62
Intellectual Property	09	Building Bridges: Recent IP Legal and Policy Developments in the Greater Bay Area	73
Employment	10	Special Considerations for Layoffs during Business Reorganizations in Guangdong Province	81
Dispute Resolution	11	Mutual Recognition and Enforcement of Court Judgments Between Mainland China and Hong Kong SAR	87
Bankruptcy & Restructuring	12	Recognition and Assistance in Cross-Border Insolvency: Collaboration and Challenges Between Mainland China and Hong Kong	92

Financial Opening and Innovation

01

Author: Simon Leung, Cui Duan

Opportunities and Challenges for Green Finance in the Greater Bay Area

Green finance, also known as "environmental finance" or "sustainable finance," is part of the environmental economy aimed at protecting the environment and achieving sustainable development through financial instruments.[1] In August 2016, the People's Bank of China, along with other ministries, jointly issued the "Guidelines on Establishing a Green Financial System," setting out the policy foundation for establishing a systematic legal framework for green finance. The guidelines define green finance as:

> ...financial services provided for economic activities that support environmental improvement and resource efficiency and tackle climate change, including financial services provided for investment and financing, project operation, and risk management in areas such as environmental protection, energy saving, clean energy, green transportation, and green buildings.

Besides, the green finance system refers to institutional arrangements that support the economic transition to greener practices through green credits, green bonds, green stock indices and related products, green development funds, green insurance and carbon finance.

Under the development philosophy that "lucid waters and lush mountains are invaluable assets" and guided by the strategic objectives of "dual carbon" goals for 2030 and 2060, the construction of a legal framework for green finance has become an area that has been attracting enormous attention in China. The Guangdong-Hong Kong-Macao Greater Bay Area ("**Greater Bay Area**") is a key region for the development of green finance in China. This article will briefly introduce China's legal framework for green finance and the latest policies and regulations in various aspects of green finance within the Greater Bay Area in recent years, and further analyze the current opportunities, challenges and risks that enterprises may face in the field of green finance.

1 See: "Green Finance Development Report of the Greater Bay Area (2024 Edition)" by HSBC Business School, Peking University and HSBC China, https://www.business.hsbc.com.cn/en-cn/campaigns/gba/sustainable-finance-report, last accessed on 17 April 2024.

I. Overview of recent policies and regulations on green finance in the Greater Bay Area

Currently, the major cities within the Greater Bay Area have successively introduced policy frameworks, legal regulatory mechanisms, and incentive and restraint systems related to green finance. Among these cities, Guangzhou, as one of the national pilot zones for green finance reform and innovation, has implemented detailed policies and legal regulations across many areas of green finance. Shenzhen has paid significant attention to the construction of a policy and regulatory framework for green finance and has focused on the development of carbon market support facilities.

In recent years, Hong Kong SAR has emphasized the development of green finance by setting out related rules and standards for investors, incorporating environmental, social and governance (ESG) factors into the governance structures, strategic decisions, risk management and disclosure processes of the financial sector. Having been focusing on the development of green bonds, significant progress has been made. In 2022, over one-third of green bonds and loans in Asia have been arranged in Hong Kong SAR.[2] Going forward, Hong Kong SAR plans to promote the development of industries related to green finance. For example, as green finance gains increasing attention in family offices, the Hong Kong government plans to further encourage green investments among family offices.[3]

Compared to Guangzhou, Shenzhen and Hong Kong SAR, the development of green finance policies in Macao SAR has been relatively slow, with specific policies and regulations on green finance yet to be introduced.

Here we provide a brief overview of the important policies and regulations concerning various aspects of green finance issued in the past three years in the major Mainland cities represented by Guangzhou and Shenzhen in the Greater Bay Area, and Hong Kong SAR.

---

2 See: "Keynote Address at Climate Business Forum: Asia Pacific," https://www.hkma.gov.hk/eng/news-and-media/speeches/2024/02/20240227-1/, last accessed on 17 April 2024.

3 See: "Family Wisdom: A Family Office Hub in Hong Kong" by the Financial Services Development Council of Hong Kong, https://www.fsdc.org.hk/media/lrej3ikz/fsdc_paper_no_45_family_wisdom_a_family_office_hub_in_hong_kong_paper_eng.pdf, last accessed on 17 April 2024.

1. Development planning and industry guidance

Target area	Policy/regulation	Date of publication	Main content related to green finance
Guangzhou	Notice on Promoting Financial Openness and Innovation in Guangzhou	May 2023	• It clearly puts forward to deepen green finance reforms and innovations, and enhance green financial services to boost green industries. It encourages financial institutions to increase capital investment and comprehensively use credit, bonds, leasing and industry funds to support low-carbon and clean energy industries. • It suggests establishing a cross-border green finance service platform.
	Notice on the 2023 Action Plan for Guangzhou's Financial Support for High-Quality Development of the Real Economy	May 2023	• It stresses deepening green finance reforms and innovations, striving to create a demonstration zone for green finance reforms and innovations. It aims for a total green loan balance of over RMB 1 trillion by the end of the year from banking institutions, consolidating the achievements in green finance reforms and better serving the city's goals for peaking carbon emissions and achieving carbon neutrality.
	Notice on the Implementation Plan for Guangzhou's Development of Green Finance to Support Carbon Peaking Actions	April 2024	It introduces the following eight actions: • Enhancing the capability of green finance • Building the green finance system • Optimizing and upgrading green financial services to industries • Innovating the carbon finance market • Enabling synergy through green finance • Enhancing cooperation and communication in green finance • Monitoring and preventing risks in green finance • Incentivizing and restraining mechanisms in green finance

Target area	Policy/regulation	Date of publication	Main content related to green finance
Shenzhen	Opinions on Financial Support for the Comprehensive Deepening of Reform and Opening Up in the Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone	February 2023	It proposes a series of measures to promote green finance development, including the following: • Supporting financial institutions within the Qianhai Cooperation Zone in innovating green financial products • Facilitating the establishment of international green finance certification institutions in the zone • Supporting local enterprises to issue green bonds and obtain green finance in Hong Kong SAR • Enhancing the performance evaluation of financial institutions in terms of green finance • Encouraging training and exchange of green finance professionals between Shenzhen and Hong Kong SAR

2. Green credit

Target area	Policy/regulation	Date of publication	Main content related to green finance
Guangdong province	Guidelines on Accelerating the Development of Green Finance in the Banking Sector of Guangdong	August 2021	It puts forward the following green financial development requirements for the Guangdong banking industry: • Continuously expanding the scale of green credit, strictly controlling the credit allocation to environmentally unfriendly enterprises, aiming to ensure that the growth rate of green credit is not lower than that of other loans, and that the nonperforming loan rate of green loans does not exceed that of small and micro-business loans • In line with the regional industrial development characteristics, continuously increasing financial support in key areas such as green manufacturing, energy conservation and environmental protection, pollution prevention, clean energy, green buildings, green transportation, green agriculture, resource recycling, new energy and new materials • Establishing a scientific green finance risk management and early warning mechanism • Incorporating social responsibility indicators into performance evaluations and increasing the weight of green finance development indicators

3. Green bonds and funds

Target area	Policy/regulation	Date of publication	Main content related to green finance
Hong Kong SAR	Green and Sustainable Finance Grant Scheme ("**GSF Grant Scheme**")	May 2021	• The GSF Grant Scheme is a three-year program announced in 2021, aiming to support green and sustainable bond issuance and lending in Hong Kong SAR. The GSF Grant Scheme provides subsidy for eligible bond issuers and loan borrowers to cover their expenses on bond issuance and external review services. • In the 2024-2025 budget speech, the Hong Kong SAR government proposes to extend the scheme to 2027, which originally is planned to expire in mid-2024, and expand the scope of subsidies to cover transition bonds and loans. This will encourage related industries in the region to make use of Hong Kong SAR's transition financing platform as they move toward decarbonization.[4]
	Green Bond Framework	First published in March 2019 and updated in February 2022	• The framework sets out provisions for issuing green bonds and for financing or refinancing green projects that contribute to environmental improvement, tackling climate change and transition to a low-carbon economy. • The updated framework reflects Hong Kong SAR's latest climate commitments and strategies, aligning with the latest international standards and practices in the green bond market. According to the updated framework, the proceeds of green bonds can be used to finance or refinance projects under nine "eligible categories," including the newly added "climate change adaptation" category and not limited to public works projects.

4 On 3 May 2024, the Hong Kong Monetary Authority (HKMA) released the details on the extension of the GSF Grant Scheme, confirming that the scheme will be extended to 2027. The HKMA has updated the guideline on the GSF Grant Scheme, which expands the scope of subsidies to cover transition bonds and loans. The updated guideline will be effective upon the extension of the scheme on 10 May 2024. See: https://www.hkma.gov.hk/eng/news-and-media/press-releases/2024/05/20240503-9/, last accessed on 7 May 2024.

Target area	Policy/regulation	Date of publication	Main content related to green finance
	Hong Kong Stock Exchange Consultation Paper on Enhancement of Climate Disclosure Under its ESG Framework	April 2023	• The consultation paper proposes to mandate all issuers to make climate-related disclosures in their ESG reports and introduce new climate-related disclosures aligned with the International Sustainability Standards Board Climate Standard. • The public consultation period for this document ended in July 2023. The Hong Kong SAR Green and Sustainable Finance Cross-Agency Steering Group indicates that mandatory climate information disclosure mechanisms are expected to be implemented before 2025.[5]
	Hong Kong Taxonomy for Sustainable Finance ("Hong Kong Taxonomy")	May 2024	• The Hong Kong Taxonomy aims to provide a consistent and internationally recognized definition of green and sustainable economic activities. The fundamental principles include: alignment with the Paris Agreement; proof from greenwashing; interoperability with other taxonomies; science-based criteria and thresholds; and foundations of do no significant harm and minimum social safeguards. • The industries covered by the Hong Kong Taxonomy include: electricity, gas, steam and air conditioning supply; transportation and storage; water supply, sewerage, waste management and remediation activities; and construction.

5 On 19 April 2024, the Hong Kong Stock Exchange (HKEX) published the results of the consultation, indicating broad market support for the climate-related disclosure requirements based on International Financial Reporting Sustainability Disclosure Standard 2-Climate-related Disclosures (IFRS S2). Starting from 1 January 2025, main board issuers (other than large-cap issuers) and GEM issuers will be required to disclose "Scope 1" and "Scope 2" greenhouse gas emissions as defined in IFRS S2. HKEX concurrently issued the Implementation Guidance to assist issuers in complying with the new climate disclosure obligations. See: https://www.hkex.com.hk/News/Regulatory-Announcements/2024/240419news?sc_lang=en, last accessed on 17 April 2024.

4. Carbon market

Target area	Policy/regulation	Date of publication	Main content related to green finance
Guangzhou	Guidelines on Financial Support for the Construction of Corporate Carbon Account Systems	September 2022	• It proposes policy measures including the construction of a complete corporate carbon account operating mechanism, giving full play to the role of financial support for enterprise carbon accounts, strengthening the pilot promotion and application of corporate carbon accounts and increasing organizational support for implementation. • Carbon accounts provide businesses with essential tools for measuring their own carbon emissions, aiding them in focusing on their operational behaviors and carbon emission data to improve carbon performance.
	Notification on the Implementation Measures for Voluntary Emission Reductions in Guangzhou	January 2023	• It encourages financial institutions to explore the opening of personal carbon accounts and issuing carbon credit cards.
Shenzhen	Shenzhen Carbon Emission Rights Trading Management Measures	May 2022	It further regulates carbon emission trading activities in the following aspects: • Integrating trading methods • Innovatively setting up public welfare carbon accounts • Establishing a comprehensive carbon inclusion system • Strengthening the regulation of trading activities
	Notification on Shenzhen's Carbon Trading Support for Carbon Peak and Neutrality Implementation Plan	November 2023	• It continues to promote innovation in carbon financial products. • It encourages enterprises to engage in green and low-carbon technology research and investment. • It pushes Shenzhen financial institutions and other green financial service organizations to participate in-depth in international green financial standards research.

II. Future opportunities and challenges for green finance

1. Opportunities for innovation in the field of green finance

(1) Increasingly comprehensive policy incentive mechanisms

Currently, green finance policies in the Greater Bay Area are progressively being implemented. From a macro perspective, green finance incentive policies cover various areas such as green credit, green bonds and funds, and the carbon market, providing policy security for enterprises and financial institutions in a diversified manner. At the micro level, specific policy incentive schemes for key areas like green bonds and green credit have been introduced in some regions. For example, Futian district in Shenzhen offers a 2% discount on green bonds, while Huadu district in Guangzhou provides subsidies calculated as 1% of the amount of green bonds issued by listed companies and companies preparing to list (capped at RMB 1 million).

In the future, to encourage the development of green finance in the Greater Bay Area, numerous substantial incentive policies are expected. One is optimizing the risk weight of green assets. As attention to green finance grows, both market participants and regulatory authorities have largely agreed on appropriately reducing the risk weights for green assets to decrease the economic capital occupation of banks in green credit operations. Policies related to these are expected to be piloted in the Greater Bay Area. Another focus is actively exploring provisions such as preferential repayment for green bonds and reducing or exempting reserve requirements for green credit risks, thereby increasing the priority of green bonds and reducing the credit risk of green assets.[6]

Particularly noteworthy is the carbon market, a key area of focus in recent years within the Greater Bay Area, where numerous practical policy incentives have been introduced. For example, Guangzhou is advancing pilot projects for corporate carbon account systems, encouraging financial institutions to develop innovative financial products such as "carbon footprint-linked loans,"[7] which offer preferential financing rates and other tangible policy incentives to low-carbon enterprises.

(2) Rapid development of ESG investing

ESG investment aims to promote responsible investment and advocate for sustainable development investment. Compared to other mature countries, the development of responsible investment and ESG concepts in China is relatively late. China's private equity investment industry is still in the early stage of exploration. However, with the acceleration of carbon neutrality

---

6 See: "Green Finance Development Report of the Greater Bay Area (2024 Edition)" by HSBC Business School, Peking University, and HSBC China, https://www.business.hsbc.com.cn/en-cn/campaigns/gba/sustainable-finance-report, last accessed on April 17, 2024.

7 See: "Interpretation of the Policy on Guiding Opinions on Financial Support for the Construction of Enterprise Carbon Account System" issued by the Office of the Financial Committee of the Guangzhou Municipal Party Committee, the Financial Work Committee of the Guangzhou Municipal Party Committee, and the Guangzhou Local Financial Supervision and Administration Bureau, http://jrjgj.gz.gov.cn/zwgk/zfxxgkml/zfxxgkml/bmwj/zcjd/content/post_8697373.html, last accessed on April 17, 2024.

policies promoting the systematization of ESG regulatory policies, A-shares being included in major international indices such as MSCI, and the quickening pace of institutional investors like pension funds and corporate annuities entering the capital market, it is anticipated that ESG investment will reach a tipping point in the capital market. An increasing number of companies have paid attention to ESG compliance and investment. These companies are actively adapting to ESG developments to simultaneously enhance their economic benefits and societal value.[8]

2. Challenges and response suggestions for green finance

Against the backdrop of rapid development in green finance policies and regulations, there are both opportunities for innovation and challenges. Currently, the regulatory framework for green finance in the Greater Bay Area is not yet fully developed, and companies should pay attention to the potential challenges and risks, thus getting prepared to respond.

(1) Lack of uniformity in green finance standards and the gap with international standards

Currently, various regions across the country, including the Greater Bay Area, have introduced green finance-related standards, but there is a lack of coordination and uniformity among different subsectors and products. For example, there are differences between the standards for green credit and green bonds in China. The "Green Bond Support Project Catalog (2021 Edition)" has eliminated projects related to fossil energy, such as "Clean Coal Production" and "Clean and Efficient Utilization of Coal," while other green finance standards, such as the "Green Low-Carbon Transformation Industry Guidance Catalog (2024 Edition)" for green credit, have not yet removed these projects, leading to a lack of uniformity in domestic green finance standards.

Moreover, the alignment of China's green finance standards with international standards should be further strengthened. For instance, to prevent "greenwashing" risks, China's green credit is limited to loans for green industry development and carbon emission reduction, whereas many international green standards also include loans that promote the greening of high-emission industries or integrate environmental risk factors into the credit process.[9]

For enterprises, it is necessary to clarify the differences between standards for different green finance subsectors and product types at both the central and local levels to prevent confusion in practice. Additionally, it is advisable to establish an internal green standard compliance self-assessment mechanism promptly, so as to adhere to relevant Chinese green standards and actively align with international green standards.

---

8 See: "Green Finance Development Report of the Greater Bay Area (2024 Edition)" by HSBC Business School, Peking University and HSBC China, https://www.business.hsbc.com.cn/en-cn/campaigns/gba/sustainable-finance-report, last accessed on 17 April 2024. See: "ESG Investment Series: The Rise, Current Status, and Prospects of ESG" by CICC.

9 See: "Green Finance in Carbon Neutrality: Guiding to Promote Services and Turning Challenges into Opportunities" by CICC.

(2) Green finance information disclosure mechanisms to be further built and improved

Currently, there are still issues existing in the green finance information disclosure mechanism in the Greater Bay Area, such as unclear disclosure indicators and narrow disclosure scopes. Taking green bonds as an example, although green bond issuers have begun to implement the requirement to disclose environmental benefits information before issuance, the indicators for disclosing the environmental benefits of green bonds are not comprehensive enough to quantify the environmental benefits generated by the funds. The lack of detailed standards throughout the entire process and at each stage of green bond information disclosure mechanisms leads to a gap between the actual environmental benefits and the expectations of some projects. Additionally, the green bond market in the Greater Bay Area still faces issues of nonuniform green project catalogs and inconsistent environmental benefit disclosure indicators. There is an urgent need for the mutual recognition and unification of green bond standards between Hong Kong SAR and Macao SAR.[10]

Recently, the green finance information disclosure mechanism in the Greater Bay Area is rapidly advancing in terms of standard refinement, completeness assessment, coordination and regional mutual recognition. It is expected that the construction of the information disclosure system will become a key area in the future regulatory focus of green finance in the Greater Bay Area. It is recommended that enterprises actively practice the requirements of green finance information disclosure, regularly perform internal green data statistics, making clear the relevant authorities in charge for information disclosure and actively implement the submission of green finance information.

III. Conclusion

The blueprint for green finance in the Greater Bay Area has been drawn, with a rapidly constructing and implementing policy and regulatory framework covering diverse fields such as green credit, green bonds and funds, green insurance, the carbon market and ESG. For enterprises and financial institutions in the Greater Bay Area, opportunities and challenges coexist, and emphasis has been equally placed on policy incentives and compliance regulation. It is crucial for these entities to closely track policy progress in the field of green finance, clarify responsibilities and rights, and proactively practice relevant green finance standards, thus enhancing their economic benefits and social value synchronously in the era of green development.

Contact Partners:

Simon Leung
Partner, Hong Kong
+852 2846 2109
simon.leung@
bakermckenzie.com

Cui Duan
Partner, Beijing
+86 10 6535 3960
duan.cui@
bakermckenziefenxun.com

10 See: "Green Finance Development Report of the Greater Bay Area (2024 Edition)" by HSBC Business School, Peking University and HSBC China, https://www.business.hsbc.com.cn/en-cn/campaigns/gba/sustainable-finance-report, last accessed on 17 April 2024.

Cross-border Investment & M&A

02

Author: Jeff Xu

Practice of and Reflection on State-Owned Enterprises' Mixed Ownership Reform in the Context of Cross-Border M&A Transactions

Introduction

As the process of global economic integration accelerates and the role of state-owned enterprises (SOEs) in the global market becomes increasingly prominent, mixed ownership reform of SOEs ("**MO Reform**") has become an important way for SOEs to enhance their core competitiveness and implement their internationalization strategy. More specifically, MO Reform refers to the introduction of nonpublic capital, collective capital and foreign capital into SOEs to allow them to participate in the restructuring and reorganization of SOEs as well as in the operation and management of SOEs, among which the introduction of overseas strategic investors is the approach widely adopted by SOEs to implement their MO Reform, which largely defines to what depth and breadth that MO Reform can succeed. This article is intended to explore the approaches and processes of introducing overseas strategic investors into the MO Reform of SOEs, the key issues, considerations and potential challenges during transaction execution and the solutions from the perspective of legal practice.

I. Approaches, main processes and considerations of MO Reform of SOEs

1. Main approaches of MO Reform of SOEs

(1) Approach 1: Transfer of equity interests/property rights by original shareholders

Under this approach, MO Reform is implemented by transferring the property rights of the original shareholders, i.e., the purpose of MO Reform is achieved through the transfer of equity interests by the original shareholders, without changing the registered capital or share capital of the SOE under MO Reform. Although the transfer of equity interest by the original shareholders can achieve the purpose of bringing in non-state owned capital, it cannot bring incremental capital into the SOE under MO Reform. In addition, the Measures for the Supervision and Administration of State-owned Assets Transactions of Enterprises provides that, in principle, no qualification conditions will be imposed on the transferee for transfer of property rights. Therefore, in transferring property rights, the SOE under MO Reform is usually unable to set any conditions on the investor regarding qualification, business, resources, etc., to fulfill the purpose of its MO Reform.

(2) Approach 2: Capital increase

Compared with transfer of property rights, a capital increase has multiple advantages, which can provide funding required by the SOE under MO Reform, and also enable such SOE to select the investor that best meets the needs for its development by setting qualification conditions on the investor, carrying out public selection and competitive bidding, etc. In practice, a capital increase is often complemented by employee equity incentive scheme. In recent years, "capital increase + employee equity incentive scheme" has become a typical approach for MO Reform.

2. Main processes and considerations of MO Reform

To carry out the MO Reform, the SOE concerned must first formulate an MO Reform proposal, which usually contains the following: a study on the feasibility of and need for the MO Reform; the basic principles and line of thought of the MO Reform; the equity structure of the SOE after the MO Reform; the main initiatives to change the operation mechanism; the conditions, requirements, methods and pricing methods for introduction of nonstate owned capital; employee incentive plans; creditors' rights/debt disposal plans; employee resettlement plans; solutions to historical legacy issues; measures for assessment and prevention of reform risks; measures for accountability for violating relevant regulations; organizational safeguards; and progress arrangements for the MO Reform.

Second, the SOEs under MO Reform must fulfill internal decision-making and approval procedures in accordance with relevant laws and regulations. In terms of internal decision-making procedures, such SOEs should first consider and form a written resolution on the MO Reform in accordance with their articles of association and the relevant internal management rules of such SOEs . In terms of approval procedures, (1) any capital increase or transfer of property rights of a SOE must be examined and approved by the state-owned assets supervision and administration authorities, as required by the Measures for the Supervision and Administration of State-owned Assets Transactions of Enterprises. If the state no longer has a controlling interest in the SOE due to a capital increase or transfer of property rights, it must be reported by the relevant state-owned assets supervision and administration authority to the people's government at the local level for approval. (2) If the MO Reform is carried out at the level of a subsidiary of a SOE by a transfer of property rights, the SOE must determine the appropriate authority for approval and administration in accordance with the rules formulated by such SOE governing the transfer of property rights of its subsidiaries, and if the MO Reform is carried out by a capital increase, it must generally be decided or approved by such SOE on its own. However, regardless of whether a transfer of property rights or capital increase is adopted, if the main business of SOE's subsidiary is in an important industry or a key sector that involves national security and the lifelines of the national economy, and mainly undertakes major special projects, it must be reported by the SOE to the state-owned assets supervision and administration authority at the same level for approval.

Third, the relevant procedures of financial auditing and asset appraisal must be performed for the MO Reform in accordance with the Measures for the Supervision and Administration of State-owned Assets Transactions of Enterprises. An appraisal institution with appropriate qualifications must be engaged to carry out such asset appraisal, and the minimum price of the subsequent transaction must not be lower than the appraisal value.

Fourth, for equity transfer or capital increase carried out for the MO Reform of SOEs, strategic investors must generally be publicly solicited through the property right exchange and be selected in an open, fair and impartial manner. In the process of selecting investors, attention must be paid to ensuring that all types of social capitals must have equal rights to participate, and the requirements for the conditions of the prospective participants must not be explicitly targeted or in violation of the principle of fair competition.

