

## China Newsletter | Summer 2020/Issue No. 47



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### Foreign Direct Investment

#### **First Significant Amendments to Rules of Foreign Strategic Investment in Listed Companies Since 2005 Promulgation**

外国战略投资上市公司规则迎来 2005 年发布后首次大修

The Ministry of Commerce (MOFCOM) recently published the *Administrative Measures for Strategic Investment by Foreign Investors in Listed Companies (Draft for Comment)* (2020 Draft), seeking public comment by July 19, 2020, purporting to significantly amend the current effective *Administrative Measures for Strategic Investment by Foreign Investors in Listed Companies* (Foreign Strategic Investment Measures), which were issued in 2005.

1. Loosening the regulatory restrictions on strategic investment by foreign investors.

Since being issued in 2005, the Foreign Strategic Investment Measures were amended once, and only slightly, in 2015. The amendment involved a minor change in governmental approval procedure. The 2020 Draft perceptibly loosens the regulatory restrictions on strategic investment by foreign investors in the following aspects:

- In addition to negotiated acquisitions, private placements by the listed company, and other means allowed by laws and regulations, the 2020 Draft further allows strategic investment in listed companies by tender offers of foreign investors;
- In addition to foreign legal persons and other organizations, foreign natural persons are further recognized under the 2020 Draft as “foreign investors”;
- According to the 2020 Draft, qualified foreign investors shall own assets of at least USD 50 million (compared with at least USD 100 million under the Foreign Strategic Investment Measures), or manage assets of at least USD 300 million (compared with at least USD 500 million under the Foreign Strategic Investment Measures);
- The lockup period after strategic investment by foreign investors is shortened from three years to 12 months.

## 2. Breakthrough: Cross-border stock-for-stock transaction.

In stock-for-stock transactions, the acquirer acquires the equity in the target company from original shareholders, or equity placed by the target company, by paying its own equity in a foreign company or equity placed by itself. Stock-for-stock transactions are common for domestic companies, yet quite rare in a cross-border context due to the barriers set by *Provisions on the Merger and Acquisition of Domestic Enterprises by Foreign Investors* (Foreign Investor M&A Provisions).

According to Foreign Investor M&A Provisions, to fulfill a stock-for-stock transaction, not only shall the equity to be paid by foreign investors be legally held and free of ownership disputes, but such equity shall also be listed in an overseas stock market, the price of which must be stable over the previous year. In addition, such transaction shall be pre-approved by the MOFCOM. These conditions make cross-border stock-for-stock transactions almost impossible.

The 2020 Draft may bring some changes to this issue. The major change lies in that the overseas companies are no longer required to be listed companies, unless the strategic investment is conducted through negotiated acquisition. Also, MOFCOM pre-approval is no longer required, but the transaction shall observe securities laws such as disclosure and filing with China Securities Regulatory Commission.

Based on this breakthrough, the 2020 Draft’s changes could extend to stock-for-stock transactions involving non-listed companies.

## **2020 Edition of Negative List Further Eases Market Access for Foreign Investment**

### **2020 版负面清单进一步放宽外国投资市场准入**

On June 30, 2020, the National Development and Reform Commission and MOFCOM jointly published the *2020 Edition of Special Administrative Measures (Negative List) for Foreign Investment Access* (2020 Nationwide Negative List) and *Special Administrative Measures (Negative List) for Foreign Investment Access in Pilot Free Trade Zones* (2020 FTZ Negative List), which will respectively supersede 2019 Nationwide Negative List and 2019 FTZ Negative List.

1. Differences between 2020 Nationwide Negative List and 2019 Nationwide Negative List.

Since 2018, China has been gradually canceling its restrictions on foreign investment in the financial and automotive industries. The 2018 Nationwide Negative List removed the restriction on the shareholding ratio of foreign investors in commercial banks. The 2018 and 2019 Nationwide Negative Lists required that foreign investors could hold no more than 51% of the equity in securities companies, futures companies, and life insurance companies, and also committed to remove the restriction on the shareholding ratio of foreign investors in securities companies, futures companies, and life insurance companies by 2021. In November 2018, UBS Securities became the first securities company in China controlled by a foreign investor, with a shareholding ratio of 51%.

Given the complicated international and economic situation in 2020, China is eager to attract foreign investment. This may be why the restriction on the shareholding ratio of foreign investors in securities companies, futures companies, and life insurance companies was canceled by the 2020 Nationwide Negative List – one year ahead of schedule. Thus, foreign investors may now establish wholly owned securities companies, futures companies, and life insurance companies in China. Indeed, in April 2020, the China Securities Regulatory Commission amended its Management Regulations on Foreign Invested Securities Companies to allow foreign investors to own 100% equity in securities companies.

In the automotive industry, the 2020 Nationwide Negative List cancels the restriction on the shareholding ratio of foreign investors in commercial vehicle (such as a lorry or a bus) manufacturing companies, as promised in the 2019 Nationwide Negative List.

Apart from the previously promised items mentioned above, the 2020 Nationwide Negative List also eases market access for foreign investment in the following aspects:

No.	2019 Edition	2020 Edition
1	<b>Selection and cultivation of new varieties of, and production of seeds of, wheat and corn, must be undertaken by a company controlled by the Chinese party.</b>	The Chinese party shall hold at least 34% of the shares of a company undertaking the selection and cultivation of new varieties of, and production of the seeds of, wheat; selection and cultivation of new varieties of, and production of seeds of, corn, must be undertaken by a company controlled by the Chinese party.
2	Investment in the smelting and processing of radioactive minerals and the production of nuclear fuels is prohibited.	<b>(Deleted)</b>
3	Investment in the construction and operation of water supply and sewage pipe networks in a city with more than 500,000 residents must be controlled by the Chinese party.	<b>(Deleted)</b>

2. Differences between the 2019 FTZ Negative List and 2020 FTZ Negative List.

China has established several pilot-free trade zones since 2014, featuring an increased openness to foreign investors. In a free-trade zone, the 2020 FTZ Negative List shall apply in the first place, rather than 2020 Nationwide Negative List.

