



Independent legal & accounting firms

Doing Business in China

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MSI's guide on Doing Business in China provides current information about the financial, regulatory and legal considerations that could affect business dealings within China. For further assistance please contact our MSI member firms in China.

Country overview

Population

China has a total population of 1.39 billion inhabitants (January 2019)

Government

The current president of the People's Republic of China (PRC) is Xi Jinping since March 14, 2013. China is governed by the Communist Party of China (CPC) with the president possessing full power over all state and government affairs. The party's members elect the President and Vice President in the National People's Congress for a specific term. The next election is expected to be held in March 2023.

There is a total of 23 provinces, five autonomous regions (Tibet, Inner Mongolia, Guangxi, Xinjiang, and Ningxia), and four municipalities (Beijing, Shanghai, Chongqing, and Tianjin.).

Languages

The national language is Chinese or Mandarin, which is based on the Beijing dialect. However, there are many more that are spoken locally like Wu (Shanghainese), Yue (Cantonese), or Tibetan in Xizang.

Currency

The national currency is the Renminbi.

Economic summary

GDP: \$14.14 Trillion USD (2019)

Income per capita: \$10,263.74

Inflation: 2.4%

Main sectors of the economy

China is one of the largest market economies in the world when taking into account its population and total economic production. Data has

confirmed that China since 2010 has been the world biggest exporter and the world's second-largest importer of merchandise goods. China, however, is undergoing economic reform away from investment and towards consumption, eventually leading China to become a service-led economy.

Overall, China is extremely well connected with many ports of entry for business. To facilitate the transportation of large quantities of goods and people, China is home to several of the world's biggest container ports and airports in the world.

The country's most important industrial activities include metal mining and ore processing, coal, consumer products, food processing, transportation equipment, and telecommunications equipment.

United States, Hong Kong, Japan, South Korea, Vietnam, and Germany, are the country's main import partners.

Setting up a business

China offers excellent opportunities for investors. When setting up and maintaining operations in China, it is essential that companies fully understand and comply with PRC regulations due to the links between business and the political environment. Before setting up the business in China, a company should know the legal types of business entities that foreign investors can establish, and then choose the most suitable one for the nature of the planned business in China.

Legal types of business entities

1. Wholly Foreign Owned Enterprise (WFOE)

A wholly foreign-owned enterprise is 100% owned by foreign investors. The Foreign Invested Enterprise Law (FIE) governs the establishment of a wholly foreign-owned enterprise.

2. Representative Office (RO)

A Representative Office can be set-up by a foreign company to render preparatory services such as liaison, and coordination on behalf of its parent company. It is essential that a representative office cannot engage in any direct profit-making activities, except for specific industries, such as law, accounting, and audit services.

3. Joint Venture (JV)

An arrangement between two or more parties that are foreign and local, and covered by the FIE regulations.

Process of how to set up a business

1. Apply for an official Chinese business name.
2. Apply for Business License.
3. Register for taxes at the Tax Bureau.
4. Application for chops / seals.
5. Register the business at other relevant authorities.
6. Open bank accounts.

Financial year of taxes and financial accounts

The financial year for all tax in the calendar year is from the 1st January to 31st December.

Accounting and auditing

By law, all foreign enterprises are required to have a statutory annual audit performed by a firm of Certified Public Accountants. These enterprises will have to provide the following:

1. Annual Report;
2. Audited Financial Report;

Economic and fiscal incentives

China has established more and more Free Trade Zones. The most popular zones in China are Shanghai, Tianjin, and Guangdong. FIEs can operate in the Free Trade zones with more business autonomy and sometimes tax reductions and other incentives.

Incentives for foreign investors / local investors

Different regions in China's Free Trade zones conduct their own incentive policy. The local government authorities will primarily focus on the business scope and registered capital of the companies before providing incentives.

Taxation

The tax system in any given country is invariably a fundamental criterion when it comes to companies finding a country of incorporation. The Chinese government is pursuing a tax reform, focused on a general reduction in the overall tax burden for creating a better tax environment for businesses and individuals.

In that framework, it is possible to obtain preferential tax policies, especially for small and micro businesses, and manufacturing businesses in specific industries. In addition, China has signed tax treaties with many other countries to prevent the occurrence of double taxation.

At the same time, Chinese tax authorities are paying more attention to the compliance of non-resident enterprises and issued Guidelines on Withholding Tax at Source for Non-Resident Enterprises.

The Chinese tax system can be divided into five categories, namely commodity

and service taxes, income taxes, property and behaviour taxes, resource taxes, and taxes for special purposes. Among all the types of taxes there are Value-Added Tax (VAT), Corporation Income Tax (CIT) and Individual Income Tax (IIT) which are the most closely linked to doing business.

VAT

Enterprises are divided into general payers and small-scale payers for separate VAT calculation methods. The general VAT rate for trading and importation is 13%. For transportation services, postal services, basic telecommunication services, construction services, real estate, and selling or importing special goods, the rate is 9%. On modern services, the rate is 6%.

