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China Implements Special Work Schedules in the Outsourcing Services Industry

Key Points:

- ***Special work schedules apply to outsourcing services enterprises in 20 cities***
- ***Details on procedures and requirements published in Beijing and Jiangsu***

On January 15, 2009 the State Council approved Ministry of Commerce ("MOFCOM") proposals on several policies supporting the development of China's outsourcing services industry. One of the supporting policies permits qualified technically advanced outsourcing services enterprises ("TAOSE") to offer special work schedules to their employees.

On March 29, 2009 the Ministry of Human Resources and Social Security ("MHRSS") and MOFCOM jointly promulgated a MHRSS and MOFCOM Circular specifying that in the 20 model cities for outsourcing services (Beijing, Tianjin, Shanghai, Chongqing, Dalian, Shenzhen, Guangzhou, Wuhan, Harbin, Chengdu, Nanjing, Xi'an, Jinan, Hangzhou, Hefei, Nanchang, Changsha, Daqing, Suzhou and Wuxi), upon approval from the provincial human resources administration and social security administration, the qualified TAOSEs may apply either (i) a flexible work schedule to software design personnel, technology research and development personnel, mid-level and senior management and other personnel who cannot work under a fixed schedule or (ii) a comprehensive calculation work schedule to personnel the nature of whose work requires continuous operation or is suited to a comprehensive calculation work schedule.

Consistent with MHRSS and MOFCOM's Circular, the Jiangsu Provincial Administration of Labor and Social Security and Beijing Municipal Bureau of Human Resources and Social Security have each promulgated separate sets of local rules for implementing the special work schedule in qualified TAOSEs (the "Jiangsu Rules" and the "Beijing Rules"). Under the Beijing Rules, an enterprise or branch division registered in Beijing may apply to the district or county level administrator of human resources and social security to implement special work schedules. The applicant is required to ask for opinions on the application of a special work schedule from the trade union, or from the affected employees in the absence of a trade union, and submit the opinions it solicits to the approval authority. In Beijing, the approved period for applications of special work schedules varies from one to three years.

The Jiangsu Rules provide more detailed requirements to TAOSEs wishing to apply special work schedules. The Jiangsu Rules also clarify that with the consent of the dispatching enterprise, the labor-receiving enterprise under a labor deployment

arrangement can apply to implement special work schedules. Applicants are required to submit a detailed plan for implementing their special work schedules, which must specify the positions and number of personnel to whom the special work schedule applies, the implementation period, their salaries, their rest and holiday periods, work protections and safety measures, and additional issues related to their employment practices. The applicants are also required to (i) provide notice to their workers of the special work schedule implementation plan for at least five working days; (ii) amend the plan by consulting with the trade union or workers; and (iii) publish and maintain an announcement of the authorities' approval of the special work schedule's implementation prominently in the workplace.

In Jiangsu, applications for implementation of a special work schedule must be submitted to the city labor and social security administration, which conducts an onsite inspection after accepting the application and may also seek the opinions of the trade union or workers on the proposed new system. It takes approximately 35 days for administrators to review and examine an application, after which they submit their preliminary review opinions, along with the application materials, to the Jiangsu Provincial Administrator of Labor and Social Security, which may issue its final decision within 10 working days of receiving the opinions and materials and publish that decision on its website. The Jiangsu Rules require that the approved period for application of special work schedules generally not exceed one year.

To apply for special work schedules, TAOSEs are required to be certified jointly by the departments of science and technology, finance, taxation, development and reform, from the city to the provincial level, based on criteria jointly set up by the Ministry of Finance, the State Administration of Taxation, MOFCOM and the National Development and Reform Commission. In addition to application of special work schedules, such certified TAOSEs may also be granted a preferential 15% taxation rate on the enterprise income tax.

– Jian (Brenda) Xu

Regional Focus: Hong Kong Civil Justice Reform

Key Points:

- ***Encourages active case management by judges***
- ***Encourages parties to settle out of court***

Hong Kong Civil Justice Reform ("CJR"), effective April 2, 2009, is embodied in detailed changes to the courts' rules and practice directions. The objective of CJR is to make litigation in Hong Kong fairer, more efficient and more cost-effective. The

reform requires more work of judges, particularly in respect to active case management, and also requires lawyers to change their attitudes and approaches to litigation. Ultimately, the CJR changes the entire landscape of Hong Kong's civil litigation system.

