
THE PRIVATE EQUITY REVIEW

EDITOR
KIRK AUGUST RADKE

LAW BUSINESS RESEARCH

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EDITOR'S PREFACE

This inaugural edition of *The Private Equity Review* contains the views and observations of leading private equity practitioners in 24 jurisdictions, spanning every region of the world. This worldwide survey reflects private equity's emerging status as a global industry. Private equity is not limited to the United States and western Europe; rather, it is a significant part of the financial landscape both in developed countries and emerging markets alike. Today, there are more than a dozen private equity houses that have offices around the world, with investment mandates matching such global capabilities. In addition to these global players, each region has numerous indigenous private equity sponsors.

As these sponsors seek investment opportunities in every region of the world, they are turning to practitioners in each of these regions and asking two key commercial questions: 'how do I get my private equity deals done here?', and the corollary question, 'how do I raise private equity money here?' This review provides many of the answers to these questions.

Another recent global development that this review addresses is the different regulatory schemes facing the private equity industry. Policymakers around the world have recognised the importance of private equity in today's financial marketplace. Such recognition, however, has not led to a universal approach to regulating the industry; rather, policymakers have adopted many different schemes for the industry. The following chapters help provide a description of these various regulatory regimes.

I wish to thank all of the contributors for their support of this inaugural volume of *The Private Equity Review*. I appreciate that they have taken time from their practices to prepare these insightful and informative chapters.

Kirk August Radke
Kirkland & Ellis LLP
New York
April 2012

Chapter 5

CHINA

Pierre-Luc Arsenault, Jesse Sheley and David Patrick Eich¹

I OVERVIEW

Private equity activity in China grew substantially in 2011, continuing on its upward trajectory since the markets started recovering in 2009 from the global financial crisis. According to AVCJ Research, the market research division of the Asian Venture Capital Journal, there were 520 private equity investments (306 of which were disclosed) in China during 2011, encompassing an aggregate amount invested of \$24.6 billion. The 2011 aggregate amount invested represents an increase of approximately 28 per cent from \$17.8 billion in 2010 (in 358 deals) and 36 per cent from an aggregate amount invested of \$15.77 billion invested in 2008 (in 617 deals). Ernst & Young LLP ('E&Y'), citing Thomson ONE and their own research, finds that the aggregate private equity deal value in China rose from \$13.4 billion in 2010 to \$20 billion in 2011. Global private equity deal volume, by contrast, declined by 19 per cent in 2011, according to E&Y. Although different sources use different methodologies to calculate the volume and value of 'private equity' activity, major sources appear unanimous in their assessment that private equity activity in China increased during 2011.

Chinese private equity transactions are still more likely to consist in a minority investment or a joint venture with a local partner than a buyout, owing to the regulatory obstacles affecting buyouts in China and the reluctance of many Chinese founders to cede control. CVSource, an online database maintained by research and consulting firm ChinaVenture Group, reports that growth equity investments remained the dominant type of deal in China in 2011, accounting for 62 per cent of the number of private

¹ Pierre-Luc Arsenault is a partner at Kirkland & Ellis International LLP, and Jesse Sheley and David Patrick Eich are partners at Kirkland & Ellis. The authors wish to thank Chuan Li, Jing Li, Douglas S Murning, Angela R Russo, Stephanie Tang, Samuel G Williamson and Ashley Young for contributing to several drafts of this chapter, and Jennifer Feng, Jenny Li, Cynthia Wang and Lining Zhang for providing excellent research assistance.

equity deals and 50 per cent of the total invested amount. Private investments in public enterprises ('PIPEs') followed with 33 per cent of the deals and 37 per cent of the invested amount, and buyouts again in 2011 came last with 5 per cent of the deals and 13 per cent of the invested amounts.

Despite the historical paucity of buyouts in China, a trend that emerged in 2011 was going-private transactions involving China-based companies, particularly companies listed in the United States. Nine major such transactions were either announced or closed in 2011, including (most notably) the take-private of Tongjitang Chinese Medicines by its management, which was the first of its kind, the \$2.3 billion take-private of Shanda Interactive, which stands out as the largest such transaction, and the acquisition of China Fire & Security by Bain Capital, the first such transaction in which a private equity investor acquired a controlling stake of the target.

According to E&Y and Thomson ONE, for 2011, the technology, life sciences and consumer products sectors attracted the highest level of private equity investment. Technology had the highest invested amount, due in large part to two mega-deals: as a result of the acquisition by Yufeng Investment, Silver Lake Partners and Digital Sky Technologies ('DST') of a 5 per cent stake in Alibaba Group for \$1.6 billion, and the \$1.5 billion investment by DST and Tiger Global Management in 360Buy.com, the aggregate amount invested in technology companies rose by 139 per cent from \$1.7 billion in 2010 to \$4.1 billion in 2011.

In contrast with the surge in acquisitions, exits declined in 2011, reflecting the plunge in global capital markets. Exits via IPOs were most adversely affected, but the number of trade-sale exits also diminished. According to E&Y, the number of PE-backed IPOs decreased by 60 per cent year on year, from 47 in 2010 to 18 in 2011, while the number of secondary and trade exits decreased by 22 per cent year on year, from 50 in 2010 to 41 in 2011. The decline in the number of Chinese PE-backed companies that completed a listing in the United States was particularly severe, going from 20 in 2010 to only six in 2011, according to E&Y.

Looking at a larger sample of IPO exits, CVSource identifies 165 IPOs in 2011 that were sponsored by either private equity or venture capital firms, 25 per cent fewer than the 220 private equity or VC-backed IPOs in 2010 (but 114 per cent more than the 77 such IPOs in 2009). The combined fundraising amount of all private equity or venture capital-backed IPOs involving Chinese issuers also fell 25 per cent from approximately \$39.5 billion in 2010 to approximately \$29.5 billion in 2011, but increased from only \$15.62 billion in 2009. Of the 165 private equity or venture capital-backed IPOs in 2011, 21 occurred on exchanges outside of mainland China (including 10 on the Hong Kong Stock Exchange ('HKSE'), nine on the New York Stock Exchange ('NYSE') and two on the Nasdaq National Market ('Nasdaq') and the remaining 144 occurred on domestic Chinese exchanges.