Finally, executing transactions at legally established property right trading institutions ("**Listed Transaction**") is one of the basic requirements under the current state-owned assets supervision and administration regime for the sale of property rights of SOEs and for the capital increase of SOEs. The key steps of a Listed Transaction (taking the capital increase of an SOE as an example) are as follows:

Pre-communication and pre-disclosure through property right exchange	The SOE under MO Reform may pre-disclose information through the property right exchange before issuing the formal announcement of capital increase.
Submission of listing application	The SOE under MO Reform must submit the Application for Release of Information on Capital Increase, its business license or other supporting documents of its entity qualifications, its registration certificates of property rights in state-owned assets, articles of association, internal decision-making and approval documents, annual audit reports for the past three years, documents related to the valuation of the enterprise, etc.
Due diligence and reverse due diligence	The intended investors conduct due diligence on the financial and legal status of the SOE under MO Reform, which in turn conducts reverse due diligence on the intended investors.
Submission of investment application by investor and investor qualification review	An investor that intends to formally participate in the capital increase must submit investment application materials to the property right exchange, including the Application for Investment, its business license or other supporting documents of its entity qualifications, its articles of association, internal decision-making and approval documents, etc. Investor qualification review must be carried out by the financial and legal advisers based on the information derived from the reverse due diligence.
Payment of deposit by investor	After the property right exchange notifies every intended investor of the result of the investor confirmation by the SOE under MO Reform, the confirmed intended investor must pay the deposit to the account designated by the property right exchange and become a qualified intended investor.
Investor selection and confirmation	The SOE under MO Reform must select the final investor through bidding, competitive negotiation, comprehensive evaluation, etc. Upon confirming the investor, a Notice of Capital Increase Result will be issued by the property right exchange.

It should be noted that the above provisions for a Listed Transaction will generally apply to the MO Reform of domestic SOEs, but it is difficult to apply a Listed Transaction to the MO Reform of SOEs' overseas subsidiaries for cross-border M&A transactions. According to the Interim Measures for the Administration of Overseas State-owned Property Rights of Central State-owned Enterprises, for a transfer of overseas state-owned property rights by central SOEs and their subsidiaries at all levels, in principle, the intended transferee can be determined by means of "multiparty comparison and selection," and such transfer must be listed and conducted at the pilot institution for the transfer of state-owned property rights of central SOEs only if conditions permit.

II. Analysis of core issues in M&A transaction documents of SOEs' MO Reform

Although overseas strategic investors introduced into SOEs' MO Reform usually have high synergies with the relevant SOE's business operations, overseas strategic investors in different geographic regions, markets and management modes and the existing management of SOEs usually have different views and demands on the formulation and implementation of the MO Reform plan, the operation and management of the company after the MO Reform, and the distribution of rights, obligations and benefits among the shareholders. Please find below our experience in drafting and negotiating share subscription or purchase agreements for the introduction of strategic investors by SOEs and shareholders' agreements and constitutional documents such as articles of association after the MO Reform ("**Constitutional Documents**," together with the aforesaid share subscription or purchase agreements and other ancillary documents, the "**Transaction Documents**") in the context of SOEs' MO Reform projects with points of common disagreements and disputes between the parties and recommendations:

1. Valuation and transaction price of assets of SOEs

According to the Law of the People's Republic of China on State-owned Assets of Enterprises, the Measures for the Supervision and Administration of State-owned Assets Transactions of Enterprises, the Circular of the General Office of the State Council on Forwarding the Implementation Opinions of SASAC about Further Standardizing the Work Relating to the Restructuring of State-owned Enterprises, and the Operational Guidelines for Mixed Ownership Reform of Central State-owned Enterprises, etc., SOEs attracting capital for the MO Reform must commission an appraisal institution with appropriate qualifications to carry out an asset appraisal of the subject property rights (i.e., the target company) and determine the transaction price based on the approved or filed appraisal results. The appraisal result/report of the appraisal institution usually remains valid for one year. If the parties to the transaction have not entered into an agreement by the expiry of the appraisal report, a new appraisal of the value of the subject property rights is required to determine a new transaction price. Once determined, the parties to the transaction may not adjust the transaction price on the grounds of gain or loss during the period.

However, in cross-border M&A transactions targeting private companies, the parties to a transaction usually agree on a price adjustment mechanism so that the transaction price can more accurately reflect the value of the target company for the valuation of the target company. There are two common types of price adjustment mechanisms, namely: (a) closing accounts or completion Accounts mechanism, which is commonly used in the US market, where the valuation is based on the valuation agreed upon by the parties and adjusted according to the target company's cash and liabilities at the time of closing; and (b) locked box mechanism, which is more popular in the European market, where the parties to a transaction agree on a date prior to the signing of the agreement as the base date (often defined as the "Locked Box Date"), determine the value of the target company based on the financial statement data on the base date and require the seller (or the target company) to refrain from engaging in anything that might transfer or diminish the value of the target company between the Locked Box Date and the closing date, i.e., no "leakage."

Considering the conflict between the above mandatory legal provisions on the price of state-owned asset transactions and the foreign investors' demand for price adjustment of investment transactions, in practice, the parties to a transaction may consider adopting a transaction mode similar to the locked-box mechanism based on a fixed price, i.e., the seller or the company undertakes that there will be no leakage by the closing date and agrees to compensate the investor by way of liquidated damages if there is any breach (i.e., leakage), thus indirectly realizing the purpose of adjusting the funds/price invested by the investor. However, it should be noted that the funds paid by the seller or the company in the name of liquidated damages and in the name of price adjustment may fall under different categories in the tax and foreign exchange declarations and payments related to the transaction, which may be subject to different procedural requirements and may lead to different tax consequences. In addition, the competent authorities of the SOE may not recognize such indirect price adjustment mechanism based on the principle of substance over form. In this regard, the parties to a transaction should fully communicate with tax advisers, banks and the competent authorities of the SOE on the determination of the transaction price and the above-mentioned indirect adjustment mechanism to confirm its feasibility.

In addition to the above scenarios regarding the determination and adjustment of the price of M&A transactions, the requirements regarding the valuation of state-owned assets are also applicable to other property rights transactions (e.g., capital increase of a company, transfer of shares by shareholders) of enterprises under MO Reform. For this reason, the provisions of the Constitutional Documents of the enterprises under MO Reform relating to property rights transactions (e.g., procedures for share transfer, increasing or reducing the capital) should consider the prerequisite requirements for the valuation of such assets and set the relevant prerequisites and time periods.

2. Payment of transaction price

As cross-border M&A transactions involve multiple jurisdictions, the conditions precedent and commitments that need to be met prior to closing (e.g., obtaining regulatory approvals, completing reorganization, etc.) are usually complex and time-consuming, and, as a result, there may be a gap of several months or even longer between the time of signing the agreement and the time of closing. In addition, investors often wish to pay the transaction price at a later date or in installments (when the enterprise achieves performance milestones) in order to mitigate the risk of post-closing defaults by the enterprise or in the event of a post-closing performance commitment or similar "valuation adjustment" mechanism with the enterprise.

However, in cases involving the transfer of state-owned property rights, the payment arrangement of the transaction price also needs to consider the requirements of state-owned assets supervision. According to the Measures for the Supervision and Administration of State-owned Assets Transactions of Enterprises, the transaction price for the transfer of state-owned property rights (not applicable to capital increase and MO Reform) must be paid in one lump sum within five working days from the effective date of the contract in principle. Only when the transaction amount is large and it is indeed difficult to pay the amount in one lump sum can it be paid in installments, in which case, the first instalment must not be less than 30% of the total price and must be paid within five working days from the effective date of the contract. Such provisions, on the one hand, allow state-owned shareholders to seek more favorable payment arrangement on the grounds of meeting the requirements of state-owned assets supervision; on the other hand, they are somewhat different from the usual practice of cross-border M&A transactions mentioned above, which, to a certain extent, limit the flexibility of the transactions.

It is worth mentioning that the Measures for the Supervision and Administration of State-owned Assets Transactions of Enterprises stipulate that the asset transactions of overseas state-owned and state-controlled enterprises must also be implemented in accordance with the provisions of the Measures, but the Interim Measures for the Administration of Overseas State-owned Property Rights of Central State-owned Enterprises are relatively lax on the requirements for payment of the price. According to Article 14 of the Interim Measures for the Administration of Overseas State-owned Property Rights of Central State-owned Enterprises, the price for the transfer of overseas state-owned property rights must be paid in accordance with the property rights transfer contract, and must be paid in one lump sum in principle. If it is necessary to pay in installments, the transferee must provide legimitate security. In practice, we believe that both parties to a transaction should, based on the above principle, consult the state-owned assets approval department and negotiate a plan that can satisfy the requirements of state-owned assets supervision and is in line with the practice of cross-border mergers and acquisitions, for example, by providing a performance guarantee by the investor (or its affiliates with commercial substance), opening a bank escrow account or issuing irrevocable letters of credit payable on demand to ensure the certainty of payment by the investor.

3. Controlling interest for state-owned capital and protection for minority shareholders

According to the Guiding Opinions of the CPC's Central Committee and the State Council on Deepening the Reform of State-owned Enterprises, the Operational Guidelines for Mixed Ownership Reform of Central SOEs and other relevant regulations, for a commercial SOE that carries out its main business in an industry or sector with full market competition, state-owned capital can either have absolute or relative control over such SOE or participate in such SOE. For a commercial SOE that carries out its main business in an important industry or a key sector that involves national security and the lifelines of the national economy and mainly undertakes major special projects, state-owned capital must maintain a controlling interest in such SOE while participation in such SOE by non-state owned capital must be supported. In practice, most of the SOEs, in their initial attempts to implement the MO Reform, wish that state-owned capital maintain its absolute control over them. One of the core principles derived from this, is that, after the MO Reform, the controlling shareholder of an SOE representing state-owned capital can still consolidate the financial statements of the SOE. According to AS 33 - Consolidated Financial Statements, consolidation of financial statements must be determined based on the consolidating party "controlling" the consolidated party. "**Control**" is the power of one entity to determine the financial and operating policies of another entity and to obtain benefits from the operations of such other entity. Generally, if an entity ("**consolidator**") owns more than one-half of the voting rights of another entity ("**consolidated**"), the consolidated will be recognized as a subsidiary of the consolidator and may be included in the consolidation of the consolidator's financial statements, unless there is evidence that the consolidator does not control the consolidated.

In contrast to the above requirement for state-owned capital to maintain its controlling position, in cross-border M&A transactions, strategic investors (as opposed to financial investors) usually wish to be more deeply involved in the management and operation of the target company and to improve and promote its business and enhance its profitability, so as to realize a return on their investment. To achieve this goal, strategic investors often require that detailed operational and management mechanisms as well as clauses for protection of minority shareholders should be included in the Transaction Documents. Customary clauses include: the right to appoint key management personnel or the right to veto the nomination of such management personnel by the majority shareholder; the right to review and veto the company's budgets, business plans, financial statements, etc.; and the right to review and veto matters material to the company (e.g., amendments to articles of association, increase or decrease of capital, merger or demerger, distribution of profits, external investment and financing, etc.). Such rights to appoint or remove senior management (such as president and chief financial officer) and to veto the company's budgets and business plans could be deemed as having a negative effect on the controlling shareholder's control over the company from a financial perspective, which may affect the controlling shareholder's consolidation of the financial statements of its subsidiaries. In view of this, the parties may consider adjusting the above mechanism for protection of investors' rights and interests, so as to weaken the absolute veto power that affects the consolidation of financial statements, provided that the investors' right to fully participate in the company's operation and management and in other important matters is guaranteed. Examples of such adjusted mechanisms are: annual budgets, statements and business plans formulated by the company after the investment must be consistent with and must not materially deviate from the forecasts provided to the investors before the investment; a mechanism must be set up for dispute resolution if there are reasonable objections raised by the investors about the financial data (e.g., hiring a third-party auditor to carry out an audit); setting up objective criteria of qualifications, educational backgrounds, skills and industry experience required for persons who will be the company's management personnel; providing the investors with the right to participate in the hiring of management personnel and to express their opinions.

4. Stability of shareholding structure after the MO Reform

In addition to raising funds to meet the company's production and operation needs, another main objective of the MO Reform of SOEs is to introduce strategic investors with high industry relevance and strong business synergies and complementarities, so as to provide SOEs with strategic resources needed for future development, such as markets, products, technologies and management. In implementing the MO Reform, SOEs usually wish that the investor will continue to commit resources to the company over a long period and that the company will maintain a stable shareholding structure to pursue long-term development. In this regard, state-owned shareholders usually want to include in the Transaction Documents that, after the transaction is closed, the investor will not withdraw from the company by transferring or selling its shareholdings to any third party without the consent of the state-owned shareholders. On the other hand, investors often require flexibility to dispose of their shareholdings, as they need to obtain a return on their investment and to meet the requirements imposed by their internal systems to manage their investment objectives.

To resolve this difference, the parties may consider setting a certain "lock-up period," i.e., neither party may sell its stake in the company for a certain period after the MO Reform. Upon expiry of the lock-up period, the transfer of equity interest by any shareholder will be subject to the rights of other shareholders (such as preemption rights and tag-along rights), and transfer to the company's competitors will be prohibited.

In certain M&A transactions where the investor is aggressive, the investor may even require that, upon expiry of the lock-up period, if it fails to find an interested buyer, the SOE and the state-owned shareholder will be responsible for repurchasing the investor's equity interest at market price to ensure the investor's smooth exit from the company. In addition, the investor may also wish to have the right to exit by selling its equity interest to the state-owned shareholder if there is deadlock between shareholders (e.g., if the state-owned shareholder and the investor are unable to agree on certain material matters) or if there is a material breach of contract by the SOE/ state-owned shareholder (such as being subject to sanctions as discussed below). During negotiation for such exit mechanism, SOEs should strictly carry out asset appraisals and comply with requirements on filing and review as described above to avoid the risk of loss of state-owned assets.

5. Protection against sanction-related risks

With the increase of geopolitical risks in recent years, the challenges faced by Chinese enterprises and investment institutions in cross-border transactions and cross-border business expansions have also intensified, as more Chinese enterprises are placed on sanction lists imposed by the US and other countries and are unable to, or find it difficult to, carry out their overseas operations. In this context, SOEs, which are controlled by state-owned capital, face a higher risk of sanctions than private enterprises. Therefore, while attracting capital for MO Reform, both SOEs and strategic investors need to conduct thorough due diligence on each other and make representations and warranties to ensure that no party is subject to sanctions or is facing the risk of being sanctioned. In addition, the parties must consider certain mechanisms to be included in the Transaction Documents to prevent and address future risks of either party being subject to or affected by sanctions that may be detrimental to the SOE. Such mechanisms include mandatory withdrawal of the party affected by sanctions from the joint venture if there is such a risk (i.e., the equity interest held by the sanctioned party must be sold or redeemed at a price to be agreed by the parties based on an asset appraisal).

III. Conclusion

The implementation of MO Reform through the introduction of overseas strategic investors has put forward higher requirements for SOEs and their subsidiaries at all levels, as they not only need to strictly comply with the relevant laws and regulations on management of state-owned assets, protect state-owned property rights and the interests of state-owned shareholders and avoid the loss of state-owned assets, but also need to consider the unique background of cross-border transactions and the international practice of M&A transactions. SOEs, state-owned shareholders and professional consultants must fully consider all relevant factors and must negotiate with investors accordingly to progress the transactions, so as to ensure that the MO Reform for SOEs where foreign parties are involved is implemented in compliance with laws and regulations and that the ultimate goal of the MO Reform is achieved as expected.

Contact Partners:

Howard Wu
Partner, Shanghai
+86 21 6105 8538
howard.wu@
bakermckenzie.com

Jeff Xu
Partner, Shanghai
+86 21 6105 5991
jeff.xu@
bakermckenziefenxun.com

Capital Markets

03

Authors: Yolanda Zheng, Daisy Chen, Emmy Lo

Going Public in Hong Kong SAR for Companies within the Greater Bay Area

Hong Kong SAR, as an international financial center backed by the Mainland market while enjoying the capital and liquidity of the international capital market, has always been one of the most popular places in the world for securities listing and financing.

The Opinions on Financial Support for the Development of the Guangdong-Hong Kong-Macao Greater Bay Area (Opinions), jointly issued by the People's Bank of China, the former China Banking and Insurance Regulatory Commission,[11] the China Securities Regulatory Commission (CSRC) and the State Administration of Foreign Exchange on 14 May 2020, explicitly encourages qualified innovative enterprises to raise funds and go public in Hong Kong SAR and Macao SAR. Since the introduction of the Opinions, Hong Kong SAR has been the preferred overseas venue for enterprises in the Guangdong-Hong Kong-Macao Greater Bay Area (GBA) to raise funds and go public. On 12 April 2024, the State Council issued Several Opinions on Strengthening Regulation, Preventing Risks and Promoting High-Quality Development of the Capital Market (New National Nine Articles). To tie in with the implementation of the New National Nine Articles, the CSRC took a series of measures to further expand and optimize the scheme of the Shenzhen/Shanghai-Hong Kong Stock Connect, and to assist Hong Kong SAR in consolidating its status as an international financial center. These measures include expanding the scope of eligible products for equity ETFs under the Shanghai/Shenzhen-Hong Kong Stock Connect, supporting the inclusion of securities traded on the RMB counter of the Hong Kong Stock Connect and supporting the listing of Mainland industry leaders in Hong Kong SAR, etc. According to incomplete statistics, during the period from January 2021 to March 2024, nearly 50 GBA enterprises landed in the Hong Kong SAR capital market, covering sectors such as artificial intelligence (AI), biotechnology, fintech and new energy vehicles.

Considering the innovative and high-tech characteristics of GBA enterprises, this article explores the pathways available to them to go public in Hong Kong SAR and the unique funding sources of the Hong Kong listing platform.

I. Diversified pathways for GBA enterprises to go public in Hong Kong SAR

The Hong Kong Stock Exchange (HKSE) is committed to being the hub for the listing of innovative companies and leveraging the power of finance to lead industrial development, upgrading and transformation. Since 2018, the HKSE has carried out a series of reforms to provide greater flexibility to the listing regime by introducing

11 It has been reorganized into the National Financial Regulatory Administration.

separate listing mechanisms for specific types of companies in addition to the traditional listing mechanism:[12]

- In 2018:
  - Allowing large innovative companies (see below for the scope of application) to adopt a weighted voting rights (WVR) structure
  - Creating a separate listing route for pre-revenue biotech companies
- In 2021: Introducing the special purpose acquisition companies (SPAC) listing mechanism
- In 2023: Creating a Main Board listing route for Specialist Technology Companies that are not yet financially qualified for listing

These regimes have significantly enriched the pathways for overseas financing by GBA enterprises and would enable them to take full advantage of Hong Kong SAR as a world-class fundraising platform to promote the advancement of the GBA's innovation and technology industry.

1. WVR structure for large innovative companies

A company with a WVR structure means that a company issues different classes of shares carrying different voting rights. Typically, founders and management usually hold Class A shares with multiple voting rights per share, while other shareholders hold Class B shares with one voting right per share. In the market, many companies wish to adopt a WVR structure to raise capital to grow their business while retaining founders' control of the company to pursue innovation.

Since 2018, the HKSE has implemented a new listing regime that allows companies in the innovative sector to adopt a WVR structure if they meet certain conditions, thereby promoting the HKSE as an important listing venue for companies in the innovative sector worldwide. Since then, Hong Kong SAR has become a popular listing venue for Mainland innovative companies. As of March 2024, 25 companies have adopted the WVR structure for listing in Hong Kong SAR, among which are technology and internet giants, including enterprises from the GBA.

In general, the HKSE will consider the following key factors in deciding whether to allow a company seeking listing to adopt WVR:

(1) The necessary characteristics of innovation: The HKSE would assess whether the company's core business applies new technologies, innovations or new business models which serves to differentiate the company from existing players, whether

---

12 Under the traditional listing regime, a listing applicant proposing to apply for listing on the Main Board of the HKSE is required to fulfill the requirements of trading record period, management continuity, ownership continuity and control, and financial qualification for listing under Rule 8.05 of the Hong Kong Listing Rules. Concerning financial qualifications for listing, the applicant must meet one of the following three tests: profit test (the profit attributable to shareholders must, for the most recent financial year, be not less than HKD 35 million and, for the two preceding financial years, be in aggregate not less than HKD 45 million); market capitalization/revenue/cash flow test (market capitalization of at least HKD 2 billion at the time of listing, revenue of at least HKD 500 million for the most recent audited financial year and positive cash flow of at least HKD 100 million for the three preceding financial years in aggregate); or market capitalization/revenue test (market capitalization of at least HKD 4 billion at the time of listing and revenue of at least HKD 500 million for the most recent audited financial year).

research and development (R&D) is a significant contributor of its expected value and constitutes a major activity and expense, whether the company's success is demonstrated to be attributable to its unique features or intellectual property, and whether it has an outsized market capitalization/intangible assets value relative to its tangible assets value.

(2) Success of the company: It can demonstrate a track record of high business growth.

(3) Contribution of WVR beneficiary: Each WVR beneficiary must have been materially responsible for the growth of the business by way of his skills, knowledge and/or strategic direction in circumstances where the value of the company is largely attributable or attached to intangible human capital.

(4) Role of WVR beneficiary: Each WVR beneficiary must be an individual who has an active executive role within the business and has contributed to a material extent to the ongoing growth of the business. Each WVR beneficiary must be a director of the company at the time of listing.

(5) External validation: Generally speaking, it must have received meaningful investment from at least one sophisticated investor, and at least 50% of such investor's total investment at the time of listing must be retained until six months after the IPO .

(6) Market capitalization and revenue thresholds: The company must have a market capitalization of at least HKD 40 billion at the time of listing; or a market capitalization of at least HKD 10 billion at the time of listing and revenue of at least HKD 1 billion for the most recent audited financial year.

2. Listing regime for pre-revenue biotech companies

The GBA is an important cluster area for China's biomedical industry. At present, the GBA already gathers a number of key biomedical industry clusters such as Hong Kong-Shenzhen Innovation and Technology Park, Guangzhou International Bio Island, Nansha Biomedical Industry Cluster, Songshan Lake Biomedical Industry Base, Shenzhen Guangming Science City, Hong Kong Science Park, and Traditional Chinese Medicine Science and Technology Industrial Park of Co-operation between Guangdong and Macao.

Compared with traditional industries, the biomedical industry presents characteristics of high input, high output, high risk and high technology intensity. In the early stage of establishment, biomedical companies usually solve their financing needs through venture capital. Due to the time-consuming process of applying for drug patents, many biomedical companies will be unprofitable for a long period before and after listing. In 2018, the HKSE introduced a new chapter — Chapter 18A — in the Hong Kong Listing Rules, which allows pre-revenue biotech companies to be listed on the HKSE, lowering the listing threshold and providing start-up biotech companies with an important financing platform, making Hong Kong SAR a leading global biotech financing center. As of March 2024, 64 biotech companies have been listed in Hong Kong SAR under Chapter 18A, raising more than HKD 120 billion through IPOs, including GBA biotech companies, such as HighTide Therapeutics and Zhaoke Ophthalmology.

The conditions for pre-revenue biotech companies to apply for listing under Chapter 18A mainly include the following:

(1) The applicant has primarily engaged in R&D, application or commercialization of biotech products, processes or technologies.

(2) The applicant has developed at least one core product beyond the concept stage.

(3) The applicant has been primarily engaged in R&D for the purpose of developing the core product and has continued such R&D during the 12 months prior to listing.

(4) Its primary reason for listing is to raise funds for R&D to bring its core product to commercialization.

(5) Ownership of registered patent(s), patent application(s) and other IP rights relating to its core product.

(6) At least one sophisticated investor has made a meaningful investment into the company at least six months before the date of the proposed listing (which must remain at IPO).

(7) Other listing requirements: The applicant has an initial market capitalization at the time of listing of at least HKD 1.5 billion, has had the existing business operated under substantially the same management for at least two financial years prior to listing, and has sufficient working capital to cover at least 125% of the group's costs for at least 12 months from the date of publication of its listing document (after taking into account the proceeds of the applicant's initial listing).

