



NAFMII publishes Panda Bond rules for non-financial issuers

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Background

China's National Association of Financial Market Institutional Investors ("**NAFMII**") recently published a much-anticipated set of Panda Bond implementing rules, the *Debt Financing Instrument Business of Overseas Non-Financial Enterprises Guidelines (for Trial Implementation)* dated January 17, 2019 ("**Guidelines**"). Panda Bonds ("**Panda Bonds**") are Renminbi-denominated bonds issued by non-Chinese issuers ("**Issuers**"), but sold in the People's Republic of China (which for these purposes excludes the Hong Kong and Macau Special Administrative Regions and Taiwan). The first Panda Bonds were issued by the International Finance Corporation and the Asian Development Bank in 2005.

The Guidelines were issued under the Panda Bond framework established by the *Administration of Bond Issuance by Overseas Institutions in the China Inter-bank Bond Market Interim Measures* (Announcement No. 16 [2018]) issued jointly by the People's Bank of China ("**PBOC**") and China's Ministry of Finance on September 8, 2018 ("**Measures**"). For more details on the Measures, please refer to our client note [In black and white letter law: China issues new Panda bond rules](#).

The Measures apply generally to all types of Panda Bond issuers, but contain detailed rules solely relating to overseas financial institutions. The Guidelines fill in the gaps by providing detailed rules for the issuance of Panda Bonds by overseas non-financial enterprises Issuers.

Content

We have outlined below the main content of the Guidelines.

(1) Registration and filing

Issuers must register the issuance of their Panda Bonds with NAFMII by submitting the following registration documents to NAFMII:

- recommendation letter of the lead underwriter;
- prospectus or private placement agreement;
- Issuer's audited financial reports for the last 3 accounting years (or last 2 accounting years in the case of private placements) and latest interim accounting statements (if any);
- Issuer's credit rating reports and follow-up rating arrangements (if any) (not required for private placements);
- legal opinions issued by a Chinese law firm and by a law firm in the jurisdiction of the Issuer respectively;
- consent letter of the Issuer's foreign accountant (if applicable);
- underwriting agreement; and
- such other documents as may be required by NAFMII.

Registration is completed on the date NAFMII accepts the registration documents and remains valid for a period of 2 years, upon which NAFMII shall issue a Registration Acceptance Notice to the Issuer.

When issuing to the public, Issuers are entitled to issue Panda Bonds within the first 12 months of registration at their own discretion, but must file with NAFMII in advance for issuances that take place more than 12 months after the completion of the registration.

The Guidelines specify that NAFMII does not make any substantive judgment on the investment value and related risks when accepting the Issuer's registration application. Investors must independently assess the investment risks and make their own investment decisions. Furthermore, completion of registration does not exempt Issuers from the legal obligation to disclose information in a truthful, accurate, complete and timely manner.

- registration report;

(2) Other requirements on the issuance

The Guidelines provide the following additional requirements:

- **Noteholders' meetings:** the Panda Bond registration and issuance documents must set out the arrangements applicable to meetings of Panda Bond noteholders.
- **Accounting standards:** the Issuer's financial reports must comply with the accounting standards and audit requirements imposed by the relevant Chinese regulatory authorities.
- **Financial statements of the parent company:** Issuers that are a subsidiary and whose financial information is consolidated into their parent company financial statements must submit and disclose their own consolidated financial statements, and in principal must also disclose financial statements of their parent company or disclose any information on the financial condition of their parent company which would have a significant impact on investors' investment decision. Such information must be disclosed in a prominent place in the registration and issuance documentation.
- **Lead underwriter requirements:** lead underwriters must be financial institutions that are qualified to underwrite debt financing instrument business in China. At least one of the lead underwriters must have a subsidiary or branch in the place where the Issuer is incorporated or mainly conducts its business. Alternatively, there must be other arrangements in place to ensure that the lead underwriter has the ability to conduct due diligence and other related work in connection with its role as the lead underwriter.

(3) Use of proceeds

Issuers may use the Panda Bond proceeds in China (by loaning them to their Chinese subsidiaries) or convert them into foreign currency and repatriate them abroad.

