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Stricter Environmental Protection Requirements

By Christophe Han and Zhengyi Zhang

The State Environmental Protection Administration (**SEPA**) has recently promulgated the *Guidelines on Strengthen Environmental Protection Inspections of Listed Companies* (**Guidelines**), which impose restrictions on highly-polluting enterprises applying for listing on domestic stock markets and applying for refinancing. In fact, since 2003, the enterprises in the industries of heavy pollution have been required to undergo an environmental inspection by SEPA when applying for listing and refinancing, according to the *Notice of the State Environmental Protection Administration on the Inspection and Verification of Environmental Protection of the Corporations Applying for Listing and the Listed Corporations Applying for Refinancing released by SEPA* in 2003 and the *Notice of the State Environmental Protection Administration on Further Regulating the Inspection and Verification of Environmental Protection of the High-polluting Corporations Applying for Listing and the Listed Corporations Applying for Refinancing* released by SEPA in 2007 (collectively referred to as Notices).

Environmental Protection Inspections and Verification

- Which Companies Should Apply for Environmental Inspection And Verification?

According to the Guidelines, companies from industries designated as heavily-polluting will have to submit to an environmental protection inspection and verification if they wish to launch an initial public offering (**IPO**) or apply for refinancing, if raised capital is to be invested in industries of heavy pollution.

The aforesaid industries of heavy pollution are temporarily defined to cover 13 industries, including metallurgy, chemicals, petrochemicals, coal, thermal power, building materials, paper making, brewing, pharmaceuticals, fermenting, spinning and weaving, tanning and mining industries.

- The Scope of Inspection and Verification

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The companies that are included in the scope of inspection and verification include branches, wholly-owned subsidiaries and holding subsidiaries of the company applying for the environmental protection inspection and verification which are in heavily-polluting industries, and the companies which would invest raised capital in heavily-polluting industries. The time period of environmental inspection and verification shall be the continuous 36 months prior to application.

- The Process of Inspection and Verification

According to the Guidelines and the Notices, companies applying for listing and refinancing shall apply for inspection and verification to the relevant environmental protection administrative authorities. Normally, they shall apply for inspection and verification to the environmental protection administrative departments at the provincial level in the place of registration. However, those engaging in industries of thermal power generation, steel, cement, electrolytic aluminum and trans-province companies in heavily-polluting industries must obtain SEPA approval.

The relevant environmental protection administrative authorities will provide opinions and suggestions of inspection and verification, and report to China Securities Regulatory Commission (**CSRC**) in the form of a letter of this authority. Subject to the notice released by the CSRC on January 9 2008, IPO applications should have to include a report of the relevant environmental administrative authorities before they are even considered.

- Practice Situations in Inspection and Verification

Since the second half of 2007, SEPA has completed environmental inspections and verifications of 37 companies, and released a list of 10 companies, including the Hong Kong-listed China Coal Energy CO. (1898), Zijin Mining Group CO. (2899) and Anhui Conch Cement CO. (0914), which had failed to pass environmental inspection and verification. The IPO plans of these 10 companies were correspondingly delayed.

SEPA has said that it delayed approval for reasons including excessive emissions, insufficient waste-treatment plants or outstanding pollution lawsuits against the companies or their subsidiaries. SEPA did not detail the changes made by the 10 companies to win approval to go ahead with their IPOs. Up until now, most of those offerings were later approved, while two companies, including Zijing Mining Group CO., still haven't won regulatory approval.

- Environmental Disclosure Requirements

The Guidelines issued by SEPA also emphasize the environmental disclosure responsibilities of listed companies. According to the Guidelines, there are two types of information subject to compulsory disclosure and voluntary disclosure by listed companies. If there is any significant environmental event which may affect the prices of securities and derivatives of a listed company, the listed company shall disclose and provide detailed descriptions. "Significant environmental events" shall include new environmental protection laws, regulations and policies which may affect a listed company, investigations or serious administrative actions against a listed company or criminal liability imposed on a listed company for breach of environmental laws and regulations, important investments which may affect the environment, and legal proceedings for important environmental disputes.

Stricter Environmental Protection Requirements

The Guidelines, together with previous notices regarding environmental protection, are a good start to strengthen the environmental consciousness of PRC-listed companies, and it is believed that SEPA and the CSRC can effectively work together to find the best mechanism for improving environmental protection through the supervision of listed companies.

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