3. SPAC listing regime

The HKSE introduced the SPAC listing regime in 2021. A SPAC is a type of shell company that raises funds through its listing first, so that sophisticated SPAC promoters can identify and acquire a suitable M&A target after listing (which is a de-SPAC transaction). The company formed as a result of such de-SPAC transaction will become the listed issuer and replace the original SPAC, subject to approval by the SPAC shareholders and review by the HKSE.

The SPAC listing regime is simpler and faster than traditional IPO, under which the sophisticated investors can raise funds on the public market before looking for M&A targets, providing start-ups with a more flexible IPO financing option. For innovative new economy companies that lack comparable companies in the market, only a small number of investors may have sufficient expertise to assess the value of these companies, making it difficult for them to determine the offer price through IPO book-building, while the valuation of SPACs' M&A targets is negotiated directly among the companies concerned, SPAC promoters and investors, providing companies seeking to raise funds with a better and clearer valuation. As of March 2024, five SPACs have completed listings on the HKSE, two of which have announced M&A targets, including a GBA gaming social platform operator. We will await for the completion of the listing of the SPAC M&A targets.

4. Listing regime for pre-profit Specialist Technology Companies

Since 2023, the AI industry has become one of the most noteworthy industries. According to the newly released White Paper on the Development of AI Industry in Shenzhen (2023), there are 1,920 AI companies in Shenzhen, with an industry scale of RMB 248.8 billion, a year-on-year growth of 32.10%. In addition, other GBA cities such as Guangzhou, Zhuhai and Dongguan are also continuing to increase their investment in the AI sector.

Against this background, the HKSE introduced the listing regime for Specialist Technology Companies in early 2023, to provide a separate financing pathway for start-up high-tech companies by allowing pre-profit Specialist Technology Companies to be listed under Chapter 18C of the Hong Kong Listing Rules. Specialist technology industries include next-generation information technology (e.g., AI, cloud-based services), advanced hardware and software, advanced materials, new energy and environmental protection; and new food and agricultural technologies.

The HKSE classifies Specialist Technology Companies into two categories — commercial companies and pre-commercial companies — depending on whether the company has revenue of at least HKD 250 million for its most recent audited financial year. The conditions for a Specialist Technology Company to be listed on the HKSE under Chapter 18C mainly include the following:

(1) The company must be primarily engaged in the specialist technology industry.

(2) For a commercial company, it has an expected market capitalization at the time of listing of at least HKD 6 billion; or for a pre-commercial company, it has an expected market capitalization at the time of listing of at least HKD 10 billion.

(3) A commercial company is normally expected to demonstrate a year-on-year growth of revenue throughout the track record period.

(4) The applicant must have engaged in the R&D of specialist technology products for at least three financial years prior to listing and must have incurred expenditure on the R&D that amounted to meet the percentage thresholds required under the Hong Kong Listing Rules (for a commercial company, at least 15% of its total operating expenditure; for a pre-commercial company with revenue of at least HKD 150 million but less than HKD 250 million for the most recent audited financial year, at least 30% of its total operating expenditure, and if the revenue is less than HKD 150 million, at least 50% of its total operating expenditure) on a yearly basis for each of at least two of the three financial years prior to its listing, and on an aggregate basis over all three financial years prior to listing.

(5) It must have received meaningful investment from sophisticated independent investors.

(6) A pre-commercial company must demonstrate and disclose to the HKSE a credible path to the commercialization of its specialist technology products that will result in it achieving the revenue requirement for a commercial company is satisfactory, and it has sufficient working capital available to cover at least 125% of its group's costs for at least 12 months from the date of publication of its listing document (after taking into account the proceeds of the new applicant's initial listing), and must have, as its primary reason for listing, the raising of fund for the R&D of, and the manufacturing and/or sales and marketing of, its specialist technology products to bring them to commercialization and achieving the revenue threshold as required for a commercial company.

As of March 2024, two Specialist Technology Companies have submitted listing applications to the HKSE, including a GBA AI company – QuantumPharm Inc. The company began trading on the HKSE on 13 June 2024, making it the first Specialist Technology Company to be listed under Chapter 18C. With the rapid development of the AI sector, we look forward to seeing more Specialist Technology Companies listing under Chapter 18C of the Hong Kong Listing Rules.

II. Unique source of funding for GBA enterprises after listing in Hong Kong SAR

Listing in Hong Kong SAR is an important milestone for GBA enterprises to step forward to overseas financing, but it is far from the end. How to manage market capitalization and enhance the capital value of a company is a key ongoing issue for every enterprise after listing. Hong Kong SAR, as the only market in the world that can link the capital pools of both Mainland China and overseas, has unique advantages over other overseas markets in terms of the source of investor capital, i.e., the Shanghai-Hong Kong and Shenzhen-Hong Kong Stock Connect Scheme and the HKD-RMB Dual Counter Model, which are more conducive to enhancing the market capitalization management of listed companies.

1. Shanghai-Hong Kong and Shenzhen-Hong Kong Stock Connect Scheme

A review of the Connect Scheme between the HKSE and Shanghai Stock Exchange/ Shenzhen Stock Exchange - Shanghai-Hong Kong Stock Connect was launched in November 2014 and Shenzhen-Hong Kong Stock Connect was launched in December 2016. Since then, qualified individual investors have been able to trade directly in eligible securities under Southbound Stock Connect. Currently, Southbound Stock Connect has become the preferred route for Mainland investors seeking to allocate their capital oversea. Mainland investors' activities on Hong Kong SAR's stock market have increased significantly and they have become an increasingly important source of liquidity. According to official HKSE data, the average daily turnover of Southbound Stock Connect increased from HKD 900 million in 2014 to HKD 33.8 billion in the first half of 2023, accounting for 14.7% of the total average daily turnover of the Main Board of the HKSE. Since its opening and until the end of 2023, the total turnover of the Southbound Stock Connect is close to HKD 40 trillion. In August 2023, the CSRC and the Hong Kong Securities and Futures Commission jointly announced that they had reached a consensus on the proposed introduction of block trading (manual trades) under Stock Connect, and that domestic investors would be able to conduct manual trades via Southbound trading on Hong Kong SAR's stock market, which would further enhance trading convenience and market liquidity.

The liquidity will be enhanced significantly once the shares of listed companies become eligible stocks under Hong Kong Stock Connect. Currently, the eligible stocks under Hong Kong Stock Connect include constituent stocks of Hang Seng Composite Large, Mid and Small Cap Indexes, with an average month-end market capitalization of no less than HKD 5 billion for the 12 months as of the regular adjustment (if the listing time is less than 12 months, the market capitalization will be calculated according to the actual time of listing), as well as the H shares of the A+H share listed companies. Accordingly, for a non-A+H share company that has just been listed on the HKSE, it has to meet the market capitalization and liquidity requirements under the Hang Seng Composite Index to be included in such index before it can be subsequently included in Hong Kong Stock Connect. The Hang Seng Composite Index is regularly reviewed twice a year, on 30 June and 31 December of each year; and for companies with market capitalization in the top 10% of the listed companies and companies listed in the first and third quarters of each year that meet the market capitalization requirements under Hang Seng Large Cap and Mid Cap Indexes, they can also be admitted to Hang Seng Indexes and Hong Kong Stock Connect through the fast-track inclusion mechanism.

2. HKD-RMB Dual Counter Model

Since 2004, Hong Kong SAR has developed offshore RMB business and become a global hub for offshore RMB business. Apart from having the world's largest offshore RMB capital pool, Hong Kong SAR offers the largest variety of offshore RMB investment products around the globe. The HKSE launched "HKD-RMB Dual Counter Model" in June 2023, which allows investors to trade securities of the same issuer in both HKD and RMB and to conduct cross-counter transactions between HKD counter and RMB counter, further promoting the issuance and trading of RMB-denominated securities. As of March 2024, there are 24 dual counter securities, including some of the largest and most actively traded companies in the Hong Kong SAR spot securities market, whose HKD counters together account for about 40% of the average daily turnover in the spot securities market. For issuers, the dual counter model gives them access to a pool of RMB funds and, in particular, the investors holding offshore RMB, which further enhances the liquidity of shares.

III. Conclusion

In summary, the HKSE, as an important financing platform for the development of GBA enterprises, has brought financial support and impetus to GBA enterprises. The HKSE's listing regime reforms in recent years are in line with the development plan of the GBA, providing large-scale innovative companies, biotech companies, SPACs and Specialist Technology Companies with more convenient and flexible access to overseas financing. Furthermore, the Shanghai-Hong Kong and Shenzhen-Hong Kong Stock Connect Scheme and HKD-RMB Dual Counter Model of the HKSE provide a unique source of funding and liquidity support for GBA enterprises after listing on the HKSE.

Contact Partners:

Yingzhe Wang
Partner, Beijing
+86 10 5649 6088
wangyingzhe@fenxunlaw.com

Hang Wang
Partner, Beijing
+86 10 6535 3866
hang.wang@bakermckenzie.com

Brian Wong
Partner, Hong Kong
+852 2846 2446
briankt.wong@bakermckenzie.com

Yolanda Zheng
Partner, Beijing
+86 10 6535 3923
yolanda.zheng@bakermckenziefenxun.com

REITs

04

Author: Jeremy Ong

Introduction to Hong Kong and China REITs

I. What is a REIT?

A real estate investment trust (REIT) is a collective investment scheme that seeks to deliver recurrent income to investors through focused investments in a portfolio of income-generating properties. REITs are usually listed and traded on exchanges, similar to stocks and exchange traded funds.

1. What are the benefits for investors?

From the investor perspective, REITs are an alternative to equities and bonds for investment diversification, offering investors exposure to a wide range of underlying properties (e.g. commercial, industrial, hospitality, diversified).

Compared to direct investment in physical properties, REIT investments require less capital, are more liquid, allow greater diversification, have lower transaction costs and are already professionally managed. They are in particular attractive to passive income investors because of their relatively stable nature (due to investment/development restrictions and maximum gearing limits) and potential for dividend yield (due to minimum distribution requirements).

2. What are the benefits for originator?

From the originator perspective, REITs can provide an alternative funding source complementary to bank loans and bonds, which may be particularly relevant if the financing environment for PRC real estate developers remains challenging.

Originators may sell mature properties to the REIT to fund new/existing development projects or repay debt, which the REIT funds by using net IPO proceeds. This cycling of capital is not limited to the assets injected at IPO, as REITs typically grow by subsequently acquiring assets from the originator after listing.

Perhaps most importantly, REITs allow the originator to retain control over the assets after disposal, as the originator will typically remain the largest unitholder of the REIT. The REIT may remain consolidated under the originator, or alternatively, deconsolidated.

In Hong Kong (but not the PRC), the originator may also own 100% of the external manager of the REIT, giving the originator management control (in addition to equity control) over the REIT subject to conflict mitigation measures such as separate boards and key officers. This also creates an external asset management platform (with ongoing recurrent income stream) for the originator which may augment its business.

3. What are the benefits for government and regulators?

In Hong Kong, the Securities and Futures Commission are very welcoming of new REIT listings and offer a subsidy of up to HKD8 million for the successful establishment of a REIT. It was also announced in the recent 2024-25 budget speech that stamp duty on the transfer of REIT units would be waived.

In the PRC, there are many policy statements endorsing the establishment of REITs, with the regulatory framework continually evolving to encourage and facilitate new REIT listings.

Perhaps the strongest evidence of this policy support are discussions between the Hong Kong and PRC regulators on the establishment of "REIT Connect" which will allow cross-border trading between of REITs listed on the Hong Kong and PRC exchanges through the existing Stock Connect infrastructure. On 19 April 2024, the China Securities Regulatory Commission ("**CSRC**") announced five new key initiatives including "REIT Connect" with further details regarding the admission eligibility criteria to be published in due course.

4. What are the key differences between the Hong Kong and PRC REIT regulations?

Below is a summary of some of the key differences between the Hong Kong and PRC REIT regulations.

In general, the Hong Kong REIT regulations are less restrictive in the following areas:

- No restriction on asset class or geographical location of the assets
- No restriction on use of proceeds (i.e. do not need to be used for developing new/existing projects)
- No mandatory lock-up on the originator
- No prescribed minimum yield requirement
- Higher gearing limit permitted (50% of gross asset value)
- Originator allowed to manage the REIT (subject to conflict mitigation measures)

Simplified REIT Comparison Table

	China REITs	Hong Kong REITs	Singapore REITs
Legal structure	Public Fund + ABS Unit Trust	Unit Trust	Unit Trust
Underlying assets	At least 80% invested in infrastructure projects with at least 3 years operations with stable cash flow (minimum yield of 3.8% but higher in practice) Infrastructure assets only, although this is subject to interpretation by regulators (e.g. commercial infrastructure). Prioritised sectors depending on policy objectives.	At least 75% invested in income generating real estate. Can be from any asset class.	At least 75% invested in income generating real estate. Can be from any asset class.
Geographical restrictions	Mainland China	None	None

Borrowing Limit	**At IPO:** REIT's total assets do not exceed 140% of net assets **Post IPO:** Loans for future acquisitions cannot exceed 20% of REIT's net assets	50% of gross asset value	50% of the deposited property
Distribution	At least 90% of the audited annual distributable amount (after adjustments) shall be distributed each year	At least 90% of the audited annual net income after tax (after adjustments) shall be distributed each year	At least 90% of the specified taxable income shall be distributed each year to qualify for tax transparency treatment
Originator retained ownership	Mandatory lock up: Originator must maintain 20% interest in the REIT for at least 5 years after listing. Further, any holding in excess of 20% is locked up for the first 3 years.	No prescribed requirement but driven by commercial considerations	No prescribed requirement but driven by commercial considerations
Connectivity to PRC	–	Dual currency trading is possible Potential for expansion of stock connect infrastructure to include REITs	–
Listing timing	Varies significantly depending on originator (can be several	6-9 months	6-9 months
Listing approvals	**NDRC:** Screening and recommendation of proposed REIT projects **CSRC:** Approval letter **SSE / SZSE:** No objection letter	**SFC:** Authorisation of REIT as a collective investment scheme; grant of type 9 license to REIT manager **HKEx:** Listing approval	**MAS:** Authorisation of REIT as a collective investment scheme; grant of capital markets service (CMS) license to REIT manager **SGX:** Listing approval

5. What are the key differences between listing a Hong Kong Company or REIT?

Below is a summary of some of the key differences between listing a Hong Kong company or REIT.

In general, the Hong Kong REIT regulations are less restrictive in the following areas:

- No track record period or size test requirements
- No management or ownership continuity requirements
- Less strict business delineation requirements (where the originator is also listed)

REIT Managers are required to obtain a Type 9 (asset management) license from the SFC, although this process is concurrently run with the REIT listing. However from our experience, many originators are happy to apply for this license as it signals the augmentation of their business into professional asset management (asset light model with recurrent fee income).

Hong Kong Companies vs REIT

	Hong Kong Listed Company	Hong Kong REIT
Track record	Track record period of 3 years	No similar requirement
Size tests	Need to meet any of the following tests: **Profits Test:** • Market capitalization of at least HK$500 million. • Profit attributable to shareholders of at least HK$80 million in the last three financial years, with profits of at least HK$35 million recorded in the most recent year and aggregate profits of at least HK$45 million recorded in the two years before that. **Market Cap/Revenue Test:** • Market capitalization of at least HK$4 billion. • Revenue of at least HK$500 million for the most recent audited financial year. **Market Cap/Revenue/Cashflow Test:** • Market capitalization of at least HK$2 billion. • Revenue of at least HK$500 million for the most recent audited financial year. • Positive cash flow from operating activities of at least HK$100 million in aggregate for the three preceding financial years.	No similar requirement
Management continuity	At least the three preceding financial years	No similar requirement
Ownership continuity	At least the most recent audited financial year	No similar requirement New properties are acceptable, although the lack of track record financials may have implications from a marketing perspective (in which case income support structures would need to be considered)
Business delineation	Listing applicants must demonstrate a clear delineation from the business of the parent company / controlling shareholder	Delineation is less strict, as SFC recognises that REITs typically rely upon Originator (e.g. for pipeline acquisitions). Focus is on corporate governance measures instead.
Type 9 licensed manager	Not applicable	REIT Manager needs to be licensed to conduct Type 9 regulated activities under the SFO

Type 13 licensed trustee	Not applicable	REIT Trustee needs to be licensed to conduct Type 13 regulated activities under the SFO
Reorganisation	Only where required	Required, and need to consider friction costs such as tax
Ongoing compliance	With rules governing HKEx listed companies	With rules governing HKEx listed companies and SFC licensed corporations
Other points to note		A subsidy is available for REITs successfully listed on HKEx to cover 70% of eligible expenses paid to Hong Kong based service providers (subject to a cap of HKD8 million).

6. Can I request further information?

For further information, you are most welcome to contact our market leading REITs practice should you have any questions. We have advised on almost all major REIT transactions in Hong Kong (including all Hong Kong REIT listings over the past five years) and also have experience with the listing of PRC REITs.

Contact Partner:

Jeremy Ong
Partner, Hong Kong
+852 2846 1642
jeremy.ong@
bakermckenzie.com

Real Estate and Infrastructure

05

Authors: Alex Gong, Rico Chan

Overview of Green Building Legal Regime on the Mainland Side of the Guangdong Greater Bay Area

I. International and national overview of green building development

China promulgated its first national green building evaluation standard in 2006. In promoting green buildings, China and all other countries share the same underlying sustainability goals, namely, environmental protection, reduction of waste, well-being of building users, conservation of energy and adapting and mitigating climate change impacts. Now that climate change is at the forefront for all governments and businesses worldwide, in addition to energy conservation, decarbonization and adapting to renewable energies are also becoming the principal measurements, drivers and direction of the development of green buildings in China.

For a number of years, China has been the world's largest emitter of carbon dioxide and other greenhouse gases. Hence it was a very significant moment for the global climate change movement that President Xi Jinping of China announced at the 75th session of the UN General Assembly in September 2020 that China will target to peak its carbon emissions by 2030 and to attain carbon neutrality by 2060. In fact, historically, China has always been highly proactive and supportive of international developments in climate change and decarbonization. When the three most important international conventions for climate change were agreed and promulgated by the UN, namely, the 1992 UN International Intergovernmental Panel on Climate Change , the 1997 Kyoto Protocol and the 2015 Paris Agreement, China formally acceded to them within one year of their promulgation.

Since China's public announcement of its 2030/2060 decarbonization commitments, China has issued a series of national policy documents to implement and fulfill its commitments, such as the following:

(1) Outline of the 14th Five-Year Plan and the Long-Range Objectives Through 2035 (中华人民共和国国民经济和社会发展第十四个五年规划和2035年远景目标纲要) (March 2021)

(2) Opinions on Full Implementation of Decarbonization (关于完整准确全面贯彻新发展理念做好碳达峰碳中和工作的意见) (September 2021)

(3) Action Plan for Peaking Carbon Emissions before 2030 (2030年前碳达峰行动方案) (October 2021)

(4) National Climate Change Adaptation Strategy 2035 (国家适应气候变化战略 2035) (May 2022)

(5) Guidelines for Establishing Carbon Peaking and Carbon Neutrality Standards (碳达峰碳中和标准体系建设指南) (April 2023)

Regarding these macro decarbonization policy documents, a number of national policy documents have been issued to actively implement decarbonization in the building and construction sectors, such as the following:

- 2020 Green Building Promotion Action Plan (2020年绿色建筑创建行动方案) (July 2020)
- Opinions on Driving Green Developments in Urban and Rural Areas (关于推动城乡建设绿色发展的意见) (October 2021)

II. Green building — national legal framework

Energy conservation and efficiency performance is the initial focus of China's green building regime. China has established its national legal framework in this area through the 1997 Energy Conservation Law (节约能源法) and the 2008 Civilian Buildings Energy Conservation Regulations (民用建筑节能条例). All civil buildings are required to meet the relevant mandatory energy conservation standards and specifications for building materials, equipment and techniques, failing which, local construction authorities will not grant relevant approvals at the building design, planning, work commencement or completion stage.

Residential and commercial buildings are major sources of carbon emissions due to the huge amount of electricity (and fossil fuel for heat generation in the colder regions of China) consumed for living and economic activities that take place in buildings. To address such operational carbon emissions of buildings, China promulgated its first Green Building Action Plan in 2013, and then promulgated its updated Green Building Evaluation Standard in 2014 (replacing its previous version issued in 2006).

The latest Green Building Evaluation Standard (绿色建筑评价标准) (GB/T50378-2019) was updated in 2019. It provides technical standards for different types of civil buildings. A building can obtain a green building rating of basic grade, one-star, two-star and three-star (the highest rating). Similar to other international rating systems, China's green building rating is granted in two stages: initially, a tentative rating at the design stage, and then a formal rating after completion of construction. In connection with the 2019 Green Building Evaluation Standard, the Green Building Label Management Measures (绿色建筑标识管理办法) were also updated in 2021.

Under the 2019 Green Building Evaluation Standard, the relevant energy conservation standards are still mainly expressed in terms of energy consumption intensity. It should be noted that China has already enacted the following technical standards for calculating and prescribing carbon emission intensity of buildings:

(1) 2019 Building Carbon Emissions Calculation Standard (建筑碳排放计算标准)

(2) 2021 General Rules for Building Energy Conservation and Use of Renewable Energy (建筑节能与可再生能源利用通用规范)

As noted above, in connection with China's drive to shift its principal energy-related sustainability measurements from energy conservation metrics to decarbonization metrics, the 2019 Green Building Evaluation Standard will be further revised in the near future to make it more aligned with the decarbonization metrics under the 2019 Building Carbon Emissions Calculation Standard and the 2021 General Rules for Building Energy Conservation and Use of Renewable Energy.

Currently, only certain types of buildings are mandatorily required to achieve a certain green building rating. Pursuant to the 2020 Green Building Promotion Action Plan (绿色建筑创建行动方案) and other policy documents, China plans that 70% and then 100% of all new buildings in China will attain a green building rating by end of 2022 and 2025 respectively. Meanwhile, the economically more developed provinces and cites, such as Guangdong province, Shenzhen and Guangzhou, set higher regulatory standards and development targets for green buildings.

III. GBA local green building legal framework

1. Principal local regulations and policy documents

The green building regime in Guangdong has been substantially updated with the promulgation of the 2021 Guangdong Provincial Green Building Regulations (广东省绿色建筑条例). These Guangdong Regulations require local governments at county level and above to prepare and promulgate their local "green development specific plan (绿色建筑发展专项规划)." Further, Shenzhen, Zhuhai and Guangzhou, as the three GBA cities granted local legislative power, have promulgated the following specific green building local regulations:

(1) 2022 Shenzhen Special Economic Zone Green Building Regulations (深圳经济特区绿色建筑条例)

(2) 2023 Guangzhou Municipal Management Measures for Green Buildings and Energy Conservation (广州市绿色建筑和建筑节能管理规定)

(3) 2023 Zhuhai Special Economic Zone Green Building Management Measures (珠海经济特区绿色建筑管理办法)

2. Local legal framework — the regulatory requirements

Similar to green building regulations in other parts of China and also other countries, the Guangdong Provincial Green Building Regulations set out a legal framework of "stick" (i.e., regulatory requirements with negative consequences for noncompliance) and "carrot" (i.e., incentive measures) to mandate and promote the development of green buildings.

The key regulatory requirements under the Guangdong Provincial Green Building Regulations for construction and development of new buildings principally include the following:

(1) Per Article 11 of the Guangdong Provincial Green Building Regulations, all new civil buildings must meet at least the basic grade green building standard. The following rules also apply:

(a) All state-funded new buildings must attain at least a one-star green building standard.

(b) Municipal-level local cities in Guangdong may set higher green building standards for new buildings.

(c) The nine GBA cities must designate certain local areas where new buildings must attain at least a two-star green building standard.

(2) Per Articles 9 and 12 of the Guangdong Provincial Green Building Regulations, a new building project must attain the required green building standard stipulated by the applicable "mandatory detailed zoning plan (控制性详细规划)." Further, the required green building standard must be specified in the land grant or allocation document, the "construction project planning permit (建设工程规划许可证)" and all design, construction and supervision contracts and project tender documents.

(3) Developers of for-sale residential real estate projects must specify the required green building standard in the sale contract, residential property usage specifications (住宅使用说明书) and residential property quality warranty certificate (住宅质量保证书).

