The Wholly Foreign Hospital
New Reforms Allow Foreign-Owned Hospitals in More Cities

One issue which has had a major impact on hospital projects in China has been the extent of foreign ownership allowed for each project. In the earliest stages of extensive foreign investment in the Chinese healthcare industry, the formula that was adopted was a maximum of 70% foreign investment with a minimum of 30% for a Chinese partner. Although there were exceptions granted, such as that given in 1998 to the pioneering Beijing United Family Hospital, which was created with 90% foreign investment and 10% Chinese investment, the bulk of the projects which were granted approval followed this guideline.

Attempts at Reform
As the Chinese government began to recognize the value of foreign investment in the neglected hospital sector, it began to loosen this policy. Over the last six years there have been a number of policy statements by the Ministry of Commerce and the Ministry of Health relaxing their regulations and allowing greater latitude in the granting of hospital licenses with different equity distribution arrangements. The government’s intentions were clear, and their motivations sound. In theory, greater foreign investment in healthcare, should benefit the overall system as international standards and practices are applied by the foreign investors to their private hospital projects.

In 2010, as a part of a massive proposed reform for medical institutions, China’s National Development and Reform Commission (NDRC), the Ministry of Health and other ministries jointly issued the “Opinions on Further Encouraging and Guiding the Establishment of Medical Institutions by Social Capital,” which established a foundation for a gradual lifting of the cap on foreign equity stakes in certain medical institutions. One of a series of reforms proposed over the last decade, this latest reform was launched with great fanfare and highly exaggerated projections for its impact. Unfortunately, the plan has now generally been accepted as a failure in its efforts to exact any meaningful reform of China’s massive healthcare system. Foreign investment in hospitals has continued at a very low level, with little real progress. After a great deal of discussion and optimistic projections, no foreign-invested hospitals of any size were developed during this period. Despite this lack of success, the government has continued in its efforts to attract foreign investors to the healthcare marketplace, and has correctly perceived that the ownership percentages currently in effect are a barrier to this goal in the minds of many potential investors.

The latest proposal to enact changes was proposed in late 2014, and allowed for the first time a far more flexible and reasonable process for establishing wholly foreign-owned hospitals. The background statement issued in conjunction with the formal release of the proposed policy stated: “The National Health and Family Planning Commission has followed the decision of the CCCPC on some major issues concerning comprehensively deepening reform and several opinions of the State Council on accelerating the development of health services, as well as requirements of deepening medical and health system reform. It has decided to carry out pilot projects of establishing a wholly foreign-owned hospital to promote health service development and better satisfy the medical needs of the public.”

In essence, what the new policy proposed was to create a series of pilot projects for wholly foreign-owned hospitals in Beijing, Tianjin, Shanghai, Jiangsu, Fujian, Guangdong and Hainan. Foreign investors would be allowed to set up these hospitals through mergers, acquisitions or other means.

The Latest Requirements
The requirements associated with this policy are, on the surface at least, reasonable and necessary. In the first case, the foreign investor should be able to "independently bear civil liabilities and have experience in medical and health investment and management.” The government wants assurance that the foreign investor is knowledgeable about operating a hospital and has the financial capability to deal with the liabilities associated with such an activity. How this would be measured, is where there appears to be considerable latitude on the part of the individual charged with making this determination for the government. This type of latitude is where many projects hit a bureaucratic wall, and there is no evidence that this would not happen in this instance.

The second requirement is that the wholly foreign-owned hospitals should meet basic national medical institute standards. This is a
rather elementary requirement, upon which the government cannot be faulted for insisting. Unlike the first requirement, there isn't a great deal of flexibility on this point, and thus there is less opportunity for disagreements and subjective judgments.

In the third requirement, major concerns arise. The government states in its guidelines: “provincial health and family planning administration and business departments will be responsible for reviewing the qualifications of the wholly foreign-owned hospitals.” At this level, the opportunity for corruption and delays becomes a factor that needs to be considered. Local officials operating under poorly defined guidelines have great power in this situation. The experiences over the years of potential foreign investors with local governments have unfortunately been very poor, and the source of many failed projects.

The fourth requirement is a reasonable statement that the wholly foreign-owned hospitals should “go through standard legal procedures and follow relevant legal requirements.” As these procedures are generally codified and not subject to extensive subjective interpretation, they do not normally cause delays in the process.

Concluding the government’s presentation of the requirements is a rather ominous statement that “Establishment of wholly foreign-owned hospitals should also meet the requirements made by provincial health and family planning administration and business departments.” What requirements? This is a major concern for a foreign-invested project. If the reference is to the normal requirements for green belts, signage, etc, then this is not a major issue, and no different from the requirements for any joint venture hospital project. But is it really true that not having a Chinese partner is desirable? A Chinese partner who can navigate through the bureaucratic maze of government regulations, who can understand the nuances of a Chinese business conversation, and who can guide the hospital administration through the multitude of inspections and reviews is certainly a desirable commodity. Is it really a good business strategy to eliminate this resource?

**Expectations Versus Results**

In the period of time since this policy guidance was issued in late 2014, there has been very little sign that it has made any impact. There have been a few announcements of foreign-invested hospital activity, but these have been for projects that were well into development prior to this announcement, and there isn’t any evidence that the new policy impacted the investment decision in these cases. Immediately following the announcement, there were the usual cries of “China is opening up its healthcare marketplace” and predictions that investors would now swarm into China to take advantage of this relaxing of the investor requirements. However, these predictions have yet to be realized. It remains to be seen if this will truly be a policy change that will profoundly impact the marketplace.

This entire policy is predicated on the belief on the part of the government that a wholly foreign-owned hospital, one without the burden of a mandatory Chinese partner, would be attractive to a foreign investor and encourage them to launch a project in China. On the whole, this is correct. Foreign investors with limited experience in China would certainly initially find the lifting of the domestic investment requirement a positive step. But is it really true that not having a Chinese partner is desirable? A Chinese partner who can navigate through the bureaucratic maze of government regulations, who can understand the nuances of a Chinese business conversation, and who can guide the hospital administration through the multitude of inspections and reviews is certainly a desirable commodity. Is it really a good business strategy to eliminate this resource?

**David Wood** is the senior partner of The ChinaCareGroup, a consulting group focused on the Chinese healthcare marketplace. Mr. Wood has assisted clients in engagements involving China market entry and strategic development, market research and feasibility studies. Under management contracts through the firm Mr. Wood has served as chief executive officer of Beijing United Family Hospital, New Century International Children's Hospital, and New Century Women’s and Children's Hospital. He is also the former managing director of PwC's healthcare practice in China and Hong Kong. For more information see [www.chinacaregroup.com](http://www.chinacaregroup.com).