



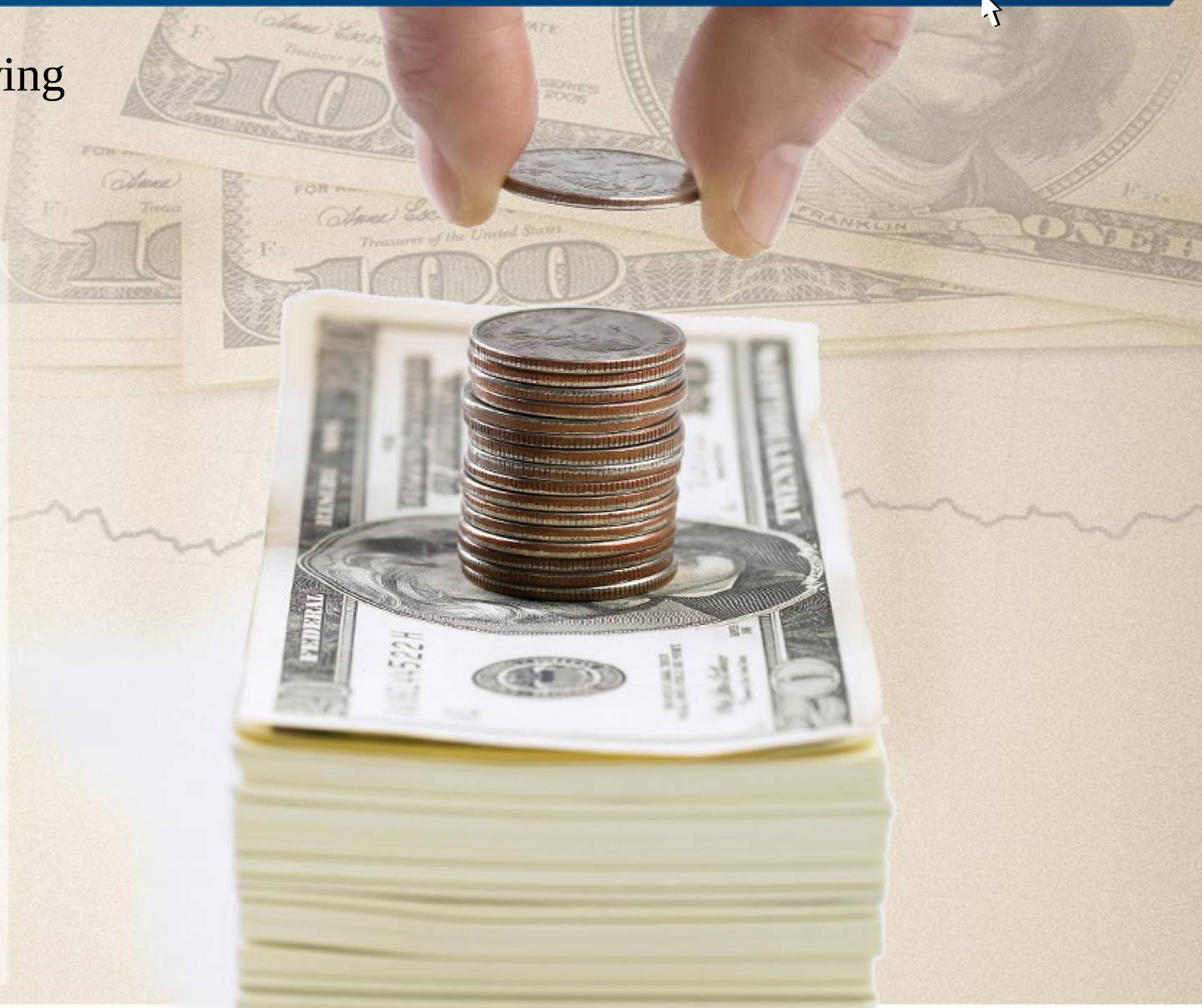
About 20% Companies Applying ChiNext Listing Fail to Pass Review

>>P2

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- P10 Fortune VC Signs Investment Agreement with Westingarea
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- P11 Lunar Capital Management Exits from Beihai BPG

D.cn Receives US\$12M from
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About 20% Companies Applying ChiNext Listing Fail to Pass Review

Written by Roc Zhao, Zero2IPO Research Center

It has been almost one year since the launch of ChiNext which is a landmark of China capital market. During this period, the ChiNext grew and expanded rapidly, the investment market has also gradually stepped into maturity and rationality from the crazy pursuing at the time of board opening. Till September 29, 2010, the number of companies listed in Shenzhen ChiNext reached 123 with a total market capitalization of RMB10.9B. While among these 123 companies, 71 companies are supported by VC/PE institutions, successful IPOs also brought enviable returns to these speculative institutions.