(4) All parties involved in the building construction progress (such as developer, designer, construction drawing vetting agency, construction supervisor, contractor and construction completion vetting agency) must carry out their work in line with the green building standard required for the project, failing which they will be subject to various regulatory sanctions and the project cannot be put into use and operation.

One important new feature of the Guangdong Provincial Green Building Regulations is the emphasis on (i) the operation of new buildings after construction completion and (ii) the green retrofitting of existing buildings. The key regulatory requirements under the Guangdong Provincial Green Building Regulations in this regard principally include the following :

(1) Per Article 21, the owner, user or the management service company of the green building is required to carry out all necessary maintenance and repair to enable the building to meet the operating metrics of its attained green building rating.

(2) Per Articles 21 and 24:

   (a) Local government at county level or above must establish systems for energy consumption statistics, energy audits, energy consumption monitoring and energy efficiency, to facilitate the operational monitoring of green buildings in a highly effective manner.

   (b) Owners, users, management services companies and other professional service providers of green buildings must not damage the building envelope, or the equipment for conservation or metering of energy or water. Further, they must assist with reporting of energy consumption statistics, energy audit, energy consumption monitoring, energy efficiency assessment and evaluation, rating and post-completion assessment for green buildings.

(3) Per Article 25, major public buildings, government office buildings and other public buildings constructed with state-owned funding or investment must comply with the applicable energy consumption limits for public buildings promulgated by the competent provincial authorities (or such stricter limits promulgated by the competent local authorities at the municipal level or above).

(4) Per Article 26, local building authorities at county level or above must monitor the operation and use of buildings after completion of construction, and they must publicize those buildings that no longer meet the requirements of their attained green building rating.

(5) Per Article 27, local government at county level or above must promote green retrofitting of existing buildings as well as energy performance contracting in connection with such green renovation. Further, if existing major public buildings or existing buildings with state funding or investment are assessed as not meeting their attained green building rating, it is mandatory to carry out green retrofitting for such existing buildings.

It is worth noting that Shenzhen, as the most advanced city among the nine GBA cities in Mainland China , has more stringent regulatory requirements in various aspects. For example:

(1) Per Article 2 of the Shenzhen Special Economic Zone Green Building Regulations, the green building regime in Shenzhen will also apply to industrial buildings, in addition to civil buildings.

(2) Per Article 6 of the Shenzhen Special Economic Zone Green Building Regulations:

 (a) All new buildings must meet at least the one-star green building standard (whereas the Guangdong Green Building Regulations only require new civil buildings to meet at least the basic grade standard).

 (b) All new major public buildings and government office buildings must attain at least a two-star green building standard (whereas the Guangdong Green Building Regulations only require such new buildings to meet at least the one-star standard).

 (c) When existing buildings undergo green renovation, they must meet the one-star green building renovation standard.

(3) Per Articles 25, 26, 27, 32 and 36 of the Shenzhen Special Economic Zone Green Building Regulations, there are more onerous green building and energy conservation compliance and data reporting obligations. For example:

 (a) Owners, users or management service companies of a building are required to provide, with the assistance of the utility companies, real-time energy consumption data to the local authorities.

 (b) Owners or users of a building with a green building rating are required to annually submit the operational data of their building (in comparison to the benchmarks corresponding to their attained green building rating) to the portal designated by the local authorities.

 (c) Local authorities will stipulate the applicable electricity consumption caps for a civil building of different types and scales. If electricity consumption exceeds the applicable cap, the building will have higher electricity tariff rates imposed.

 (d) The energy consumption level of newly built public buildings must not exceed the average between (i) the applicable controlling level and (ii) the applicable aspirational level for such type of buildings. Further, the energy consumption level of existing major public buildings, government offices and buildings constructed with state funding or investments must not exceed the controlling level stipulated by national and local regulations. If the stipulated energy consumption level is not complied with, the building owner or user concerned is required to carry out an energy audit and take steps to reduce the energy consumption level. If the actual energy consumption level has exceeded the applicable level by more than 50% for two consecutive years, then the building owner or user must carry out a green retrofitting for the building.

3. Local legal framework — the incentives

The key incentives authorized by the Guangdong Provincial Green Building Regulations for construction, acquisition and operation of new green buildings or green retrofitting of existing buildings principally include the following (per Article 33 of the Guangdong Provincial Green Building Regulations):

(1) Building floor area needed for green building features (such as the building envelope, sun shelter, noise contract, etc.) may be excluded for calculating the plot ratio and real estate title registration floor area.

(2) Building floor area needed for adopting modular construction methodology may be excluded for calculating the plot ratio and real estate title registration floor area (but subject to caps stipulated under national and local regulations).

(3) R&D expenditures for new green building technologies and products may enjoy preferential tax treatments in line with applicable national tax regulations.

(4) Financial institutions are encouraged to provide green loans, green insurance and green bonds for green building and construction in line with applicable national regulations. Specifically, when a citizen applies to the local housing provident fund for a mortgage loan on residential property, the mortgage loan ratio may be increased (subject to caps per local regulations), if the residential property concerned carries a green building rating of one-star or above.

IV. Green building, energy consumption and carbon emissions

Following China's accession to the Kyoto Protocol in 1998, China has set up seven local carbon emissions trading exchanges in Beijing, Tianjin, Shanghai, Chongqing, Guangdong, Hubei and Shenzhen. Certain building and hotel projects have been selected to participate in the local carbon emissions trading exchanges in Beijing, Shanghai and Shenzhen on a trial basis.

Based on the experience of these local exchanges, China issued the Management Measures for Trading of Carbon Emission Rights (Trial Implementation) (碳排放权交易管理办法(试行)) in 2020 to set up the China National Carbon Emissions Trading Scheme (ETS) in Shanghai. Trading on the National ETS Exchange started in July 2021, while trading on the local exchanges continues. At this stage, only the major electricity power generation companies are mandated to participate in trading the carbon emissions quotas on the National ETS Exchange. Other sectors with heavy carbon emissions (such as steel, cement and chemicals) will also be mandated to participate in the National ETS Exchange in the near future.

As noted above, the Building Carbon Emissions Computation Standard (GB/T51366-2019) (建筑碳排放计算标 准) was promulgated. The General Rules for Building Energy Conservation and Use of Renewable Energies (建筑节能与可再生能源利用通用规范) (GB 55015-2021) was issued in September 2021. These general rules are highly significant in several respects, as follows:

(1) The energy efficiency and carbon emission standards for all building types have been raised quite significantly and mandatorily with effect from 1 April 2022.

(2) National and local authorities have been setting up online platforms to collect, analyze and report energy consumption and carbon emission data of buildings.

(3) These technical standards are very important and necessary to adding carbon emissions (both emission quantum and intensity) as China's new principal energy-related sustainability measuring yardstick, switching from the preexisting focus on only measuring energy consumption.

In fact, prior to the promulgation of the foregoing technical standards for carbon emissions of buildings, Shenzhen (as well as Shanghai and Beijing) already required the owners of some major buildings in Shenzhen to participate in the Shenzhen Emission Rights Exchange.

Per Article 24 of the Shenzhen Special Economic Zone Green Building Regulations, the local authorities must establish and publicize a "Catalogue of Carbon Emissions of Major Buildings" and use it to establish the energy consumption and carbon emission baselines for the building sector. (Such local catalogue is not yet publicly accessible.) However, Shenzhen authorities have been publishing annual reports on the energy consumption performance of major public buildings in Shenzhen in recent years. According to the 2022 Shenzhen Building Energy Consumption Monitoring Report, by the end of 2022, 1,020 government offices and major public buildings (with a total gross floor area of 6.59 million square meters) have been connected to the Shenzhen local energy consumption monitoring portal. Such reporting portal and annual energy consumption monitoring reports provide a solid basis for assisting Shenzhen (and other GBA cities) to switch to using carbon emission as the principal energy-related sustainability measuring yardstick for the building sector, in line with China's national policy.

Contact Partners:

Alex Gong
Partner, Shanghai
+86 21 6105 8516
alexander.gong@
bakermckenziefenxun.com

Rico Chan
Senior Consultant, Hong Kong
+852 2846 1971
rico.chan@
bakermckenzie.com

Wealth Management

06

Authors: Jason Wen, Zhang Fan

Observations on private wealth management practice in GBA

On 10 May 2023, the Hong Kong Legislative Council passed the Inland Revenue (Amendment) (Tax Concessions for Family-owned Investment Holding Vehicles) Bill 2022, which provides profits tax concessions for eligible family-owned investment holding vehicles managed by single family offices in Hong Kong ("**HKFO Tax Concession**"). As a core city in GBA, it is expected that the introduction of HKFO Tax Concession will bring in more development opportunities to GBA.

The High Net Worth Individual ("**HNWI**") population in China has shown significant increase in the last decade. According to the Hurun Wealth Report 2023, by the end of 2022, the number of "High Net Worth Families" in China with assets of more than RMB 10 million has reached 2.08 million, and Guangdong has become the region with the highest number of "High Net Worth Families" in China. Under such backdrop, sound family wealth management and succession planning has become a topic garnering more attention in recent years. In this article, we will discuss some key considerations for Chinese HNWIs to plan for their wealth management and succession, and our observations on the new opportunities and development potentials in GBA.

I. Key considerations for HNWIs in Mainland China

1. Tax

(1) PRC tax residence rules

A common issue in cross-border wealth management is the determination of tax residence status and source of income (i.e., PRC-sourced or overseas-sourced), which is not always straightforward and largely depends on the analysis of factual patterns.

<u>PRC Tax Residency Rules for Individuals</u>

Under the prevailing Individual Income Tax ("**IIT**") regime in Mainland, a non-PRC tax resident individual is only subject to IIT in PRC on PRC-sourced income; whereas, a PRC tax resident is generally subject to IIT in PRC on his/her worldwide income.

A PRC-domiciliary should be considered a PRC tax resident and be liable to IIT in Mainland on his/her worldwide income. A PRC-domiciliary refers to a person who habitually resides in Mainland due to family, economic and/or household (户口) connections with Mainland.

Further, a non-PRC domiciled individual who stays in Mainland for at least 183 days in a calendar year will be a PRC tax resident in that year ("**a non-domiciliary PRC tax resident**"). As an exception to the worldwide income tax liability for PRC tax residents, a non-domiciliary PRC tax resident can be exempt from IIT on income that is both foreign-sourced and foreign-paid unless he/she has stayed in Mainland for at least 183 days per year for a continuous 6-year period since January 2019 (i.e., when the new IIT Law took effect) and is not absent from Mainland for more than 30 days in a single trip in any year within such 6-year period.

PRC Tax Residency Rules for Enterprises

Under the prevailing PRC Enterprise Income Tax ("**EIT**") regime, resident enterprises are enterprises incorporated in Mainland or enterprises incorporated outside Mainland but with its "place of effective management" in Mainland.[13] Resident enterprises are liable to EIT at 25% on both PRC-sourced and foreign-sourced income.

Non-resident enterprises are companies incorporated outside Mainland with no "place of effective management" in Mainland. They are not liable to EIT on foreign-sourced income, and are generally liable to EIT at only 10% on their PRC-sourced passive income unless reduced under an applicable tax treaty. The PRC-sourced passive income includes interest, dividends, or royalties paid or borne by a PRC tax resident, capital gains derived from a transfer of equity interests in PRC resident enterprises, etc. However, in the case where a non-resident enterprise has a permanent establishment ("**PE**") (or "establishment or place" under PRC domestic tax rules if there is no applicable tax treaty), the non-resident enterprise will be subject to EIT at 25% on profits attributable to the PE or "establishment or place" (as the case may be).

(2) Trend towards strengthening tax enforcement on HNWIs

Over the past years, we have observed that local tax authorities have been tightening their supervision over tax compliance as a means to increase tax collection and ease the fiscal pressure on local governments under slowing economic momentum. Below are a few key recent developments in the Chinese tax administration landscape that can be relevant to the HNWIs:

(a) China is continuing to strengthen its tax collection and enforcement tools to enable more efficient tax risk screening and audits. With the construction of Golden Tax IV System, Chinese tax authorities are provided with greater visibility into taxpayers' tax-related information, with more extensive information sharing across government departments and across all tax categories within the tax authority. Besides, the Chinese tax authorities are also more accustomed to utilizing Big Data analysis to monitor and target tax risk points, which reduces the frequency of tax audits, but also makes the selected audits more fruitful (i.e. more extra tax payments collected from the audits).

(b) Stronger international cooperation in information exchange also enables the Chinese tax authorities to have access to information relating to Chinese HNWIs' onshore and offshore financial assets. Specifically, as of April 2023, China has had a total of 106 information exchange partner jurisdictions under the Common Reporting Standard ("**CRS**"), which include many of the popular "tax havens" such as the British Virgin Islands, Bermuda, the Cayman Islands,

13 A "place of effective management" is defined as a place where the overall management and control over the business operations, staffing, finance and assets of the enterprise are exercised in substance.

etc. Under the CRS, the financial account information of Chinese resident individuals in a partner jurisdiction will be provided by the in-charge overseas tax authority to the Chinese tax authorities.

(c) Recently, the Chinese tax authorities have specifically focused on certain key areas in their tax supervision on individuals. For example, to eliminate the regulatory loophole of untimely tax filing and underpayment of IIT on capital gains derived from equity transfers, many local governments (including Beijing, Shanghai, Shenzhen, etc.) have issued regulations specifying that the local Administration of Market Regulation ("**AMR**") should verify the relevant IIT payment or filing status when conducting AMR registration for change of shareholder. Besides, China also realized and took measures to crack down the illegitimate tax planning or tax avoidance arrangements. Under Ministry of Finance and State Taxation Administration Bulletin [2021] No. 41, effective from 1 January 2022, all sole proprietary enterprises and partnerships holding equity investments (including stocks, shares, shares in partnership, etc.) shall be subject to IIT on the basis of their actual income, as opposed to the income assessed by the in-charge tax authority (which might reduce the overall tax burden of an individual).

In view of the above, the Chinese tax authorities may become more active and aggressive on tax collection and enforcement on HNWIs. HNWIs should be mindful of their tax liabilities and compliance obligations in China, review the sustainability of their existing arrangements, identify potential tax risks and take necessary measures to address potential tax audit risks.

2. Other legal considerations for HNWIs in China

Proper estate and legacy planning is central to the longevity and success of one's wealth and family. In addition to the necessary caution in dealing with the complexities in PRC tax rules and the higher risks under the strengthened tax compliance supervision landscape, there are other general legal considerations that may impact the goal to achieving sustainability and ensuring a smooth handover of family wealth to the younger generation.

Where the family members and assets are located in several different jurisdiction, the execution of a will and passing of assets to heirs may need to undergo a rather complicated procedure. For example, transferring ownership of real estate located in Mainland to heirs appointed in a will signed in another jurisdiction might involve procedures including probate and notarization in the foreign jurisdiction, and in Mainland, review and delivery of the notarized will by a specified agent, on-site visit to the real estate registry, etc. The specific timeline and documentation requirements may also vary from place to place, therefore it is necessary to consult with the in-charge authority in advance.

The occurrence of divorce may also pose challenges on the sustainability of family wealth and stability of the corporate control structure. Division of property due to divorce may involve the transfer of stocks or even disputes on the company's controlling rights, which have been observed in the cases of controlling shareholders of many A-share listed companies. It is recommended to make advance planning to minimize the negative impacts if necessary.

For long-term succession planning and passing on wealth for multiple generations, HNWIs may consider putting in place succession planning structures with appropriate family governance mechanisms. Depending on various factors including but not limited to the tax residence status of the HNWIs and their family members as well as the location and place of management of their assets, there may be different related legal and tax considerations. Professional advice shall be sought in order to plan ahead and cater for the family's needs and circumstances.

II. Opportunities and potentials in GBA

Hong Kong is committed to creating a conducive and competitive environment for the businesses of global family offices to thrive in Hong Kong. Among all policy supports, the recently introduced HKFO Tax Concession provides tax concessions and certainty at the level of Family-owned Investment Holding Vehicle ("**FIHV**").

Specifically, eligible FIHVs satisfying the below key conditions are entitled to the tax concession in Hong Kong for profits derived from transactions in specified assets (which generally include most of the typical financial assets that the family would invest in) ("**Qualifying Transactions**") and transactions incidental to the carrying out of the Qualifying Transactions (subject to a 5% threshold) at a tax rate of 0%:

1. At least 95% of the beneficial interest of the FIHV must be (directly or indirectly) held by one or more members of the family. The shareholding ratio can be reduced to 75% where a charitable entity (which is recognized by the Hong Kong Inland Revenue Department for its tax-exempt status under section 88 of the Hong Kong Inland Revenue Ordinance) is involved.
2. The FIHV must be normally managed or controlled in Hong Kong.
3. The FIHV must be managed by an eligible single family office ("**SFO**"); key requirements for the eligible SFO are set out as below:
    (1) It is a private company (incorporated in or outside Hong Kong) which is normally managed or controlled in Hong Kong, and at least 95% beneficial interests of which are held (directly or indirectly) by members of the family (except where a charitable entity is involved);
    (2) At least 75% of the SFO's assessable profits are derived from services provided to the FIHV, underlying Family-owned Special Purpose Entities or family members; and
    (3) The SFO must manage family assets of at least HKD 240 million in aggregate.
4. The FIHV must carry out its core income generating activities ("**CIGAs**") in Hong Kong and meet the substantial activity requirements, which require the FIHV (or SFO, to the extent such CIGAs are outsourced to the SFO) must have, as a minimum, at least 2 full-time employees in Hong Kong who carry out the CIGAs and have the qualifications necessary for doing so and at least HKD 2 million operating expenditure per year incurred in Hong Kong for carrying out the CIGAs.

The HKFO Tax Concession allows HNWIs to explore having their assets managed by their own family office in Hong Kong in order to diversify their wealth with tax certainty provided under the Hong Kong tax regime if properly structured. Interested parties looking to take advantage of the HKFO Tax Concession should seek professional advice on the detailed tax treatment so as to structure their family office and investment holding vehicles carefully.

There are many other policies in the wider GBA to boost the wealth management industries. A variety of supporting policies are issued and implemented to facilitate the interconnection between Mainland and Hong Kong in various perspectives.

In September 2021, the Detailed Implementing Rules relating to Pilot Scheme of Cross-boundary Wealth Management Connect within the Greater Bay Area was issued. Under these rules, eligible Mainland, Hong Kong and Macau residents can invest in wealth management products distributed by banks in each other's market through a closed-loop funds flow channel established between their respective banking systems ("**Cross-border WMC**"). The Cross-border WMC provides more investment channels for individual investors, and also brings about more new business opportunities for financial institutions in GBA. On 24 January 2024, enhancement measures for the Cross-border WMC were announced to refine the eligibility criteria of Mainland investors, scope of participating institutions and eligible products, and the individual investor quota.

Besides Hong Kong, other core cities in the GBA are also making efforts to construct wealth management centre in the region. Both Guangzhou and Shenzhen have released comprehensive action plans at the municipal government level, setting out the roadmap and specific measures to promote the development of wealth management and related industries. Pursuant to the *Guangzhou Implementation Plan for Building a Wealth Management and Asset Management Centre* in GBA, it is proposed to attract financial institutions of various forms (including banks, securities companies, insurance companies, funds, trusts, etc.) to settle in Guangzhou, and to encourage asset management institutions to develop innovative products that can satisfy the diversified investment needs of GBA residents leveraging the Cross-border WMC, Mainland-Hong Kong stock connect and various other investment channels. Similar proposals can also be found in the *Opinions on Accelerating the Construction of Shenzhen International Wealth Management Centre*, which proposes to explore the development of equity-related family trusts, and to support eligible Hong Kong family offices to establish professional institutions in Shenzhen, apply for private equity fund manager registration (and other relevant financial licenses) and develop the Mainland market. The local governments have also taken specific measures to implement the above high-level proposals, e.g. granting government awards to eligible financial institutions newly established and operating in the region, etc.

III. Conclusion

Since the tax and legal regime related to the private wealth management is highly complex, HNWIs should seek professional advice and take into account of different considerations when planning for their family wealth management and succession. Advanced thorough cost-benefit analysis would also be helpful for individuals and families who wish to take advantage of the supportive policy environment in GBA.

Contact Partners:

Amy Ling
Partner, Hong Kong
+852 2846 2190
amy.ling@
bakermckenzie.com

Jason Wen
Senior Tax Consulting
Director, Beijing
+86 10 6535 3974
jason.wen@
bakermckenziefenxun.com

Luis Zhang
Partner, Shanghai
+86 21 6105 5989
luis.zhang@
bakermckenziefenxun.com

Compliance

07

Authors: Vivian Wu, Yiwei Sun

Focus on the Greater Bay Area: Enterprises "Going Global" with Compliance at the Forefront

I. Enterprises "going global": compliance risks that cannot be ignored

1. Long-arm jurisdiction laws in the US

In recent years, the US has frequently utilized its domestic laws to impose trade bans or sanctions on Chinese companies and individuals, or to restrict or even prohibit Chinese companies from conducting normal investment and business activities in the US. Although these laws are domestic laws of the US, they possess strong extraterritorial jurisdiction and are commonly referred to as US "long-arm laws," such as the Foreign Corrupt Practices Act (FCPA), Defend Trade Secrets Act, Anti-Money Laundering Act as well as trade sanctions and export control regulations. Additionally, the US may conduct national security reviews on "covered transactions" between foreign entities and "US businesses" on the grounds of "national security."

For foreign companies, if accused of violating the aforementioned US long-arm laws, they may face criminal, administrative or civil charges from US authorities, and even class action lawsuits in the US and other countries. In response to these accusations, companies often end up paying substantial amounts to settle with regulatory agencies and plaintiffs (for example, in 2023, Binance agreed to pay a USD 4 billion fine for violations of anti-money laundering and sanctions regulations).[14] Many fined companies may even find themselves unable to afford the hefty fines, putting their survival at serious risk (for instance, Odebrecht/Braskem, a Brazilian company fined USD 3.5 billion by US regulatory agencies for FCPA violations in 2016).[15]

Using the FCPA as an example, the table below lists typical cases where the US imposed substantial fines on certain entities.

14 See Office of Public Affairs | Binance and CEO Plead Guilty to Federal Charges in $4B Resolution | United States Department of Justice, last accessed 12 June, 2024.

15 Odebrecht/Braskem appeared on the top 10 list of FCPA cases at the end of 2016, but due to its lack of ability to pay, the total fine imposed by the US Department of Justice was reduced. As a result, the case was removed from the top 10 list in April 2017. See Odebrecht and Braskem Plead Guilty and Agree to Pay at Least $3.5 Billion in Global Penalties to Resolve Largest Foreign Bribery Case in History | United States Department of Justice, https://www.justice.gov/opa/pr/odebrecht-and-braskem-plead-guilty-and-agree-pay-least-35-billion-global-penalties-resolve, last accessed 12 June, 2024..

Number	Company	Fine (billion dollars)	Year
1	Odebrecht S.A.	3.56	2016
2	Goldman Sachs	2.62	2020
3	Airbus SE	2.09	2020
4	Petrobras	1.79	2018
5	Telefonaktiebolaget LM Ericsson	1.27	2018

In addition to hefty fines, companies may also face other collateral consequences, such as loss of specific licenses, missed business opportunities, market loss, being "shunned" by business partners, affecting investors' valuation and confidence in the company, influencing the company's future development strategies and falling behind competitors.

The prominent feature of the US long-arm law is its broad jurisdictional scope. In recent years, the US has frequently utilized its domestic laws to enforce extraterritorial jurisdiction over foreign companies and their executives and even to bring criminal charges against executives of foreign companies who have never set foot in the US. The US government's aggressive enforcement of long-arm jurisdiction has led to significant misunderstandings domestically about some aspects of US long-arm laws. For example, many mistakenly believe that merely using the US dollar or having the slightest connection to the US would subject them to the FCPA. In recent years, some cases prosecuted by the US Department of Justice have faced judicial obstacles regarding jurisdictional issues, demonstrating that there are still certain boundaries to the extraterritorial jurisdiction of the FCPA.