Restrictions on the shareholding ratio of foreign investors in securities companies, futures companies, life insurance companies, and commercial automotive manufacturing companies are also canceled in the 2020 FTZ Negative List.

The 2020 FTZ Negative List additionally eases market access in the following respects:

- Cancels the prohibition on foreign investment in the application of the processing techniques of traditional Chinese medicine decoction pieces as steaming, frying, cauterizing and calcining, and the manufacturing of Chinese patent medicine products with a secret formula;
- Cancels the prohibition on foreign investment in vocational education institutions within the educational system.

3. Master plan for construction of the Hainan Free Trade Port.

On June 1, 2020, the Central Committee of CPC and the State Council published the *Master Plan for the Construction of the Hainan Free Trade Port* (Master Plan). In the Master Plan, Hainan Province will explore further opening to foreign investors as follows:

- Gradually cancelling the restrictions on the shareholding ratio of foreign investors in value-added telecommunications;
- Safely and orderly opening up basic telecommunications to foreign investors;
- Allowing the establishment of high-quality universities and vocational colleges in science, engineering, agriculture, and medicine.

However, the Master Plan does not provide clear timing of such opening-up measures.

## National Security

### National People's Congress Enacts Law on Safeguarding National Security in the Hong Kong SAR

#### 全国人大颁布香港特别行政区维护国家安全法

On June 30, 2020, the National People's Congress enacted the *Law on Safeguarding National Security in the Hong Kong Special Administrative Region* (HK National Security Law), sparking wide attention around the world. In response, the U.S. government took countermeasures. Companies should pay attention to compliance obligations under the HK National Security Law given the intricate global political arena.

1. Four types of criminal offenses.

The HK National Security Law provides four types of criminal offenses endangering national security. In serious cases, a criminal may be sentenced to life imprisonment. Anyone convicted of any of the criminal offenses under the HK National Security Law will be disqualified as a candidate for public office or removed from his/her incumbent offices.

- Crime of secession

Crime of secession refers to any of the followings:

- separating the Hong Kong Special Administrative Region (SAR) or any other part of the PRC from the PRC;
- altering by unlawful means the legal status of the Hong Kong SAR or of any other part of the PRC; or
- surrendering the Hong Kong SAR or any other part of the PRC to a foreign country.

Acts of inciting or funding the crime of secession also constitutes a crime.

- Crime of subversion

Crime of subversion refers to any of the following:

- overthrowing or undermining the basic system of the PRC established by the PRC Constitution;
- overthrowing the body of central power of the PRC or the body of power of the Hong Kong SAR;
- seriously interfering in, disrupting, or undermining the performance of duties and functions in accordance with the law by the body of central power of the PRC or the body of power of the Hong Kong SAR; or
- attacking or damaging the premises and facilities used by the body of power of the Hong Kong SAR to perform its duties and functions, rendering it incapable of performing its normal duties and functions.

Acts of inciting or funding the crime of subversion also constitutes a crime.

- Crime of terrorist activities

Crime of terrorist activities refers to any of the following:

- serious violence against a person or persons;
- explosion, arson, or dissemination of poisonous or radioactive substances, pathogens of infectious diseases or other substances;
- sabotage of means of transport, transport facilities, electric power or gas facilities, or other combustible or explosible facilities;
- serious interruption or sabotage of electronic control systems for providing and managing public services such as water, electric power, gas, transport, telecommunications, and the internet; or
- other dangerous activities which seriously harm public health, safety, or security.

Acts of inciting or funding the crime of terrorist activities also constitutes a crime.

- Crime of collusion with a foreign country or foreign powers to endanger national security

Crime of collusion with a foreign country or foreign powers to endanger national security refers to (1) acts of stealing, spying, obtaining with payment, or unlawful provision of state secrets or intelligence concerning national security for a foreign country/institution/person, and (2) acts of requesting a foreign country/institution/person, or colluding with a foreign country/institution/person, or being directed/funded by a foreign country/institution/person to commit any of the following:

- waging a war against the PRC, or using or threatening to use force to seriously undermine the sovereignty, unification and territorial integrity of the PRC;
- seriously disrupting the formulation and implementation of laws or policies by the Government of the Hong Kong SAR or by the Central People’s Government, which is likely to cause serious consequences;
- rigging or undermining an election in the Hong Kong SAR, which is likely to cause serious consequences;
- imposing sanctions or blockade, or engaging in other hostile activities against the Hong Kong SAR or the PRC; or
- provoking by unlawful means hatred among Hong Kong residents towards the Central People’s Government or the Government of Hong Kong SAR, which is likely to cause serious consequences.

Shortly after the HK National Security Law was enacted, the U.S. Congress passed the Hong Kong Autonomy Act, purporting to impose sanctions on certain individuals and entities that “materially contribute to China’s failure to preserve Hong Kong’s autonomy”. At the same time, according to the definition of crime of collusion mentioned above under HK National Security Law, being directed by a foreign country to impose sanctions against the Hong Kong SAR or the PRC may constitute a crime. This points to potentially conflicting compliance obligations on enterprises, especially financial institutions, imposed respectively by Hong Kong Autonomy Act and HK National Security Law. Companies doing business in Hong Kong and subject to U.S. jurisdiction should prudently assess the compliance risks under both the HK National Security Law and the Hong Kong Autonomy Act.

