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Client Alert (January 16, 2020)

Analysis on Financial Services Sectors under the Sino-US Trade Agreement

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On January 15, 2020, the United States and China signed an historic *Economic and Trade Agreement between United States of America and the People's Republic of China (Phase One)* (the "**Agreement**"), which includes a commitment by China that it will make substantial additional purchases of U.S. goods and services in the coming years.

The Financial Services Chapter (Chapter 4) of the Agreement addresses a number of longstanding trade and investment barriers to U.S. providers of a wide range of financial services, including banking, insurance, securities, and credit rating services, among others. These barriers include foreign equity limitations and discriminatory regulatory requirements. Removal of these barriers should allow U.S. financial service providers to compete on a more level playing field and expand their services export offerings in the Chinese market.

According to media report, Liu He, Vice Premier of China, commented that based on the principle of fair treatment, non-U.S. financial service providers should benefit from the Agreement and receive the same treatment as well.

The Agreement shall enter into force within 30 days of signature by both parties or as of the date on which both parties have notified each other in writing of the completion of their respective applicable domestic procedures, whichever is sooner. Further, except as otherwise provided in the Agreement, each party shall provide no less than 45 days for public comment on all proposed measures implementing the Agreement. Each party shall consider concerns raised by the other party in any final measure or amendment intended to implement the Agreement.

Set forth below are excerpts of the Financial Services Chapter of the Agreement and our quick comments.

1. Objectives

Provisions	The Parties believe that they have a significant opportunity for cooperation and mutual benefit in bilateral services trade. Each Party requests that the other Party ensure fair, effective, and non-discriminatory participation in its market for services and services suppliers of the other Party. The Parties shall work constructively to provide fair, effective, and non-discriminatory market access for each other's services and services suppliers. To that end, the Parties shall take specific actions beginning with the actions set forth in this Chapter with respect to the financial services sector.
Llinks Comment	This is a summary on the general principles. Concrete further action is required under the Agreement although there have been some high-level opening-up policies and/or implementing rules in place before signing of the Agreement.

2. Securities Investment Fund Custody Services

Provisions	China commits that when a qualified subsidiary of a U.S. financial institution provides or seeks to provide securities investment fund custody services, its parent company's overseas assets shall be taken into consideration in order to fulfill applicable asset requirements. **Within five months after the date of entry into force of this Agreement**, China shall allow branches of U.S. financial institutions to provide securities investment fund custody services, and the parent company's overseas assets shall be taken into consideration in order to fulfill applicable asset requirements. China shall review and approve qualified applications by U.S. financial institutions for securities investment fund custody licenses on an expeditious basis.
Llinks Comment	At the moment, foreign-owned banks have to meet the eligibility requirements of a clearing participant in order to carry out securities investment fund custody business. However, most of foreign-owned banks fail to meet such requirements due to insufficient net assets. According to an in-charge officer of CSRC on a press release regarding the further opening up of the capital market on June14, 2019, CSRC is to relax entrance requirements imposed on foreign-owned banks in carrying out securities investment fund custody business in China, taking into account the asset size and operational experience of their parent banks. Considering that parent banks have good standing and are experienced in custody

	business, CSRC would reasonably adjust relevant arrangements for foreign-owned banks to engage in securities investment fund custody business. Under such arrangement, quality foreign-owned banks are eligible to run investment fund custody business, while another qualified institution would be responsible for clearing. CSRC approved the securities investment fund custody business of Standard Chartered Bank in 2018. However, no other foreign-owned banks have been granted such business license yet. Now, with the Agreement in place, CSRC is expected to review and approve applications submitted by foreign-owned banks on an expeditious basis, as a five month target has been set up in the Agreement.