Despite the boundaries of the US long-arm law, using the US dollar in the dollar-dominated international monetary system increases the risk of foreign companies falling under the jurisdiction of US long-arm laws, especially the risk of triggering money laundering offenses. This is because the extraterritorial jurisdiction of US anti-money laundering laws tends to be broader. Under the US anti-money laundering legal framework, US prosecutors can not only bring criminal charges against foreign individuals present in the US (territorial jurisdiction) but also against foreign individuals whose financial transactions, wholly or partially, occur outside the US but involve the US. In some cases, while the US Department of Justice faces significant challenges regarding FCPA charges against foreign entities at the judicial level, there appears to be an overwhelming trend in anti-money laundering cases (such as *US v. Lawrence Hoskins*). This has led to the frequent use of this charge by US law enforcement agencies. Many FCPA and sanction cases are often accompanied by related money laundering charges. For example, in recent years, some FCPA cases involving China have been accompanied by money laundering charges, including cases such as *US v. Chi Ping Patrick Ho* (He Zhiping, former Hong Kong secretary for Home Affairs and former member of the National Committee of the Chinese People's Political Consultative Conference) and *US v. Ng Lap Seng* (Wu Lisheng, a Macau entrepreneur and former member of the Chinese People's Political Consultative Conference).

2. Overseas risks for executives

Under the US long-arm law system, if a company is subject to enforcement by US regulatory agencies for violating relevant laws, company executives may also face charges and could potentially encounter both criminal and civil risks, including imprisonment and fines. Under certain legal frameworks in the US, executives may face a maximum sentence of up to 20 years for violating individual laws (such as the FCPA and sanction-related laws). It is worth noting that executives may face additional charges, and the sentences for different charges can be cumulative. Among the additional charges that may be brought, money laundering is quite common.

For example, former Alstom executive Frédéric Pierucci mentioned in his book "The American Trap" that US prosecutors charged him with 10 counts, totaling a potential sentence of up to 125 years. This immense psychological pressure led Pierucci to ultimately choose to sign a plea agreement and receive a sentence of 30 months in prison.

China has been the jurisdiction with the highest number of bribery-related cases in the history of FCPA enforcement.[16] The US government has repeatedly brought criminal or civil charges against executives of multinational corporations' Chinese subsidiaries in its enforcement practices.

For example, in February 2016, Yu Kai Yuan, the sales director of the Chinese subsidiary of Parametric Technology Corporation, was implicated in bribing Chinese government officials. He entered into a three-year deferred prosecution agreement with the US Securities and Exchange Commission (SEC).

In November 2018, the US government launched the "China Initiative," implemented by the Department of Justice, to enhance monitoring and conduct arrests of Chinese citizens (including corporate executives) in the US and third countries on grounds such as violations of the FCPA, violations of US sanctions, infringement of US trade secrets and endangerment of US national security.

In November 2019, the US government brought criminal charges under the FCPA against Li Yanliang and Yang Hongwei, executives and employees of the Chinese subsidiary of the globally renowned healthcare company, Herbalife, in Mainland China. The reason was their alleged bribery of Chinese government officials to obtain licenses and conduct business. In June 2022, the US court imposed a civil penalty of USD 550,092 on Li Yanliang for this.

Although the "China Initiative" was declared terminated on 23 February 2022, the US government's attention to China continues substantially. Therefore, executives of Greater Bay Area companies listed in the US and executives of multinational corporations in the Greater Bay Area should remain vigilant and take precautions against related enforcement risks.

3. Joint law enforcement between the US and foreign governments

From past enforcement practices, it's evident that sharing information and evidence with allied law enforcement agencies and conducting joint law enforcement actions are crucial measures for the US government to implement its long-arm jurisdiction.

---

16 According to the data from [Foreign Corrupt Practices Act: FCPA Matters Dataset (stanford.edu)] as of May 2023, there are 106 entries related to FCPA cases involving China.

In recent years, these international collaborations have led to significant success for US regulatory agencies in enforcing global misconduct by some multinational corporations. As a result, US regulatory agencies have been continuously strengthening international cooperation in recent years, and collaboration and joint law enforcement with regulatory agencies of US allied countries have become the norm.

For example, in December 2022, Honeywell and its US subsidiary paid a USD 160 million fine for bribery activities in Brazil and Algeria, with assistance from Brazilian authorities. In a 2020 case involving export control and FCPA issues related to a European aircraft manufacturer, joint law enforcement was conducted between the US, France and the UK, resulting in a USD 3.9 billion fine imposed on the company. Similarly, in a 2020 FCPA case involving an investment bank, investigative agencies from seven countries were involved (the US, the UK, France, Singapore, Switzerland, Luxembourg and Malaysia), as well as assistance from at least 18 global law enforcement agencies. The breadth of investigative agencies involved in this case is rare in the history of US enforcement.

Based on publicly available information from US regulatory agencies regarding enforcement cases in areas such as the FCPA, anti-money laundering and sanctions, the US has maintained very close cooperation with countries such as the UK, France, Sweden, Brazil, the Netherlands, Germany, Singapore, Norway, Austria, Türkiye and Thailand in terms of cross-border enforcement. The US government shares information with regulatory agencies in these countries and may jointly conduct law enforcement actions against entities of the same company in various jurisdictions.

As of 2024, the trend of international cooperation among US regulatory agencies continues to strengthen, expanding into more areas and countries, particularly in emerging fields such as digital currency, cybersecurity and environmental protection.

In the current situation, Greater Bay Area companies with overseas operations should strengthen compliance control over their overseas entities to prevent noncompliant behavior by overseas subsidiaries and personnel from being enforced by local regulatory agencies and then shared with the US and its allied countries, leading to investigations conducted against the company globally.

II. Safeguarding Greater Bay Area enterprises with compliance

1. Thoroughly reviewing "US-related factors" and making adjustments and responses

In the current international landscape, it is crucial to assess the "US-related factors" in both current and future business development strategies. While the US possesses various long-arm laws, the specific risks under US jurisdiction that need attention vary depending on factors such as a company's core business, operational model, geographic distribution and scale.

For instance, for companies in the Greater Bay Area listed in the US, compliance with the FCPA is one of the key regulatory risks to consider. Although US regulatory agencies have expanded the scope of FCPA jurisdiction to include "any foreign entity, even if not within US territory, that assists, induces, conspires or acts as an agent representing a subject under US jurisdiction in bribery," the most targeted entities are still those listed or registered in the US, including their subsidiary executives in terms of actual enforcement risks. This is because it is relatively easy for US regulatory agencies to find means to regulate these companies and their executives, such as delisting them. Even if US regulatory agencies find it difficult to collect evidence of Chinese companies bribing government officials and, therefore, cannot apply the FCPA's anti-bribery provisions for punishment, they can still impose penalties on Chinese companies and their executives under the FCPA's accounting provisions. Therefore, Chinese companies and their executives listed in the US need to pay close attention to and manage FCPA risks.

For Greater Bay Area companies engaged in cross-border trade, equipment manufacturing and technological research and development, particular attention should be paid to trade compliance, especially regarding export control risks. For example, if a company's operations rely on goods or technology subject to US export control from US suppliers, or if its products contain US components subject to US export control, it needs to evaluate and assess US export control risks to prevent being placed on entity lists by US regulatory agencies or subjected to other sanctions. This could lead to US suppliers ceasing to supply the company, forcing it to find alternative solutions or undergo business restructuring.

Additionally, Greater Bay Area companies engaged in overseas engineering contracts and construction should also focus on the sanction risks under the World Bank system. Once sanctioned by the World Bank, it means that the company may face joint sanctions from other multilateral banks. The resulting sanctions could lead to the company's inability to participate in projects funded by the World Bank and other multilateral banks, and removal from these sanction lists is extremely difficult and time-consuming. This could significantly impact the company's financing and expansion of new businesses globally and even endanger its survival.

In summary, Greater Bay Area companies should comprehensively assess the "US-related factors" based on their current core business, operational models, geographic distribution, distribution of customers and suppliers, scale and international competitiveness, and future development strategies. They should identify potential compliance risks, the likelihood of falling under US jurisdiction, the likelihood of potential violations and the likelihood of enforcement actions by US long-arm laws. Subsequently, based on the assessment results, adjustments should be made to the current business model and future development strategies. For example, considerations could include whether to replace suppliers from the US, diversify customer layouts to mitigate the impact of Western sanctions and implement alternative currency options.

2. Developing and implementing comprehensive and effective compliance mechanisms and measures

Developing and implementing comprehensive and effective compliance mechanisms and measures is crucial for businesses to mitigate compliance risks both domestically and internationally. Given the current legislative and enforcement trends in Europe, the US and China, robust compliance mechanisms and measures not only help companies reduce the likelihood of illegal conduct but also assist them in mitigating or even avoiding penalties during investigations by regulatory authorities following any misconduct by the company or its employees. This implies that establishing and enforcing a comprehensive and effective compliance framework can help companies mitigate compliance risks on a global scale.

(1) Comprehensive and effective compliance mechanisms can prevent overseas risks

Under US law, the Department of Justice evaluates the completeness and effectiveness of corporate compliance mechanisms based on its released "Evaluation of Corporate Compliance Programs" when handling various cases such as FCPA, sanctions and export controls, anti-money laundering and others, in order to assess how to resolve corporate-related illegal activities, including whether to prosecute, whether to settle, the manner of settlement and the amount of fine reduction. The SEC operates similarly in its enforcement mechanism. Historically, many companies have successfully avoided prosecution by the SEC due to their comprehensive and effective compliance mechanisms. In such cases, the SEC only charges the executives involved. For example, *SEC v. Asante K. Berko (2020)*, Goldman Sachs was exempted; *SEC v. Junping Zhang (2016)*, Harris Corporation was exempted; *SEC v. Garth Ronald Peterson (2012)*, Morgan Stanley was exempted.

From the perspective of risk prevention, it's much easier to prevent issues beforehand than to address them afterward. Taking the example of the US Department of Commerce's Entity List for export controls, it's extremely challenging and time-consuming for companies listed on the Entity List to apply for removal. This is primarily due to several reasons, as follows:

(a) Companies listed on the Entity List often don't know the exact reasons for their listing.

(b) There are no precedents to refer to because the US Department of Commerce doesn't publicly disclose the factors considered when making removal decisions.

(c) Removal decisions require unanimous agreement from multiple US regulatory agencies.

(d) Cooperating with US law enforcement investigations may trigger compliance issues under Chinese laws such as the "National Security Law" and the "Blocking Statute on the Improper Application of Foreign Laws and Measures."

(e) The prohibitive cost of compliance, as applying for removal entails agreeing to numerous compliance commitments and obligations.

(f) Limited avenues for recourse if removal applications are denied, as the only recourse is judicial review by a court, but courts generally won't overturn the Department of Commerce's decision to deny removal.

(2) Comprehensive and effective compliance mechanisms can also prevent risks within China's borders

It's worth noting that China's legislative and enforcement trends in recent years have been continuously guiding and encouraging Chinese enterprises to establish comprehensive compliance mechanisms in all aspects, helping them prevent and manage compliance risks.

At the legislative level, legislation in many areas is encouraging and guiding enterprises to establish sound compliance systems in relevant fields, for example:

(a) The Export Control Law encourages exporters to establish internal compliance systems for export control.

(b) On 28 April 2021, the Ministry of Commerce issued the "Guiding Opinions on the Establishment of Internal Compliance Mechanisms for Export Control by Dual-use Item Exporters," providing guidance for relevant enterprises.

(c) The Data Security Law requires enterprises to establish comprehensive data security management systems throughout the entire process.

(d) The "Shanghai Regulation on Anti-Unfair Competition" encourages operators to establish sound management systems for anti-commercial bribery and other unfair competition practices and requires the market supervision and administration departments to conduct inspections on the implementation of anti-commercial bribery management systems by enterprises in investigating commercial bribery cases.

At the enforcement level, the Supreme People's Procuratorate has launched compliance reform pilot projects in several provinces and cities, including Guangdong. The procuratorate is responsible for handling cases involving private enterprise leaders in business-related crimes, adopting a principle of "not arresting if not necessary, not prosecuting if not necessary and suggesting probation instead of imprisonment if possible" in accordance with the law. Meanwhile, efforts are being made to encourage compliance management in implicated enterprises and promote the institutionalization of a "strict supervision" system.[17]

3. Monitor trends closely and adjust strategies timely

It is important to note that companies in the Greater Bay Area should closely monitor the dynamics of significant compliance risk areas relevant to their businesses, including legislative and enforcement developments by domestic and foreign regulatory agencies, as well as relevant countermeasures taken by the Chinese government.

In September 2020 and January 2021, the Ministry of Commerce issued the "Provisions on the Unreliable Entity List" and the "Measures for Blocking the Improper Extraterritorial Application of Foreign Laws and Measures" respectively. In June 2021, the Standing Committee of the National People's Congress promulgated the "People's Republic of China Anti-Foreign Sanctions Law."

The "Provisions on the Unreliable Entity List" explicitly state that foreign entities that threaten China's national sovereignty, security and development interests, or adopt discriminatory measures against Chinese individuals or entities in violation of market norms, may be included in the entity list.

The "Measures for Blocking the Improper Extraterritorial Application of Foreign Laws and Measures" authorize the Ministry of Commerce to issue prohibitions against the recognition or compliance with foreign laws that improperly apply to individuals or entities in China and to take necessary countermeasures accordingly.

The "People's Republic of China Anti-Foreign Sanctions Law" stipulates that China has the right to take corresponding countermeasures against any form of oppression or discriminatory restrictions imposed on China, Chinese citizens or Chinese organizations under various pretexts, including its own national laws. Additionally, any organization or individual is prohibited from "enforcing" or "assisting" in the enforcement of discriminatory restrictions imposed by foreign countries on Chinese citizens or organizations.

---

17 "The Supreme People's Procuratorate issued a work plan to orderly advance the corporate compliance reform pilot program. The second phase expands to 10 regions, including Beijing and Zhejiang," Supreme People's Procuratorate, 8 April, 2021, https://www.spp.gov.cn/xwfbh/wsfbt/202104/t20210408_515148.shtml#1, last accessed 12 June, 2024.

Based on the above provisions, the Chinese Ministry of Commerce has already placed certain foreign entities on the "Unreliable Entity List." Additionally, authorities such as the Chinese Ministry of Foreign Affairs have announced sanctions against certain overseas enterprises or individuals who have harmed the legitimate rights and interests of Chinese companies, as well as jeopardized national sovereignty, security and development interests.

This implies that companies in the Greater Bay Area, when reviewing and adjusting their compliance mechanisms based on foreign laws and regulations, should also be mindful of the risks of violating China's relevant countermeasures. At the same time, they should promptly follow up on relevant developments and measures, making corresponding adjustments and improvements to their business operations and compliance mechanisms.

Contact Partner:

Vivian Wu
Partner, Beijing
+86 10 6535 3860
vivian.wu@
bakermckenziefenxun.com

Data Protection

08

Authors: Jay Ruan, Chris Jiang

New rules on cross-border transfers of personal information in the Greater Bay Area

After concluding an intergovernmental memorandum of understanding for cooperation on cross-border data transfer facilitation on 29 June 2023, the Cyberspace Administration of China (CAC) of Mainland China ("**Mainland**") and the Innovation, Technology and Industry Bureau (ITIB) of Hong Kong Special Administrative Region ("**Hong Kong**") issued a joint announcement on 10 December 2023 on implementing the Guidelines on the Implementation of the Standard Contract for the Cross-Border Flow of Personal Information within the Guangdong-Hong Kong-Macao Greater Bay Area (between Mainland and Hong Kong) ("**New GBA Rules**"), effective from the same date. The New GBA Rules are intended to facilitate cross-border personal information[18] flows within the Guangdong-Hong Kong-Macao Greater Bay Area (GBA).

While the GBA generally includes Macao SAR as well, the New GBA Rules are not relevant to Macao SAR, due to the lack of a similar agreement or memorandum of understanding for cooperation between Mainland and Macao SAR authorities in respect of cross-border data flows (which so far seem to be much less common and frequent than those between Mainland and Hong Kong). The New GBA Rules are only applicable to enterprises and other organizations established or incorporated in, or individuals resident in, nine designated cities in Guangdong province (i.e., Guangzhou, Shenzhen, Zhuhai, Foshan, Huizhou, Dongguan, Zhongshan, Jiangmen and Zhaoqing) ("**Mainland Part**") and Hong Kong.

The New GBA Rules have brought some positive and restriction-lifting changes to the current regulatory regime of outbound personal information provision from Mainland (even compared to the CAC's latest nationwide rules on facilitating cross-border data flows issued in March 2024 (after the New GBA Rules), which will also be briefly introduced at the end of this article). Such changes will be addressed below mainly from a Mainland perspective. We will also share some high-level comments and observations of the reaction of enterprises to the New GBA Rules.

18 The terms "personal information" and "personal data" may be used interchangeably in this article, as the applicable laws in Mainland and Hong Kong have used slightly different terms.

I. Regulatory background of the New GBA Rules

1. Mainland

In Mainland, personal information is protected under the Personal Information Protection Law of the PRC as promulgated in August 2021 (PIPL) and other applicable laws and regulations. Under the PIPL, a personal information processor (PIP, which is akin to the concept of data controller under the EU GDPR) is obliged to perform several obligations in respect of its export of personal information ("**PI Export**"). Those obligations mainly include providing specific notification to relevant individuals located in Mainland, obtaining separate consent from those individuals, conducting a personal information protection impact assessment (PIA) and fulfilling the required formality (i.e., following one of the three currently available routes as applicable to the specific PIP, unless an exemption is applicable) for the PI Export.

In particular, according to Article 38 of the PIPL, there are three routes for a PIP in Mainland to provide personal information to an overseas recipient, and only one of the three routes that is applicable to the PIP needs to be followed prior to the proposed PI Export, as follows:

(1) Passing a security assessment as organized by the CAC and its relevant provincial office ("**Security Assessment**")

The Security Assessment will be conducted in accordance with the Measures for the Security Assessment of Outbound Data Provision ("**Security Assessment Measures**") issued by the CAC (effective from 1 September 2022).

Under either of the following circumstances, the PI Export must be subject to a Security Assessment (in other words, a PIP must follow this first route once the relevant conditions are fulfilled and may not choose either of the other two routes):[19]

(a) The PI Export involves the export of any important data[20] (whether or not personal information is involved) under Mainland laws.

(b) The PIP is a critical information infrastructure operator (CIIO).[21]

---

19 These circumstances have been stipulated in the Security Assessment Measures, as amended (relaxed) by the CAC's latest nationwide rules on facilitating cross-border data flows in March 2024, after the New GBA Rules. Before the issuance of the New GBA Rules (without consideration for the CAC's latest nationwide relaxation), the thresholds triggering the Security Assessment were even lower so that more PIPs in Mainland could be required to apply for and complete a Security Assessment before their PI Export.

20 "Important data" refers to any data, once manipulated, destroyed, leaked, illegally accessed or illegally used, that may endanger national security, operation of the economy, social stability, public health and security, etc., under the Security Assessment Measures. It has been widely believed and recently explicitly confirmed by the CAC that unless certain data (x) has been clearly identified by competent governmental authorities as important data, or (y) falls into any published catalogues of important data, a PIP may treat its data as non-important data.

21 There are separate regulations on identification of CIIOs, and competent central and local governmental authorities may issue detailed guidelines and catalogues for identification of CIIOs. To avoid uncertainties, the CAC has clarified that a CIIO will be notified by competent governmental authorities of its status of CIIO. It means that if a PIP has not received a clear and formal notification on its status of CIIO, it can assume that it is not a CIIO.

- Where the PIP is not a CIIO, since 1 January of the current calendar year and until the submission date of the Security Assessment application, the PIP has exported the personal information of 1 million or more individuals residing in Mainland or sensitive personal information[22] of 10,000 or more individuals residing in Mainland.

(2) Passing a voluntary personal information protection certification ("**Certification**") by a qualified institution in China in accordance with the Announcement on the Implementation of Personal Information Protection Certification issued by the CAC and the State Administration for Market Regulation and its related rules (if the Security Assessment is not triggered and applicable).

(3) Concluding a personal information export contract based on the Standard Contract for Outbound Personal Information Provision ("**China SCCs**") with the overseas recipient in accordance with the Measures for Standard Contracts for Outbound Personal Information Provision ("**China SCCs Measures**") issued by the CAC (effective from 1 June 2023) (if the Security Assessment is not triggered and applicable)

China SCCs are prescribed by the CAC and provide for extensive personal information protection rights and obligations of the parties thereto. The parties may not deviate from China SCCs and are only allowed to enter into supplemental agreements that do not contradict with China SCCs.

According to Article 7 of the China SCCs Measures, a PIP in Mainland must file the executed China SCCs, together with a PIA report concerning the PI Export, with the relevant provincial office of the CAC for recordal within 10 working days after the China SCCs take effect.

In practice, where the Security Assessment is not triggered and applicable, between the second and third routes for PI Export (i.e., Certification and China SCCs filing), most PIPs in Mainland prefer to choose China SCCs filing (as this route is relatively more straightforward and a PIP can complete it on its own or with necessary support by professional advisers). So far, only five successful cases of Certification for PI Export have been reported.

Under the New GBA Rules, a PIP located in the Mainland Part of the GBA is now allowed to follow an alternative and less stringent route for its PI Export, if the conditions set forth in the New GBA Rules are fulfilled.

2. Hong Kong

In Hong Kong, Section 33 of the Personal Data (Privacy) Ordinance (Cap. 486) (PDPO) prohibits the transfer of personal data to places outside of Hong Kong except where specified conditions are met. While this provision has not come into force, the Office of the Privacy Commissioner for Personal Data (PCPD) has issued two nonbinding guidelines in 2014 and 2022 to prepare for the implementation of Section 33, including two sets of Recommended Model Contractual Clauses for Cross-border Transfers of Personal Data, one for transfers from a data user (i.e., the equivalent concept to a PIP under the PIPL and a data controller under the EU GDPR) to another data user, and one for transfers from a data user to a data processor.

22 "Sensitive personal information" means personal information that, once divulged or illegally used, may easily cause harm to the dignity of natural persons or endanger personal or property safety. Examples include biometric information (e.g., fingerprint, voice, face, heart rhythm), religious belief, medical and healthcare information, financial accounts, location tracks, as well as personal information of minors under the age of 14.

II. Highlights of the New GBA Rules and main differences from the existing PI Export regime in Mainland

In general, the New GBA Rules allow PIPs/data users and their recipients (on the other side of the border) located in the Mainland Part of the GBA and Hong Kong to conclude GBA SCCs for PI Export (from Mainland to Hong Kong, or vice versa), if the PI Export does not involve any important data.

Like the existing China SCCs, the GBA SCCs provide for the respective obligations and responsibilities of the parties thereto, as well as certain rights of relevant individuals (as subjects of the personal information exported).[23] The GBA SCCs cannot be deviated from, but additional terms and conditions that do not conflict with the GBA SCCs may be incorporated into them. The parties must set out the details of the PI Export, such as the purposes and methods of personal information processing and the categories of personal information to be exported. If there is any change to these details, or if there is any other circumstance that affects or may affect either party's performance of the GBA SCCs, the PIP/data user must conduct an updated PIA, conclude a supplemental agreement to the prior GBA SCCs between them or conclude new GBA SCCs, and complete the GBA SCCs filing again. These requirements are all quite similar to those under the China SCCs Measures that have been implemented nationwide in Mainland for a while.

However, the following are some of the key aspects in which the GBA SCCs take a different approach (a more lenient approach than the China SCCs for PI Export in most aspects):

1. **No volume threshold for GBA SCCs:** Under the China SCCs regime, there is a maximum volume of personal information that non-CIIO PIPs are allowed to provide overseas (even though this maximum volume has been substantially raised under the CAC's latest relaxation rules issued in March 2024). If a proposed PI Export has reached an applicable threshold (i.e., personal information of 1 million or more individuals, or sensitive personal information of 10,000 or more individuals, in any calendar year), then the PIP must go through a Security Assessment process, during which a high granularity of the application documents is required and the CAC would conduct a more careful review (and not just a formality review), which has proven to be rather time-consuming and costly. Furthermore, there is a chance that the PIP may fail the Security Assessment entirely or partially, as the CAC may block the proposed export of certain data fields of personal information, or block the proposed PI Export in certain business scenarios, in certain manners or for certain purposes.