## 2. Newly-established law enforcement authorities.

To enforce the HK National Security Law, some new authorities or departments have been established.

- The Committee for Safeguarding National Security

The Committee for Safeguarding National Security (National Security Committee) is the main authority responsible for safeguarding national security and reports to the Central People’s Government. Chief Executive is the chairman of the National Security Committee, and other major officers in the government of Hong Kong SAR are members of the National Security Committee. In addition, the Central People’s Government will designate a consultant to the National Security Committee to provide advisory opinion.

The duties and functions of the National Security Committee include:

- analyzing and assessing developments in relation to safeguarding national security in the Hong Kong SAR, making work plans, and formulating policies for safeguarding national security in the Hong Kong SAR;

- advancing the development of the legal system and enforcement mechanisms of the Hong Kong SAR for safeguarding national security; and
- coordinating major work and significant operations for safeguarding national security in Hong Kong SAR.

The decisions of the National Security Committee are not subject to judicial review.

- Specific departments under the Hong Kong Police Force and Department of Justice

The HK National Security Law also requires that the Hong Kong Police Force and Department of Justice respectively form specific departments responsible for law enforcement and prosecution. Specifically, Hong Kong Police Force may take the following measures to investigate suspected crimes, apart from its existing purview:

- search of premises, vehicles, vessels, aircraft, and other relevant places and electronic devices that may contain evidence of an offence;
- ordering any person suspected of having committed an offence endangering national security to surrender travel documents, or prohibiting the person concerned from leaving Hong Kong;
- freezing of, applying for restraining order, charging order and confiscation order in respect of, and forfeiture of property used or intended to be used for the commission of the offence, proceeds of crime, or other property relating to the commission of the offence;
- requiring a person who published information or the relevant service provider to delete the information or provide assistance;
- requiring a political organization in a foreign country, an agent of foreign authorities, or an agent of political organization of a foreign country, to provide information;
- upon approval of the Chief Executive, carrying out interception of communications and conducting covert surveillance on a person who is suspected, on reasonable grounds, of being involved in the commission of an offence endangering national security; and
- requiring a person, who is suspected, on reasonable grounds, of possessing information or material relevant to an investigation, to answer questions and furnish such information or produce such material.

The Central People’s Government shall establish the Office for Safeguarding National Security (Office). Major duties and functions of the Office include:

- analyzing and assessing developments in relation to safeguarding national security in the Hong Kong SAR, and providing opinions and making proposals on major strategies and important policies for safeguarding national security;
- overseeing, guiding, coordinating with, and providing support to the Hong Kong SAR in the performance of its duties for safeguarding national security;
- collecting and analyzing intelligence and information concerning national security;
- handling cases concerning offences endangering national security, in accordance with the law; and
- together with the government of the Hong Kong SAR, strengthening the management of and services for organs of foreign countries and international organizations in Hong Kong, as well as non-governmental organizations and news agencies of foreign countries.

3. Scope of effect.

The Hong Kong National Security Law applies to:

- any crime committed by anyone in the Hong Kong SAR (including in vessels/aircrafts registered in Hong Kong), if either the result or act happens therein;
- any crime committed outside the Hong Kong SAR by anyone who is a permanent resident in Hong Kong; and
- any crime committed outside the Hong Kong SAR by anyone who is not a permanent resident in Hong Kong.

4. Jurisdiction.

In most cases, the government of Hong Kong (Hong Kong Police Force, the Department of Justice and the court system) shall have jurisdiction over cases arising under the HK National Security Law.

However, under the following circumstances, the Office shall exercise its power of investigation:

- the case is complex due to the involvement of a foreign country or external elements, thus making it difficult for the Hong Kong SAR to exercise jurisdiction;
- a serious situation occurs where the government of the Hong Kong SAR is unable to effectively enforce the HK National Security Law; or
- a major and imminent threat to national security has occurred.

If a case is investigated by the Office, a procuratorate designated by the Supreme People's Procuratorate will be responsible for the prosecution and a court designated by the Supreme People's Court for the trial.

5. Aftermath.

In early August 2020, the U.S. Treasury imposed sanctions on Hong Kong chief executive Carrie Lam and 10 other top officials from Hong Kong and mainland China. U.S. assets of these individuals are blocked. Unless authorized by a general or specific license issued by the U.S. Office of Foreign Assets Control (OFAC) or otherwise exempt, OFAC's regulations generally prohibit all transactions by U.S. persons or within (or transiting) the United States that involve any property or interests in property of the 11 blocked persons. "Conflicting compliance obligations" mentioned above have therefore been realized by the sanctions on the 11 individuals and the HK National Security Law.

## Civil Law

### National People's Congress Enacts China's First Civil Code

#### 全国人大颁布中国首部《民法典》

On May 28, 2020, the National People's Congress enacted the first Civil Code of China, which will come into effect Jan. 1, 2021, annulling the Law of Marriage, Law of Succession, General Principles of Civil Law, Law of Adoption, Law of Security, Law of Contract, Law of Property, Law of Tort Liability and General Rules of Civil Law. Although the Civil Code combines the separate laws referenced above, it changes some rules to which people are accustomed, and also introduces some new rules (some of which are

incorporated from judicial interpretations issued by the Supreme People's Court). This article highlights some major features of the Civil Code relating to contract, property rights, and personal rights; the full Civil Code contains 1,260 articles.