In its early days of inception, facing the huge wealth-creation effect brought by the ChiNext which has characteristics of "three highs", i.e. high P/E ratio, high offer issue price and high oversubscription rate, it was difficult for small and medium enterprises to feel indifferent, almost all of them exerted all measures they could do and expected to be listed on the board and became one of the lucky stars of the ChiNext. However, the reality is very cruel. Till now, among 184 listing applications reviewed by issuance and review committee

of the ChiNext, 36 companies did not pass the review, accounting for 19.6% of total applications. (See Table 1)

Among these companies that did not pass the review, 15 companies are supported by VC/PEs, accounting for 41.7% of the companies that did not pass the review, mainly in machinery manufacturing, IT and clean-tech industries. Because a listed company in the ChiNext needs to have characteristics of "two highs and six news", namely high growth, high technology content as well as new economy, new service, new agriculture, new material, new energy and new business mode. Therefore, whether the company can reach the above requirements becomes the important criteria for the review. The root reason for a number of companies' failure in passing the review is that their net profit and

sustainable growth are not identified and qualified. For instance, Hunan Kenon Technology Co., Ltd. is a company engaged in the producing industrial explosive engineering explosive materials, because its net profit sized at RMB20M in 2009 can not ensure its future growth, it was rejected by the Issuance and Review Committee of CSRC. TJ Innova Engineering & Technology, which is engaged in the design of complete automobile vehicles and parts, was not approved, because its profit in 2008 was lower than that in 2007, which leads to unqualified financial index. Among other reasons that may cause a company can not pass the review of ChiNext, all situations such as material changes in the controlling person of the applying party, problems of registration and incorporation of the applicant, lacking of independence of the applying company, intentionally hiding information disclosure can cause the applying company's failure of listing application.

The following table is the name list of all companies supported by VC/PEs but did not pass the review of ChiNext till now. (See Table 2 and Table 3) ■

Table 1 List of Applicants for Listings on ChiNext

Review	No. of Applicants	% of Total
Approved	145	78.8%
Fail to be approved	36	19.6%
Cancel review	2	1.1%
Uncertain	1	0.5%
Total	184	100.0%

Source: Zero2IPO Research Center

Table 2 List of VC / PE - backed Enterprises without Passing ChiNext Listing Review

Enterprise Name	Industry	Application Date	VC/PE Institution
Hunan Kenon Technology Co., Ltd.	Chemical Raw Materials &	2010-6-28	Beijing Zhaoxing Investment Co., Ltd.
GMG International Tendering Co., Ltd.	Others	2010-6-25	Guangdong Finance Investment
Suzhou Goldengreen Technologies Ltd.	Electronic & Opto-electronics Equipment	2010-6-11	Jiangsu Suzhou New & Hi-tech Venture Jiangsu Changshengfu Venture Capital Suzhou Industrial Park Chenrong
Shandong Tongda Island New Material Co., Ltd.	Clean-tech	2010-5-14	Sureland Capital Group Qingdao Haikerui Investment Consulting
Shining 3D Tech Co., Ltd.	Machinery Manufacturing	2010-4-23	Merill Lynch Ventures Hangzhou Tianhui
Shanghai Canature Environmental Products Co., Ltd.	Machinery Manufacturing	2010-4-16	Lute Investment
Hangzhou Zhengfang Software Co.,Ltd	IT	2010-3-31	Guangfa Xinde Investment Management
Grandhope Biotech Co., Ltd.	Bio/Healthcare	2010-3-31	Venture Star Shanghai
Shanghai Magus Technology Co., Ltd.	IT	2009-12-29	Beijing Zhongtonheda Venture Capital Shzhen Yuanyu Investment Co., Ltd. Shenzhen Hangyuanfu Venture Capital
Shenzhen Joaboa Technology Co., Ltd.	Clean-tech	2009-12-25	Shenzhen Cowin Capital Co., Ltd.
Wuhan Intime Power Technology Co., Ltd.	Clean-tech	2009-12-1	Shenzhen Capital Group Co., Ltd. Wuhan Torch Technology Investment
Anhui Suanaking Co., Ltd.	Machinery Manufacturing	2009-11-20	Kunwu Jiuding Capital Co., Ltd. Good Capital Group Jiangsu Tianshi Venture Capital Co., Ltd. Jiangsu Xingke Venture Capital Co., Ltd.
Tianjin Sainteagle Welding Co., Ltd.	Others	2009-11-17	Keruiyin Investment Tianjin Technology Venture Capital Ltd.
Shanghai QXQC Chemical Technology	Chemical Raw Materials &	2009-11-10	Shanghai Industrial Investment
TJ Innova Engineering & Technology Co., Ltd	Automobiles	2009-9-22	China Science & Merchants Venture Sino-JP Fund Co.,Ltd Shenzhen Fortune Venture Co., Ltd. Shanghai Bofeng Venture Capital Co., Shenzhen CDF-Capital Company Preipo Capital Partners