One of the most successful IPO exits has been that of online video company Tudou Holdings Limited, backed by Granite Global Ventures and other funds, which became listed on the NYSE in August 2011. On 12 March 2012, less than a year after the offering, Tudou announced having entered into a merger agreement for a stock-for-stock merger with its rival, Youku Inc, which would lead to the formation of China's leading online video company, Youku Tudou Inc. The combination valued Tudou at approximately 74 per cent above its IPO price. Also noteworthy is the Nasdaq IPO of Renren Inc, a social networking

platform operator backed by General Atlantic and DCM. Having raised \$855 million, Renren was the largest private equity-backed IPO of 2011.

II REGULATORY FRAMEWORK

i Acquisition of control and minority interests

China's Company Law, which became effective on 1 January 2006, sets out the governance framework for the two types of Chinese companies: the company limited by shares ('CLS') and the limited liability company ('LLC'). A Chinese entity in which a non-Chinese investor owns an equity interest is called a foreign-invested enterprise ('FIE'), of which there are several types, including a wholly foreign-owned enterprise ('WFOE'), an equity or cooperative joint venture, and a foreign-invested company limited by shares ('FICLS'). FIEs are subject to separate statutes in addition to the Company Law, including the Law on Wholly Foreign Owned Enterprises (which applies to a WFOE), the Law on Sino-Foreign Equity Joint Ventures and the Law on Sino-Foreign Cooperative Joint Ventures (which respectively apply to the two types of joint ventures), and the Interim Provisions on the Establishment of Foreign Invested Companies Limited by Shares (which applies to a FICLS), including their respective implementation rules. The Regulations on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors ('the M&A Rules'), jointly issued by six Chinese governmental agencies in 2006 and amended in 2009, establish a general legal framework in which non-Chinese investors can acquire the equity or assets of a Chinese company. Other statutes and rules govern transfers of equity, mergers and other transactions involving FIEs.²

Government approval regime

An acquisition of or investment in a Chinese company by a non-Chinese investor is subject to a multilayer government approval and registration process. The highest scrutiny is directed at an onshore investment (that is, a direct acquisition of equity in a Chinese company), which requires the approval of the National Development and Reform Commission ('NDRC') or its provincial counterpart and the central Ministry of Commerce ('MOFCOM') or, if the size of the transaction falls below \$300 million, MOFCOM's provincial counterpart. Approval at the provincial level typically can be obtained within one month, but approval from central MOFCOM and NDRC often takes several months or longer. If a transaction is subject to antitrust or national security review as discussed below, MOFCOM or its provincial counterpart typically withhold approval until such reviews are cleared.

Whether MOFCOM and NDRC will grant approval of a transaction depends in part on the Catalogue for the Guidance of Foreign Investment Industries ('the Foreign

2 These rules include the Certain Provisions on Change of the Equity Interests of the Investors of A Foreign-Invested Enterprise, the Provisions of the Ministry of Foreign Trade and Economic Cooperation and the State Administration for Industry and Commerce on Merger and Division of Foreign-Invested Enterprises, and the Interim Provisions on Investment Made by Foreign-Invested Enterprises in China.

Investment Catalogue'), jointly published by MOFCOM and the NDRC, which classifies sectors of the Chinese economy as 'prohibited', 'restricted', or 'encouraged' (with unclassified sectors deemed as 'permitted'). Whereas a non-Chinese investor can acquire full ownership of a company in most 'encouraged' and 'permitted' sectors (and often benefits from special advantages when acquiring a company in an 'encouraged' sector), to invest in most 'restricted' sectors, a non-Chinese party is required to team up with a Chinese partner (and, in some cases, the Chinese partner must maintain a controlling stake). Investments by a non-Chinese party in a 'prohibited' sector are typically prohibited regardless of what percentage of the target is acquired.

In addition to these general approval requirements, foreign investment in several industries, such as construction or telecommunications, is subject to approval from the regulatory authorities governing the applicable industry.

An indirect investment in China by way of an investment in a holding company that owns equity of a Chinese FIE is not subject to the MOFCOM or NDRC approvals applicable to an onshore investment; however, both an onshore and an offshore investment may be subject to China's antitrust and national security review schemes. Under the Anti-Monopoly Law, which became effective 1 August 2008 ('the AML'), an antitrust filing with MOFCOM is required for any transaction involving a change of control if the individual sales in China in the prior accounting year of each of at least two of the parties involved exceed 400 million renminbi and either the parties' aggregate worldwide sales in the prior accounting year exceed 10 billion renminbi or the parties' aggregate sales in China in the prior accounting year exceed 2 billion renminbi. Since the law came into effect, the Chinese antitrust authorities have reviewed more than 400 antitrust cases.³

Further adding to the barriers facing a non-Chinese investor in the Chinese market, China's State Council issued Circular 6 in February 2011, which established a national security review scheme for the acquisition of a Chinese business by one or more non-Chinese investors. Two broad transaction types are subject to Circular 6 review: (1) the 'acquisition' of any stake (regardless of the size) in a military enterprise, a supplier to a military enterprise, a company located near sensitive military facilities, or any other company relating to national defence; and (2) the 'acquisition' involving 'control' of a Chinese company whose business involves 'key' agricultural products, energy and resources, infrastructure, transportation services or technologies or manufacturing of equipment and machinery 'affecting national security'.

Both China's antitrust and national security review schemes provide Chinese authorities with wide discretion to determine whether a transaction is subject to review or, if subject to review, whether it should be blocked. Under Circular 6, the meanings of 'key' and 'affecting national security' are undefined. Under both the AML and Circular 6, 'control' is defined broadly and includes, *inter alia*, having voting rights sufficient to exercise a major impact on board or shareholder resolutions, particularly with respect to key business or operational decisions. As such, private equity investments involving certain customary protections (for example, veto rights, supermajority voting requirements, negative covenants) arguably could be interpreted to involve 'control' under both statutes.

3 'More Muscle', *China Law & Practice*, February 2012, p. 9.

If there is ambiguity as to whether a filing is required, it is usually prudent for an investor to make a filing in order to avoid adverse consequences later. If a transaction is subject to national security or antitrust review, MOFCOM conducts a policy-driven review process to determine whether the transaction can proceed unimpeded: it considers not only the effect of a transaction on national security or competition, as applicable, but also takes into account its effect on the public interest and the stability of the national economy and social order, as well as the views of industry associations and other market participants.

The M&A Rules contain, in effect, a prohibition on ‘round-trip’ investments by requiring approval by MOFCOM of any acquisition by an offshore company formed or controlled by any Chinese company or individual affiliated with the Chinese target company. Ordinarily, this approval is not granted. Where the offshore structure was in place prior to the adoption of the M&A Rules in 2006, however, the acquisition of a Chinese target by the offshore entity is still permitted.