1. Contracts Section

a. New types of contract: guaranty contract

In the past, guaranty contracts were regulated by the Law of Security. Major differences between the Civil Code and Law of Security are as follows:

- The guarantor's liability is now presumed to be general guarantee liability when there is no agreement on the forms of guarantee, or the agreement is unclear on this issue.

The forms of guarantee include general guarantees and guarantees with joint and several liabilities. A general guarantor may in most cases refuse to perform the guarantee obligations before the creditor has initiated a litigation or arbitration and sought enforcement against the obligor (*beneficium excussionis* of a general guarantor), while a guarantor with joint and several liabilities has no such defense. With this change, emphasis is placed on the protection of guarantors' liability.

- Exceptions to general guarantor's *beneficium excussionis*

A general guarantor may not resort to *beneficium excussionis* to refuse to perform the guarantee obligations in the following circumstances:

- The whereabouts of the obligor are unknown, and there is no property for enforcement;
- A people's court has accepted the obligor's bankruptcy petition;
- Where the creditor has evidence to prove that the obligor's property is insufficient to fulfill all the obligations, or the obligor is not able to perform the obligations; and
- The guarantor has indicated in writing a waiver of the right mentioned in this paragraph.

The third circumstance above is newly added by the Civil Code, out of economic concern that in such cases it would be unreasonable to ask the creditor to go through the lengthy judicial procedure before seeking repayment by the guarantor.

- Guarantor's right of recourse and subrogation

If certain credit is guaranteed by more than one guarantor (joint and several guarantors), or is guaranteed by a guarantor and secured by some property (e.g., by a mortgage) offered by others ("securers"), or is secured by more than one securer with different property, does one of these guarantors/securers, after assuming the obligation of guarantee/security to the creditor, have the right of recourse or subrogation against the obligor and other guarantors/securers? Yes, under the Law of Security, Law of Property, and Civil Code, such guarantor/securer has recourse to the obligor.

Rights against other guarantors/securers have historically been addressed by the courts according to the rule set by the Law of Security and its judicial interpretation, according to which a guarantor/securer shall have recourse against the obligor or the right of recourse that the other guarantors/securers shall answer for the ratio to be assumed by them.

In November 2019, the Supreme People's Court published its ninth *Summaries of the National Conference for the Work of Courts in the Trial of Civil and Commercial Cases* (Ninth Summary), quoting Article 176 of the Law of Property, which only says that when a credit is guaranteed by a guarantor and a securer, such guarantor/securers only have recourse against the obligor, without mentioning the recourse against other guarantors/securers. The Law of Property also provides that it shall prevail over the Law of Security in case of any conflicts. The Supreme People's Court therefore holds that recourse against other guarantors/securers shall be denied unless otherwise agreed by the parties.

The Civil Code basically follows the wording in the Law of Property, and only provides that such guarantor/securer shall have the right of recourse against the debtor (Article 392 and 700). It is widely believed that under the Civil Code, right of recourse against other guarantors/securers is denied, same as stated in the Ninth Summary. However, the Civil Code also provides that in this case, a guarantor (securer is not mentioned) shall have the right of the creditor against the debtor (right of subrogation, Article 700). Does such "right" include the guarantee or security right enjoyed by the creditor? If the answer is yes, it seems that the guarantor may still ask other guarantors/securers to repay, not based on the right of recourse, but on the right of subrogation. Judicial interpretation addressing this issue may issue late 2020.

b. Factoring contract

Factoring is not defined as an independent type of contract but regulated by the rules of assignment of creditors' rights under the Law of Contract. Though the judicial practice of factoring is common and mature in China, it is still helpful to unify the rules in the Civil Code.

Under the Civil Code, a factoring contract refers to a contract whereby the creditor of accounts receivable assigns its existing or future accounts receivable to a factor, who provides services such as financial accommodation, management or collection of accounts receivable, and guarantees for payment by obligors of accounts receivable.

In the case of recourse factoring, the factor may assert a claim against the creditor of accounts receivable for the repayment of principal and interest of the factoring financing funds or repurchase of the accounts receivable, or assert against the obligor of accounts receivable. It is unclear whether the factor may simultaneously assert the claim against both the creditor and the obligor.

Rules of challenge in case of multi-factoring on the same account receivable: a registered factor shall have priority over unregistered factors in collecting the accounts receivable; a factor registered earlier shall have priority over a factor registered later. "Challenge by registration" is a consistent rule in the Civil Code, which will be further discussed in the rules of mortgage on chattel below.

2. Property Rights Section.

a. Effect of *pactum commissorium*

*Pactum commissorium* refers to a special arrangement of the mortgaged/pledged property, in which the creditor and obligor agree that the property mortgaged/pledged will be appropriated by the creditor in case of non-payment of the principal obligation within the stipulated period. Traditionally, this arrangement is deemed invalid under the Law of Security and Law of Property, as it is an exploitation of an obligor who is in a position of weakness. The Civil Code brings some changes to this rule, and provides that in case of *pactum commissorium*, a creditor may still seek preferential repayment in the mortgaged/pledged property. That is to say, a creditor still enjoys its rights as a mortgagee/pledgee.

b. Challenge by registration in chattel mortgage

A mortgage on chattel is established when the contract becomes effective, but a bona fide third party can challenge the mortgage if it is not registered (Article 403). The common law procedure for perfection of a security interest is similar.

“Challenging a bona fide third party” means that the mortgage still exists notwithstanding that the property may have been transferred to a third party. The Civil Code is silent on the determination of “bona fide”. The prevailing theory is that if a third party has no knowledge of the mortgage has looked up the registry of mortgage, and commits no gross negligence, such party is a “bona fide” third party.