The major changes to the system include:

1. **Active Case Management.**. The courts have traditionally left the parties to decide how to conduct their litigation in terms of defining the issues and setting the pace. With the implementation of CJR, the courts can be expected to take a greater degree of control, both in terms of the issues that are being litigated and the time that is allowed for parties to put their case across and bring it to trial. Cases will be managed proactively, and the proliferation of unnecessary interlocutory applications, which take up time and constitute a heavy drain on the resources of both the courts and the parties, will be discouraged.

2. **Sanctioned Offers and Sanctioned Payments.** Under the new court rules, not only defendants can make sanctioned payments into court and sanctioned offers to the plaintiffs, but plaintiffs will also be able to make sanctioned offers in respect of their own monetary and nonmonetary claims to the defendants. Another important change is that severe financial penalties may be imposed on a party that rejects a sanctioned offer or sanctioned payment and then fails to achieve a better result at trial. The rules clearly encourage parties to settle the case, rather than conducting a full trial.

3. **Mediation.** The courts have a duty to encourage the parties to use an alternative dispute resolution procedure if the court considers it appropriate. The parties to any proceedings and their legal representatives are also under a duty to assist the courts to further this objective. The new court rules make it clear that unreasonable failure to engage in mediation could potentially entail adverse consequences.

4. **Pre-Litigation Preparation.** Under the new rules, it is to the advantage of both the lawyers and the parties involved to identify the real issues in a case at a relatively early stage, as opposed to the situation under the pre-CJR rules. This inevitably will increase front-end costs, because some legal work that might not have been done previously until quite late in the proceedings will need to be done earlier. The judges believe this change will encourage parties to focus on what the real issues are and what their case is really all about at an early stage. In turn, this will cut out wasted costs incurred due to lack of focus on the issues, unnecessary interlocutory appeals.

5. **Statements of Truth.** To confirm the proper function of pleadings, pleadings must now be verified by a statement of truth. The new rules introduce this requirement by identifying the persons who may sign a statement of truth, setting out the effect of a statement of truth and also outlining the consequences of failing to verify a document for which a statement of truth is required. In principle at least, quasi-criminal sanctions (orders for committal for contempt of court) may be imposed on parties that provide an untruthful or fraudulent statement of truth.

6. **Wasted Costs.** The wasted costs regime has now been expanded to cover legal representatives and to allow the court to make such orders on its own motion. Wasted costs will be dealt with in a two-stage procedure and should not be used to threaten the other side's legal representatives.

Although the changes above are not comprehensive, they make it clear that after implementation of the CJR, the court will be more proactive in case management and will encourage out-of-court dispute settlement. This is not only because the court system is an expensive dispute resolution forum, but because settlement by amicable agreement is always preferable to resolution by court judgment. Since parties in a court dispute will now be required to clarify their issues at an early stage of the proceedings, early involvement of barristers and solicitors will be important to litigants in all cases in Hong Kong.

– Daniel Leung

New IPO Measures and Shenzhen Stock Exchange Listing Rules for GEM Board

Key Points:

- ***Issuing conditions for IPO on Growth Enterprise Market (GEM) outlined***
- ***Lock-up requirements applicable to stocks held by different types of shareholders***

As part of a longstanding effort to develop China's multilayer capital market, on March 31, 2009 the China Securities Regulatory Commission ("CSRC") published the Interim Measures for Initial Public Offerings and Listing of Stocks on the Growth Enterprise Market ("GEM IPO Measures"), which took effect on May 1, 2009. On May 8, Shenzhen Stock Exchange ("SZSE") posted a draft Stock Listing Rules of Growth Enterprise Market ("Draft GEM Listing Rules") on its website to solicit public comment. The GEM IPO Measures, in combination with the Draft GEM Listing Rules, are intended to lay down the regulatory framework for GEM, which could be formally launched as early as August 2009.

GEM IPO Conditions

Under the GEM IPO Measures, issuers that apply for initial public offering of shares must fulfill the following criteria:

1. They must be a company limited by shares that has been in continuous operation for three years or more;
2. They must have been profitable:
   - **a)** for the most recent consecutive two years, with an aggregate net profit in the most recent two years of no less than RMB10 million and with profit growth; or
   - **b)** in the most recent year, with a net profit of no less than RMB5 million, a business income in the most recent year of no less than RMB50 million and a growth rate of business income in the most recent two years of no less than 30%. (The basis for calculating net profit will be the lower of the figures before and after deducting nonrecurring gains and losses);
3. Their net assets at the end of the most recent reporting period must not be less than RMB20 million, and they must not have any losses not made up; and
4. Their total share capital after the offering must be no less than RMB 30 million (Article 10).