3. Credit Rating Services

Provisions	China affirms that a wholly U.S.-owned credit rating services supplier has been allowed to rate domestic bonds sold to domestic and international investors, including for the interbank market. China commits that it shall continue to allow U.S. service suppliers, including wholly U.S.-owned credit rating services suppliers, to rate all types of domestic bonds sold to domestic and international investors. **Within three months after the date of entry into force of this Agreement**, China shall review and approve any pending license applications of U.S. service suppliers to provide credit rating services.
Llinks Comment	PBOC and CSRC has declared to open the inter-bank bond market and exchange bond market to foreign credit rating agencies ("**CRA**") since 2017. On September 4, 2018, the *Announcement of the People's Bank of China and the China Securities Regulatory Commission on Issues Concerning the Provision of Bond Rating Services by Credit Rating Agencies on the Inter-bank Bond Market and the Stock Exchange Bond Market* was released. It is stipulated that PBOC, CSRC and the National Association of Financial Market Institutional Investors (NAFMII) would work together on the review of the qualification or registration procedures of CRAs, with a green channel set up for mutual accreditation of qualifications for CRAs that have been in operation in the inter-bank or exchange bond market. On January 28, 2019, S&P Ratings (China) Co., Ltd. was authorized to provide a full spectrum of credit rating services in China's inter-bank bond market, including credit rating

	in relation to bonds issued by financial institutions, debt financing instruments for non-financial institutions, structured products and bonds issued by foreign entities in China's inter-bank bond market. Moody's and Fitch have also set up WFOEs in 2018 but have not obtained relevant licenses yet. With the Agreement in place, PBOC and CSRC will advance the opening-up of the credit rating sector, continuously expand the rating scope of foreign CRAs, and permit more qualified foreign CRAs to conduct all kinds of credit rating businesses in China's inter-bank and exchange bond markets.

4. Financial Asset Management (Distressed Debt) Services

Provisions	China shall allow U.S. financial services suppliers to apply for asset management company licenses that would permit them to acquire non-performing loans directly from Chinese banks, beginning with provincial licenses. When additional national licenses are granted, China shall treat U.S. financial services suppliers on a non-discriminatory basis with Chinese suppliers, including with respect to the granting of such licenses.
Llinks Comment	CBIRC revised its regulatory rules, lifting the foreign shareholding limit in a financial asset management company ("**AMC**") in 2018, but there have been no foreign controlled AMC yet. With the Agreement in place, the first foreign controlled AMC is expected to be set up and approved by CBIRC in the near future.

5. Insurance Services

Provisions	**No later than April 1, 2020**, China shall remove the foreign equity cap in the life, pension, and health insurance sectors and allow wholly U.S.-owned insurance companies to participate in these sectors. China affirms that there are no restrictions on the ability of U.S.-owned insurance companies established in China to wholly own insurance asset management companies in China. **No later than April 1, 2020**, China shall remove any business scope limitations, discriminatory regulatory processes and requirements, and overly burdensome licensing and operating requirements for all insurance sectors (including insurance intermediation),

	and shall thereafter review and approve expeditiously any application by U.S. financial services suppliers for licenses to supply insurance services. In accordance with this commitment, China affirms that it has eliminated the requirement of thirty-years of insurance business operations for establishment of new foreign insurance companies.
Llinks Comment	Among the 11 measures for further opening up the financial sector by the State Council's Office of Financial Stability and Development Committee in July 20, 2019, the requirement that the total share of an insurance asset management company held by domestic insurers shall be no less than 75% will be removed, and the foreign ownership will be permitted to exceed 25%. According to a CBIRC spokesperson interviewed by the Financial Times in July 20, 2019, as a next step, CBIRC will revise the *Provisional Rules on Insurance Asset Management Companies* to implement the opening-up measure. Meanwhile, CBIRC will continue to improve the regulatory rules of insurance asset management companies, strengthen the management of shareholder suitability, and further reinforce the compliance requirements over insurance asset management companies, so as to prevent various risks in an effective manner. With the Agreement in place, we understand that amendment of relevant regulatory rules will be greatly facilitated, and relevant approval procedure is expected to be improved.

6. Securities, Fund Management, Futures Services

(1) General Principle

Provisions	Each Party shall, on a non-discriminatory basis, review and approve a qualified application of a financial institution of the other Party for a securities, fund management, or futures license. The Parties affirm that licensed financial institutions of the other Party are entitled to supply the same full scope of services in these sectors as licensed financial institutions of the Party.
Llinks Comment	Equal treatment principle is set up, which means all business licenses are expected to be open to foreign invested securities companies, fund management companies and futures companies. Implementing measures are yet to be formulated and implemented for some business areas.