However, under the Civil Code, there are two exceptions to this effect of challenge by registration:

- The mortgagee cannot challenge a buyer who has paid a reasonable price and obtained the property in the ordinary course of business (Article 404).
- Purchase-money security interest (PMSI): if the principal obligation secured by the mortgage is the purchase price of the mortgaged chattel, and the mortgage is registered within ten days after delivery, the mortgagee’s right shall prevail over other security right owners, except for lienors (Article 416). In this case, even if PMSI is established or registered later, it shall prevail over other security rights, including an ordinary mortgage right that has been registered.

An important change relevant to Article 403 and Article 404 lies in Article 406, which provides that the mortgagor may transfer the mortgaged property (including chattel) without the prior approval of mortgagee, unless otherwise agreed by the parties. Under the Law of Property, the mortgagor has no right to transfer without approval. According to the Civil Code, such transfer is valid, and so is the mortgage after the transfer. However, combining the rules of Article 403, Article 404 and Article 406, we may draw the following conclusions in case of a mortgage on chattel:

- If the mortgage on the chattel is registered, the mortgage exists even if the chattel is transferred to a third party and the third party has obtained ownership of the chattel, except when the transferee obtained the property in the ordinary course of business;
- If the mortgage on the chattel is not registered, the mortgage: a) if the transferee is a bad faith transferee, the mortgagee’s right of mortgage may challenge the transferee’s ownership, in which case the transferee acquires the chattel with the mortgage on it; b) if the transferee is a good faith (bona fide) transferee, the mortgage perishes.

c. A uniform registration system of security rights on chattel?

In current practice set by the Law of Property, registration of security rights on chattel is handled by various governmental authorities. Mortgages on civil aircrafts are registered by the civil aviation department; mortgages on civil vessels are registered by maritime administration; mortgages on ordinary chattel and pledge on equity of private companies are registered by the administration for market regulation; pledges on accounts receivable are registered by the credit department of People’s Bank of China; pledges on intellectual property (copyright, trademark and patent) are registered by respective administrations of different types of intellectual property, etc.

The Civil Code does not reference a specific registration authority for security rights. A uniform registration system of security rights on chattel may soon be established.

In the Contracts Section, the Civil Code introduces a new rule on registration of ownership of leased property in cases of financial leasing, saying that the ownership enjoyed by the lessor cannot challenge a bona fide third party if it is not registered. In contrast, in current practice set by the Law of Contract and relevant judicial interpretations, to protect its ownership against a third party (for example, when a transferee claims ownership or a secured party claims security right), the lessor usually: (1) place notices on the leased property or (2) causes the lessee to mortgage the leased property to the lessor (meaning the owner of the leased property is also the mortgagee of such property). This rule of registration in the Civil Code may also be incorporated into the uniform registration system of security rights, in that the ownership enjoyed by the lessor in financial leasing is, economically, a sort of security over the payment of rent.

### 3. Personal Rights Section.

China's legislation on cybersecurity and protection of personal information has been a heated topic over the past years. The Civil Code introduced a whole chapter on protection of privacy and personal information rights.

As with General Rules of Civil Law, the Civil Code distinguishes privacy from personal information, but for the first time in the legislative history of China, gives "privacy" a clear definition:

- The private peaceful life of a natural person and the private space, private activities and private information that a natural person does not wish to be known by others.

Personal information is defined as various kinds of information that is electronically or otherwise recorded and can, separately or in combination with other information, identify a specific natural person. Under the Cybersecurity Law, the definition of personal information is more or less the same.

The responsibility to protect personal information is placed on any entity that "processes personal information". "Processing" under the Civil Code refers to collection, storage, use, processing, transmission, provision, disclosure of personal information, etc. Processing personal information shall follow the principles of legality, rightfulness and necessity. In particular, the following conditions must be met:

- Consent from the natural person or his/her guardian is obtained;
- Rules on processing the information is publicized;
- Purpose, form and scope of collecting the information is clear;
- Laws and regulations and mutual agreements are observed.

However, as set forth in the national standard for information security technology — personal information security specification, in current practice, such responsibility is placed on "personal information controllers" who are able to decide on the purpose and form of processing personal information. The Civil Code may have extended the liability to personal information processors in addition to personal information controllers.

## Compliance

### China's Top Legislative Body Starts Second Reading of Draft Law on Biosecurity

#### 《生物安全法（草案）》再次提请最高立法机关审议

The draft law on Biosecurity (the Draft) got a second reading at the 17th session of the Standing Committee of the 13th National People's Congress. The draft was first deliberated in October 2019 and has become an urgent legislative item following the Coronavirus Disease 2019 (COVID-19) outbreak. Notably, biological security is now introduced as "part of the national security," and the draft will become the first unified legal framework for biosecurity in China. According to Yesui Zhang, spokesperson for the third session of the 13th NPC, the draft is expected to be finalized within the year.

With 85 articles, the draft has 10 chapters and namely addresses biosecurity in eight categories: prevent and control the outbreak of emergent epidemics; research, develop, and use of biotechnologies; manage laboratory biosafety; manage the security of human genetic resources and biological resources; prevent the invasion of non-native species and the preservation of biodiversity; respond to microbial drug resistance; prevent bioterrorist attacks and defend against the threat of biological weapons; and other activities related to biological security.

#### *Key Points*

##### 1. Information Sharing and Emergency Response.

The draft for the second reading introduces an information sharing and emergency response system. Pursuant to the draft, the biosecurity information should be issued at the state level or at the local government level as necessary and authorized by the State, instead of unauthorized organizations or individuals.

