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New Education Rule in China

Coming into force on
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The recent Regulation coming into force this September has introduced significant limitations on investment structures, governance and curricula affecting foreign schools operating in China. Close attention must be paid to the differentiation made in the scope of restrictions for pre-K (kindergarten), K-9 (compulsory school), K-12 (high school) and higher education. Further, different provisions will apply depending on whether the school operates for profit or non-profit.

Investment Structures & Control

The Regulation has limited the scope of acceptable investment structures in private schools providing compulsory education, which may discourage foreign investors. Foreign direct investment in schools providing compulsory education has always been prohibited, but in the past VIE structures have been used successfully to circumvent that restriction. These have now been expressly outlawed. Most investment therefore needs to come from PRC sources. It needs to be noted that no foreign ownership is permitted for K1-9 and non-profit kindergarten, but K12 schools and for-profit kindergarten can be supported by foreign investors. Non-profit private schools that offer pre-school education, need to be transformed into “for-profit private schools”, however, this does not apply to K12. The New Education Rule does not distinguish between for-profit and non-profit K12.

Our view: A Propco/Opco structure may offer a solution though lease payments.

VIE

Currently, some private Chinese education institutions bypass the foreign investment access restrictions through a VIE structure. This is a variable interest equity structure whereby proxies and voting rights are given to foreign parties that provide funding putting them effectively in the position of quasi-shareholders. These structures will no longer be permitted going forward in compulsory education and non-profit kindergartens and it remains to be seen what will happen to existing funding arrangements. However, VIE structure can still be applied to education other than compulsory education and non-profit kindergartens.

Our view: Investors are well-advised to review restructuring options.

Franchising

The Regulation has no impact on franchising, as it is not understood as a form of control. Therefore, franchise fees or service fees are not affected. If a franchise agreement is adopted, the relationship between the Chinese school and the foreign school is that of licensor and licensee. The references in the regulations to agreement control refer to the VIE structures where control is given to foreign investors by agreement putting them in a position where they can exercise the voting rights of shareholders.

Naming Convention

At present, the main applicable rules for the naming of private schools are the “State Administration and Ministry of Education Regulations concerning the Registration and Administration of For-profit Private Schools (2017 No.156)”, which restrict the Choice of permitted names. All school names must:

- Comply with company registration management and education-related laws and regulations; this includes the requirement that every name must consist of two or more Chinese characters. As such, each school must have a Chinese name. This could be a transliteration or translation of the foreign name.
- Naturally, the corporate name of the school is the property of the Chinese entity.
- However, in our view, schools may use a registered trademark in addition to their Chinese name. A trademark may contain foreign characters.

Furthermore, certain names are expressly prohibited:

- Schools must not use misleading names.
- Must not use the names of existing registered schools. This means there cannot be a chain of schools under the same school name; however, we would argue that the same trademark or logo can still be used by several schools operating under the same system.
- Must not include “China”, “Zhonghua”, “National”, “International”, “World”, and “Global” in the title.
- Companies that are not schools must not use the words “university”, “college”, “kindergarten”, “high school”, “specialty”, and “further training”.

The final chosen name requires formal approval. This needs to be checked at national and local level as more than 20 provinces and cities in China have issued implementation rules, all restricting the naming of private international schools. The official Chinese school name must be owned by the local legal entity.

Our View: To solve naming challenges it could be provided that the Chinese school name must be discontinued after termination of the franchise agreement.

Curriculum

The new regulation prohibits the use of overseas teaching materials in private schools that provide compulsory education (K9). The Chinese curriculum must be taught. All schools should adhere to the leadership of the Communist Party of China and enhance core socialist values. Note that K-12, A-Level and International Baccalaureate (IB) programmes are still permitted, as they do not form part of the compulsory education. It is not prohibited to teach the curriculum in English at any stage.

Additional subjects/courses

Article 29 of the Implementing Regulations of the PRC Law on the Promotion of Private Education (Revised in 2021) does not prohibit the offering of additional subjects by schools outside the official curriculum:

(1) K12, Higher education and secondary vocational and technical education schools can independently set up courses and select teaching materials in accordance with the school’s mission and training objectives.

(2) Private schools for compulsory education (K9) can offer voluntary additional special courses provided they do not conflict with national curriculum standards. Self-established courses should be notified to the competent education administrative department for the record. It is our recommendation that such courses be named “voluntarily formation programs” to distinguish them from the regular teaching day. Because official approved textbooks must be used for the national curriculum, teaching materials for the additional voluntary formation programs should not be in the form of textbooks. Private schools that implement compulsory education must not use foreign textbooks (so additional materials should not be textbooks).