(2) Timeline

Provisions	**No later than April 1, 2020**, China shall eliminate foreign equity limits and allow wholly U.S.-owned services suppliers to participate in the securities, fund management, and futures sectors.
Llinks Comment	CSRC announced on a press release on October 11, 2019 that foreign ownership limit in foreign invested futures companies, public fund management companies ("**FMC**") and securities companies will be removed as of January 1, April 1, and December 1, 2020 respectively. Now, opening up of securities companies has been further accelerated, while the timeline set for WFOE FMC and WFOE futures companies remain unchanged. To summarize, unless otherwise further accelerated by CSRC, the timeline now is: ✓ WFOE FMC: April 1, 2020 ✓ WFOE futures company: January 1, 2020 ✓ WFOE securities company: April 1, 2020

(3) Eligibility Requirement for Foreign Invested Securities Companies

Provisions	China affirms that it substantially reduced the high net asset value requirement on majority shareholders of securities services suppliers **on July 5, 2019**.
Llinks Comment	According to the currently effective *Provisions on the Administration of Equities of Securities Companies*, which is applicable to all securities companies (foreign invested securities companies included), net asset of the majority shareholder of a securities company shall not be less than RMB20 billion. With such requirement to be substantially reduced, more foreign invested securities companies are expected to be set up in China.

(4) Private Fund Managers

Provisions	The Parties shall ensure there are no discriminatory restrictions for private fund managers of the other Party. China shall ensure that there is no prohibition on U.S.-owned private fund managers investing in H shares (i.e., shares of mainland Chinese companies listed on

	the Hong Kong stock exchange) and that qualified U.S.-owned private fund managers may be approved to provide investment advisory services on a case-by-case basis.
Llinks Comment	On June 14, 2019, CSRC declared that in order to further open up China's finance industry, build a sound business environment for foreign investments, enrich the types of private funds by foreign invested private fund manager ("**PFM**"), and to satisfy demands of the industry and the market, CSRC would create a level playing field by allowing private funds of foreign invested PFMs (including WFOE PFMs) to invest into H shares through Stock Connect Scheme. CSRC would instruct AMAC to accept filing of the fund products of foreign invested PFMs, which includes H shares investment through Stock Connect Scheme in their investment targets, in order to offer national treatments. In practice, AMAC has implemented such rules according to our project experience. By investment advisory services, we understand it still refers to the policy that WFOE PFM meeting the 1+3+3 requirement[1] is allowed to provide investment advisory services to certain asset management products (e.g., private securities funds of other PFM, private asset management products of FMC, securities companies and futures companies).

(5) Derivatives

Provisions	The Parties affirm that there are no discriminatory restrictions for institutions of the other Party in futures products, including by allowing the institutions of the other Party to invest in the full scope of futures products in which domestic institutions can invest (including financial, interest-rate, and exchange-rate futures).

[1] The 1+3+3 requirement refers to: registered with the AMAC as a private securities investment fund manager for more than 1 year; being an AMAC member; no serious violation of laws or regulations; having at least 3 investment management personnel with continuous traceable track record in securities and futures investment management for more than 3 years and with a clean practicing record.

Llinks Comment	According to a consultation paper on the Measures for the Administration of Domestic Securities and Futures Investment by QFII and RQFII, issued by CSRC on January 31, 2019 for public comment, the permitted derivatives investment will be extended from stock index futures only to: ✓ Financial futures contracts listed and traded on the China Financial Futures Exchange(CFFEX); ✓ Commodity futures contracts listed and traded on futures exchanges approved by CSRC; ✓ Options listed and traded on futures exchanges approved by the State Council or CSRC; and ✓ Eligible foreign exchange derivatives for qualified investors according to regulations of SAFE. With the Agreement in place, and along with other recent legislative progress (e.g., SAFE issued a consultation paper on combing QFII and RQFII regimes, eliminating quota and account opening and maintenance on December 13, 2019), we understand that the updated rules on qualified foreign investors are expected to be issued soon.