Governance of and exit from onshore joint ventures

The Chinese corporate law and regulatory framework applying to FIEs make it difficult for shareholders in a Chinese company to obtain or enforce contractual rights that are considered fundamental for private equity investors in other jurisdictions, including rights pertaining to governance and exit. First, members of an onshore equity joint venture have rights of proportional representation on the board, meaning that a Chinese partner typically has the right to appoint at least one director. Further, certain important corporate acts of any joint venture must be unanimously approved by the board, including: (1) any amendment to the articles of association (which is required in connection with any equity transfer); (2) any liquidation or dissolution; (3) any increase or decrease in registered capital; and (4) any merger or division. As a result, a non-Chinese investor with a minority stake in a joint venture cannot obtain complete control because the minority partner has statutory veto rights via its representative on the board.

Moreover, it may be difficult for a non-Chinese investor to enforce certain exit-related provisions that are often key terms of a private equity investment. Transfers of equity in an onshore joint venture are subject to a statutory consent right and right of first refusal by all other members. Theoretically, such rights can be waived in advance in the joint venture contract. In practice, however, a transfer of a shareholder’s interest in a Chinese joint venture requires amendments to the joint venture contract and articles of association as well as the approval of MOFCOM or its provincial counterpart. Because an amended joint venture contract (review of which MOFCOM expects in order to approve a transfer) requires signatures from all shareholders, the other shareholders’ cooperation is necessary in connection with any transfer. The same difficulties arise for a private equity investor seeking to enforce a call right, put right or drag-along right against the Chinese shareholders (a tag-along right is easier to enforce, as the party with the tag right can attempt to block a transfer if the transferor fails to comply with the other shareholders’ tag-along right). If the Chinese shareholder is a state-owned enterprise (‘SOE’), enforcement is even more difficult, as a transfer of a SOE’s interest in a joint venture is subject to a statutory appraisal and an open bid procedure, unless waived by appropriate authorities. Regardless of what rights may be contained in a joint venture contract, a local Chinese court injunction granting specific performance against a Chinese shareholder and in favour of a foreign investor is far from certain.

Implications of regulatory framework on transaction structure

To avoid seeking NDRC and MOFCOM approval and to enhance structuring flexibility, foreign private equity investors typically prefer to invest in China through an offshore investment. The ideal transaction structure, when feasible, is for the foreign investor to invest alongside a Chinese partner in an offshore Cayman or British Virgin Islands company, with such company owning 100 per cent of a Chinese WFOE (often indirectly through a Hong Kong entity, to obtain preferential treatment on dividends). This structure also allows the foreign investor to benefit from transaction agreements governed by foreign law and to avoid the need to enforce its rights in China. Because of foreign ownership limitations and the prohibition on ‘round-trip’ investments, however, this offshore structure is seldom available for foreign investments in Chinese targets that have not formed an offshore holding structure prior to the effectiveness of the M&A Rules.

In the past, many non-Chinese investors used a ‘variable interest entity’ (‘VIE’) structure to invest (indirectly) in China without seeking Chinese regulatory approval. Under a VIE structure, Chinese individuals, often the founders, are the registered shareholders of a domestic operating company, which holds the required licences and permits needed for the business to operate. An investor (often in conjunction with the founders) then forms a WFOE through an offshore entity it owns, and the WFOE enters into a series of contractual arrangements with the operating company and its registered shareholders pursuant to which the WFOE obtains control and an economic interest in such operating company. These contractual arrangements can take many forms, but often include an exclusive service or licence agreement, a voting proxy agreement, share pledge agreement and loan agreement, and an exclusive option agreement (together with a form of equity transfer agreement) allowing the WFOE or its affiliates to acquire the equity interests or assets of the operating company when permitted by PRC law.

ii Fiduciary duties and liability

Fiduciary duties of directors, officers and supervisors

The Company Law is the primary statute regulating the actions and duties of directors, officers and supervisors of a Chinese company. Pursuant to the Company Law, a director, officer or supervisor must abide by laws, administrative regulations and the articles of association of the company, and has a duty of loyalty and duty of care to the company. As in many other countries, a breach of duty may give rise to civil, administrative or criminal liability. A particular concern to a private equity investor in China, however, is that a director, officer or supervisor may be liable for criminal liability not only for his or her own wrongdoing, but also for crimes committed by the company if he or she is the ‘manager directly in charge’ or ‘person directly responsible’ for the management of the matter with respect to which a specific criminal act was committed. This risk of personal liability for company wrongdoing is more acute for a director or officer who is also the chairman of the board, executive director or legal representative of the company or who otherwise serves in a senior management capacity, such as general manager or chief financial officer. Most non-Chinese private equity funds are comfortable appointing their representatives to the boards of Chinese companies notwithstanding the risk of liability, often while seeking to ensure that their representatives are not assigned responsibility for any specific matters. While directors and officers insurance and indemnification agreements may protect against civil liability,

many types of administrative or criminal liability cannot be mitigated with insurance and indemnification.

PRC tax exposure

An offshore vehicle established by a non-Chinese private equity investor to make an investment in a Chinese company will be treated as a ‘PRC-resident enterprise’ under the PRC Enterprise Income Tax Law and subject to the uniform 25 per cent enterprise income tax on its worldwide income where such offshore vehicle’s ‘*de facto* management body’ is in China. Although the law is unclear, factors that the State Administration of Taxation may take into account in determining tax residency include whether:

- a* the offshore vehicle locates its senior management and core management departments in charge of daily operations in China;
- b* financial and human resources decisions of the offshore vehicle are subject to determination or approval by individuals or bodies in China;
- c* the offshore vehicle’s major assets, accounting books, company seals, and minutes and files of board and shareholders’ meetings are kept or located in China; and
- d* at least half of the offshore vehicle’s directors or senior management reside in China.

To mitigate the risk that any dividends, sale proceeds or other income received by an offshore vehicle is subject to such tax, an offshore vehicle should take steps to establish that it is not effectively managed and controlled in China.