##### 2. Security of Human Genetic Resources.

The draft provides specific restrictions on China's human genetic resources (CHGR). Foreign organizations and individuals, as well as organizations directly controlled by them, are not allowed to collect or preserve CHGR, nor provide such resources abroad. However, collaborative international scientific research in which Chinese units substantively participate, using CHGR, is legal; however, approvals shall be obtained from scientific administrative departments of the PRC. Market authorization is allowed for new drugs using CHGR in China, that do not involve outbound transfer during the multi-regional clinical trial, but those seeking authorization should file such information with the scientific administrative departments of the PRC.

##### 3. Penalties.

Foreign organizations and individuals failing to comply with the draft shall bear corresponding legal responsibilities, including a fine of RMB 1 million to RMB 10 million, depending on the amount of illegal income.

## China's Top Legislative Body Adopts Law Revision to Curb Solid Waste Pollution

### 最高立法机关通过修订后的《固体废物污染环境防治法》

On April 29, 2020, Chinese lawmakers adopted a revision to the *Law on the Prevention and Control of Environmental Pollution by Solid Waste* (the Law). The revision took effect on Sept. 1, 2020.

Notable changes to the Law are as follows:

#### 1. Industrial Solid Waste Emission Permits.

Pursuant to the Law, emission of industrial solid waste is now included in the pollutant emission permit system. Each entity generating industrial solid waste shall obtain a discharge permit. Entities failing to comply with the Law, generating industrial solid waste without a discharge permit, shall bear corresponding legal responsibilities, including a fine of up to RMB 1 million, and suspend doing business for internal rectification, etc.

#### 2. Extended Producer Responsibility.

The revised Law establishes a management system for products at the end of their useful lives, including electrical and electronic products, lead storage batteries, vehicle batteries and other products. Producers of such products are required to establish (or entrust any other to establish) a waste product recycling system matching the sales volume and should make the public aware of such recycling system. Automobile Sales Service Shop and entities of this kind should especially pay attention to this article.

#### 3. Zero Imports of Solid Waste.

China is currently allowing the import of several types of solid wastes as raw materials. However, according to the Law, China shall gradually realize zero imports of solid waste. Illegal importers will face a fine of RMB 50,000 to RMB 5,000,000. Carriers shall hold joint liability for smuggling solid waste.

Since 2017, China has introduced several bans on solid waste in the tightening of waste markets. In a press meeting held on June 30, 2020, the environment administrative departments of the PRC announced that it would no longer accept import applications for solid waste from 2021.

## SAMR and SCA Issue the Catalog of Commercial Cryptographic Products Subject to Certification (First Batch) and the Rules for Certification of Commercial Cryptographic Products

### 国家市场监督管理总局、国家密码管理局发布《商用密码产品认证目录（第一批）》和《商用密码产品认证规则》

On May 9, 2020, the State Administration for Market Regulation (SAMR) and the State Cryptography Administration (SCA) issued (1) the *Catalog of Commercial Cryptographic Products Subject to Certification (First Batch)* (the Catalog) and (2) the *Rules for Certification of Commercial Cryptographic Products* (the Rules). The Catalog and the Rules were issued to implement the Encryption Law and to establish and improve the certification system for commercial cryptographic products.

The Catalog lists 22 kinds of products (such as smart key, smart IC card, POS password application system, ATM password application system, multi-function password application, Internet terminal) and their respective product descriptions and basis for certification. The Rules' application scope covers the 22 kinds of products listed in the Catalog and basic principle and requirement to implement the certification for commercial cryptographic products. According to the Rules, commercial cryptographic products are certified as follows: type test + initial factory inspection + post-certification supervision. The certification body may entrust the extended product certification to the certified product manufacturer to reduce or exempt the initial factory inspection. The Rules further stipulate the certification implementation procedures, including certification commission, certification evaluation and decision, and certification time limit. In addition, the Rules provide the valid term of a certification certificate as five years, and continuous effectiveness through post-certification supervision by the certification body (but with a new certificate issued after the five-year term expires).

## **Information Security Technology – Implementation Guide for the Construction of Information Security Protection in Industrial Control Systems Sought Public Comment as A National Standard**

### **《信息安全技术 工业控制系统信息安全防护建设实施规范》征求意见**

On May 25, 2020, the National Information Security Standardization Technical Committee (the Committee) released a *Draft for Comment of Information Security Technology – Implementation Guide for the Construction of Information Security Protection in Industrial Control Systems* (Implementation Guide Draft), with public comment due July 25, 2020. Together with the Implementation Guide Draft, the Committee released a standard form for public comment summary and an explanation for the drafting of the Implementation Guide Draft. The explanation provides that the preparation work for this Implementation Guide Draft began in May 2017, and in February 2018, the preparation group invited experts from industries of cigarettes and tobacco, petrifaction, automobile, and electricity to comment on the general requirements for protection. After rounds of seeking advice and revision, the on-site pilot test for the Implementation Guide Draft was conducted at companies of State Grid Corporation of China, Hikvision, Chengdu Gas, and PetroChina Changqing Branch. The explanation also provides the necessity of the Implementation Guide Draft – the industrial control system is the most important constituent of national key infrastructure, covering the power grid, rail transportation, and nuclear. If the network information system of these industries were attacked, key infrastructure could be threatened, with potentially significant losses to the national economy and defense.

Given the continued trend from automation to intellectualization, there are increasing security risks hidden in various industries that may cause significant threat to societal stability and fortune. Therefore, the Committee drafted the Implementation Guide Draft as a voluntary national standard for related entities' reference.