   On the contrary, under the GBA SCCs, no volume threshold is imposed, which means that the GBA SCCs can be concluded, regardless of the number of individuals involved in the proposed PI Export. Hence, even if a huge amount of personal information is exported from Mainland to Hong Kong, a PIP located in the Mainland Part of the GBA would still not be required to apply for a Security Assessment, unless such huge amount of personal information constitutes important data (which is not unlikely). This can save time and costs for the PIP,

23 In Hong Kong, such individual is also referred to as a "data subject" as defined under the PDPO.

allow it to proceed with the proposed PI Export earlier and, most importantly, result in a greater chance of a positive outcome.

(1) **No different treatment of sensitive personal information to be exported:** Under the China SCCs regime, sensitive personal information is treated differently from other personal information. More specifically, the CAC has stipulated a much lower volume threshold for export of sensitive personal information (10,000 compared to 1 million for nonsensitive personal information) and the CAC did not raised this volume threshold under its latest relaxation rules issued in March 2024. It implies that the CAC generally discourages export of sensitive personal information from Mainland. Given the relatively broad and vague definition of sensitive personal information under the PIPL, in most real cases we have seen, at least certain data fields of the personal information proposed to be exported by PIPs in Mainland could constitute sensitive personal information. In that case, if the number of relevant individuals reaches 10,000 (which is not a lot and can be easily reached if a PIP does not merely process and propose to export sensitive personal information of its employees), a Security Assessment will be triggered and applicable. For that reason, even under the CAC's latest relaxation rules issued in March 2024, quite a few PIPs in Mainland are still required to apply for and complete a Security Assessment.

On the contrary, under the GBA SCCs, no volume threshold for export of sensitive personal information has been imposed, to the effect that sensitive personal information would be actually treated in the same manner as nonsensitive personal information. Hence, those PIPs in the Mainland Part of the GBA who are required to pass a Security Assessment due to export of sensitive personal information could benefit from this relaxation under the New GBA Rules if the personal information will only be transferred, stored and processed within the GBA.

2. **Applicable to CIIOs:** Under the Security Assessment Measures, if a CIIO exports any personal information, it must apply for and complete a Security Assessment, and may not use the China SCCs. However, under the New GBA Rules, there is no limitation on the use of the GBA SCCs by a CIIO PIP in the Mainland Part of the GBA. This may benefit CIIOs and relieve them from the heavy burden of a Security Assessment arising out of any PI Export.

3. **A more straightforward PIA required for PIPs/data users:** Both regimes require PIPs to conduct PIAs and formulate PIA reports before carrying out the proposed PI Export. Under the China SCCs regime, this obligation has been considered onerous, and in practice concerns have been raised about the level of detail required to be included in such reports and the substantial comments that PIPs in Mainland may receive from the CAC's provincial offices. However, under the GBA SCCs regime, the required PIA reports can be streamlined to some extent, with a focus of assessment on (1) the legality, legitimacy and necessity of the purposes and methods of personal information processing by PIPs/data users and their overseas recipients, (2) the impact on the rights and interests of relevant individuals/data subjects and the security risks, and (3) the obligations that the overseas recipients undertake to assume, and whether the administrative and technical measures and capabilities to fulfill the obligations can ensure the security of personal information exported. Furthermore, under the New GBA Rules, data users in Hong Kong are also required to conduct PIAs and formulate PIA reports (for their proposed PI Export to Mainland), while the China SCCs regime only impose such obligation on PIPs in Mainland.

4. **Regulatory oversight:** Under the China SCCs regime, overseas recipients are obliged to accept the CAC's direct supervision and administration and demonstrate their compliance with the China SCCs by responding to the CAC's inquiries and providing the CAC with written evidence of their compliance from time to time, etc. This is a typical example of extraterritorial extension of the CAC's jurisdiction to enterprises outside Mainland, which is not expressly stipulated in the PIPL and may concern many multinational enterprises. Under the refined wordings of GBA SCCs, recipients are only subject to regulatory oversight of the local regulatory authorities. It implies that the CAC's cross-border regulatory oversight of recipients in Hong Kong is excluded under the GBA SCCs, and those recipients in Hong Kong are only directly regulated by local governmental authorities in Hong Kong such as the ITIB and the PCPD. However, given the existence of the regulatory cooperation relationship between Mainland and Hong Kong authorities, we believe that in practice the CAC would still be able to indirectly regulate recipients in Hong Kong.
5. **Governing law:** The China SCCs must be governed by Mainland laws, which may be a common concern for many multinational enterprises. Under the GBA SCCs, the laws in the jurisdiction of the PIP/data user will be the governing law. This means that the mandate on the governing law under the China SCCs still applies where the PI Export is from Mainland to Hong Kong. However, where the PI Export is conducted by a data user in Hong Kong to Mainland, the governing law of the GBA SCCs will be Hong Kong laws, rather than Mainland laws.
6. **Arbitration institution:** Due to the geographic limitation under the GBA SCCs, if the parties prefer arbitration to court litigation, the parties can only choose one of the five arbitration institutions listed in the China SCCs.[24] In addition to a list of common choices of arbitration institution, China SCCs also allow the parties to agree upon an unlisted arbitration institution that has become a signatory to the 1958 New York Convention (with respect to recognition and enforcement of foreign arbitral awards).
7. **Filing requirement applicable to both sides:** Under the China SCCs regime, the obligation of China SCCs filing is only imposed on PIPs in Mainland. However, under the New GBA Rules, both PIPs/data users and their recipients (located in the Mainland Part of the GBA and Hong Kong) are required to file the executed GBA SCCs with their respective regulatory authorities in Guangdong province and Hong Kong within 10 working days after the GBA SCCs take effect. It means that a recipient in the Mainland Part of the GBA also needs to make the filing simply for receipt of personal information from a data user in Hong Kong, which is actually an extra burden for such Mainland recipient.
8. **Simplified filing requirement:** For the required filing, the China SCCs regime requires submission of PIA reports to the CAC's provincial offices. As mentioned above, this obligation has been considered onerous, and concerns have been raised about the level of detail required to be disclosed in such report and the substantial comments that PIPs may receive from the CAC's provincial offices. The New GBA Rules do not require filing of PIA reports (although such PIA reports should still be formulated and put in place). In other words, the CAC's Guangdong office will not

24 They are: (1) China International Economic and Trade Arbitration Commission; (2) China Maritime Arbitration Commission; (3) China Guangzhou International Arbitration Commission; (4) Guangdong-Hong Kong-Macao Greater Bay Area International Arbitration Center; or (5) Hong Kong International Arbitration Center.

review PIA reports and thus not have a chance to raise any possible comments on PIA reports under the New GBA Rules. This ensures a more predictable and quicker completion of the GBA SCCs filing.

9. **No onward provision of personal information outside the GBA:** Both the New GBA Rules and the GBA SCCs contain an explicit restriction that recipients of personal information must not further provide the personal information received to any organization or individual outside the GBA. This may, to some extent, limit the appeal of this new regime to some multinational enterprises. While the New GBA Rules have not specified whether a recipient in Hong Kong may somehow use its servers located outside the GBA for storage or other processing of personal information received from a PIP in the Mainland Part of the GBA under the GBA SCCs, we tend to believe that this approach may constitute a circumvention of the restriction under the New GBA Rules, cause data security risks beyond the control of Mainland and Hong Kong authorities, and thus not be permissible.

III. Detailed implementation of the GBA SCCs regime

1. Guangdong province

On 4 January 2024, the CAC's Guangdong office issued a circular on the implementation of the New GBA Rules.[25] This circular further clarifies the specific methods (electronic preview, followed by formal submission on paper), procedures and materials required for the GBA SCCs filing that apply to PIPs or recipients located in the Mainland Part of the GBA.

When contacted by phone, the CAC's Guangdong office declined to disclose a rough estimate of the number of filings already made with it under the New GBA Rules but indicated that it has received many telephone inquiries. Given the relatively new GBA SCCs regime and the highly fluid and evolving nationwide regulatory regime for PI Export in Mainland, presumably quite a few enterprises in the GBA are still assessing the compliance route for PI Export they intend to follow or preparing for their submissions.

2. Hong Kong

On 13 December 2023, the PCPD issued the Guidance on Cross-boundary Data Transfer: Standard Contract for Cross-boundary Flow of Personal Information Within the Guangdong — Hong Kong — Macao Greater Bay Area (Mainland, Hong Kong) to guide data users in Hong Kong on how to use the GBA SCCs.

- Data users in Hong Kong are still required to comply with the requirements under the PDPO for PI Export, including the six Data Protection Principles set out in Schedule 1 to the PDPO.
- The requirements under the Implementation Guidelines on the GBA SCCs do not affect the privacy commissioner's supervisory and administrative roles within the scope of its functions under the PDPO, including the handling of complaints and reports relating to personal data protection, conducting investigations and dealing with activities involving unlawful handling of personal data.

---

25 See https://cagd.gov.cn/v/2024/01/4401.html.

If a data user in Hong Kong proposes a PI Export to Mainland and the recipient is located in the Mainland Part of the GBA, the privacy commissioner encourages the data user to adopt the GBA SCCs. For other PI Exports, the privacy commissioner states that data users and their recipients may continue to use the Recommended Model Contractual Clauses for Cross-border Transfers of Personal Data.

An "early and pilot implementation" arrangement for the GBA SCCs facilitation measure, which invites participation from banking, credit referencing and healthcare sectors, is being implemented as a first phase of the GBA SCCs regime by the Office of the Government Chief Information Officer of Hong Kong (OGCIO). According to enquiries with the OGCIO, as of 31 December 2023 (as the deadline for submission of Expressions of Interest (EoIs)), the OGCIO had received about 70 EoIs, about half of which came from the healthcare sector, with the rest coming from the banking and credit referencing sectors. According to the EoIs received, about one-third of the respondents expected to conclude the signing of the GBA SCCs with their Mainland partners, conduct PIAs and complete the filing procedures within three months, while another one-third expected to complete the related work within six months. After the deadline of EoI submission, the OGCIO continued to receive dozens of EoIs (including some from other sectors), which, the OGCIO suggested, was an indication that the GBA SCCs facilitation measure had been well received by enterprises. The ITIB and the OGCIO plan to review the arrangements in mid-2024, with a view to extending the facilitation measure to different business sectors.

IV. The CAC's latest relaxation rules and what enterprises should do

On 22 March 2024, the CAC issued the Provisions on Facilitating and Standardizing Cross-Border Data Flow ("**New CBDT Rules**"), which came into effect on the same date. This is a long-awaited moderate relaxation of the stringent restrictions on PI Export under previous rules issued by the CAC (including the Security Assessment Measures and the China SCCs Measures), almost half a year following the CAC's release of a draft in September 2023.

This article will not illustrate the New CBDT Rules, which are not the main topic here. In short, the highlights of the New CBDT Rules include the following:

- Raising the volume threshold for a Security Assessment (note that the adjusted volume threshold has already been reflected above in this article), so that more PIPs are eligible to conclude China SCCs with overseas recipients without going through a Security Assessment
- Stipulating a few exempted scenarios where PIPs in China would be exempted from a Security Assessment, Certification or China SCCs filing (the details of those exemptions are set out in the Appendix to this article)

As mentioned above, as the New GBA Rules have not stipulated any volume threshold for both sensitive and nonsensitive personal information and do not exclude the applicability to CIIOs, they still have large appeals to PIPs located in the Mainland Part of the GBA, especially those processing a large volume of personal information and having a regional office, affiliate or partner in Hong Kong with a close business relationship. However, if they follow this compliance route, the personal information exported can only be processed by the recipient in Hong Kong and may not be further provided to any third party for processing outside the GBA. This restriction may frustrate many multinational enterprises' global data processing arrangements.

Meanwhile, the New GBA Rules are the result of a regulatory cooperation between governmental authorities in Mainland and Hong Kong and provide a special compliance route in parallel with those rules issued by the CAC that apply nationwide. How the New GBA Rules and those other rules issued by the CAC may work together is not clear. For example, if a PIP in the Mainland Part of the GBA concludes GBA SCCs with a recipient in Hong Kong and a part of the personal information exported can be exempted under the New CBDT Rules, whether that part of the personal information can be not covered by the GBA SCCs and thus can be provided onward to a third party outside the GBA remains to be clarified by the CAC. In addition, if a PIP in the Mainland Part of the GBA has filed its GBA SCCs with the CAC's Guangdong office, whether and how it can switch to a more attractive compliance route stipulated by the CAC that applies nationwide is also not clear. However, at least where PIPs in the Mainland Part of the GBA may leverage one or more exempted scenarios under the New CBDT Rules, we believe that they may choose not to conclude the GBA SCCs with recipients in Hong Kong, but simply rely on those exempted scenarios. In that case, they still need to conduct PIAs, formulate PIA reports and perform other general obligations under the PIPL.

In addition, certain parts of China (Guangdong) Free Trade Zone are within the Mainland Part of the GBA, so negative lists may be issued in the near future by authorities in the free trade zone, which could exempt PIPs located in it from concluding the China SCCs. Hence, those negative lists might be more attractive than the New GBA Rules.

We now live in an era characterized by globalization and intricate digital connections. The access, utilization and exchange of data across borders is crucial for many multinational enterprises operating in various sectors, which heavily rely on data and its global flow, and yet the regulatory restrictions in Mainland on outbound data flows are still rapidly evolving. While the GBA SCCs regime has certain advantages, it may not necessarily be the best compliance route for PIPs in the Mainland Part of the GBA as its disadvantages are also obvious. How a PIP should choose its compliance route is subject to a case-by-case analysis. Still, enterprises in the GBA should closely keep abreast of the regional regulatory development in terms of cross-border data flow, carefully assess their data processing activities in the region and take prompt compliance actions.

Appendix

Exemptions under the New CBDT Rules

1. **Exemption for data-in-transit:** The personal information exported is limited to personal information collected and generated outside China and transmitted into Mainland for domestic processing, during which no personal information or important data collected or generated within Mainland is incorporated into the personal information exported (i.e., pure storage of overseas personal information in Mainland or transit of overseas personal information through Mainland).
2. **Contracting exemption:** A PIP in Mainland exports personal information where it is necessary to do so for concluding or performing a contract to which the individual is a party, such as for cross-border shopping, cross-border posting and delivery, cross-border fund remittance, cross-border payment, cross-border account opening, air ticket and hotel booking, visa application, examination services, etc.
3. **HR management exemption:** A PIP in Mainland exports employees' personal information where it is necessary to do so for implementing cross-border HR management in accordance with labor rules and policies formulated in accordance with laws and collective contracts concluded in accordance with laws.
4. **Emergency exemption:** A PIP in Mainland exports personal information where it is necessary to do so for protecting the life, health and property safety of individuals under emergency conditions.
5. **Small-scale data exporter exemption:** A PIP in Mainland is not a CIIO and it has exported nonsensitive personal information of fewer than 100,000 individuals since 1 January of the current calendar year.
6. **Free trade zone exemption:** Authorities in various free trade zones in China have been empowered to issue their respective negative lists to further ease cross-border data transfer activities within the national framework of data classification and grading, so PI Export that falls outside of those negative lists can be exempted.[26]

Contact Partner:

Jay Ruan
Partner, Shanghai
+86 21 6105 8577
zhenyu.ruan@
bakermckenziefenxun.com

26 For the time being, authorities in free trade zones in Lingang, Shanghai and Tianjin are reported to be in the process of formulating negative lists, and their negative lists are expected to be made available to the public in the near future.

Intellectual Property

09

Authors: James Lau, Bertha Ho, Harrods Wong

Building Bridges: Recent IP Legal and Policy Developments in the Greater Bay Area

In the past few years, the Guangdong-Hong Kong-Macao Greater Bay Area (GBA) has witnessed remarkable developments in its innovation landscape, marked by growing awareness of intellectual property (IP) protection, increasing integration and significant governmental efforts to establish the region as an innovation hub. This article explores the latest developments in IP policies, laws and regulations in the GBA that aim to enhance IP protection. It also highlights the collaborative initiatives within the GBA that are shaping a robust framework for safeguarding IP rights at the regional level and fostering a dynamic environment for innovation and creativity.

I. Overview of policy direction

The Outline Development Plan for the Guangdong-Hong Kong-Macao Greater Bay Area (粤港澳大湾区发展规划纲要) highlights the importance of enhancing cross-border collaboration within the GBA in, among others, the areas of IP protection, enforcement and dispute resolution. It voiced support for Hong Kong SAR ("**Hong Kong**") to develop into a regional IP trading center and to enhance its IP protection regime to encourage innovation and creativity within the GBA. On 11 March 2021, the Outline of the 14th Five-Year Plan for National Economic and Social Development and the Long-Range Objectives Through the Year 2035 (中华人民共和国国民经济和社会发展第十四个五年规划和 2035 年远景) ("**14th Five-Year Plan**") was approved by the National People's Congress. The 14th Five-Year Plan further pledged to support Hong Kong's development in the innovation and technology realm, and to consolidate the role of Hong Kong in China's overall development plan as a center for international financial services, IP trading and legal services in the Asia Pacific region.

Guided by these overarching goals and principles, the governments of Guangdong Province, Hong Kong and Macao SAR ("**Macao**") have formulated more specific policies and initiatives to foster mutual collaboration and development and, at the same time, address shared challenges.

In December 2021, the Guangdong provincial government issued the 14th Five-Year Plan of the Guangdong Province for Protecting and Utilizing Intellectual Property Rights (广东省知识产权保护和运用"十四五"规划), setting out the overall goal of comprehensively enhancing the effectiveness of IP protection, utilization and optimization, and facilitating deeper regional and international cooperation in the IP field. Specifically, it included concrete tasks to be performed to ensure the steady progress in constructing an international IP cooperation center within the GBA, such as through cross-border enforcement against IP infringing activities and the development of "cooperation zones."

In line with this overall direction, in February 2023, the Authority of Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone of Shenzhen Municipality (深圳市前海深港现代服务业合作区管理局) and the Commerce and Economic Development Bureau of the Hong Kong government jointly formulated and published the 16 Co-operation Measures for the Development of the Qianhai Shenzhen-Hong Kong Intellectual Property and Innovation Hub (关于协同打造前海深港知识产权创新高地的十六条措施), with a view to leverage the advantages of Hong Kong in the IP landscape and support the development of the Qianhai Shenzhen-Hong Kong IP and innovation cooperation hub as a whole.

On the Macao side, in September 2023, the Guangdong Administration for Market Regulation (Guangdong Intellectual Property Administration) (广东省市场监督管理局(知识产权局）) and the Economic and Technological Development Bureau of the Macao government also signed the Agreement on Guangdong-Macao Intellectual Property Cooperation (2023-2025) (粤澳知识产权合作协议（2023-2025年）) to facilitate further collaboration between Guangdong and Macao in terms of IP protection, knowledge exchange, promotion and education, adding one more brick to the foundation for cross-border coordination in IP protection within the GBA.

II. Enhancing the regional IP framework

IP rights are largely territorial in nature. Within the GBA, the nine cities in Guangdong province adopt the relevant IP laws in Mainland China, while Hong Kong and Macao each have their own laws and regulations on conferring and protecting IP rights. Nonetheless, we have seen a number of developments taking place in Hong Kong and in other parts of the GBA toward the same goal of strengthening IP protection and future-proofing the IP legal framework.

1. Trademark

On the Mainland China side, the Chinese National Intellectual Property Administration (CNIPA) issued draft amendments to the Trademark Law of the People's Republic of China for public comments on 13 January 2023.

The proposed changes are intended to help tackle the long-standing problem of bad faith trademark filings in Mainland China, and various new elements have also been proposed to the trademark system — such as the requirement for filing statements of use, the prohibition of duplicated trademark registrations and a mechanism for compulsory transfer of bad faith trademark registrations. Over 3,400 comments were received during the consultation period, and the CNIPA is in the process of further revising the draft amendments. While the amendment details and implementation timeline are yet to be confirmed, this will be an important area to watch out for.

The trademark system in Hong Kong is also poised to receive an upgrade. China has been a member country of the Madrid System (international trademark system) for many years, so Mainland Chinese companies looking to register trademarks abroad, as well as overseas businesses hoping to register trademarks in Mainland China, have long been able to take advantage of the streamlined and convenient trademark registration procedure offered by the Madrid System, which allows applicants to file a single international application through the World Intellectual Property Organization (WIPO) to apply for trademark protection in up to 130 jurisdictions. Hong Kong, as a special administrative region of China, is not currently a member of the Madrid System. However, the Hong Kong government recognizes the value of joining the Madrid System and has taken significant steps toward implementing it in Hong Kong. The Central People's Government has also given its in-principle support for the proposed implementation of the Madrid System in Hong Kong. In the near future, once all preparatory work is complete, foreign trademark owners (not including Mainland Chinese owners) will be able to include Hong Kong as a designated jurisdiction in their international registrations, while Hong Kong trademark owners will also be able to designate one or more foreign member countries in which to register their marks. The implementation of the Madrid System will align Hong Kong with international standards, further facilitate cross-border trade and promote the harmonization of IP practices.

2. Copyright

The Standing Committee of the 13th Guangdong Provincial People's Congress considered and adopted the Guangdong Copyright Regulations (广东省版权条例) on 29 September 2022, and the regulations came into force on 1 January 2023. This is said to be the first local regulation in Mainland China that is aimed at promoting the high-quality development of the copyright industry. The Guangdong Copyright Regulations have provided a model for local copyright legislation in China, fostering copyright protection, technological innovation and economic development in Guangdong province.

In Hong Kong, the latest amendment to the Copyright Ordinance (Cap. 528) came into force in May 2023 to strengthen copyright protection in the digital environment. Major updates include the introduction of a technology-neutral communication right for copyright owners, additional copyright exceptions (such as parody, satire, caricature, pastiche and current events commentary), safe harbor provisions for online service providers and additional factors to consider when awarding additional damages in civil cases.

In light of the rapid development of artificial intelligence, the Hong Kong government is set to release a consultation paper later this year to further review the copyright regime and to ensure that it remains relevant and robust.

3. Patent

The Hong Kong government has been working to foster the development of the patent system in Hong Kong. In particular, the original grant patent (OGP) system was introduced in December 2019 to bring the patent system on par with those of other developed economies. The OGP system provides a direct route for applicants to seek standard patent protection in Hong Kong, and it runs parallel to the existing "reregistration" route.

"The Chief Executive's 2023 Policy Address" further pledged to proactively prepare for the implementation of regulatory arrangements for local patent agent services. This includes establishing professional qualification requirements, registration procedures and a regulatory framework, all aimed at improving the quality of patent agency services and fostering talent in this field. Additionally, a "patent box" tax incentive will be introduced to reduce the tax rate for qualifying profits generated from patents. The objective is to promote and incentivize research and development and patent commercialization endeavors in Hong Kong.

At the same time, a pilot project with the CNIPA was launched on 1 January 2023 to enable Hong Kong applicants to enjoy expedited examination of qualified invention patent applications in Mainland China. On 1 July 2023, the project was extended to cover Macao applicants. Such measure allows patent owners in Hong Kong and Macao to register and protect their rights in Mainland China more efficiently, so that the fruit of scientific research and technological achievements may be transformed and commercialized across the GBA and China smoothly.

III. Strengthening collaboration and integration within the GBA

In addition to the progress achieved in the respective jurisdictions, the GBA as a whole has also witnessed a concerted effort to strengthen collaboration in safeguarding IP rights. In line with the overall plans outlined above, a number of specific policy initiatives have been implemented to enhance cooperation and foster a favorable ecosystem for businesses operating in the GBA.

1. Joint enforcement actions against IP infringing activities

The Guangdong/Hong Kong Expert Group on the Protection of Intellectual Property Rights ("**Expert Group**"), which was set up in August 2003, has been embracing the national plans on GBA development by promoting in-depth IP cooperation. From 2020 to mid-2022, the Expert Group completed 19 cooperation items, including the regular exchange of intelligence and information on detected IP infringement cases and the conducting of joint enforcement operations against cross-boundary IP infringement in focus areas targeting major boundary crossings. In November 2022, it endorsed an action plan for 2022-2023, agreeing to further enhance and expand the scope of cooperation. In particular, the Expert Group has been working on strengthening the collaboration mechanism between the customs authorities within the GBA to combat cross-boundary IP infringing activities.

