

Clean Tech Investment in China

According to Chinese media reports, the Chinese government is working on an extensive strategy paper to define the national aims and measures for fighting the climate change. Apparently the paper sets out very concrete implementation measures. As the *UN Climate Change Conference* to be held in Copenhagen in December approaches, international pressure on the world's largest carbon dioxide emitter is growing. Also, the environmental impact of more than 20 years of virtually uncontrolled economic growth is no longer deniable, even for the Chinese government. For these reasons clean tech investments in China have moved into the focus of both the Chinese government and foreign technology companies and venture capital investors. Many regulations are in place already and have to be observed by foreign companies.

Naturally, the generation of energy will be central to the measures aiming to curb carbon dioxide emissions; in China, coal-fired power plants still produce about 80% of the country's energy. The Chinese government has been promoting renewable energies for some time now: According to the 2005 *Renewable Energies Act*, by 2020 at least 15% of China's energy shall be supplied by renewable sources. This has to be taken with a grain of salt, however. For instance, considering the adverse consequences experienced in other areas, the initial euphoria about biomass energy has yielded to a growing reservation: The *Catalogue for the Guidance of Foreign Investment Industries* as amended in early 2008 classifies the production of biofuel as "restricted", and biofuel projects are subject to more detailed examination by the Chinese regulatory authorities than before.

All projects involving wind and solar energy, however, have made it into the "subsidised" category again, which means that foreign investors in any such projects enjoy certain privileges in the approval procedure and during project implementation. A multitude of additional detailed requirements must be observed when planning an investment, however. For example, the *Renewable Energies Act* requires a 70% localisation rate for the construction of wind energy plants, which makes investments into component manufacturing very interesting but imposes additional specifications on plant engineering as such.

Despite all the investments in renewable energies, however, China wants and will have to continue using its enormous coal resources to generate energy for a while yet. Thus, new power plant technologies are highly interesting, as are the latest technologies for underground and undersea storage of large quantities of carbon dioxide to prevent its emission into the atmosphere ("carbon storage"). Chinese investment laws do not mention the latter possibility of reducing carbon dioxide emissions, which is not being applied on a commercial scale yet. As the carbon dioxide is intended to be stored in exhausted oil and gas reservoirs, the projects might possibly fall within the scope of the development of oil and gas recovery; in consequence, under the latest *Guidance Catalogue*, foreign companies could normally only get involved in the form of joint ventures.

Experts agree, however, that the greatest progress in consumption figures will be achieved through increasing energy efficiency over the medium term. Given the partly ancient technologies that are used in China in both the commercial and the private sector, the potentials are easily recognisable, while their optimum utilisation calls for intelligent solutions employing modern technologies, which often have to be acquired from foreign companies. The legal basis is supplied by the revised *Energy Conservation Act*, which took effect on 1 April 2008 and provides many measures for improving energy efficiency. For example, there will be a growing number of legal standards for consumer goods. Noncompliance with these standards will entail manufacturing and marketing bans. The Act is expected to have an impact on the construction industry as well: Although construction still remains a highly price-sensitive sector, the

increasingly challenging standards will force property developers to address aspects of energy efficiency. Local administrations are authorised to enact standards that are stricter than the national regulations.

As in many technology sectors, investors also are hesitant to transfer, and thus risk to turn over, technologies and know-how to China. This calls for deal structures which properly safeguard the interest in a practical protection of one's intellectual property. In some areas, however, details in the investment regulations put limits to such endeavours. For instance, only joint ventures are permitted to manufacture machinery for exploiting renewable energies – in joint ventures, it is generally more difficult to control one's own know-how than in wholly owned subsidiaries.

A local clean tech industry with increasingly innovative products is developing in China as well. However, there is a need for experienced, financially strong cooperation partners to help the ideas become ready for marketing and commercially successful. US and European venture capital investors therefore increasingly invest in China. Investor interest is growing in emissions trading in connection with the Clean Development Mechanism (CDM) market, which plays a prominent part in China. Shanghai, while trying to establish itself as a centre for venture capital investors, enacted local regulations early this year which offer attractive financial incentives to financial investors. The regulatory framework for corporate and tax aspects, however, remains a challenge for those seeking to structure and organise their venture capital and private equity investments.

China was hit hard by the ongoing global recession as well. Will China's next economic upturn be a clean tech boom? The anticipated strategy paper could be a further step on this way, provided it not only serves to justify the practices of the world's largest greenhouse gas emitter but offers specific measures reaching beyond the present regulations, which will only be useful if they are actually implemented by the country.

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