

Panda Bonds: Measures and Guidelines for foreign investors

In the first half of 2018 the issuance of the so-called *Panda Bonds* amounted to RMB 51.49 billion, more than 70% of the total issuance in 2017 and, by the end of 2018, a total of 57 overseas institutions (mainly non-financial enterprises) have been registered or approved for bond issuance in the Chinese Interbank Bond Market ("CIBM") with an approved issued amount of RMB 453.3 billion.

As a preliminary remark, the term *Panda Bond* refers to bond denominated in renminbi, which a non-Chinese organization issues in China Mainland (Hong Kong, Macau and Taiwan excluded) with the aim to raise capital from investors located in the People's Republic of China ("PRC").

The vigorous opening up of the Chinese bond market and the increasing number of overseas institutions allowed to issue Panda Bond has led Chinese government to promulgate new more sophisticated rules which officially abolish the old PRC legal framework of 2010 and have greater alignment with international practices.

On **September 8, 2018**, the People's Bank of China ("PBOC") and the Ministry of Finance ("MOF") jointly issued the *Interim Measures of the Administration of Offshore Institutions' Bond Offering in National Interbank Bond Market* ("Measures").

In addition, the National Association of Financial Market Institutional Investors ("NAFMII") issued the *Guidelines for Debt Financing Instrument Business of Overseas Non-financial Enterprises* (for Trial Implementation) ("Guidelines"), immediately effective from the date of issuance, **January 17, 2019**.

The Guidelines, to be read together with the Measures, set out major requirements and clarifications for overseas investors regarding the following three main aspects as: information disclosure, use of funds raised and requirements for intermediary agencies.

The Measures apply to the following overseas issuers: (i) Foreign governmental organizations; (ii) International development institutions (i.e. any multilateral, bilateral or regional international development financial institution that makes development loans and investments); (iii) financial institutions (i.e. banks) and (iv) non-financial enterprise (i.e. foreign companies).

Particularly, Articles 6, 7, 8 of the Measures establish the eligibility criteria of each category of issuers, as listed here below.

- Foreign governmental organizations and international development institutions are required to have experience in issuing bonds and good solvency.
- An eligible overseas financial institution shall satisfy the following conditions for issuing bonds in the CIBM:
 1. Its paid-up capital shall not be less than RMB10 billion or an equivalent amount in a foreign currency;
 2. It shall have in place sound corporate governance and a robust risk management system;
 3. It shall be in a stable financial condition, have a well-established creditworthiness and have earned profits for the past three consecutive years;
 4. It shall have experience in bond issuance and remain solvent to repay its debts;

5. It is subject to effective regulation of the financial regulators in its home jurisdiction, and its key risk regulatory indicators comply with the requirement of its home financial regulators.

- No special express requirements are specified for foreign non-financial enterprises with legal personalities.

The procedure of issuance of Panda Bonds, as well as the authorities in charge for the prior approval and/or application process and qualifications for different types of issuers, as showed here below, may vary depending on the nature of the bonds' issuer.

a. Non-financial institutions

Governing authority and registration procedures		Remarks
1.	Apply to NAFMII for registration	Applicable for both public issuance and private placement
2.	If the proceeds will be remitted offshore or if there is the need for a waiver beyond the authority of NAFMII, PBOC's consent is required	
Qualifications		Remarks
1.	<p>Issuer's qualification</p> <ol style="list-style-type: none"> 1. The issuer possesses legal person status; 2. The issuer is a non-financial corporation; 3. The issuer is a member of NAFMII; 4. The historical development of the issuer complies with laws and regulations; 5. The issuer is validly existing. 	Applicable for both public issuance and private placement
2.	<p>Material requirement</p> <p>If the issuer intends to issue a mi-term note or short-term commercial paper through public offering, the amount of the issuer's outstanding bonds shall not exceed 40% of the issuer's net assets.</p>	Only applicable for public issuance
3.	<p>Restrictions on use of proceeds</p> <p>If the proceeds are to be used onshore, it shall be used in compliance with the PRC laws, regulations and policies.</p>	Applicable for both public issuance and private placement