In September 2023, the three customs administrations of Guangdong, Hong Kong and Macao held the third Guangdong-Hong Kong-Macao Customs Intellectual Property Enforcement Cooperation Meeting in Hong Kong. They summarized recent enforcement outcomes of IP rights protection and agreed on the collaboration directions, including strengthening cooperation on real-time intelligence exchange, risk management and the use of big data to proactively monitor and analyze the trends of related crimes. Between January 2020 and June 2022, the Guangdong Customs, Hong Kong Customs and Macao Customs conducted seven joint enforcement operations to combat cross-boundary IP infringements, resulting in the seizure of over 6.98 million items of infringing goods by Guangdong Customs and detection of 153 cases by Hong Kong Customs, involving approximately 170,000 infringing articles. More recently, in 2023, the three customs administrations conducted three joint operations and seized a total of about 51,000 items of suspected counterfeit goods with an estimated market value of about HKD 25.5 million in these operations.

2. Facilitation of data flow

Pursuant to the Memorandum of Understanding on Facilitating Cross-boundary Data Flow within the Guangdong-Hong Kong-Macao Greater Bay Area signed by the Innovation, Technology and Industry Bureau of the Hong Kong government and the Cyberspace Administration of China, the Hong Kong government and the Guangdong provincial government promised to jointly promote cross-boundary data flows within the GBA. By the end of 2023, the Standard Contract for the Cross-boundary Flow of Personal Information within the Guangdong-Hong Kong-Macao Greater Bay Area (Mainland, Hong Kong) was launched to streamline the cross-border flow of personal data within the GBA. With this new voluntary standard contract, the safe and orderly movement of data within the GBA can be facilitated, making it easier for multinational corporations with a presence in the GBA to manage and process their data.

IV. Cross-border dispute resolution

On the road to developing a collaborative IP protection mechanism across the GBA and fostering an innovative region as a whole, having a robust and reliable cross-border dispute resolution mechanism is of paramount importance to promoting investor confidence and creating a harmonious business environment.

1. Litigation

In 2021, a significant court ruling was issued by the High Court of Hong Kong, confirming that Hong Kong courts have the authority to grant IP injunctions that have extraterritorial effect, based on the principle of double actionability. In that case (*Biozeal LLC & Ors v. Nature's Story Company Limited & Ors*), the court granted an interlocutory injunction that effectively prohibited the defendants from engaging in acts of passing off and infringement in Mainland China, indicating that Hong Kong courts can serve as a potential recourse for addressing acts of infringement taking place in Mainland China. This is an encouraging ruling for those involved in or considering business activities in Hong Kong and other areas in the GBA.

Further, following the signing of the Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Courts of the Mainland and of the Hong Kong Special Administrative Region in 2019, the Mainland Judgments in Civil and Commercial Matters (Reciprocal Enforcement) Ordinance (Cap. 645) came into force in Hong Kong on 29 January 2024, providing for a mechanism for the reciprocal recognition and enforcement of judgments in civil and commercial matters between Hong Kong and Mainland China. The mechanism covers IP judgments, if they relate to specified IP rights, such as copyright and trademark, but notably excludes judgments for tortious infringement of patents as well as nonmonetary remedies for certain IP infringement disputes. The mechanism allows cross-border disputes to be resolved and judgments to be enforced with more certainty and efficiency, and judgment creditors will also be offered more protection as they can register and enforce Mainland judgments in Hong Kong against the defaulting parties who, for example, may have substantial assets in Hong Kong to pay damages, without having to relitigate the same dispute in Hong Kong.

2. Arbitration

Another crucial limb of the dispute resolution mechanisms is arbitration. Hong Kong has long been a well-recognized international arbitration hub. Both the Central People's Government and the Hong Kong government have indicated their support for Hong Kong to continue to play a leading role in international alternative dispute resolution. In 2023, there were a total of 500 matters submitted to the Hong Kong International Arbitration Center (HKIAC), of which 209 were domain name disputes.

As a result of the Arrangement Concerning Mutual Assistance in Court-ordered Interim Measures in Aid of Arbitral Proceedings by the Courts of the Mainland and the Hong Kong Special Administrative Region (关于内地与香港特别行政区法院就仲裁程序相互协助保全的安排) signed in 2019, Hong Kong is the first and only non-Mainland jurisdiction where parties to arbitral proceedings can apply to the Mainland courts for interim relief (such as property, evidence and to conduct preservation orders) before an arbitral award is made. Since the introduction of the arrangement and until the end of 2023, the HKIAC had processed 105 applications to different Mainland Chinese courts, resulting in court orders that preserved assets worth a total of RMB 15.8 billion (approximately USD 2.2 billion).

3. Mediation

Finally, mediation is also a widely promoted method to resolve IP disputes. The GBA Mediation Platform was set up by the Guangdong, Hong Kong and Macao legal departments to enable high-level cooperation between the three jurisdictions. Since its establishment in 2021, the GBA Mediation Platform has published the GBA Mediator Accreditation Standards and GBA Mediator Code of Conduct Best Practice. The GBA Mediation Platform is expected to promote the wider use of mediation by businesses within the GBA. In December 2023, the Guangdong, Hong Kong and Macao legal departments held an annual meeting to discuss the promotion of the rule of law development in the GBA. Among other things, the three parties reached a consensus on the joint development of a collaborative online dispute resolution platform, which will start with information and resources sharing among arbitration and mediation institutions in the GBA. This echoes the policy initiative of the "Chief Executive's 2022 Policy Address" to establish an online mediation platform in the GBA.

On 9 December 2023, the Guangdong High People's Court signed a cooperation agreement with the WIPO Arbitration and Mediation Center. With the mutual consent of the parties, certain courts in Guangdong province (including, for example, the Guangdong High People's Court, Guangzhou IP Court, Shenzhen Intermediate People's Court, Guangzhou Internet Court and the Primary People's Court of Guangdong-Macao In-depth Cooperation Zone in Hengqin) can refer foreign-related, Hong Kong-related and Macao-related IP cases to the WIPO Arbitration and Mediation Shanghai Service for mediation. With Guangdong being the province with the highest number of IP cases and cases involving foreign and Hong Kong/Macao parties, this agreement reflects the GBA's commitment to facilitating alternative dispute resolution and provides an additional pathway to resolve cross-border IP disputes amicably through WIPO mediation.

V. Conclusion

From policy initiatives to regional IP protection and strengthened collaborations within the GBA, significant strides have been made in establishing a robust framework for safeguarding IP rights and fostering a dynamic environment for innovation and creativity. Looking ahead, the future of the GBA's IP landscape holds immense promise. It is essential for businesses and stakeholders to stay informed and keep pace with the evolving IP policies, laws and regulations. By embracing these developments and actively engaging in the vibrant IP ecosystem, stakeholders can seize the opportunities that rise and contribute to the continued growth and success of the GBA as a leading innovation hub.

Contact Partners:

Isabella Liu
Partner, Hong Kong
+852 2846 1689
isabella.liu@
bakermckenzie.com

Andrew Sim
Partner, Hong Kong
+852 2846 2314
andrew.sim@
bakermckenzie.com

Employment

10

Authors: Jonathan Isaacs, Weiling Zhong

Special Considerations for Layoffs during Business Reorganizations in Guangdong Province

Business reorganizations and layoffs, as a common phenomenon in the life cycle of an enterprise, are one of the areas that give rise to the most legal disputes during economic downturns. A practical decision on reorganization and layoffs requires not only an accurate understanding of China's labor laws but also insights into local judicial practice and the political environment.

I. Designing a Strategy for Implementing Lay-offs

In Guangdong, if an enterprise relies solely on the provisions in the Employment Contract Law (the core piece of national legislation in China's employment law system) to design its layoff plan for legal compliance, it is very likely that such enterprise will go in the wrong direction and run into obstacles in reality. For example, when many enterprises plan for a mass layoff, the first thing that comes to mind is Article 41 of the Employment Contract Law, which provides for "economic layoffs", and they believe that they must consult with their labor union 30 days in advance and obtain the "approval" of the labor administrative authority before carrying out such layoff. Some enterprises may therefore make great efforts to explore how to comply with these complex procedural requirements, or fail to respond effectively when employees question the legality of its layoff plan.

In fact, the economic layoff procedures provided for under Article 41 of the Employment Contract Law are not the optimal choice for enterprises in Guangdong that seek to reduce their workforce; in particular, in Shenzhen, Article 41 is likely to be an impossible "choice". As the frontier of China's reform and opening up, Shenzhen generally pays more attention to the principle of party autonomy of both employers and employees in terms of labor policy, and the local government seldom intervenes on its own initiative or plays the role of "endorser" for either party (this can also be seen from the name of the characteristic local regulation, i.e. the "Regulations of the Shenzhen Special Economic Zone on the Promotion of Harmonious Employment Relationships"). For this reason, very few enterprises in Shenzhen have been able to successfully complete the process of reporting to the administrative authority and then implementing "economic layoffs". In Guangzhou, the procedural requirements for economic layoffs are also more stringent, and the administrative authority may require an enterprise to provide a third-party audit report to prove the necessity of economic layoffs.

If an enterprise in Guangdong (especially in Shenzhen) needs to restructure and lay off its employees, it is wiser to use "mutual termination" (i.e., Article 36 of the Employment Contract Law) as its preferred option and choose another approach for unilateral termination as its back-up option in light of the actual situation. Generally speaking, the more common potential reason for unilateral termination in the case of corporate restructuring is the one provided for under Article 40(3) of the Employment Contract Law, i.e., "a significant change in the objective circumstances under which the employment contract was concluded makes it impossible to continue to perform the employment contract". It should be noted, however, that what constitutes a "significant change in the objective circumstances" depends to a large extent on the judge/arbitrator's interpretation of the law.

At the national level, the *Ministry of Labor's Explanation on Certain Provisions of the Labor Law* enumerates several generally recognized "objective circumstances", including force majeure, relocation of the enterprise, merger, transfer of enterprise assets, etc. In practice, the shut down of an entire division or production line of an enterprise is also often recognized by judges as a "significant change in objective circumstances". By contrast, it is very unlikely that termination of only a few employees of an enterprise where the overall organizational structure of the enterprise remains intact will be recognized as a real "significant change in the objective circumstances". Of course, factors such as the age and physical condition of the affected employees, and how their employment contracts were concluded, etc. shall also be taken into account when deciding what kind of termination strategy shall be adopted. Employment laws are all about "people", and there is no one-size-fits-all solution.

II. Calculation of Severance Pay

Once the basic principles and plan of layoff have been determined, the next technical challenge that enterprises would face is the calculation of severance. In particular, the accuracy of calculating statutory severance (often known as "N" in everyday contexts) not only has a direct bearing on the legality of the termination of employment relationship, but also affects the design of other termination payments and the techniques that the enterprise shall use in communicating with its employees. With respect to the calculation of statutory severance, Guangdong courts follow a rule which differs from many other cities, and such difference mainly affects employees who started their employment before the Employment Contract Law came into effect (i.e., January 1, 2008). In short, in many cities (e.g., Beijing and Shanghai), when calculating the statutory severance for an employee who started his/her employment before 2008, many courts will divide his/her years of service into two segments, i.e. before and after 2008, and calculate the severance for the two segments separately.

However, in Guangdong, the prevailing judicial practice is to calculate the severance in accordance with the rule established in Article 47 of the Employment Contract Law for all years of service without regard to the year of 2008 as a dividing line, i.e., if the average monthly salary of an employee in the twelve months before termination of his/her employment exceeds three times the local average monthly salary in the previous year, the base for calculating statutory severance shall be three times the local average monthly salary (i.e., what is commonly known as the "social average salary cap"), and the maximum number of years of service for the purpose of calculating statutory severance shall not exceed twelve years.

Such "one-size-fits-all, non-segmented" rule adopted in Guangdong for calculating statutory severance has a particularly significant impact on employees with high salary and long years of service. In extreme cases, these employees are likely to receive lower statutory severance than lower-paid employees with similar years of service. By contrast, in regions where the segmented calculation rule is adopted, the interests of higher-paid senior employees regarding severance are better balanced.

Understanding the nuances of judicial practices in different regions can help companies design better compensation packages and better communicate them to employees. For example, in the case of a mutual termination, many companies are willing to pay additional compensation beyond what is statutory as an incentive for the employees to sign a "mutual termination contract" that settles all outstanding payments and disputes between the parties once for all. Based on the rule for calculating severance in Guangdong, enterprises may need to pay more attention to the fairness of the compensation package when determining the amount of such additional economic compensation, for example, by differentiating employees with different years of service and offering them such additional compensation at different levels to ensure that senior employees will not be materially under-compensated.

III. Effect of Equity Incentives on Termination of Employment Relationship

Employee equity incentives, which have attracted increasing attention in recent years, are also an inescapable topic when considering the calculation of termination payments. In the past, employment arbitration institutions and courts, when handling labor disputes, have often excluded equity incentives from employee compensation and refused to include equity incentive disputes in the scope of labor dispute trial, which is especially the case when the equity incentive is granted by a foreign company. As a result, in the past, if an employee had claimed that the equity incentive received should be counted in the base for calculation of his/her severance or that the employer should compensate the employee for the unvested equity incentive, the courts usually did not support such claim.

However, the Interpretation of the S*upreme People's Court on the Application of Law to the Trial of Labor Dispute Cases (II) (Draft for Public Comment)*, which was made public in December 2023, took the unprecedented step of explicitly including equity incentive disputes within the scope of an employment dispute litigation. Although the draft has not yet been formally finalized and come into effect, many local courts, especially in Beijing and Guangdong, have already been actively exploring new ideas in practice for adjudicating equity incentive disputes, even before the Supreme Court's publication of the draft.

For example, in a landmark case in recent years (i.e. the labor dispute between Oppein Home Group Inc. and Yang), the Guangzhou Intermediate People's Court for the first time specified that the proceeds from equity incentives received by an employee pursuant to his/her employment relationship should be deemed as a part of his/her labor remuneration and should be counted in the base for calculation of his/her severance. More specifically, when calculating the severance in this case, the proceeds from the stock price spread over certain months which fall within both (i) the period in which the employee held the restricted stocks and (ii) the twelve months prior to the termination of his/her employment were counted in the base for calculation of the severance by the court.

In Shenzhen, we have also seen some, though not all, courts include equity incentives in the calculation of severance or order the company to compensate for the loss of equity incentives in individual cases, and it remains to be seen where this new trend in adjudication will end up.

IV. Non-compete Restrictions after Termination of Employment Relationship

In China's economic landscape, the Greater Bay Area has its own distinctive economic types - Guangzhou, as a traditional first-tier city, is the home base of many manufacturing companies; while Shenzhen, as an emerging metropolis adjacent to Hong Kong and full of the spirit of experimentation, has incubated and attracted many Internet, financial and high-tech companies. For the latter, given the core value of trade secrets in the competitiveness of the local businesses, the importance of properly designing and implementing employee non-compete restrictions is self-evident.

To this end, Shenzhen has also gradually developed its own legal regime related to non-compete restrictions. For example, the R*egulations of Shenzhen Special Economic Zone on the Protection of Technical Secrets of Enterprises* stipulate that the non-compete compensation agreed in the non-compete agreement, calculated on a monthly basis, shall not be less than one-half of the average monthly salary of the last twelve months prior to the employee's departure from the enterprise. In contrast, national and many other local legislations have no mandatory requirement on the minimum amount of non-compete compensation.

Another example is that, under the national legislation, non-compete restrictions are designed as a contract between the original employer and the employee, without imposing any obligation on the competitor company that recruits the employee. However, according to the *Regulations of Shenzhen Special Economic Zone on the Protection of Technological Secrets of Enterprises*, if an enterprise knowingly recruits an individual who shall refrain from taking up employment in such enterprise under a non-compete obligation, it may constitute a tort under which the enterprise needs to bear administrative responsibility and joint and several liability for damages under civil law. On the whole, the regulation of non-compete restrictions in Shenzhen is more stringent than that in other cities, which requires special attention by enterprises.

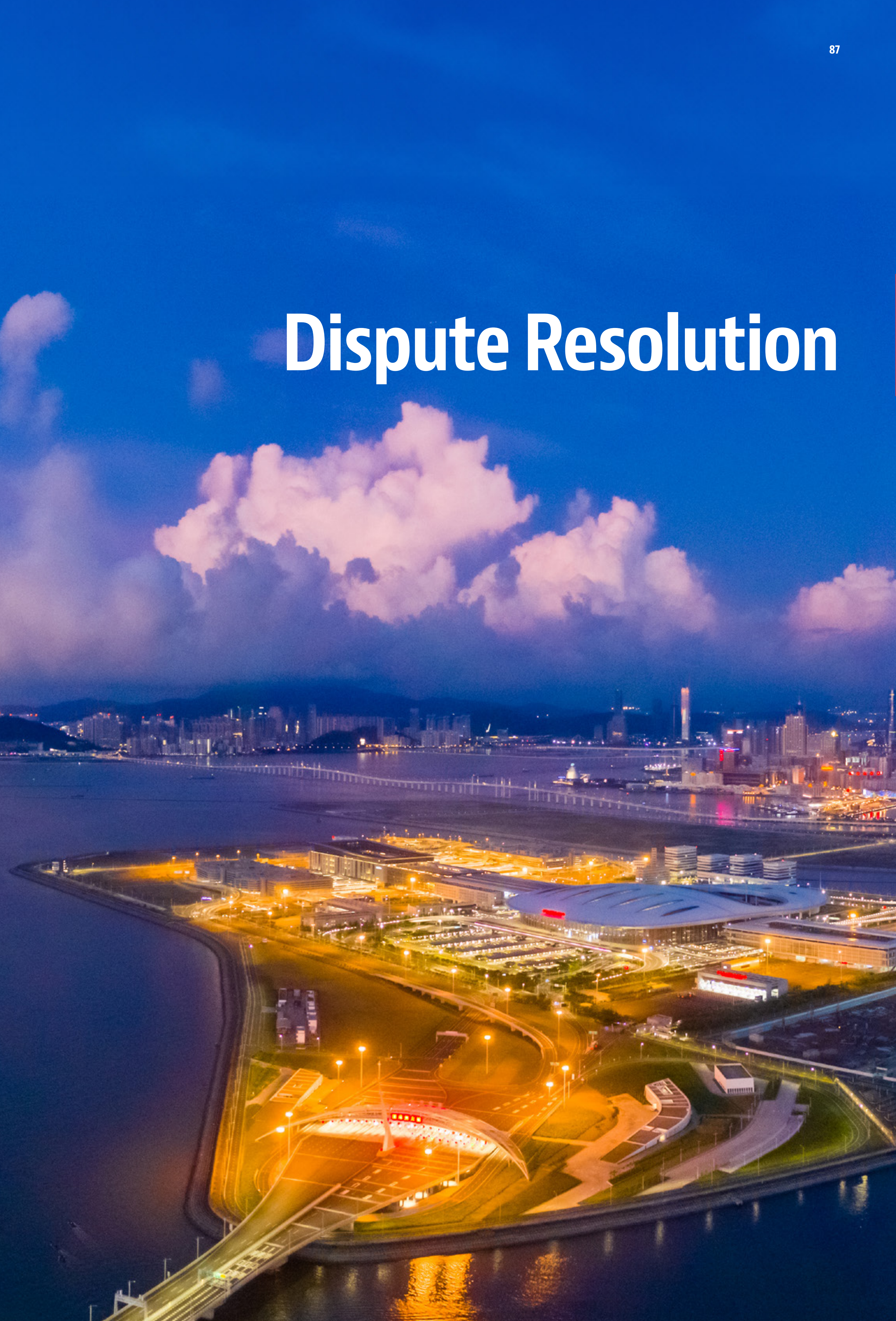
V. Conclusion

China has a vast and complex labor law framework. Despite the existence of the Employment Contract Law and the Labor Law, which serve as the cornerstone of such framework, yet it may be necessary to resort to local policies and practice for answers to questions regarding interpretation and implementation of many legal provisions. With respect to layoffs in the context of corporate reorganization, Guangdong has distinguishing features from other regions in terms of strategies for termination of employment relationship, calculation of severance, handling of equity incentives, and enforcement of non-compete restrictions, etc. Therefore, enterprises need to have a comprehensive understanding of the labor law system and also be well-versed in the local legal practices, so as to not only survive but also thrive in this young, dynamic and promising land.

Contact Partner:

Jonathan Isaacs
Partner, Hong Kong
+852 2846 1968
jonathan.isaacs@
bakermckenzie.com

Dispute Resolution



11

Authors: Bryan Ng, Victor Yip

Mutual Recognition and Enforcement of Court Judgments Between Mainland China and Hong Kong SAR

I. Introduction

The Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Courts of the Mainland and of the Hong Kong Special Administrative Region ("**Arrangement**") came into effect on 29 January 2024.

This is an important development for parties with assets and business interests in Mainland China and Hong Kong SAR. It provides for a wider and more comprehensive regime for the reciprocal recognition and enforcement of judgments in civil and commercial matters between Mainland China and Hong Kong SAR. It also reduces the potential risk of having to relitigate the same dispute, as well as the time and costs involved in cross-border litigation between Mainland China and Hong Kong SAR.

II. In more detail

The Arrangement is implemented in Hong Kong SAR through the Mainland Judgments in Civil and Commercial Matters (Reciprocal Enforcement) Ordinance (Cap. 645) ("**New Ordinance**"). There are also supplementary provisions on practice and procedures, such as the Mainland Judgments in Civil and Commercial Matters (Reciprocal Enforcement) Rules (Cap. 645A).

The existing regime under the Mainland Judgments (Reciprocal Enforcement) Ordinance (Cap. 597) ("**Existing Ordinance**") will continue to apply to judgments made prior to **29 January 2024**. The Existing Ordinance is more restrictive because of the following:

- It only applies in cases where there is an **exclusive jurisdiction agreement** in favor of the courts in Mainland China or Hong Kong SAR. The New Ordinance, on the other hand, **does not have such a requirement** and is thus broader in terms of its scope of application. It suffices if there is a sufficient connection with Mainland China at the time when the proceedings were accepted in Mainland China.
- It only applies to **monetary judgments**, whereas the New Ordinance covers **both monetary and non-monetary judgments**.

The effect of a registration is that it would render a Mainland judgment as enforceable in Hong Kong SAR as though it were a judgment of the Court of First Instance of the High Court of Hong Kong.

1. Registration of a Mainland judgment in Hong Kong SAR

Not all Mainland judgments are registrable under the Arrangement. Broadly speaking, the key requirements are as follows:

(1) Nature of proceedings in which judgment was given

The Arrangement applies to **civil or commercial matters** and to **certain criminal matters** (i.e., where the judgment contains an order for the payment of a monetary amount as compensation or damages by a party to the proceedings).

(2) Timing of the Mainland judgment

The Arrangement applies to judgments made on **or after 29 January 2024**.

(3) Time limit for registration

The registration application must be made **within two years** from the date on which non-compliance with the Mainland judgment first occurs or the date on which the Mainland judgment takes effect.

(4) The judgment is effective in the Mainland

Broadly speaking, the New Ordinance covers the following:

(a) Judgments given by the Supreme People's Court

(b) Judgments given at second instance by a high people's court or an intermediate people's court

(c) As to judgments given at first instance by a high people's court, an intermediate people's court or a primary people's court, the judgment is one that cannot be appealed under Mainland law, or the time limit for appeal has expired and no appeal has been filed

2. Registration of a Hong Kong judgment in Mainland China

Likewise, not all Hong Kong judgments are enforceable in Mainland China. Broadly speaking, the key requirements are as follows:-

(1) Nature of proceedings in which judgment was given

The Arrangement applies to **civil or commercial matters** (other than judicial reviews or any other proceedings arising directly out of the exercise of an administrative power), as well as **certain criminal matters** (i.e., where the judgment contains an order for the payment of a monetary amount as compensation or damages by a party to the proceedings).

(2) Timing of the Mainland judgment

The Arrangement applies to judgments made **on or after 29 January 2024**.

(3) The judgment is effective in Hong Kong SAR

The judgment must be enforceable in Hong Kong SAR and was given by one of the following courts in Hong Kong SAR:

(a) Court of Final Appeal

(b) Court of Appeal

(c) Court of First Instance

(d) Competition Tribunal
(e) District Court
(f) Lands Tribunal
(g) Labour Tribunal
(h) Small Claims Tribunal

3. Enforcement of a foreign judgment under common law

Although the aforementioned statutory mechanism will usually be the quickest and least costly way of seeking enforcement of a Mainland judgment in Hong Kong SAR, it is not the only means of doing so.