(4) Cash flows and bank account structure

The account opening, cross-border remittance and information reporting in connection with Panda Bond proceeds must comply with the requirements imposed by China's State Administration of Foreign Exchange and by PBOC, including the *Circular on Matters concerning the Cross-Border RMB Conversion of RMB Bonds Issued within China by Overseas Institutions* (No. 258 [2016]) issued by the General Office of the PBOC on December 23, 2016 ("**PBOC Circular**").

Pursuant to the PBOC Circular, the proceeds from the Panda Bond issuance must be deposited in:

- (i) a RMB bank settlement account for overseas institutions ("**Non-Resident Account**" or "**NRA**") opened by the Issuer with a Chinese bank ("**Account Bank**"); or
- (ii) a custody account opened by the lead underwriter with a Chinese bank ("**Custodian Bank**").

The Account Bank and the Custodian Bank are responsible for handling the transfer of the Panda Bond proceeds from the NRA into China (which would be regulated as a cross-border remittance) or overseas (which would be unrestricted, as a NRA is essentially treated as offshore for regulatory purposes).

As noted above, Issuers can use Panda Bond proceeds to provide shareholder loans to their Chinese subsidiaries, but what is particularly noteworthy is that those shareholder loans do not count against the foreign debt quota of the China subsidiaries in question, pursuant to the *Circular on Matters relating to the Full Bore Macprudential Administration of Cross-*

Border Financings (No. 9 [2017]) issued by the PBOC on January 11, 2017 (for more information, please refer to our client note: [New PBOC Circular potentially raises the overseas borrowing ceiling for borrowers in China: but is it a game changer?](#)).

(5) Disclosure

Issuers are required to comply with the following ongoing disclosure requirements:

- **Ongoing disclosures:** disclose, on an ongoing basis during the term of the Panda Bonds, relevant financial information, including financial statements, major matters that may affect the solvency of the Issuer, corrections to errors in the disclosed information, and modifications to the Issuer's accounting policies or accounting estimates.
- **Supplemental information:** disclose supplemental information describing matters arising between the acceptance of the registration and the issuance of the Panda Bonds which may have a significant impact on investment value and investors' investment decisions.
- **Use of proceeds:** disclose any change to the stated use of Panda Bond proceeds at least 5 working days before the modification takes effect.

The disclosed documents must be published through websites recognized by the NAFMII (www.nafmii.org.cn; www.chinamoney.com.cn/中国货币网; www.chinabond.com.cn/中国债券信息网; www.cfae.cn/北京金融资产交易所网), or be disclosed to investors participating in private placements through the integrated business and information service platform of the NAFMII.

(6) Governing law

The Measures do not contain any particular governing law requirement. The absence of any such requirement in the Measures appeared to suggest that the Measures intended to eliminate

the Chinese governing law requirement provided under the previous legislative framework (abolished and replaced by the Measures). However, against the expectations of many, the Guidelines instead expressly provide that the Panda Bonds and the related transaction documents must be governed by Chinese law.

Conclusion

Based on the Measures, the new Guidelines provide a more detailed framework for issuance by overseas non-financial issuers. The Guidelines clarify the specific registration requirements, and the disclosures required to be made before the issuance and during the term of the Panda Bonds. In addition, they confirm the right of Issuers to use the proceeds abroad and the methods by which RMB funds can be transferred. However they somewhat counterintuitively re-impose Chinese law as the governing law for the Panda Bonds themselves and the related transaction documents, restoring a requirement provided by the legislative framework in force prior to the Measures but that did not appear in the Measures themselves. This seems to be a step backwards compared with the expectations created by the Measures on this point. Additionally, as the Issuer is, by definition, not a Chinese entity, such requirement – although consistent with the previous legislative framework – provides an exception to the basic principle in Chinese law that where there is at least one foreign (non-Chinese) party, a choice of foreign governing law is permitted. It is a debatable point whether the Guidelines which are essentially a lower-level "normative document" (规范性文件) – and considering that the Measures are silent on the governing law – can overrule the provision in Article 3 of the *PRC Law on the Application of Laws governing Civil Relations involving Foreign Elements* which states that "*The parties may, in accordance with legal provisions, make an*

express choice of the law governing civil relations involving foreign elements" which is a much higher-level document with the status of a law (法律). To that extent at least, the silence of the Measures on the governing law applicable to Panda Bonds seemed to be more in line with the strict letter of the law.

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