

A long-term, sustainable and effective way to invest into China

An overall map of the updated QFI Mechanism

In brief

On 21 June 2021, the first batch of four real estate investment trust funds in the field of infrastructure (REITs) was successfully listed at the Shenzhen Stock Exchange (SZSE). Over the past year, these products have operated smoothly, the supporting system has been continuously improved, investors have actively participated, and the market function has been gradually brought into play — realizing the phased targets of "a stable and good start." In June 2022, SZSE said that it will promote the high-quality development of the infrastructure REITs market from five aspects, one of which is to "continue to support QFII and RQFII to invest in domestic REITs products."¹ It is a clear signal that among various channels for foreign investors to participate into the Chinese domestic market, the QFI mechanism is still the one being paid special attention to by the market participants and with unique advantages for investors.

Updated QFI rules attracting investors from all over the world

On 25 September 2020, the China Securities Regulatory Commission (CSRC), together with other relevant authorities, promulgated the **Measures for the Administration of the Investment in Domestic Securities and Futures by Qualified Foreign Institutional Investors and Renminbi Qualified Foreign Institutional Investors** (《合格境外机构投资者和人民币合格境外机构投资者境内证券期货投资管理办法》) and its implementation rules ("**QFI Rules**"), which took effect on 1 November 2020. Upon the official launch of the QFI Rules, the **Administrative Measures for Securities Investment Made in China by Qualified Foreign Institutional Investors** issued by the CSRC, the People's Bank of China (PBOC) and the State Administration of Foreign Exchange (SAFE) on 24 August 2006 ("**QFII Rule**") and the **Measures for the Pilot Program of Securities Investment Made in China by RMB Qualified Foreign Institutional Investors** issued by the CSRC, PBOC and SAFE on 1 March 2013 ("**RQFII Rule**") were repealed.

The QFI Rules have made it more convenient for QFII/RQFII to invest in mainland China by merging the QFII and RQFII qualifications and system rules into one, lowering the entry threshold, relaxing access conditions, simplifying application documents, and shortening the time limit for examination and approval. Also, the QFI Rules have steadily and systematically expanded the scope of investment.

According to the CSRC website,² from 1 November 2020 to 30 June 2022, up to 197 foreign investors from various jurisdictions, including the United States, Singapore, Australia and France, successfully obtained the QFI approvals from the CSRC.

Although the epidemic is still not completely over and various uncertainties still exist, based on the market news and frequent inquiries from our offshore clients, we understand that foreign investors are still full of enthusiasm for China's domestic market. Therefore, understanding the relevant QFI application requirements and processes, as well as the functions of the relevant participants, should be valuable for foreign institutions' business decision making.

¹ <https://baijiahao.baidu.com/s?id=1736360373943612428&wfr=spider&for=pc>, 2022.08.01,

² <http://www.csrc.gov.cn/csrc/c101900/c1029652/content.shtml>, 2022.07.31.



QFI Rules with enlarged investment scope provides more investment opportunities

QFI Rules permit QFII and RQFII to invest into almost all the products at the secondary market, including securities listed on National Equities Exchange and Quotations, private investment funds, financial futures, commodity futures and options. Moreover, QFII and RQFII are allowed to participate in bond repurchases, margin trading and short selling on stock exchanges, securities lending for refinancing purposes, REITs, and even financial derivative transactions. We categorized the detailed products by the authorities in charge for your easy reference, which will provide a clear and overall picture of the investment scope.

Regulators	CRSC	PBOC	SAFE
Products	<ul style="list-style-type: none"> Stocks, depository receipts, bonds, bond repos, and asset backed securities traded or transferred on the Shanghai Stock Exchange (SSE) or SZSE Shares quoted on the National Equities Exchange and Quotations (NEEQ, i.e., China's OTC board) Public securities investment funds Financial futures listed and traded on CFFEX-subject to CSCR's approval Commodity futures listed and traded on futures exchange-subject to CSCR's approval Options traded on futures exchanges approved by the State Council or the CSRC Private investment funds, the investment scope of which shall comply with the permitted scope of QFII/RQFII Participate in the subscription of the initial public offering, bonds issuance, asset-backed securities issuance, new share issuance, and allotted shares on SSE, SZSE and NEEQ Participate in margin financing and stock lending, and refinancing securities lending on SSE and SZSE Other instruments approved by CSRC 	<ul style="list-style-type: none"> Products traded in the inter-bank bond market (CIBM) Other products under the PBOC's jurisdiction (such as bond, currency and interest rate derivatives). 	<ul style="list-style-type: none"> Foreign exchange derivatives approved by the SAFE for hedging purposes

Simplified QFI application criteria makes application more promising

Based on the below criteria clearly listed in the QFI Rules, it can be seen that the CSRC does not set any solid threshold of QFIs, i.e., as long as the foreign investors are legally established, being healthily operated, as well as with competent staff and sound internal structures, they may consider applying for QFI approvals.

Financial and credit status	<ul style="list-style-type: none"> Stability and credibility Experience in securities and futures investment
Employees	<ul style="list-style-type: none"> The main personnel in charge shall meet the requirements of the relevant regulations/



Governance structure and internal control system, as well as business operations	<ul style="list-style-type: none"> • Sound and effective • Inspectors appointed to supervise the legal and compliance of the domestic investment activities of the applicant • Normative business conduct, which has not been severely punished by regulatory authorities in the past three years or since the establishment
Others	<ul style="list-style-type: none"> • There is no circumstance that has material impact on the operation of the domestic capital market.

Simplified application documents and efficient online submission system greatly shorten the application period

As part of Chinese government's digitalization reform, to apply for QFI qualification, an application form must be entered online through the website of the CSRC and the following application documents must be submitted to the CSRC through a domestic custodian ("**Custodian**"):

1. A written application signed by the legal representative or the authorized representative
2. Business license or registration certificate and supporting materials of business operation qualification
3. Statement on whether the applicant has received any serious punishment imposed by the regulatory agency in the last three years or since its formation
4. Power of attorney issued to the Custodian
5. Other documents required by the CSRC according to the principle of prudential regulation

For purposes of the preceding paragraph, "legal representative" means a natural person who may, on behalf of the applicant, handle matters relating to the administration of securities and futures investment made in China by qualified foreign investors upon authorization by the board of directors or as prescribed in the bylaws of the company where the applicant works, or in compliance with the laws of the country or region where the applicant is located (e.g., chairman of the board of directors or the chief executive officer).

Where the written application is signed by the authorized representative of the applicant's legal representative, the power of attorney issued by such legal representative to their authorized representative shall be presented.

A Chinese translation must be provided if application materials are prepared in a foreign language (the Chinese version shall prevail).

An international organization, a sovereign fund or a pension fund that applies as a qualified foreign investor is not required to provide the documents set forth in (2) and (3) above with the consent of the CSRC.

In addition, the application documents must be submitted by the applicant's Custodian, which may also be considered as a convenience measure for offshore applicants. CSRC shall, within 10 working days from the date of accepting the application documents, review and verify such materials, and make a decision on whether or not to approve the application.

Conclusion

There are now many channels by which foreign investors may participate in the Chinese domestic market. For example, the interconnection mechanisms such as stock connect and bond connect provide diversified and convenient investment channels for foreign investors to invest in the domestic capital market, which have an obvious crowding out effect on QFI. However, we believe that the QFI mechanism, especially with the substantial expansion of the investment scope, is expected to fully demonstrate its own comparative advantages in the competition with the interconnection mechanisms, and it will still be an attractive and efficient investment channel for foreign investors in the future.



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