Under common law, a foreign judgment for a debt or definite monetary amount, which is final and conclusive, given by a foreign court with jurisdiction to give such judgment may be enforced by a claim for the amount due under the judgment. This is more commonly known as **common law enforcement of a foreign judgment**.

The judgment of a Mainland court is regarded as "foreign" for such purposes, in the sense that it is from another jurisdiction that operates under a system of law that is separate from that of Hong Kong SAR.

Essentially, the way how common law enforcement of a foreign judgment works is that the judgment creditor has to commence fresh court proceedings in Hong Kong SAR to sue upon the foreign judgment as a debt. It will have to satisfy the Hong Kong court that the foreign judgment meets the following criteria:

- It is for a debt or definite monetary amount.
- It is made by a court of competent jurisdiction over the parties and the subject matter.
- The judgment is between the same parties or their privies on an identical issue.
- It is final and conclusive on its merits.
- The judgment is not impeachable according to the rules on conflict of laws of Hong Kong SAR.

III. Practical considerations and implications

Clients should consider the following implications from the outset of every business transaction that has a Mainland China or Hong Kong SAR dimension to it. This development may have the following far-reaching implications:

1. Wider range of enforceable judgments

As explained above, the New Ordinance applies generally to judgments made in civil or commercial matters, as well as certain criminal matters. It is no longer subject to the requirement of there being an exclusive jurisdiction agreement, and will be expanded to cover non-monetary judgments as well.

This eliminates the traditional hurdles that litigants may face when seeking to enforce certain types of judgments, such as where the agreement at issue only contains a non-exclusive jurisdiction clause.

2. Further enhances Hong Kong SAR's role and status in resolving China-related disputes

Hong Kong SAR is the only jurisdiction to have such an arrangement with Mainland China. Likewise, in the arbitration context, Hong Kong SAR is the first arbitration venue outside of Mainland China where parties may obtain interim relief in support of arbitration proceedings from Mainland courts, by virtue of the PRC-HK Interim Measures Arrangement. These arrangements give Hong Kong SAR a significant edge in respect of China-related litigation and arbitration.

Hong Kong SAR also benefits from being the only common law jurisdiction in China. It has a bilingual legal system (with both Chinese and English being official languages of the region), and attracts a wide pool of lawyers and business professionals from around the world. It plays a crucial role as a major gateway to Mainland China and in facilitating business between the East and the West.

Contact Partner:

Bryan Ng
Partner, Hong Kong
+852 2846 2923
bryan.ng@
bakermckenzie.com

Bankruptcy & Restructuring

12

Authors: Simon Hui, Hailin Cui, Yanfei Zeng

Recognition and Assistance in Cross-Border Insolvency: Collaboration and Challenges Between Mainland China and Hong Kong

I. Introduction

In the context of the globalized economy, cross-border business operations by enterprises are becoming increasingly common, leading to the growing prominence of cross-border insolvency issues, which have become important topics in current Chinese legal practice. In recent years, high-profile cross-border insolvency cases involving large enterprises such as Evergrande, Luckin Coffee and Huiyuan Juice have emerged. These cases exhibit similar characteristics: although the main business operations and profits of these enterprises are primarily derived from the Mainland China, they have chosen to list or establish headquarters and subsidiaries overseas in places like Hong Kong SAR, as well as holding companies in jurisdictions like the British Virgin Islands and the Cayman Islands. This cross-border organizational structure exposes these enterprises to the risk of being subject to insolvency or liquidation proceedings in multiple jurisdictions.

Against this backdrop, cross-border insolvency issues between Mainland China and Hong Kong SAR have attracted widespread attention in both regions. In response to this challenge, relevant authorities in Mainland China and Hong Kong SAR have engaged in close cooperation to enhance interregional judicial assistance. The promulgation of documents such as the "Summary of Meetings between the Supreme People's Court and the Government of the Hong Kong Special Administrative Region on the Mutual Recognition and Assistance in Insolvency Proceedings of Mainland China and the Hong Kong Special Administrative Region" and the "Opinions of the Supreme People's Court on Conducting Pilot Work on Recognizing and Assisting Insolvency Proceedings in the Hong Kong Special Administrative Region" ("**Pilot Work Opinion**") provide a clear legal basis for judicial assistance in cross-border insolvency cases between the two regions. Furthermore, the "Opinions on Fully Leveraging the Functions of Bankruptcy Adjudication to Serve the Construction of the Guangdong-Hong Kong-Macao Greater Bay Area" issued by the Guangdong Provincial Higher People's Court emphasizes the importance of enhancing exchanges and cooperation in judicial adjudication of cross-border insolvency within the Greater Bay Area. This article will primarily focus on the breakthroughs and progress made by Mainland China and Hong Kong SAR in recognizing and enforcing insolvency procedures in recent years. Through case analysis, it will address unsettled issues in judicial practice and ultimately provide targeted recommendations on how creditors can maximize the protection of their legitimate interests.

II. Breakthroughs in judicial assistance in insolvency between Mainland China and Hong Kong SAR

Article 5(2) of the "Enterprise Bankruptcy Law of the People's Republic of China" ("**Bankruptcy Law**") stipulates as follows:

> Where any legally effective judgment or ruling made by a foreign court involves any debtor's assets within the territory of the People's Republic of China and if the debtor applies with or requests the people's court to recognize or enforce it, the people's court shall, according to the relevant international treaties that China has concluded or acceded to or according to the principles of reciprocity, conduct an examination thereon and, when believing that it does not violate the basic principles of the laws of the People's Republic of China, does not damage the sovereignty, safety or social public interests of the state, does not damage the legitimate rights and interests of the creditor within the territory of the People's Republic of China, grant recognition and permission for enforcement.【此处引用的是北大法宝破产法英文版原文】

Although the above provision indicates that Chinese courts may recognize and enforce effective bankruptcy-related judgments and rulings of foreign courts, it still follows the approach of "recognizing judgments and rulings on a one-by-one basis," which does not meet the needs of bankruptcy procedures. In fact, bankruptcy procedures require the trustee to perform its duties and the bankruptcy court to issue rulings from time to time to advance the process. The provision seems to require that every ruling made by a foreign bankruptcy court undergo a rerecognition process, which is clearly impractical. Furthermore, the provision fails to address the legal effects arising from the recognition and enforcement of foreign bankruptcy judgments and rulings, which poses challenges in providing clear guidance for judicial practice.

On the other hand, the Pilot Work Opinion takes a more focused approach, catering directly to the need of bankruptcy procedures. In particular, it explicitly designates the bankruptcy procedure itself as the object of recognition, rather than individual judgments or rulings within bankruptcy cases. It also clarifies the legal effects arising after recognition. Second, the opinion introduces the concept of assistance, specifying procedural aspects of foreign bankruptcy proceedings that need to be implemented, especially regarding the trustee's duties and the protection of bankruptcy assets.

Specifically, regarding the legal effects of recognizing insolvency procedures, the Pilot Work Opinion provides clear provisions as follows:

Implementation of automatic relief. The Pilot Work Opinion explicitly stipulates that after the People's Court recognizes the Hong Kong bankruptcy procedure, any actions taken by the debtor to repay individual creditors will become invalid. Additionally, a series of other legal effects will be triggered simultaneously: civil lawsuits or arbitration proceedings initiated by the debtor but not yet concluded will be suspended accordingly and resumed after the Hong Kong trustee takes over the debtor's assets; preservation measures and enforcement procedures regarding the debtor's assets will be lifted or suspended accordingly. Consequently, once Mainland courts recognize the Hong Kong bankruptcy procedure, domestic creditors will no longer be able to individually recover debts from the debtor but will only receive unified repayment according to the statutory order of priority for repayment and corresponding repayment ratio within the bankruptcy procedure. This will greatly enhance the orderly and fair protection of creditors' interests.

Recognition of the trustee's powers. The Pilot Work Opinion explicitly grants Hong Kong trustees recognized by Mainland courts several powers to be exercised in Mainland China, such as taking over the debtor's assets and documents, managing and disposing of assets, and representing the debtor in legal proceedings. This to a certain extent addresses the difficulties faced by foreign insolvency administrators in dealing with Mainland assets in the past. For example, foreign insolvency administrators often encounter obstacles such as refusal by the Mainland management to return company seals, certificates and other documents when replacing legal representatives and directors of Mainland subsidiaries. In such cases, foreign insolvency administrators often have to resort to filing civil lawsuits in Mainland courts to demand the return of company seals and certificates, thus gaining actual control over the debtor's Mainland subsidiaries. However, after the issuance of the Pilot Work Opinion, foreign insolvency administrators can directly apply to Mainland courts for recognition of the Hong Kong bankruptcy proceedings and the trustee's identity to obtain management authority over Mainland assets. For instance, in the bankruptcy case of Hong Kong Ozner Company ((2022) Shanghai 03 Recognition of Hong Kong Insolvency No. 1 Case), the management of Ozner Company's Mainland subsidiaries refused to cooperate with the liquidation of the company, resulting in the inability of the Hong Kong trustee to accurately understand the financial situation of the Mainland subsidiaries, thereby impeding the progress of the liquidation work. Therefore, the Hong Kong trustee applied to the Mainland court, requesting recognition of its powers and duties such as taking over and managing assets, and representing the company in lawsuits in Mainland China, thus facilitating the smooth progress of the liquidation work.

In addition to the above, regarding the exceptions to the recognition of insolvency procedures, the Pilot Work Opinion also provides clearer standards. The phrasing of Article 5(2) of the Enterprise Bankruptcy Law, which states that an action "does not damage the legitimate rights and interests of the creditor within the territory of the People's Republic of China," appears somewhat ambiguous. This vagueness could potentially confuse the courts and result in misinterpretations. For example, in (2022) Beijing 01 Bankruptcy Application No. 786 Case, although the Beijing First Intermediate People's Court recognized the ruling of a German court, its reasoning might give the impression that the court considers the presence of creditors of foreign debtors in China as a factor in its decision-making process.[27] However, the Pilot Work Opinion clearly stipulates that only when creditors can provide evidence to prove the existence of specific circumstances (such as unfair treatment of Mainland creditors or fraud in the Hong Kong bankruptcy procedure) will the court refuse to recognize or assist the Hong Kong bankruptcy procedure. This provision clearly delineates the boundaries for creditor protection and offers specific guidance for the court's judicial proceedings.

It should be noted that the Pilot Work Opinion explicitly stipulates that the pilot work of recognizing and assisting Hong Kong bankruptcy procedures is only conducted in three cities: Shanghai, Xiamen in Fujian province and Shenzhen in Guangdong

27 The Beijing First Intermediate People's Court stated: "The German Bankruptcy Law provides that the German bankruptcy procedure is a collective settlement procedure, and there is no discriminatory provision for creditors in China. Rhein Limited Liability Company (Rhein GmbH) has no litigation or arbitration cases in China, and there are no creditors in China in its bankruptcy procedure. Apart from the buyer, there are no other claimants to its assets within China, and during the notice period of this case, no interested parties have raised objections to this court."

province. In the civil arbitral award disputes such as *Zheng Dasen v. The Hongkong and Shanghai Banking Corporation Limited*, the Supreme People's Court once again emphasized that the Pilot Work Opinion is "currently being piloted only in the people's courts of Shanghai, Xiamen and Shenzhen." However, this does not mean that the Pilot Work Opinion is meaningless for other local courts. In fact, China's courts have gradually relaxed their criteria for determining reciprocal relations between China and foreign jurisdictions, transitioning from initially strict factual reciprocity[28] to a dual reciprocity standard where factual reciprocity is primary and presumed reciprocity[29] is secondary, and now adopting a more lenient standard of legal reciprocity.[30] Therefore, although other courts cannot directly invoke the Pilot Work Opinion as the legal basis to recognize Hong Kong bankruptcy procedures, they may still recognize judgments and rulings in Hong Kong bankruptcy cases based on the principle of reciprocity between Mainland China and Hong Kong SAR. The courts may also provide corresponding judicial assistance and even refer to relevant provisions of the Pilot Work Opinion in its decision. Further observation of judicial practice is needed in this regard.

III. Judicial practices regarding recognition and enforcement of bankruptcy proceedings between Mainland China and Hong Kong SAR

Since the issuance and implementation of the Pilot Work Opinion, there have been limited judicial cases where Hong Kong bankruptcy proceedings have been recognized based on this opinion. However, even though these cases are few in number, they hold significant value in enhancing the pertinent regulations and effectively addressing cross-border bankruptcy matters. This article will take the case of the Ozner Group's cross-border bankruptcy as an example to illustrate the complexity of cross-border bankruptcy cases and the need for cross-border judicial cooperation.

The bankruptcy liquidation of Ozner Water International Holding Limited. Ozner Water International Holding Limited is an investment holding company registered in the Cayman Islands ("**Cayman Ozner**"). Concurrently, Cayman Ozner is a non-Hong Kong company registered in Hong Kong SAR, with its principal place of business located in Hong Kong SAR, and is listed on the Main Board of the Hong Kong Stock Exchange. In March 2021, the Hong Kong court issued a winding-up order

---

28 Factual reciprocity refers to courts examining whether there is a factual reciprocity between two countries, which in practice typically involves reviewing whether the other party has ever recognized or enforced judgments from China.

29 Presumed reciprocity refers to situations where one party has made reciprocal commitments, and the court deems reciprocity to exist if there is no evidence indicating that the country has refused to recognize or enforce Chinese judgments. For specific reference, see the ruling of the Xiamen Maritime Court (2020) Fujian 72 Civil Preliminary Hearing No. 334 Case. Specifically, due to the existence of the Second China-ASEAN Chief Justices' Roundtable Nanning Declaration, reciprocal commitments are not required to establish reciprocity with ASEAN countries.

30 Legal reciprocity refers to the examination at the legal level, whereby judgments from China can be recognized and enforced in another country based on its laws. If this is possible, reciprocity is deemed to exist. For specific reference, see the ruling of the Shanghai Third Intermediate People's Court in the civil retrial case of Shanghai International joint-stock corporation (Kabushiki Kaisha).

against Cayman Ozner and appointed a liquidator to take control of the company. As the main assets of Cayman Ozner are located in Shenzhen, the liquidator of Cayman Ozner applied to the Hong Kong court, hoping to obtain a letter of request and seek assistance from the Shenzhen Intermediate People's Court. The Hong Kong court considered that although Cayman Ozner is not registered in Hong Kong SAR, its main place of business is in Hong Kong SAR, and, therefore, its main center of interest can be deemed to be located in Hong Kong SAR. Based on this, the Hong Kong court agreed to send a letter to the Shenzhen Intermediate People's Court requesting judicial assistance. As of writing this article, the Shenzhen Intermediate People's Court has not yet published any judicial cases recognizing the bankruptcy ruling of the Hong Kong court mentioned above.

The bankruptcy liquidation proceedings of Hong Kong Fresh Water International Group Limited. Hong Kong Fresh Water International Group Limited, incorporated in Hong Kong SAR ("**Hong Kong Ozner**"), is a subsidiary of Cayman Ozner. The primary assets of Hong Kong Ozner in China include the equity of its four wholly owned subsidiaries registered in Shanghai and one subsidiary located in Shanxi. In March 2021, the Hong Kong court issued a winding-up order against Hong Kong Ozner. In July 2021, the Hong Kong court appointed a liquidator. The liquidator of Hong Kong Ozner also applied to the Hong Kong court, requesting it to send a letter seeking recognition and assistance for the bankruptcy proceedings to the Shanghai Third Intermediate People's Court. The Shanghai Third Intermediate People's Court ruled to recognize the liquidation proceedings of Hong Kong Ozner and the identity of the liquidator, and allowed the liquidator to perform relevant duties in Mainland China.

The bankruptcy liquidation proceedings of Shanghai Ozner Water Purification Science & Technology Development Co., Ltd. Shanghai Ozner Water Purification Science & Technology Development Co., Ltd. ("**Shanghai Ozner**") is a wholly owned subsidiary of Hong Kong Ozner in Mainland China. In October 2022, Shanghai Ozner was petitioned for bankruptcy liquidation by creditors. Shanghai Ozner has raised objections to the bankruptcy liquidation application, highlighting its critical role as a key asset for Hong Kong Ozner in Mainland China. This significance is underscored by the ongoing restructuring efforts led by the liquidator in Hong Kong SAR, aimed at reorganizing Ozner Group's entire domestic and overseas entities. Shanghai Ozner emphasizes that pursuing a separate bankruptcy liquidation process would result in asset devaluation, impede the overall restructuring and jeopardize the interests of creditors in both regions. Therefore, Shanghai Ozner requested the court to equally protect the legitimate interests of creditors at home and abroad through a restructuring process. The Shanghai Third Intermediate People's Court determined that Shanghai Ozner failed to provide evidence to substantiate its claims regarding the overall restructuring plan and the feasibility of restructuring. Moreover, it failed to demonstrate that separate bankruptcy liquidation would depreciate asset value and harm the interests of creditors. Therefore, the court ruled to accept the bankruptcy liquidation application against Shanghai Ozner.

The aforementioned cases demonstrate the Chinese courts' openness and support for cross-border bankruptcies, while also revealing some unresolved issues in cross-border bankruptcy, as listed below:

Determination of the primary place of interest for non-Hong Kong companies. According to the Pilot Work Opinion, only companies with their "primary place of interest" in Hong Kong SAR will receive recognition and assistance from Mainland courts for bankruptcy proceedings in Hong Kong SAR. Article 4 of the Pilot Work Opinion specifies that the primary place of interest generally refers to the debtor's place of registration, while the courts should also consider factors such as the location of the debtor's main offices, principal business operations and primary assets. As the place of registration for Hong Kong Ozner is not in Hong Kong SAR, it remains uncertain whether Mainland courts will recognize and assist the winding-up orders issued by the Hong Kong court. This also serves as a reminder for companies engaged in global operations to carefully plan their organization structures and operational strategies.

The issue of parallel bankruptcy proceedings also urgently needs to be addressed. The parallel bankruptcy proceedings conducted by members of the Ozner Group in both Hong Kong SAR and Mainland China highlight the importance of coordinating domestic and international bankruptcy procedures to comprehensively safeguard the interests of all parties involved. This also signals the need for judicial authorities to engage in deeper cooperation on such issues in the future. We look forward to the issuance of more specific and detailed guidance in the future to ensure fair and proper treatment of the rights of all creditors in cross-border bankruptcy scenarios involving group companies. For example, the Greater Bay Area could consider drawing on the principles and rules established in the UNCITRAL Model Law on Enterprise Group Insolvency, allowing administrators to develop a set of bankruptcy solutions applicable to the entire group or certain members in the bankruptcy of cross-border group enterprises. These solutions would focus on the overall financial condition and operational efficiency of the group, rather than treating each member entity in isolation. Through this approach, the interdependence and synergies within the group can be more comprehensively assessed, enabling the adoption of holistic restructuring measures when necessary to restore the group's ongoing operational capability, rather than simply liquidating each group member individually.

IV. Targeted recommendations

Based on the aforementioned, the issuance of the Pilot Work Opinion and judicial practices have certain inspiring implications for both domestic and foreign creditors.

For domestic creditors, it is crucial to closely monitor the situation of the debtor. Upon detecting the debtor's financial distress or default, prompt action should be taken to initiate legal proceedings as early as possible. This allows for the seizure, freezing or auctioning of the debtor's assets within the country through legal means, before the debt issues worsen or foreign procedures are recognized by domestic courts, thereby safeguarding the creditors' interests as much as possible. Additionally, domestic creditors should enhance communication and collaboration with legal advisers to stay informed about the latest developments and potential risks of relevant legal proceedings, ensuring a favorable position in legal procedures.

For foreign creditors, engaging in transactions using offshore shell companies may pose certain risks. Therefore, before entering into any transactions, foreign creditors should conduct thorough due diligence to verify the offshore company's true financial status, operational condition and potential legal risks. Additionally, to ensure the security and reliability of transactions, foreign creditors can request guarantees from the onshore operating companies. This not only helps to mitigate the foreign creditors' risk exposure but also enhances the stability and credibility of the transactions to some extent.

Contact Partner:

Simon Hui
Partner, Shanghai
+86 21 6105 8521
simon.hui@
bakermckenzie.com

About Us

Founded in 1949, Baker McKenzie advises many of the worlds most dynamic and successful business organizations through more than 12,000 people in 74 offices in 45 countries and regions. The Firm is known for its global perspective, deep understanding of the local language and culture of business, uncompromising commitment to excellence, and world-class fluency in its client service. For the twelve consecutive years, Thomson Reuters has named Baker McKenzie the world's strongest law firm brand, has named our Firm the world's strongest law firm brand, ranking us No. 1 in each of the four core brand measures - Awareness, Favorability, Multijurisdictional litigation and Multi-jurisdictional deals

In 2015, Baker McKenzie FenXun (FTZ) Joint Operation Office in China (Shanghai) Free Trade Zone was established in order to combine top-tier international legal service as well as PRC legal service to better serve our clients. The Joint Operation allows Baker McKenzie and FenXun to provide collaborative responses to client needs, including joint execution of client matters, secondments of lawyers between the firms and exchange of know how. Through the Joint Operation Office, they are able to provide PRC law related legal advice as well as legal opinions for our Chinese and Multinational clients.

FenXun is a law firm established in Beijing in 2009. Ever since FenXun has been growing very fast and now there are more than 150 legal professionals in our Beijing, Shanghai and Shenzhen offices. Our main practice areas include: M&A, Capital Market, Asset Securitization, Fund Formation & Investment, Competition & Anti-trust, Banking & Finance, Financial Services, Intellectual Property, Dispute Resolution, Employment, Real Estate and Taxation.

Awards and Rankings

Baker McKenzie

- Baker McKenzie is the most ranked firm (with 23 rankings) under the international category in Chambers Greater China Region 2024 edition
- Best Overall International Law Firm for China Work in 2023, 2022, 2021, 2020, 2019, 2018, 2017, 2016, 2014, 2013, China Business Law Journal
- International Law Firm of the Year 2020, 2016, 2014, 2011, China Law & Practice

Baker McKenzie FenXun (FTZ) Joint Operation Office

- Joint Operation Office Award, Law Firm of the Year, Chambers Asia Pacific, Chambers China Awards, 2020

FenXun Partners

- Top 10 Fastest growing firms in China, Asia Legal Business, 2020, 2019, 2018, 2017
- Notable Achievers, China Business Law Journal, 2019

Integrated Legal Services

Our breadth of expertise: Antitrust and competition; Banking and finance; Capital markets; Compliance and investigations; Data and technology; Dispute resolution; Employment and compensation; Financial services; Intellectual property; International commerce and trade; Investment funds; Mergers and acquisitions; Private equity; Projects; Real Estate; Restructuring and insolvency; Tax

Industry sectors: Consumer Goods & Retail; Energy, Mining & Infrastructure; Financial Institutions; Industrials, Manufacturing & Transportation; Technology, Media & Telecommunications; Healthcare & Life Sciences

Baker McKenzie lawyers based in Hong Kong and mainland work closely with FenXun Shenzhen office, which enhanced the efficiency and flexibility of providing services to local clients in the Greater Bay Area. We have also set up a "GBA Core Team", including members of Hong Kong office who have obtained GBA practice license, to work together to deliver true "one-stop" legal services in the area.

Acknowledgements

We would like to express our sincere gratitude to the editorial team of the Guide to Legal and Regulatory Practice in Guangdong-Hong Kong-Macao Greater Bay Area ("GBA").

We would also like to extend our thanks to Ms. Shirley Wang, Mr. Samuel He and Mr. Zeng Li for their dedication and professional contributions. Their meticulous attention to detail and relentless pursuit of excellence have ensured that this guide is presented accurately and comprehensively to our readers.

Baker & McKenzie FenXun (FTZ) Joint Operation Office

Established in April 2015 in the China (Shanghai) Free Trade Zone, it is the first that has been approved by the Shanghai Justice Bureau. The Joint Operation is staffed by both locally admitted and foreign-licensed lawyers from Baker McKenzie and FenXun Partners, advising leading Chinese and multinational companies on both China domestic and cross-border issues across the full spectrum of corporate and commercial law.

Scan the QR code to follow us on WeChat