- The introduction of the Implementation Guide Draft provides that the industrial control system should include a programmable logic controller (PLC), distributed control system (DSC), supervisory control and data acquisition (SCADA), which are broadly applied to important national fields such as nuclear facilities, aerospace, advanced manufacturing, petroleum and petrochemical industry, oil and gas pipeline network, power system, transportation, water conservancy, and urban facilities.
- The normative references include three national voluntary standards: (1) GB/T 25069-2010 Information Security Technology - Glossary, (2) GB/T 32919-2016 Information Security

Technology – Application Guide to Industrial Control System Security Control, (3) GB/T 36323-2018 Information Security Technology – Security Management Fundamental Requirements for Industrial Control Systems.

- The Implementation Guide Draft sets five goals for industrial control system security protection:
  1. S-1 programming and construction: an entity is capable of mapping out the basis and condition of protective structure on industrial control system information security.
  2. S-2 single point of protection: for key core sections such as industrial control system, industrial mainframe, industrial network, an entity is capable of applying digital tools and information technology means, to carry out security protection and solve security problems for each section.
  3. S-3 integrated management and control: For the equipment, mainframe, system, network, data of an industrial control system, and based on the existing security protection of each section, the entity is capable of realizing integrated management and control of industrial control system information security and improving security protection ability, via integrated tools and systems.
  4. S-4 integrated collaboration: for an industrial control system of different production lines, plant areas, and factories, the entity is capable of carrying out information security protection construction and developing multi-level collaborative security management system, and realizing comprehensive protection via technical means such as situation awareness and unified monitoring.
  5. S-5 intelligent guarantee: the entity is capable of applying advanced technology such as artificial intelligence and active defense, and comprehensively reinforcing an industrial control system, as well as realizing smart development of a security protection system, via security knowledge and intelligent modeling.

The Implementation Guide Draft contains two appendices. Appendix A provides a verification method for information security protection of an industrial control system, with seven sections (introduction, build evaluation team, develop security evaluation plan, carry out on-site evaluation, form evaluation conclusion, verification of security protection level, and evaluation report of security protection effect). Appendix B provides evaluation standard methods of the information security protection effect of an industrial control system.

## **Intellectual Property Law**

### **China’s Lawmaker Mulls Draft Amendment to the Copyright Law**

#### **最高立法机关审议《著作权法修正案（草案）》**

China’s 1991 Copyright Law was substantively revised in 2001 and 2010. On April 26, 2020, a draft amendment to the Copyright Law (the Amendment) was submitted to the 17th session of the Standing Committee of the 13th National People’s Congress (NPC). The public comment period ran from May 9 to June 13.

The Amendment's proposed changes to the Copyright Law include:

- setting up a copyright registration and documentation system for all kinds of works, to make it easier for the public to determine ownership;
- extending the subject matter of a copyright; for instance, the expression of “the cinematographic works and works created by a process analogous to cinematography” is changed to “audio-visual works,” “computer software” is changed to “computer program,” etc. Such broadening of copyright subject matter aims to better address technology development and to include and regulate more kinds of copyright;
- extending the length of the protection period granted to photographic works, from 50 years to the duration of the author's life and another 15 years after the author's death.

The availability of punitive damages is another notable change stemming from the Amendment. The amount of compensation could be up to five times actual damages, to a maximum of RMB 50,000,000. To better determine the amount of compensation, during the court hearing, the court could order a shift in the burden of proof from the plaintiff to the defendant, in certain circumstances.

## Epidemic-Related

### **Supreme People's Court Issues Guiding Opinions on Several Issues Concerning Enforcement Cases Related to the COVID-19 Epidemic**

**最高人民法院印发《关于依法妥善办理涉新冠肺炎疫情执行案件若干问题的指导意见》**

On May 13, 2020, the Supreme People's Court issued the Guiding Opinions on *Several Issues concerning Law-based and Proper Handling of Enforcement Cases Related to the COVID-19 Epidemic* (Guiding Opinions). The Guiding Opinions set the tone to “protect the legitimate rights and interests of the prevailing parties, especially those having difficulties in production and life due to the impact of the epidemic.”

Prevailing parties enjoy a two-year period for applying the execution/enforcement of a judgment according to the *Civil Procedure Law of PRC* (revised in 2017). And the *Interpretation of the Supreme People's Court on Certain Issues Concerning the Application of Enforcement Procedures under the Civil Procedure Law of PRC* provides in its Article 27 that during the last six months of the above-referenced application enforcement period, where it is impossible to exercise claim rights due to force majeure or any other obstacle, such application period shall be suspended and resumed from the date on which the grounds for the suspension disappear. For the suspension, the Guiding Opinions provide the epidemic or the prevention and control measures taken for the epidemic as the basis for a creditor to claim for the suspension of the enforcement time limit, and the people's court shall support such claim.

To prevent sell-off of property for the enforcement of a judgment, the Guiding Opinions encourage the usage of online judicial auction, to take advantages of transparency, openness, low costs, high efficiency, and to effectively maximize the realization of property value. On the other hand, if a person subject to the enforcement believes that an online quotation or evaluation is too low, and can offer another realization method to pay off the debt at a price no lower than such online quotation/evaluation, then the people's court shall determine to agree on such proposed disposal method if such method will not harm the creditor's interest, and the people's court may supervise such disposal to ensure its completion within the time limit.

The Guiding Opinions provide that the relevant rent relief policy during the epidemic shall be implemented. If there is a claim for rent relief during the epidemic according to relevant policy (which supports small- and medium-sized enterprises and individual businesses), for the lease of state-owned operating houses, the people's court shall support such relief if the relevant policy and facts are confirmed upon investigation. For the lease of non-state-owned operating houses by small- and medium-sized enterprises and individual businesses, if the parties involved claim that agreement is reached on rent relief for the period of epidemic, the people's court shall support such relief if the relevant agreement and facts are confirmed upon investigation.