Source: Zero2IPO Research Center

Table 3 List of Enterprises without Passing ChiNext Listing Review

Company Name	Review	Application Date	Planned Issuance Scale (10,000)
SVG Optronics Co., Ltd.	Fail to be approved	2010-9-29	1550
Sinomine Resource Exploration Co., Ltd.	Fail to be approved	2010-9-29	2200
Shenzhen Easttop Supply Chain Management Ltd.	Fail to be approved	2010-9-13	3340
Zhuhai Topsun Electronic Technology Co., Ltd.	Fail to be approved	2010-9-13	1670
Hunan Kenon Technology Co., Ltd.	Fail to be approved	2010-6-28	1200
Y&J Industries Co., Ltd.	Fail to be approved	2010-6-25	2200
GMG International Tendering Co., Ltd.	Fail to be approved	2010-6-25	2000
JiangSu YuXing Film Technology Co., Ltd.	Fail to be approved	2010-6-23	1000
Suzhou Goldengreen Technologies Ltd.	Fail to be approved	2010-6-11	2000
Guizhou Gaofeng Petroleum Machinery Co., Ltd.	Fail to be approved	2010-6-4	4200
DNT Shanghai Science and Technology Co., Ltd.	Fail to be approved	2010-5-17	1700
Shenzhen Maslong Information Technology Co., Ltd.	Fail to be approved	2010-5-17	1500
Shandong Tongda Island New Material Co., Ltd.	Fail to be approved	2010-5-14	1110
Shanghai Kingstar Winning Software Co., Ltd.	Fail to be approved	2010-4-30	1350
Shining 3D Tech Co., Ltd.	Fail to be approved	2010-4-23	1000
Beijing Jurassic Software Co., Ltd.	Fail to be approved	2010-4-20	800
Shanghai Canature Environmental Products Co., Ltd.	Fail to be approved	2010-4-16	2750
Hangzhou Zhengfang Software Co., Ltd.	Fail to be approved	2010-3-31	1050
Grandhope Biotech Co., Ltd.	Fail to be approved	2010-3-31	1400
Shenzhen Kingsunsoft Technology Co., Ltd.	Fail to be approved	2010-3-30	1100
Beijing Ehoo information Technology Co., Ltd.	Fail to be approved	2010-1-26	2400
Beijing Bohui Innovation Technology Co., Ltd.	Fail to be approved	2010-1-26	2560
Shanghai Magus Technology Co., Ltd.	Fail to be approved	2009-12-29	1340
Shenzhen Joaboa Technology Co., Ltd.	Fail to be approved	2009-12-25	2100
Shenzhen Advanced Video Info-Tech Co., Ltd.	Fail to be approved	2009-12-25	2400
Shenzhen Hirisun Technology Incorporated	Fail to be approved	2009-12-22	1300
Sailun Co., Ltd.	Fail to be approved	2009-12-1	9800
Wuhan Intime Power Technology Co., Ltd.	Fail to be approved	2009-12-1	2800
Beijing Dawn Aerospace Bio-tech Co., Ltd.	Fail to be approved	2009-11-24	2000
Anhui Suanaking Co., Ltd.	Fail to be approved	2009-11-20	1875
Tianjin Sainteagle Welding Co., Ltd.	Fail to be approved	2009-11-17	2400
Wuhu Andhra Logistics Co., Ltd.	Fail to be approved	2009-11-13	4550
Jiangxi Hengda Hi-Tech Co., Ltd.	Fail to be approved	2009-11-13	1900
Shanghai QXQC Chemical Technology	Fail to be approved	2009-11-10	2000
TJ Innova Engineering & Technology Co., Ltd.	Fail to be approved	2009-9-22	4540
Nanjing Paneng Technology Development Co., Ltd.	Fail to be approved	2009-9-21	1450