GEM Underwriting Rules

The GEM will attach greater importance to the role of the sponsors. The sponsor of the issuer's offering of shares and their listing on the GEM should conduct a due diligence investigation, make an informed judgment of the issuer's growth potential and issue an opinion as to that potential. If the issuer is an enterprise that provides proprietary innovations, it must specify in its dedicated opinion the issuer's capability for proprietary innovation (Article 32).

The sponsorship period (during which the sponsor must oversee and propel the issuer's compliance with and fulfillment of various pre-IPO commitments) after an issuer's IPO on GEM runs through the remaining months of the year of its IPO plus three years thereafter – one year longer than that required for listing on the main board. In the meantime, however, in recognition of the fact that fluctuations in performance are common to growth enterprises, the CSRC will not impose the same sanction on the sponsor as is applicable to a main board IPO if the issuer reports a 50% slump of its year-on-year profit during the sponsorship period.

GEM's Stock Lock-Up Requirement

According to the Draft GEM Listing Rules, the shares held by the controlling shareholder or actual controlling party can be sold only three years after the IPO of the issuing company (Article 5.16).

The shares that are held by other shareholders who acquired those shares within 6 months before the IPO application cannot be sold for the first 12 months after the IPO of the issuing company and only 50% of the total can be sold by these shareholders during the period between the 13th and 24th months (Article 5.17).

Meanwhile, other existing shares are generally subject to a one-year lock-up period after the IPO, according to PRC Company Law.

In addition, the Draft GEM Listing Rules include provisions covering information disclosure, trading suspension, delisting conditions and procedures, and internal control rules for various aspects of corporate governance that the listed company must maintain. The Draft GEM Listing Rules can be found at the SZSE website.

– Yi (Peter) Wang

Beijing Issues Revised Headquarters Rules for Multinational Corporations

Key Points:

- ***More government grants and incentives available to attract corporate headquarters***
- ***More convenient facilities provided to headquarters established in (or relocated to) Beijing***

On May 21, 2009 Beijing's municipal government issued Several Provisions on Encouraging Multinational Companies to Establish Regional Headquarters in Beijing (北京市关于鼓励跨国公司在京设立地区总部的若干规定). Shanghai issued similar rules in 2008.

The provisions are designed to encourage multinational corporations to establish or relocate their headquarters in Beijing. Companies outside China that set up their regional headquarters (the location managing branches and offering services in different administrative regions) in Beijing will enjoy preferential policies and receive financial support from the municipal government during their startup periods including the following:

1. Government subsidies will be available for three years for regional headquarters established after January 1, 2009 with a registered capital of over RMB100 million.
2. Regional headquarters newly registered in, or newly relocated to, Beijing that lease office

premises will receive three years' government-subsidized lease assistance.

3. Regional headquarters constructing or purchasing offices in Beijing will be granted funding assistance in the form of a lump sum amount.
4. Financial incentives will be available for three years to regional headquarters in Beijing enjoying annual revenues of over RMB100 million.
5. Chief executive officers, high-level managers and technicians working for regional headquarters in Beijing will be eligible for undefined government "rewards."
6. Immigration procedures will be eased for foreign employees of regional headquarters in Beijing. High-level managers and technicians will be eligible to obtain multiple-entry visas valid for five years and mid-level employees will be eligible for visas valid for three years, while regular employees will be eligible for one-year multiple-entry work visas. Foreign employees of such companies will also be permitted to apply for a Chinese visa after their arrival in Beijing, rather than being required to obtain one before they travel.
7. Foreign employees of Beijing regional headquarters will also enjoy simplified residency permit procedures. High-level managers and technicians will be eligible to obtain long-term residency permits valid for five years and mid-level employees will be eligible for residency permits valid for four years, while regular employees will be eligible for three-year residency permits.

This is not the first time Beijing has sought to attract more global enterprises. In 1999, the city government issued "Provisions on Encouraging Multinational Corporations to Set up Regional Headquarters." Those provisions have been updated by this newest set of incentives. Aiming to become a major global financial center, Shanghai revised its rules for encouraging regional headquarters in October 2008 and, as of March 2009, boasted 224 regional head offices of global companies. By comparison, Beijing is currently home to 121 Asia-Pacific headquarters for global enterprises.