Bribery statutes

Foreign private equity investors in China also face risks posed by western corruption laws, including the US Foreign Corrupt Practices Act (‘the FCPA’) and the UK Bribery Act. Typically, foreign companies that are entirely privately held and do not have US business connections should not themselves be exposed to FCPA jurisdiction; however, if a US fund discovers corrupt practices during the pre-transaction due diligence and permits them to continue post-closing, then that fund would likely be liable for the corrupt conduct that occurred on its watch. This theory of liability was evident in the 2010 prosecution by the US Department of Justice (‘the DoJ’) of RAE Systems, in which the DoJ stated that during due diligence on a potential acquisition, RAE learned of ‘improper commissions, kickbacks and ‘under table greasing to get deals’ by employees’. However, according to the DoJ, RAE ‘chose to implement internal controls only “halfway” so as not to “choke the sales engine and cause a distraction for the sales guys”’. As a result of the enforcement action, RAE paid \$1.7 million in fines to the DoJ, and disgorged \$1.25 million to the SEC. Given this sort of precedent and the DoJ’s increased scrutiny of corruption in Chinese companies in recent years, foreign private equity investors in China have increasingly begun to conduct rigorous anti-corruption due diligence during the pre-transaction period, and then to take steps to ensure that any improper conduct has ceased prior to closing. In many instances, the required steps are fairly limited; however, in high-risk circumstances, such as in transactions involving companies with significant government interactions necessary for operations, the remedial process can be complex and expensive.

III YEAR IN REVIEW

i Recent deal activity

Going-private transactions

Perhaps the most notable trend of the year in Chinese private equity has been that of the founders of US-listed companies based in China taking their companies private. Tongjitang Chinese Medicines was the first of its kind, announcing in November 2010 that it had entered into a merger agreement under which its chairman and other minority shareholders, which together owned more than 80 per cent of the company, would acquire the remaining shares. During 2011, eight other notable US-listed Chinese companies followed in Tongjitang's footsteps by entering into merger agreements with groups of buyers that include their top management (one more, Global Education & Technology, a provider of test preparation services for Chinese students learning English, agreed to be acquired by global publisher Pearson plc without management participating in the buyer group). As of mid-March 2012, seven of these transactions have closed, including Tongjitang. Countless more US-listed Chinese companies have since either received a going-private offer or formed a special committee of independent directors (and, in many cases, retained financial advisers or legal counsel) to consider their strategic options.

Going-private transactions involving US-listed Chinese companies signed or closed in 2011

<i>Target</i>	<i>Jurisdiction</i>	<i>Signing date</i>	<i>Closing date</i>	<i>Value (\$)</i>	<i>Business</i>
Chemspec	Cayman Islands	21 March 2011	15 August 2011	292 million	Speciality chemicals
China Advanced Construction Materials	Delaware	24 October 2011	Pending	47 million	Ready mix concrete materials
China Fire & Security	Florida	20 May 2011	4 November 2011	266 million	Fire protection systems
China Real Estate Information Corporation	Cayman Islands	28 December 2011	Pending	600 million	Real estate information and consulting services
China Security & Surveillance	Delaware	20 April 2011	16 September 2011	583 million	Electronic surveillance and safety products
Funtalk China	Cayman Islands	31 May 2011	26 August 2011	443 million	Wireless communications devices and accessories
Harbin Electric	Nevada	19 June 2011	4 November 2011	745 million	Development and manufacture of electric motors
Shanda Interactive	Cayman Islands	22 November 2011	14 February 2012	2.3 billion	Online gaming
Tongjitang Chinese Medicines	Cayman Islands	29 October 2010	15 April 2011	117 million	Modernised traditional Chinese medicine

Regulatory agencies, market research firms and short sellers all contributed to sparking the going-private trend by calling attention to accounting failures and fraud at US-listed Chinese companies, targeting most severely those that listed through a reverse takeover ('RTO'). In an RTO, a private company merges with a publicly traded shell company and, as a result of the merger, the (formerly) private company becomes listed on the NYSE or Nasdaq without having paid the cost or fulfilled the burdensome disclosure requirements of an IPO. In April 2011, Mary Schapiro, chairman of the US Securities and Exchange Commission ('the SEC'), wrote that, over the past several months, the SEC had revoked the securities registration of at least eight Chinese companies that became public through an RTO and suspended trading in at least three such companies.⁴ Around the same time, the Public Company Accounting Oversight Board ('PCAOB') published a research note identifying potential concerns in audits performed by US-registered accounting firms.⁵ In addition to taking action against Chinese companies, the SEC filed an enforcement action against US audit firm Moore Stephens Wurth Frazer & Torbet LLP alleging improper conduct in connection with their work for China Energy Savings. As a result of SEC investigations into certain firms' audit practices, in March and April 2011 alone, 24 PRC-based companies had publicly disclosed auditor resignations or accounting problems (or both). In June 2011, Interactive Brokers, an automated global electronic broker that caters to financial professionals, added to the alarm by banning clients from borrowing money to buy any of 160 Chinese securities.

Market research firms like Muddy Waters, Citron Research and GeoInvesting also focused their scrutiny on Chinese companies, often furnishing regulatory agencies with grounds to investigate. In one of the most high-profile cases, after Muddy Waters' June 2011 report accusing Toronto-listed Sino-Forest Corporation of operating a 'multi-billion-dollar Ponzi scheme', the company's stock dropped by more than 80 per cent overnight, leading the Ontario Securities Commission to suspend trading and investigate the company for fraud. Many of the firms that issued critical research reports were simultaneously taking short positions in the Chinese companies they were attacking, often making substantial gains from the negative publicity.

Unsurprisingly, the US plaintiffs' bar did not fail to notice. Cornerstone Research finds that during the first half of 2011, lawyers filed 25 class action lawsuits against Chinese companies, accounting for 26 per cent of all federal securities fraud class-action filings during this period.⁶ These actions alleged various securities laws violations, including violations of Section 10(b) and Rule 10b-5 of the Securities and Exchange Act and Section 11 of the Securities Act.

4 Letter, dated 27 April 2011, from Mary Schapiro, Chairman, Securities and Exchange Commission, to the Honorable Patrick T McHenry, Chairman, Subcommittee on TARP, Financial Services and Bailouts of Public and Private Programs.

5 'Activity Summary and Implications for Reverse Mergers Involving Companies from the China Region: January 1, 2007 through March 31, 2010', PCAOB, Research Note #2011-P1, March 14, 2011 (PCAOB Note 2011).