Source: Zero2IPO Research Center

The 10th China Venture Capital & Private Equity Annual Forum

Time: December 8th-9th, 2010

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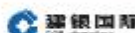
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Qualified Foreign Limited Partner - The Latest Development on Foreign Investment in RMB-denominated Private Equity Fund

Written by Steven Wei Su

In March 2010, Shanghai Municipal Government proposed a trial program ("Trial Program"), known as qualified foreign limited partner program ("QFLP"), to the central government for its approval. The Trial Program will relax current restrictions on conversion of foreign-currency capital to enable qualified foreign investors to directly invest in a RMB-denominated private equity fund ("RMB Fund"). In early October 2010, it was reported that the Trial Program has been approved "in principle" by the State Administration of Foreign Exchange ("SAFE") and other departments of the State Council. As a local policy, the Trial Program will only apply to RMB Funds established in Shanghai. However, other cities keen to foster private equity fund investment such as Beijing, Tianjin and Chongqing are also reportedly lobbying for a similar program.

The Trial Program is envisaged, on the one hand, to serve as a test of possible effect in granting foreign investors limited access to China's domestic private equity market following China adopting the system of Qualified Foreign Institutional Investors

("QFII") to allow limited foreign access to its domestic security market. On the other hand, it is intended to send an encouragement message to foreign private equity investors by tackling with a few practical problems that foreign investors will face in investing in RMB Fund.

This article focuses on current foreign exchange issues of private equity fund and the changes the Trial Program will bring in this regard.

1. Background

Through onshore structures, foreign investors are able to raise RMB for the purpose of private equity investment and manage the operation of such fund. In Beijing and Shanghai, for example, the local regulations allow foreign investors to set up onshore fund management entities to manage RMB Fund. From 1 March 2010, the effective date of the *Administrative Regulation on the Registration of Foreign Invested Partnerships*, foreign investors can organize the onshore structures in the form of foreign-invested lim

ited partnership ("FILP") besides limited liability company.

Theoretically, foreign investors may either play the role of a general partner ("GP") or a limited partner ("LP"). In a typical structure of RMB Fund, foreign investors often act as a GP and offer fund management services. As such, it needs to contribute to the fund a percentage of its total capital. However, most foreign GPs or LPs (except those use their RMB capital to invest in a RMB Fund) will face various problems while attempting to invest directly in a RMB Fund with foreign currency capital. For example, the fund will have a problem to settle the capital into RMB. Moreover, foreign investment in a RMB Fund may convert the fund into a foreign invested fund, which will make it subject to restrictions from foreign investment industrial policies. To play down the unwanted influence, foreign investors take different approaches. In Shanghai, for example, one of the popular structures is the so-called "indirect model". As the name suggests, foreign investors establish consulting or

management foreign-invested enterprises ("FIE") and use the onshore entities to invest in a RMB Fund. Some simply use the RMB settled from the registered capital of the FIE on equity investment. This practical approach may conceal the nature of the fund as foreign fund, and thus enable the investment to go around the control of China's industrial policies for foreign investment and to expedite the deals. However, it was challenged by a SAFE regulation in 2008, known as the *Circular on Relevant Operating Issues Concerning the Improvement of Administration of Payment and Settlement of Foreign Capital by Foreign-invested Enterprises* ("Circular 142").

2. Current Foreign Exchange Restrictions on Equity Investment by FIEs

Circular 142 provides that the RMB settled from registered capital of FIE shall only be used for the approved business purposes of the FIE, and unless otherwise provided in a law. It also provides that a non-investment FIEs shall not conduct equity investment within China with their registered capital settled in RMB. Circular 142 requires FIEs to provide proof on the use of the RMB when apply for foreign exchange settlement and the designated foreign exchange banks

to examine the reality and legality of such usage. Under the *Administrative Regulations of Foreign Exchange*, using the RMB settled from foreign exchange for any purpose other than the approved can subject the FIEs to the penalties including a fine, confiscation of gains directly derived from the use etc.. This provision clearly prohibits FIEs with no investment business scope from conducting private equity investment with its registered capital.

