

Law Society of Hong Kong Convention 2002

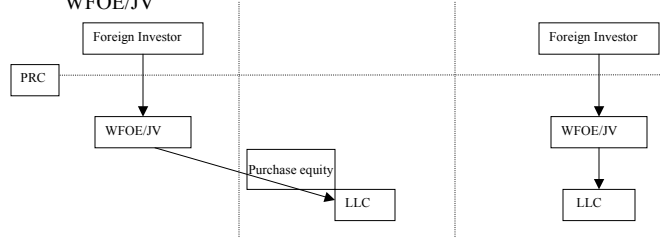
Do's and Don'ts of M & A in PRC - Acquisition of an Interest in Domestic Companies

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1. How to acquire LLCs in PRC – Entry Strategy

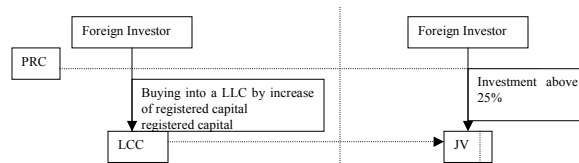
LLC

- acquiring equity in a LLC by a new / existing WFOE/JV



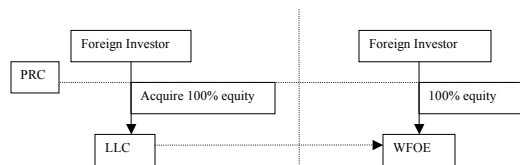
LLC

- Buying into a LLC by increase of registered capital



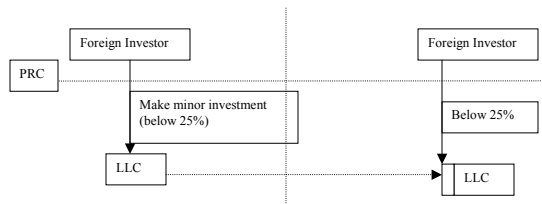
LLC

- acquire 100% equity interest in a LLC



LLC

- Making a minority investment in a LLC



Joint Stock Company

Acquisition of shares in an unlisted FIJSC

- Buying into a JV and transform the JV into a FIJSC:

Criteria for establishment of a FIJSC

- Above 25% of the registered capital of the JSC;
- Three consecutive years' profits making history
- Subject to MOFTEC's approval

- Subscription of new shares in a JSC

- Below 25%, treated as a domestic JSC;
- Above 25%, treated as a foreign invested JSC.

Listed JSC

Acquisition of shares in a listed JSC

- onshore vehicles (excluding FIHC and FIVC) to subscribe publicly traded marketable shares;
- onshore vehicle (excluding FIHC and FIVC) to purchase “legal person”shareholders’ shares by agreement; and
- Indirect acquisition – acquiring equity interest in the “legal person”shareholders including “promoter shareholders”of a listed JSC.

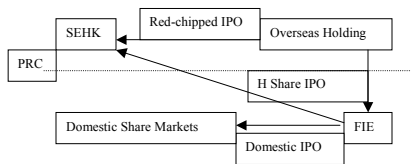
2. How to exit a PRC M & A? – Exit Strategy

Buy-out of equity interest in a JV

- direct buy-out of equity interest in a JV;
- buy-out of equity interest at the overseas investment vehicle level;
- transform the JV into a WFOE and then buy-out 100% equity interest in the WFOE.

Initial Public Offering

- domestic IPO
- H share form IPO
- Red-chipped form IPO



Liquidation

Liquidation of a FIE

- Ordinary Liquidation Procedures
- Special Liquidation

Redemption

Formation of an offshore JV to hold 100% equity interest in a WFOE. Redemption is to be realized at the offshore JV level.

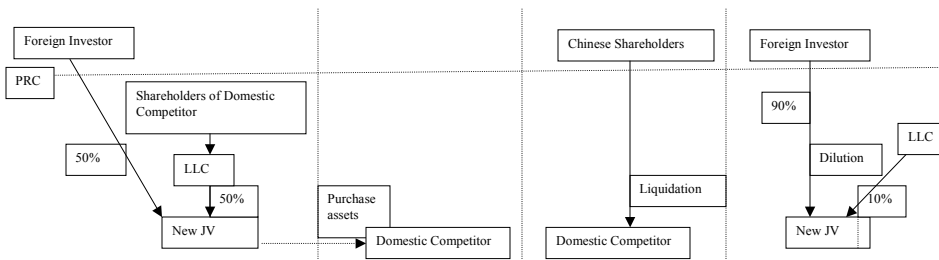
3. Cases Analysis

1: Acquisition of a domestic competitor (“Domestic Competitor”) in the form of a LLC in Shenzhen

A foreign investor intended to enter Shenzhen’s local IT service market. However, it faced fierce competition from a local LLC. Then, it used the following strategies to acquire the Domestic Competitor:

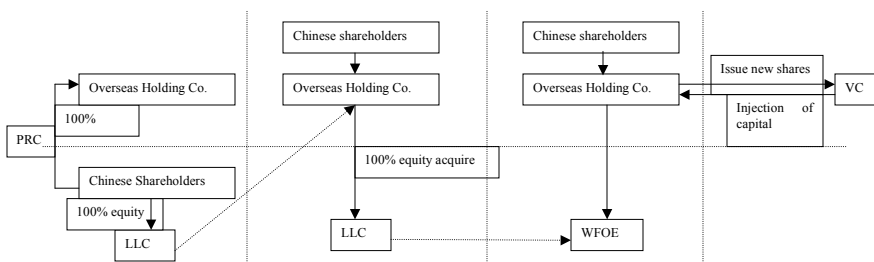
- (i) Establish a new JV;
- (ii) Acquires key assets from the Domestic Competitor including equipment, machinery, business contracts, account receivable, employees, land and properties, and particularly enter into non-competition agreement with the directors and key management of the Domestic Competitor;
- (iii) Deferred payment so as to push the shareholders of the Domestic Competitor to liquidate the Domestic Competitor; and
- (iv) Dilution

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Case 2: Acquisition of 100% Equity Interest in a LLC in Shenzhen by a VC

- (i) Formation of an overseas holding company by the original individual shareholders of LLC;
- (ii) Overseas holding company acquires 100% equity shares in the LLC and transforms the LLC into a WFOE;
- (iii) VC subscribes preferred shares of the overseas holding company by injecting capital into the overseas holding company; and
- (iv) Overseas holding company settles the purchase price for acquisition of the LLC with the original individual shareholders of LLC.



4. Factors to be considered for acquisition of an interest in Domestic Companies

- Deal Structuring;
- Due diligence;
- Governmental approval and supervision;
 - (i) authorization;
 - (ii) foreign investment guideline and market access;
 - (iii) overseas investment and foreign exchange control;
 - (iv) state-owned assets appraisal and approval;
 - (v) CSRC's special requirement on IPO and;
 - (vi) anti-trust and anti-unfair competition.
- Intellectual property rights;
- Tax; and
- Non-compete, confidentiality and anti-unfair competition.