6 Cornerstone Research, Securities Class Action Filings, July 2011, p. 13

Suffering from the regulatory crackdown, negative research reports and shareholder lawsuits, stock prices in Chinese companies that listed through an RTO had fallen by more than 45 per cent as of mid-2011 and by more than 62 per cent by year-end.⁷ Although attacks targeted companies listed through an RTO, the valuation of other US-listed Chinese companies was also materially and adversely affected. By comparison, the Hang Seng China-Affiliated Corporations Index, which tracks the performance of PRC-controlled companies listed in Hong Kong, decreased by approximately only 12 per cent during 2011. For management shareholders and private equity investors, this mismatch creates a potential opportunity to privatise a US-listed company with the aim of relisting it in, for example, Hong Kong, where the trading multiples for Chinese companies tend to be higher and market research coverage is seen as being more positive and understanding of the Chinese context. Importantly, the going-private trend was not limited to entities resulting from an RTO; five of the nine significant Chinese companies that announced or closed a going-private transaction in 2011 were Cayman Islands companies that accessed the public markets through a conventional IPO. Companies that list in the United States through a conventional offering may be appealing targets for a private equity investor given that, although their market valuations may have been materially reduced by the current investor mood disfavouring Chinese companies, they may be less likely to have the same types of accounting or securities law compliance problems as have had companies that became public through an RTO.

Of the nine significant going-private transactions announced prior to the end of 2011, the acquisition of China Fire by Bain Capital is the only one that involved a third-party private equity investor acquiring a controlling stake in the target company (in the China Fire deal, the founders exchanged a portion their shares for a stake of approximately 25 per cent in the post-closing company and cashed out the remainder of their shares on the same terms as the public shareholders). In the eight other transactions, management either retained a controlling stake in their company or shared control with other investors. In three of these transactions, the founders obtained equity financing from a private equity firm, which became a minority shareholder of the company after closing: Primavera, in the case of Chemspec; PAG Asia, in the case of Funtalk; and Abax, in the case of Harbin Electric (conglomerate Fosun Industrial also provided equity financing in the Tongjitang going-private transaction).

The seven transactions that have closed so far took an average of around four and a half months to close. The Shanda and Funtalk transactions, both involving Cayman companies, closed in under three months. All nine transactions were structured as a one-step, negotiated merger (as opposed to a two-step transaction consisting of a first-step tender offer followed by a second-step squeeze-out merger, which is the other basic approach to acquiring a US public company). In a one-step merger, a company incorporated in a US state will be subject to the US proxy rules, which require the company to file a proxy statement with the SEC and, once the proxy statement is cleared, to mail the definitive proxy statement to the stockholders and set a date for its stockholders' meeting. Because all nine transactions involved management retaining

7 See, e.g., Bloomberg Chinese Reverse Mergers Index (ticker symbol: CHINARTO).

(either by themselves or with others) a controlling stake (or, in the case of China Fire, a substantial minority stake), they were all ‘going-private’ transactions as defined under Rule 13e-3 of the Securities and Exchange Act, also commonly referred to as ‘13e-3 transactions’. A 13e-3 transaction requires making additional disclosures to the public shareholders, including as to the buyer’s position on the fairness of the transaction. An important implication is that, whereas the SEC reviews only a fraction of all proxy statements, it routinely reviews 13e-3 transactions, which can lengthen the process by several months. Companies incorporated outside the United States that are listed on US stock exchanges (including the recent going-private targets that are incorporated in the Cayman Islands) are known as foreign private issuers (‘FPIs’). FPIs are not subject to the proxy rules, but they are subject to 13e-3 disclosure obligations and are required to include as an exhibit to their 13e-3 filings most of the information that is required to be disclosed in a proxy statement by a US domestic issuer. Accordingly, both a transaction involving a US domestic company and a 13e-3 transaction involving an FPI follows a comparable timetable for purposes of SEC review.

At least four going-private targets had a VIE structure: China Advanced Construction Material, CRIC, Funtalk and Shanda. China Fire, which does not have a VIE structure, is the only one of the nine going-private transactions that was subject to MOFCOM antitrust review. The other transactions escaped antitrust review either because they did not involve a change of control (as the founders had a controlling stake in the company both before and after the transaction) or the parties did not meet the sales thresholds set out in the AML. Since MOFCOM is not known ever to have approved of a VIE transaction that was subject to an antitrust approval process, practitioners generally believe that the presence of a VIE structure would be a significant impediment to a private equity investor seeking to acquire a controlling stake in a company.

PIPEs and other transactions

Although going-private activity may have been in the spotlight, 2011 also saw a number of successful PIPE deals involving Chinese companies. Temasek closed the largest private equity acquisition with its \$2.8 billion investment in China Construction Bank in August. This purchase allowed the sovereign wealth fund to rebuild its holdings in the Chinese bank for a per-share price approximately 20 per cent lower than what it had received just one month earlier, when it disposed of \$1.2 billion of stock in China Construction Bank.

In April 2011, Goldman Sachs completed its acquisition of a 12 per cent minority stake in Taikang Life Insurance, the fifth-largest life insurance company in the PRC. Goldman purchased the stake from French insurance giant AXA for \$940 million, overcoming the competition as well as Chinese regulatory burdens. Newspapers had reported that AXA’s stake in Taikang had attracted private equity giants Blackstone, KKR and Temasek, but that the sale process had stalled due to PRC regulatory hurdles: Chinese regulations prohibit non-Chinese groups from having financial interests in more than one domestic Chinese insurance company. Goldman Sachs said it would have one seat on the board of Taikang. Already hinting at a possible exit opportunity for Goldman, Dongsheng Chen, the company’s chairman, told local media in August that Taikang is slated to list in Shanghai and Hong Kong within three years.

Other notable private placements involved US-listed Chinese companies. Apparently taking advantage of the same opportunities as did management and private equity investors in going-private transactions, Morgan Stanley gave a vote of confidence to two Nasdaq-listed Chinese companies under fire by short sellers, Yongye International and China XD Plastics. Morgan Stanley purchased \$50 million in convertible preferred shares of Yongye notwithstanding fraud allegations by short-seller Absaroka Capital Management. In that transaction, the fraud allegations' effect on Yongye's value may have been what made the target so appealing for Morgan Stanley. In another similar transaction, Morgan Stanley purchased \$100 million in redeemable preferred shares of China XD Plastics, another company that became listed on the Nasdaq through a RTO.