Detailed rules for the implementation of these provisions are expected in a few months, following review and approval by the relevant local government.

– Cong Yang

Outbound USA Focus: Managing the CFIUS Hurdle to US Investment

Key Points:

- ***Non-US acquisitions of US-based companies are subject to expanded US security review***
- ***Measures and planning can reduce security concerns***

Investments in US entities by non-US firms are increasingly subject to US government review. This is due in large part to a recently broadened understanding of transactions involving national security issues, as directed in legislation passed by the US Congress and implemented by the US Department of Treasury, Committee on Foreign Investment in the United States ("CFIUS"). Once confined largely to foreign acquisitions related to the US defense industry, CFIUS now embraces a broad range of transactions as a result of its expanded authority under the Foreign Investment and National Security Act of 2007 ("FINSA") (Pub. L. No. 110-49) and its recent interpretive guidance. Under FINSA, CFIUS review is required for any transaction that could have an impact on US national security related to the country's "critical infrastructure" and critical information technology.

The move toward including critical infrastructure sectors within the realm of national security review began in earnest after 9/11 and is well-illustrated by the Dubai Ports CFIUS review. The tern "critical infrastructure" is now defined by FINSA to include businesses and assets so vital to the United States that their failure "would have a debilitating impact on national security, national economic security, national public health or safety." Sectors specifically identified as critical infrastructure now include telecommunications, public health, chemical industries and hazardous materials, energy, and banking and finance.

For China-based firms, particularly those with government ties, the prospect of a CFIUS investigation can be daunting. This is due in large part to several highly publicized attempted acquisitions of US companies by China-based firms that were determined to have a potentially negative impact on critical US infrastructure. Most notable among these are the Chinese National Offshore Oil Company's (CNOOC) failed attempt to purchase Unocal in 2005 and the proposed merger between the China-based electronics firm Huawei and 3Com in 2008, which was terminated due to the parties' inability to remedy CFIUS' concerns. These examples are, no doubt, discouraging to would-be investors. In many cases, however, upfront planning and forethought in careful selection of targets and tailoring investments with an understanding of likely CFIUS concerns can make the process far more predictable, manage costs and avoid missteps.

CFIUS is an interagency committee chaired by the US Department of Treasury with membership that includes, among others, the Department of State, the Department of Justice, the Office of Homeland Security and the Department of Defense. It is officially tasked with reviewing transactions that could result in control of a US business by a non-US person (a so-called "covered transaction"), to determine the effect of such a transaction on US national security. "Control" as the term is used here does not mean only majority ownership; a non-US acquisition of a minority stake – particularly a dominant minority stake – can also be subject to CFIUS review.

Notifying CFIUS of a proposed transaction is voluntary, but in most cases is recommended. Covered transactions of which CFIUS is voluntarily notified enjoy a "safe harbor" from further review while others risk government intervention, even post-transaction. Whether or not they choose to file a voluntary notification with CFIUS, China-based firms considering a US acquisition are advised to address national security issues as early as possible in the process. In many cases, careful planning of the structure of proposed transactions can help minimize or address national security considerations, even with respect to transactions that would result in control of a US business by the government of another country or its agencies or state-owned enterprises. Measures parties can take to address such risks in advance of a CFIUS notification include adoption of governance structures that provide for a measure of autonomy, and ensuring transparency as to the investment purpose, arrangements and finances of the acquiring firm. Finally, investors should consider, before voluntarily notifying CFIUS, possible mitigation agreements with the US government that will successfully address and resolve national security concerns.

– Christopher H. Skinner

Squire Sanders China Practice Focus: China Environmental Law Issues and Practice

Interview with Charles R. McElwee, Counsel, Shanghai

What are the top three environmental law compliance issues facing outside investors in China?

China regulates end-of-pipe emissions in a similar fashion to that of many Western countries. What the US investor usually finds most surprising are the following programs:

- Environmental Impact Assessments are required for all new construction in China (not just government-backed projects, as in the United States).
- China has adopted several laws that incorporate sustainable development

principles, such as the Clean Production Law, that require audits of the product design and production process to certify that there is no way to, for instance, make the product with fewer hazardous raw materials, or with less water or energy.

- In the product sale and post-consumer arenas, China has enacted regulations similar to the EU's Restriction of Hazardous Substances (RoHS) and Waste Electrical and Electronic Equipment (WEEE) directives. These regulations impose a complex set of obligations upon those who sell certain types of products in China, ranging from the attachment of specific labels to payment into a fund to support the proper disposal of discarded products.