The Guiding Opinions also encourage the promotion of "smart courts" for smooth and orderly operation of the judicial enforcement work during the epidemic, by preferentially adopting online enforcement measures such as online investigation and control, online inquiry, online judicial auctions and online receipt and payment of money involved in applicable cases, and actively carrying out online case filing, inquiry and conversation, enforcement reconciliation, complaint letters and visits, and enforcement assistance.

## **Supreme People's Court Issues Three Guiding Opinions on Several Issues concerning the Proper Trial of Civil Cases Related to the COVID-19 Epidemic**

**最高人民法院发布三个《关于依法妥善审理涉新冠肺炎疫情民事案件若干问题的指导意见》**

Between April and June, the Supreme People's Court Issued three guiding opinions, respectively the *Guiding Opinions (I)*, *Guiding Opinions (II)*, and *Guiding Opinions (III) on Several Issues concerning the Proper Trial of Civil Cases Related to the Covid-19 Epidemic According to the Law* (collectively, the Guiding Opinions (I), (II), (III), and individually the Guiding Opinions (I), Guiding Opinions (II), or Guiding Opinions (III)).

The Guiding Opinions (I) have 10 clauses: (1) giving top priority to the non-litigation dispute resolution mechanism, (2) accurately applying rules for force majeure, (3) comprehensive consideration of the impact of the epidemic, (4) adoption of flexible working method and ground for termination of labor contract, (5) applying punitive compensation related to anti-epidemic items, (6) suspension of the limitation of action, (7) extension of the time period for action, (8) strengthening judicial assistance, (9) taking flexible preservation measures, (10) consistency of application of law to ensure uniform standards for judgment.

For labor disputes, the Guiding Opinions (I) provide that the court shall not uphold an employer's request to terminate a labor relationship if based only on the grounds that the employee is a confirmed COVID-19 patient, or an asymptomatic infected person, or a person who has been quarantined in accordance with the law, or that the employee comes from a region seriously affected by the epidemic.

For disputes related to supply of anti-epidemic items such as masks, goggles, protective clothing, disinfectants (as well as foods and drugs), the people's court shall uphold the consumers' requests for punitive damages if such supply involves fraudulent practice, or clear awareness by business operators that the goods or the services have defects when providing to customers (which causes death or serious damage to health), or if consumers are damaged by the food that does not meet food safety standards, or if any counterfeit or inferior drugs are sold or produced knowingly.

The Guiding Opinions (II) have 3 sections: provides opinions on trials of (1) contract cases, (2) financial cases, and (3) bankruptcy cases.

For trials of contract cases, the Guiding Opinions (II) repeatedly emphasize application of the fairness doctrine for determination of adjustment, continued performance, and termination of contract. In respect of fee-based online games and live streaming (popular in recent years), the Guiding Opinions (II) support the request to refund payment for fee-based online games and live streaming if such payment is made by a person with limited capacity for civil conduct without consent of his or her guardian. This supportive attitude towards refunds may be in response to the prevalence of minors paying large sums using their parent's account when watching live video streaming by web celebrity.

For trials of financial cases, the Guiding Opinions (II) also refer to the application of fairness doctrine and a series of financial support policies. In respect of medical insurance contract disputes related to the epidemic or epidemic prevention and control measures, a fully supportive attitude towards compensation payment by insurers is provided. The Guiding Opinions (II) provide that the people's court shall not support the defense of non-coverage raised by the insurer (a) where COVID-19 does not fall within the scope of major diseases or is not an insurance accident as agreed in the commercial medical insurance contract, (b) where the treatment for COVID-19 or other disease is received at medical service institutions not provided in the insurance contract (but such failure to receive treatment at designated medical institutions is caused by the epidemic or epidemic prevention and control measures). In addition, for gift insurance activities launched by insurers during the epidemic (including gift insurance given to medical personnel and people who participated in epidemic prevention and control), the people's court shall support the request for compensation raised from such gift insurance.

For trials of bankruptcy cases, the Guiding Opinions (II) encourage multiple measures by adopting installments, extending the time limit for performance of obligations, changing the contract price, or resolution by out-of-court mediation, out-of-court reorganization, pre-reorganization, to achieve early rescue of enterprises. However, for the enterprises which experienced difficulties before the outbreak of the epidemic and further deteriorated due to the epidemic or epidemic prevention or control measures (already qualified as cause for bankruptcy), the people's court shall accept bankruptcy applications in a timely manner and in accordance with relevant laws. In addition, the Guiding Opinions (II) underscore the doctrine of maximizing the value of the property disposed of, and provide that the people's court shall actively instruct the administrator to fully assess the impact of the epidemic or epidemic prevention and control measures on asset disposal prices, and accurately grasp the timing and method of disposal, to avoid improper devaluation of asset values.

The Guiding Opinions (III) cover proper trying of cases involving disputes over foreign-related commercial or maritime affairs related to COVID-19. If the notarization and authentication or other certification for identification document and power of attorney fail to be done, or relevant evidence fails to be provided due to the epidemic or epidemic prevention and control measures, the people's court shall approve the parties' request for reasonable extension in light of the actual circumstances of the case and in accordance with law. However, if there is evidence proving malicious prolongation of the lawsuit by the party concerned, the extension request shall not be approved.

*\* This GT Newsletter is limited to non-U.S. matters and law.*

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