Also noteworthy is Kohlberg Kravis Roberts' ('KKR') \$114 million investment in convertible bonds issued by Singapore-listed Chinese water treatment firm, United Envirotech, which gave KKR three board seats. The convertible bonds can be converted into equity after five years, which could give KKR 38 per cent of the firm if fully converted.

ii Deal terms

Deal terms in going-private transactions

Eight of the nine Chinese going-private transactions identified above involved all-cash consideration. The per-share acquisition price represented an average premium of 41 per cent over the trading price on the day before announcement, but an average loss of approximately 11 per cent over the trading price at the beginning of 2010, when the trading price of US-listed Chinese companies was near its peak. In the one such transaction involving non-cash consideration, the going-private of China Real Estate Information Corp ('CRIC'), E-House, which owned approximately 54 per cent of CRIC, agreed to acquire the shares of CRIC it did not already own for a combination of cash and E-House shares, representing a premium of 19 per cent over the trading price on the day before the announcement. E-House, a China-based company trading on the NYSE as a foreign private issuer, filed a registration statement on form F-4 to register its securities to be issued to CRIC shareholders.

In a 13e-3 transaction, the board of directors of the target typically appoints a special committee of independent directors to evaluate and negotiate the transaction and make a recommendation. If the target is incorporated in the United States, the transaction almost inevitably will be subject to shareholders' lawsuits for, *inter alia*, claims of breach of fiduciary duties, naming the target's directors as defendants. Because the target's independent directors often include US residents, a key driver of a transaction's terms is the concern for mitigating shareholders' litigation risk. So far, the Chinese going-private transactions involving Cayman companies have not given rise to litigation claims for breach of fiduciary duties; however, it remains possible that, as the going-private trend persists, plaintiffs' firms may start articulating creative arguments in Cayman mergers and the Cayman courts may look to the body of Delaware law as persuasive precedent for adjudicating claims of breach of fiduciary duties. As a result, whether a going-private transaction involves a US or Cayman-incorporated target, targets typically insist that certain key merger agreement terms (in addition to the deal process) be within the realm of what is 'market' for similar transactions in the United States.

An important negotiated term in many going-private transactions is the required threshold for shareholder approval. Delaware law requires that a merger be approved by shareholders owning a majority of the shares outstanding, and Cayman law requires the approval of two-thirds of the votes cast at a shareholders' meeting. Special committees often insist on a higher approval threshold, however, because under Delaware law, the burden of proving that a going-private transaction is 'entirely fair' to the unaffiliated shareholders shifts from the target directors to the complaining shareholders if the transaction is approved by a majority of the shareholders unaffiliated with the buyer group (i.e., the majority of the minority). In this type of US shareholder litigation, this burden shift is often seen as outcome determinative. All four going-private transactions involving a US-incorporated issuer had a majority-of-the-minority condition requiring a majority of the outstanding shares held by shareholders unaffiliated with the buyer group to approve the transaction. This creates a high bar for approval: in China Fire, for example, the management group held approximately 59 per cent of the shares and, as such, the approval of nearly 80 per cent of the outstanding shares was required for the closing condition to be satisfied. The transactions involving FPIs had more diverse shareholder approval thresholds: CRIC had the same majority-of-the-minority condition as the transactions involving US-incorporated issuers; Chemspec required the approval of a majority of the votes cast (as opposed to a majority of the shares outstanding) by shareholders other than the buyer group; and Funtalk, Shanda and Tongjitang did not have a majority-of-the-minority condition (Funtalk and Shanda required the approval of only two-thirds of the shares present and voting at the meeting, and Tongjitang required the approval of 75 per cent of all shares present and voting at the meeting, reflecting the higher statutory threshold under Cayman law at the time the transaction was signed). This means that, in the case of Funtalk, Shanda and Tongjitang, the buyer group unilaterally had the authority to approve the transaction without the minority shareholder, as they held shares in excess of the approval threshold. Under Cayman law, there is no well-defined benefit for the company to insist on a higher approval threshold than the statutory requirement.

Another key negotiation point is whether the target would benefit from a go-shop period, which is a period following signing of a merger agreement during which the target can actively solicit competing bids from third parties. When defending against a claim of breach of fiduciary duty in Delaware, a company and its directors may point to a go-shop period in a merger agreement as a potentially helpful fact. Each of China Advanced Construction Materials, China Fire and China Security & Surveillance, each of which involved a US-incorporated company, had a go-shop period. Harbin Electric (also a US-incorporated company) did not, but because Harbin Electric, with the assistance of its financial adviser, had conducted an extensive market check before signing the merger agreement, it arguably was less crucial that the company continue exploring other opportunities after signing. Importantly, the go-shop period was included in the merger agreement even though, in all of these cases, no third party would have been able to close a transaction with the target without the participation or consent of the management shareholders, which owned a majority stake of the target. None of the merger agreements for the Cayman targets involved a go-shop period, and most of these transactions (Tongjitang being an exception) also did not involve a pre-signing market check.

Another interesting issue in Chinese going-private transactions is how the parties address the conflict between the company founder's interest as part of the buyer group and his or her influence over the target and its management. A key consideration for the target is obtaining certainty that if, after signing a merger agreement, the founder determines (for any reason) that he or she no longer wishes to consummate the merger, he or she would not exercise influence as head of the company to block or hamper the transaction. To address this conflict, most merger agreements in going-private transactions provide that the target will not be in breach of a representation or warranty if such breach was known by those members of management who are participating in the buyer group and, likewise, the company would not be in breach of a covenant as a result of an action by such members of management. This approach provides the target with comfort that the founder, as a leader of the buyer group, would not be able to terminate the merger agreement as a result of any action or inaction that was within his or her control or any matter known to him or her prior to signing the merger agreement. Of the nine going-private transactions, the only merger agreement that did not include this concept was that of China Fire, in which case management was participating in, but not leading, the buyer group.

Deal terms in growth equity investments

Deal terms are more difficult to evaluate and synthesise in private transactions, where terms are not publicly disclosed. Generally, in the context of a growth equity investment (which, as we have seen, remains the dominant type of deal both by number of deals and by aggregate amount invested), private equity investors often continue to expect aggressively pro-buyer terms. This expectation applies whether a transaction involves an onshore Sino-foreign joint venture or an investment offshore alongside a Chinese partner. In a subscription agreement for a growth equity deal, an investor typically benefits from extensive representations and warranties against which the company makes only limited disclosures; in some cases, an investor has knowledge that some representations may not be accurate, but still insists on a representation to facilitate a potential indemnification claim later. It is not uncommon for an investor to also enjoy an indemnity provision with a cap on the amount of losses subject to indemnification as high as the purchase price (or no cap at all), no deductible or threshold and an unlimited survival period. Shareholders' agreements often contain similarly pro-investor terms, such as extensive veto rights (even in the case of a relatively small minority stake) and various types of affirmative covenants binding the company and its Chinese shareholders. If an investment is structured offshore (through, for example, a Cayman company that owns a Chinese subsidiary), a private equity investor may enjoy 'double-dip' economics pursuant to which, in the event of a liquidation or sale of the company, the investor is entitled to, first, a liquidation preference before any of the Chinese shareholders receive any proceeds, and second, such investor's *pro rata* share of the remaining proceeds based on the number of shares it owns on an as-converted basis. Because there is no well-defined 'market' when it comes to transaction terms in Chinese growth equity deals (unlike in going-private transactions), however, issuers also have opportunities to request, and sometimes obtain, terms that are very favourable to them. In Chinese growth equity investments, the parties' respective leverage and degree of sophistication are more likely to dictate the terms that will apply to a transaction than any market practice or standard.