Circular 142 permits FIEs approved by the Ministry of Commerce and primarily engage in investment to conduct equity investment, but requires such FIEs seek and obtain the approval from SAFE or its local counterparts when settling the investment capital in RMB. Under the PRC laws, foreign-invested venture capital enterprise ("FIVCE") is one of the investment business entities permitted to carry out private equity investment. FIVCE is regulated by a special regulation, known as the *Administrative Provisions on Foreign Invested Venture Capital Investment Enterprises* (2003). Circular 142 permits FIVCEs to use its registered capital for equity investment purpose, but requires that each investment project be approved by SAFE. In practice, FIVCE cannot directly invest in another company from its settlement account, but must obtain prior approval on the investment project from

SAFE before transferring the investment capital. SAFE's approval will focus on issues such as the investment project, the investor's qualification, approvals from other governmental agencies, the foreign exchange compliance history etc.. Only when the SAFE approval is granted, the capital can be transferred and settled in RMB by the recipient.

It should be noted that foreign-invested private equity investment management entities are not regarded as investment entities. Therefore, a management entity cannot directly engage in private equity investment with its registered capital according to Circular 142. Prima facies, a FILP with approved business scope of investment appears not falling into the restriction of Circular 142. It is, however, not explicitly provided by law if such a FILP can settle its capital into RMB without SAFE approval for the purpose of equity investment. It is likely that SAFE applies the FIVCE model to administering FILPs' private equity investment activities until any other specific rules are issued.

In summary, for the onshore structures that are not approved as investment entity, Circular 142 clearly has increased the complexity in arranging settlement of foreign exchange and the risk of noncompliance.

Although it may not dry the business through this channel, there is no doubt many investors are compelled to consider setting up onshore investment entity or use a direct foreign investment model. For the onshore structures with government-approved investment capability such as FIVCEs or investment FILP, China's current foreign exchange administration system places them in an inferior position when competing with those pure domestic funds which have no issue of foreign exchange conversion in China investment.

In China, the power of regulating foreign exchange is rested with the central government. Therefore, the local regulations or policies can do little on the foreign exchange issues concerning private equity fund. For example, the *Tentative Measures for Establishing Foreign-invested Equity Investment Management Enterprises in Pudong New District of Shanghai* issued by the government of the Pudong District of Shanghai in June 2009 do not deal with the issue of foreign exchange settlement. In the Carlyle-Fosun deal, it was reported that the contribution of Carlyle's investment from its Asia Growth Fund in the RMB Fund was

3. Changes may be Brought by the Trial Program

If the Trial Program is implemented, what changes will it bring to the foreign investors from foreign exchange angle? Generally speaking, it will permit the qualified foreign investors to directly invest in an onshore RMB Fund. The Trial Program broadly follows the QFII model with respect to the foreign exchange administration and will adopt a quota system. Foreign investors that meet certain qualifications can apply for a foreign exchange conversion quota. In particular, with the quota, the RMB Fund will be able to convert the capital contributed by a foreign partner in foreign currency into RMB for investment purpose, and to purchase the foreign exchange back while repatriating the capital. According to the latest report, under the Trial Program, RMB Fund will be permitted to convert foreign currency from the qualified foreign investors (GPs and LPs) into RMB at the amount of no more than US \$100 mil or 50% of the aggregate size of the fund, whilst the conversion of foreign exchange from each qualified foreign GP is limited to 5% of the aggregate size of the

accumulative US \$5 bil during a prescribed period of time. Moreover, the RMB Fund must be a fund established in Shanghai pursuant to the local rules in Shanghai.

The investors qualified under the QFLP program will be able to directly invest into RMB Funds in foreign currency. The investments from the qualified foreign investors will no longer need SAFE approval for foreign exchange conversion provided that the investments do not exceed the quota approved by SAFE. This program will afford qualified foreign investors a more convenient channel to directly participate in RMB Fund, and foreign-invested RMB Funds with significant convenience in investment.

The Trial Program may be a modest step forward. However, if it is implemented successfully and other key cities can follow suit, the whole picture of regulatory system could be changed gradually in favor of the foreign investment in RMB Fund. ■

About the author:

Steven Wei Su is a partner at Guo Lian PRC Lawyers based in Beijing. His practice focuses on private equity/venture capital funds formation and operation, merger and acquisition transactions, general corporate and commercial dispute settlement. Before joining Guo Lian PRC Lawyers,

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