b. Foreign governmental agencies and international development institutions

Governing authority and registration procedures		Remarks
1.	Apply to NAFMII for registration	Applicable for both public issuance and private placement
2.	Consent from PBOC before registration	
Qualifications		Remarks
1.	The governmental agency is a sovereign entity	Applicable for both public issuance and private placement
2.	International development institution is a multilateral, bilateral or regional international development financial institutions which lends development loans and makes investments and it is duly incorporated and validly existing pursuant to relevant treaty	

c. Financial institutions

Governing authority and registration procedures		Remarks
1.	Submit to PBOC for approval	Applicable for both public issuance and private placement
2.	Before each issuance, the issuer shall file with PBOC the updated offering circular, credit rating report (if any), underwriting agreement and syndication agreement, legal opinion and other final documents	
Qualifications		Remarks
1.	Actual paid-in capital not less than RMB 10 billion or an equivalent amount in a foreign currency	Applicable for both public issuance and private placement
2.	Sound corporate governance and comprehensive risk management system	
3.	Stable financial condition, good credit standing, and profitability for the latest three consecutive years	
4.	Experience in bond issuance and sound debt repayment ability	
5.	Being effectively regulated by the financial regulatory authority of the country or region where the issuer is incorporated, and the issuer's key risk regulatory indicators being in compliance with the requirements of the said authority	

Once Panda Bonds have been sold, the issuer is required to carry out registration of the bonds with a registration and custody organization that must be recognized by the PBOC.

As for the accounting principles and auditing, it is worth to be noted that prior to the promulgation of the Measures, the only accounting principles accredited by the MOF, as being equivalent to the Chinese Accounting Standards for Business Enterprises (“CASBE”), were the International Financial Reporting Standards adopted by EU listed companies for their consolidated financial reports, and the Honk Kong Accounting Standards for Business Enterprises. Nevertheless, such equivalent account principles are used by a very limited number of Panda Bond issuers, which generally prefer to put their issuance plans on hold. Now, the new Measures allow issuers using non-equivalent accounting principles to apply for public issuance if they provide supplementary information; if not possible, they may choose private placement as an alternative.

With regard to the disclosure of information, Panda Bond issuers shall comply with specific requirements and meet the obligations as set forth by the Measures, as specified by the Guidelines as well, mainly regarding the disclosure of information prior to the bonds' issuance and during the life of the bonds.

It should further be noted that the Measures, do not explicitly mention the applicable law or dispute resolution mechanisms for Panda Bonds. However, based on the current practice, the competent authorities still require the transaction documents of Panda Bonds issuance to be governed by PRC law and for the resolution of any dispute, including the litigation and arbitration, to be resolved in China.

In addition to the above, overseas institutions should consider that, being the issuer's place of registration and the place of listing in different jurisdictions, in order to properly manage the legal activities on Panda Bond issues, there would generally be two law firms involved (i.e., the issuer's PRC legal counsel and their local legal counsel). Consequently, a division of work, namely of tasks and responsibilities, to be divided amongst the legal counsels involved in the process of Panda Bond issuance should be assessed in advance.

As closing remarks to be considered, although the Measures clarify and standardize issuance procedure for Panda Bonds, they do not provide a comprehensive description of all the issues that need to be addressed when making an application to issue Panda Bonds and Chinese authorities shall continue to have discretionary powers when assessing the merits of an application. Furthermore, Chinese government continues to apply strict capital controls and PBOC and the State Administration of Foreign Exchange (“SAFE”) will continue to exercise discretion in approving cross-border remittance.

Please note that the above is simply an overview of the subject matter and it is not, nor is it intended to be, a legal opinion or legal advice. Should you have any questions concerning the new law's requirements set out above or should you wish to receive information on our annual package, please do not hesitate to contact us.

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