For a private equity investor with sufficient commercial leverage, the key challenge often lies not in convincing the investee company or its Chinese shareholders to agree to adequate contractual terms, but rather in getting comfort that an enforceable remedy will be available in the event that the Chinese counterparty reneges on its contractual obligations. One potential antidote to the difficult enforcement environment onshore is to seek a means of enforcement offshore. An investor can get comfort if it obtains, for example, a personal guarantee of the Chinese founder backed by assets outside China, governed by New York or Hong Kong law and providing for arbitration in Hong Kong as a dispute resolution venue. Such a guarantee, however, is rarely available (because the Chinese founder may not have assets outside of China) and, even when potentially available, is often unacceptable to the founder. A more realistic alternative is for a private equity investor to seek the right to appoint a trusted nominee in a chief financial officer or similar position (who could monitor an investee company's financial dealings and compliance with its covenants to its shareholders). An investor may also seek co-signatory rights over the target company's bank account, in which case, an independent third party (the bank) will ensure that funds are not released other than for purposes agreed by the investor.

iii Debt finance

Third-party debt financing continues to be available for acquisitions of Chinese companies by private equity investors. One key challenge, however, is that a PRC target does not generally have the ability to give credit support (by way of guarantee or security over its assets) to a lender of offshore acquisition finance debt.

Many of the going-private transactions of US-listed Chinese companies involved debt financing, but they showed little consistency in the terms of the financings, reflecting varying commercial and structural challenges. The acquisition debt was typically borrowed by an offshore acquisition vehicle with the borrower giving security over its assets (including shares in its offshore subsidiaries) to secure repayment of the debt. The lenders spanned a wide range of financial institutions, from international investment banks (such as Standard Chartered in the case of Chemspec) to policy banks and offshore arms of other PRC banks (such as China Development Bank in Harbin Electric and CITIC in Tongjitang). Each of the financings consisted of US or Hong Kong-dollar financing initially advanced, in most cases, on a bilateral basis by lenders located or incorporated in Hong Kong. The Shanda transaction was one exception, involving a Singapore branch of JPMorgan providing a term loan.

The China Fire financing stands out among the others for at least two reasons: it was the only financing made available by a consortium of international banks (Bank of America Merrill Lynch, Citibank and HSBC) and the only financing involving a combination of offshore acquisition debt and onshore working capital facilities. Since the working capital facilities were made available onshore, these were able to benefit from credit support, in the form of guarantees and security, from the PRC companies. Although the onshore lenders were not able to share the benefit of that credit support with their affiliates lending the offshore acquisition debt, the security still provides defensive value against onshore trade creditors.

In addition, because in the China Fire transaction the target was incorporated in the United States (Florida), as opposed to, for example, the Cayman Islands, it was subject to

US tax laws that limit the security that can be given to secure the acquisition debt without adverse US tax consequences. Typically, lenders expect to receive a pledge of 100 per cent of the shares of any operating subsidiary of the borrower so that they can sell the entire borrower group to a purchaser upon an enforcement of the security. However, Section 956 of the US Internal Revenue Code of 1986, as amended ('the IRC') provides that if the credit or assets of a non-US subsidiary have been used, directly or indirectly, to support the debt of the US borrower, the earnings and profits of that non-US subsidiary are subject to taxation in the United States, unless the security given is essentially limited to a 65 per cent pledge of the shares of any first-tier non-US subsidiary. Section 956 of the IRC thus has the effect of limiting the security that can be given to secure the acquisition debt to a pledge of 65 per cent of the shares of any first-tier non-US subsidiary of a US borrower, even if that subsidiary is the main operating entity. This limitation also can have a significant impact where the offshore vehicles consist only of holding companies, with the result that a pledge of 65 per cent of the shares is only available in one of those companies (and not over the borrower's shares).

There may also be significant tax consequences in attempting to remove a US company (whether it is the target or otherwise) from corporate structures in the context of going-private acquisitions of US-listed PRC businesses, whether for the purposes of increasing the percentage of stock that can be pledged to acquisition financiers or for longer-term tax planning. Removal may trigger significant US tax liability and, where any historical shareholder retains an interest in the PRC business after removal of the US company, it may also trigger the US anti-inversion rules, which may cause the non-US entity holding the PRC business to be subject to US federal income tax as if it were a US company and subject to US tax on its worldwide income. This can be a deterrent for some private equity investors to acquire certain US-listed companies.

iv Exits

The banking sector has been one of the most active when it comes to sizeable exits. According to AVCJ Research, of the top 10 exits in Asia in 2011, five were open-market sales of stakes in Chinese banks. The year's largest exit, involving a series of related transactions, belongs to Carlyle. Completed in three tranches – the first two only two days apart in late December 2010 and early January 2011 for \$2.66 billion and the third in July for another \$990 million – Carlyle's divestment from Hong Kong and Shanghai-listed China Pacific Insurance enabled the private equity firm to achieve a return of six times its initial investment of \$740 million (made in two tranches in 2005 and 2007). According to AVCJ Research, this divestment was the second-largest open market exit ever recorded by a private equity firm in China. Temasek earned the year's top exit in one single transaction in its \$2.4 billion sale of a portion of its Bank of China shares in the open market.