Are environmental laws implemented and enforced uniformly from city to city and region to region in China? How can a foreign-invested enterprise (FIE)'s compliance program manage the vagaries in the practice among different jurisdictions in China?

To answer the first question, no; there are wide variations in environmental law implementation and enforcement at the subnational level in China. As a rule, the laws are more uniformly applied and enforced in China's prosperous eastern coastal regions and Tier 1 cities. In less populated and prosperous regions, enforcement can be spotty at best.

An FIE's compliance program should ignore these regional vagaries and conform to the national standards wherever the company operates in China (adopting stricter local rules where applicable). A program that seeks only compliance with the prevailing local custom invites serious trouble in the event of an audit of the locality by national officials or exposure by a green nongovernmental organization (NGO). Sometimes one of the biggest environmental compliance challenges in China is insisting that local authorities issue you a permit that they have never before required of your local peers.

Are the administrative and judicial remedies for decisions by the environmental authorities effective?

If you are fined by a local Environmental Protection Bureau, you have the right to challenge the imposition of the fine in a local People's Court. Regardless of the facts of the case, the chances of an FIE prevailing in such a challenge are small. On the bright side, the imposition of penalties is usually a last resort in China (after informal attempts to ensure the FIE corrects a violation have failed) and the penalties authorized by China's environmental laws are very low compared to US penalties; the average penalty is well below US$10,000. Having said this, the fact that you have been fined will be

picked up quickly by local and international media and result in negative publicity.

Charlie McElwee has practiced environmental and energy law for more than 20 years, all at Squire, Sanders & Dempsey L.L.P., now in its Shanghai office. He represents a wide range of clients in the United States and China in a variety of matters including counseling regarding environmental, energy and import/export compliance issues; product labeling and content regulations (RoHS); post-consumer obligations (WEEE); and structuring carbon trades and cleantech project deals. He received Shanghai's Magnolia Award, the highest award bestowed by the city on foreigners, in 2008, and in 2009 was awarded Shanghai Jiao Tong University's President's Prize for exceptional contributions to the university.

Articles, Publications and Other Media

Nicholas Chan, partner in our Hong Kong office, and **Louise Ng,** associate in our Hong Kong office, at the invitation of the Hong Kong government, presented the public seminars "Starting a Business: Negotiating Contracts" on May 21 and "Starting a Business: Insurance, Copyright and Employment Laws" on May 26, as well as "Negotiating Arts Contracts," a public seminar for the Hong Kong Arts Development Council, on May 27.

Amy L. Sommers, national partner in our Shanghai office, along with Rebekah J. Poston, partner in our Miami office, was quoted by leading Chinese-language business publication *21st Century Business Herald* on May 23 regarding the US government prosecution of Chinese nationals who embezzled money from the Bank of China.

James M. Zimmerman, partner in our Beijing office, was quoted by Chinese-language business publication *Top China* on April 16 regarding US-China relationships. He appeared on Tianjin TV on May 8 discussing the importance of Tianjin to non-China-based companies operating in Northern China. He also delivered a keynote address at three events in May: the Lanfang-Hebei Provincial Trade Conference in Lanfang on May 18, the Global Outsourcing Investment & Exploratory Delegation to China in Wuhan on May 21 and the Second Annual International Outsourcing Business Development Summit in Hangzhou on May 25.

Squire Sanders released the following China Alerts in May and June: PRC's Supreme People's Court Permits PRC Courts to Modify Contract Terms in Response to Commercial Risks and Key Points in the Draft Administrative Measures on Food Distribution License.

Upcoming Events

Squire Sanders and Ernst & Young will be co-presenters of **FCPA/Anticorruption Developments: What They Mean to You and Your Company** on July 22 at the Squire Sanders office at 600 Hansen Way, Palo Alto, California. The event will feature a discussion led by Squire Sanders Miami partner **Rebekah J. Poston;** Christopher Richardson, senior manager in Ernst & Young's Fraud Investigation & Dispute Services practice; and Squire Sanders Palo Alto of counsel **David A. Saltzman** on the most relevant FCPA issues, recent global enforcement actions and how these cases demonstrate common pitfalls for companies doing business outside the United States. It will include a special focus on China, with an in-person appearance by

Amy L. Sommers sharing her perspectives on recent anticorruption actions in China and their ramifications for companies doing business there. To attend, register now online.

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