On July 24, 2021, the General Office of the CPC Central Committee and the General Office of the State Council officially issued the *Opinions on Further Reducing Students’ Homework and Off-campus Training Burden in Compulsory Education*:

- i. This requests that local authorities no longer approve new *off-campus tuition* for students in compulsory education; This affects the National Compulsory Education Curriculum in the subjects

of morality and rule of law, Chinese, history, geography, mathematics, foreign languages (English, Japanese, Russian), physics, chemistry and biology (“core subjects”).

- ii. existing off campus curriculum training institutions will be uniformly registered as non-profit institutions; they can no longer be funded through a stock market listing. This puts an end to capital market financing of fee paying private cramming schools.
- iii. No off-campus training in core subjects is permitted during national statutory holidays, rest days and summer and winter holidays; advertising for these services will also be restricted.

On July 30, 2021, the website of the Ministry of Education issued the *Notice on Further Defining the Scope of Off-campus Training Subjects and Non-disciplines in Compulsory Education Stage*, and notified the following about the scope of off-campus disciplinary and non-disciplinary subjects in compulsory education stage:

- i. according to the provisions of the National Compulsory Education Curriculum, the following subjects are restricted core subjects: morality and rule of law, Chinese, history, geography, mathematics, foreign languages (English, Japanese, Russian), physics, chemistry and biology.
- ii. Off-campus training in sports (or sports and health), art (or music, art) as well as comprehensive practical activities (including information technology education and technical education) are non-core and remain permitted within the restraints above.

Our view: Guidance is to further restrict private cramming schools, which had been mushrooming in China, and does not directly affect the teaching of additional learning materials on campus during involuntary formation programs.

Governance

The decision-making bodies of private schools implementing compulsory education should be 100% Chinese and must have representatives appointed by the examination and approval authorities. The entire governing body must be Chinese and no foreign governors are allowed.

Our view: However, the representative of the foreign school can have the position of observer or advisor. In our opinion, you should also reserve the right to require the school to change its name so that it is no longer affiliated with your school in the event that further regulation makes it impossible to maintain uniform standards of quality education and ethos. You may wish to consider a termination fee or ongoing royalty to protect your investment.

Pre-school, ordinary high school and higher education institutions can be run through Chinese-foreign cooperation, but it must be led by the Chinese side (the principal or chief administrative person in charge should have Chinese nationality, and the Chinese members of the council, the board of directors or the joint management committee should not be less than ½ of the total).

Enrolment

The regulation has prohibited private schools that implement compulsory education from organizing entrance examinations. Limitations were also put on cross-regional enrollment. Much will depend on the local education department. In our view, opportunities will be found in the larger secondary cities. The new rules stipulate that private schools should admit students openly, fairly and impartially. Private schools that implement compulsory education must not organize, or disguisedly organize, entrance examinations related to subject knowledge, and must not admit students in advance. It is understood that if the school is not a private school that delivers compulsory education, its enrollment will not be restricted.

Our view: It may still be possible to enroll students through interviews. For instance, adding English parts to the interview. Schools should expect regional differences in the application of these requirements.

Summary table:

	Pre-K	K-9	K-12	Post-K
Foreign Control	Yes if for profit	No	Yes	Yes
VIE	Yes if for profit	No	Yes	Yes
Franchise	Yes			
Foreign Curriculum	No	No	Yes	Yes
Entry Exams	n/a	No	Yes	Yes
Foreign Governance	50/50	100% Chinese	50/50	50/50

Relevant laws, policies and opinions:

1. Implementing Regulations for the Law of the People's Republic of China on the Promotion of Private Education (Revised in 2021)
2. Special Administrative Measures (Negative List) for the Access of Foreign Investment (2020)
3. Special Administrative Measures (Negative List) for the Access of Foreign Investment in Pilot Free Trade Zones (2020)
4. Non-state Education Promotion Law of the People's Republic of China (2018 Amendment)
5. Regulations of the People's Republic of China on Chinese-foreign Cooperative Education (2019 Revision)
6. Foreign Investment Law of the People's Republic of China
7. Regulation for Implementing the Foreign Investment Law of the People's Republic of China
8. Opinions on further strengthening and standardizing the management of education fees
9. Opinions on Further Reducing Students' Homework and Off-campus Training Burden in Compulsory Education
10. Notice on Further Defining the Scope of Off-campus Training Subjects and Non-disciplines in Compulsory Education Stage



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