Going-private transactions also served as exit opportunities for some private equity investors, including some going-private transactions that did not involve a US-listed target. In one landmark transaction, Nestlé entered into a partnership agreement with the controlling family of Singapore-listed Chinese confectionary company Hsu Fu Chi. Pursuant to this agreement, Nestlé acquired a 60 per cent stake in Hsu Fu Chi. The transaction allowed Baring Private Equity Asia to exit from its 16.5 per cent stake in

the company of Hsu Fu Chi and collect approximately \$464 million from Nestlé. *The Wall Street Journal* observed that Hsu Fu Chi traded for a discount to similarly situated companies in Hong Kong, seen as the natural home of Chinese food companies, showing a rationale for the transaction quite similar to the rationale behind the going-private transactions involving Chinese companies listed in the United States. In another such transaction, the acquisition of Global Education by Pearson was a private equity exit for India-based SAIF Partners.

The year has also seen several high-value trade sales, with clean energy technologies a particularly active sector. In June 2011, Affinity Equity Partners and Unitas Capital exited from Beijing Leader & Harvest Electric Technologies, a manufacturer of medium voltage drives, through a \$650 million sale to French energy management company Schneider Electric. Through this trade sale, Affinity and Unitas realised a return of three times their initial investment made in late 2009. Beijing Leader's financial adviser had conducted a dual-track sale and IPO process, and Schneider reportedly was chosen over other bidders that included global energy players ABB, Emerson Electric and Siemens.

Other noteworthy trade sales agreed in 2011 include the sale by Bain Capital of two Chinese portfolio companies to French chemical company Arkema. Bain agreed to sell Zhangjiagang-based Hipro Polymers, a producer of bio-renewable polyamides, and Hengshui-based Casda Biomaterials, a world leader in sebacic acid, for an aggregate purchase price of \$365 million. Both companies were predominantly owned by a joint venture between private Chinese chemical company Feixiang Chemicals and Bain Capital. The deal closed in February 2012 after Chinese governmental approvals were obtained.

IV REGULATORY DEVELOPMENTS

i Challenges for VIE structures

A number of developments in 2011 raise potential challenges for private equity investors investing in a VIE structure. In its 25 August 2011 implementing rules to its national security review scheme, MOFCOM introduced a broad anti-avoidance provision to the effect that a non-Chinese investor may not evade review by any means, including by the use of nominee structures, loans or control by agreement. These explicit references suggest that MOFCOM specifically intended to target transactions involving VIE structures, to the extent that they raise national security concerns.

Revealing that authorities in Hong Kong are also concerned about certain uses of a VIE structure, in November 2011 the HKSE published a revised listing decision with more restrictive requirements for VIE structures. Although the HKSE reaffirmed its 2005 decision that applicants for listing in Hong Kong that use a VIE structure are eligible for consideration, the HKSE's decision requires any applicant using a VIE structure to:

- a* provide reasons for the use of the VIE structure;
- b* terminate any VIE-related contractual arrangements as soon as PRC law allows the business to be operated without them; and
- c* include as part of the VIE contracts:

- a power of attorney from the shareholders of the VIE granting the applicant's directors the power to exercise all rights of the VIE's shareholders;
- a provision that the liquidator can seize the VIE's assets in a liquidation (for the benefit of the applicant's shareholders or creditors); and
- an arbitration clause allowing the award of remedies over the shares or land assets of the VIE, injunctive relief or winding-up of the VIE.

The decision also indicates that any application would be referred to the Listing Committee if a listing applicant uses a VIE structure in an industry in which foreign investment is not restricted under PRC law. The decision does not indicate why the HKSE is concerned about companies that use a VIE structure when foreign investment is not restricted, but one possible cause of concern would be a company using a VIE structure to circumvent the prohibition on 'round-trip' investments contained in the M&A Rules – that is, a company owned by a Chinese individual gaining control of a PRC target owned by the same individual or his or her affiliates through VIE arrangements in order to avoid seeking MOFCOM's approval, which would constitute a potential violation of the M&A Rules.

The HKSE listing decision may have been driven in part by an internal report from the China Securities Regulatory Commission ('the CSRC') leaked to the public in September 2011. The report questioned the legality of the VIE structure and recommended that CSRC insist that future overseas listings using a VIE structure obtain MOFCOM and CSRC approval. Although this report was written by a CSRC official to his superior and did not purport to represent the official position of the CSRC, it nonetheless raised concern.

ii The 2012 Foreign Investment Catalogue

MOFCOM and NDRC jointly issued the latest edition of the Foreign Investment Catalogue in December 2011, replacing the previous version released in 2007. On balance, this was perceived as a positive development for non-Chinese investors, including private equity investors, as the new catalogue increased the number of encouraged sectors and reduced the numbers of restricted and prohibited sectors. Among the new sectors that now fall within the encouraged classification are certain sectors relating to mining, specialised equipment manufacturing, electricity supply, wholesale and retail and commercial services. Other sectors that were previously restricted are now permitted, including some relating to manufacturing, health care, wholesale and retail, and the operation of financial leasing companies. Only a few industries have been added to the category of prohibited sectors in which a non-Chinese investor is not allowed to conduct business, including the construction and operation of villas (as regulators seek to control housing bubbles) and the operation of domestic postal services.

iii New antitrust measures

Another important recent development is MOFCOM's publication at the very beginning of 2012 of new Interim Measures for Investigating and Disposing of Suspected Concentration of Business Operators Failing to Be Notified in Accordance with Law. Sending a signal that MOFCOM intends to strenuously enforce the Anti-Monopoly

Law, these measures announce for the first time that MOFCOM may penalise businesses that fail to make an antitrust filing when required to do so. If MOFCOM determines that a company has failed to make such a filing, if a transaction has not been completed, it will order the parties to suspend the completion of the transaction and require the non-complying company to submit the filing within 30 days and if a transaction has been completed, MOFCOM may impose on the parties a fine of up to 500,000 renminbi and order them to rescind such transaction. Although the amount of the fine is negligible, a rescission of a transaction that has already been consummated could be costly and damaging. In addition, the measures provide that any person has the right to report a suspect transaction and the informant's name will be kept confidential, further strengthening a company's incentive to comply with the filing requirement.

V OUTLOOK

A review of 2011 activity demonstrates that the volume, scale and sophistication of private equity transactions relating to China continue to grow, consistent with the general development of the Chinese economy in the context of long-term regional economic growth and development in Asia. Initial indications are that 2012 will be another strong year for Chinese merger and acquisition and private equity transactions. While unique political, legal and regulatory hurdles remain to cause challenges for dealmakers seeking to replicate in China-related transactions some features integral to private equity transactions undertaken in more developed economies, local and foreign private equity firms that have been proactive in generating opportunities, creative in structuring solutions to various novel risks and patient and flexible in execution have fomented an increasingly vibrant and nuanced deal market.

Appendix 1

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