Individual income tax (IIT)

The tax base for income tax purposes is divided into the following:

1. Comprehensive income;
2. Income from operation;
3. Interest, dividends;
4. Income from lease of property;
5. Income from transfer of property;
6. Contingent income; and
7. Other taxable income determined by the financial authorities of the State Council.

IIT is levied on comprehensive income at the progressive rates from 3% to 45%. Foreigners working in China have special exemptions until 2021 for housing, schooling, meal and laundry, flights home, etc. And local employees now can claim six deductions from their taxable income.

Corporate income tax

All domestic enterprises and FIEs are subject to Corporate Income Tax (CIT) at a unified tax rate of 25%. However, location and industry incentives can be sought, and SMEs have special incentives of 5% on the first RMB1m and 10% on the next RMB2m profit. However, once above RMB3m, all profit reverts to 25% as it is not progressively applied. RO's are taxed on a deemed profit method or actual profit, depending upon their type.

Registration procedures

After obtaining the business license, a newly incorporated enterprise or an RO is required to perform basic tax registrations with the local branch of the state tax bureau will provide a Tax Registration Certificate.

Urban Construction Tax and Education Surcharge

All foreign entities in China are liable for this surcharge. The surcharge is calculated based on the VAT paid, and the rates range from 6% - 12% of the VAT.

Social insurance

All enterprises must register with the local social insurance bureaus, participate in social insurance schemes and pay social insurance premiums monthly based upon the average monthly comprehensive income from the past year to the time of the annual reset, which varies by location. The portion of the payable premium by individual workers will be withheld and deducted from their salary and paid to the relevant authorities by the enterprises, and enterprises also have a company contribution. The amount payable depends on location. Foreigners are subject to social insurance on all parts except the housing fund. Social welfare covers five insurances and one fund:

1. Basic Pension
2. Basic Medical Insurance
3. Work-Related Injury Insurance
4. Unemployment Insurance
5. Maternity Insurance
6. Housing Fund (local only, not expatriates)

Withholding taxes (WHT)

The most common withholding tax rate is 10% on revenues derived by a non-resident from China. Such revenues include:

1. Dividends
2. Interests
3. Royalty
4. Rental
5. Other passive income

The rate may be reduced depending on the relevant tax treaties. For instance, certain countries have a reduced WHT on dividends of 5% in their Double Taxation Agreement (DTA) with China. To take advantage of DTA benefits there must be substance within the organisation and the use of a preferential DTA not related to using the DTA for tax reduction purposes.

Some DTAs have a reduced rate on royalties and loan interest.

HR/ Labour Law

Employment law

The Labour Contract Law of the People's Republic of China is the primary source of labour law in China effective since January 1, 2008. The law is comprehensive on all the rights employees have, which must not be violated. It covers areas such as severance pay, probationary periods, lay-offs, non-compete clauses, and collective bargaining. An amendment which took effect on July 1, 2013, tightens the hiring of dispatched employees and better protect their interests.

Employees are required to have a formal contract of employment in place within one month of their employment. Failure to arrange this causes the company to pay double salary until such a time as this is in place, up to one year, and thereafter double salary becomes permanent. Normally the staff contract will reference the Staff Handbook, which is a company policies book, abiding by labour law, but also it can include other policies such as leave policy, training policy, use of IT policy, policy against fraud, creation of IP policy etc.

Social Welfare

There are five distinct categories of the social welfare system that employers should be aware of:

1. Pension
2. Medical Insurance
3. Unemployment Insurance
4. Maternity Insurance
5. Work-related Injury Insurance

Both the employer and employee contribute to each of the abovementioned categories, but at different percentages. Due to the variation in regulations issued by different local governments, also many different factors can determine how much each employee is entitled to, for example, the amount to contribute may vary depending on the employee's Hukou (national identification Card), nationality, employment type (full-time/part-time), and location of work etc.

Total Social Welfare Rates for the Top Five Cities in China

The Social Welfare rates are based on the monthly average salary of employee in the previous year. The limits of the Social Welfare contribution is based on three times the city's average salary the previous year.

<u>Employer Rates</u>	<u>Employee Rates</u>
Beijing 27.8% -29.5%	10.2%+RMB3
Shanghai 27.2%-28.9%	10.5%
Shenzhen SZ Hukou: 20.55% - 22.25% Non SZ Hukou: 19.55% - 21.25%	10.3%
Guangzhou 21.2% + RMB24.23 22.9% + RMB24.2	10.2%
Tianjin 27.2%-28.9%	10.5%

Pension

The retirement age in China currently is 60 for men and 55 for female civil servants and 50 for female workers. Anyone within the specific age range who has paid into the pension system for a minimum of 15 years can get a Government pension, including foreigners.

Payroll

When starting a business and employing staff, the company must register an employee to the social security and tax authorities on the first month of employment.

Companies must be in line with national and local minimum salary standards. Employers in China have to withhold the monthly social welfare and individual income tax and pay as withholding agents.

Visa and Work Permits

A visa is required for expatriates working in or moving to China, along with their accompanying family members. Before their departure to China, expatriates need to apply for a visa at a Chinese diplomatic mission, embassy, consulate or other representative offices in foreign countries authorised by the Chinese Ministry of Foreign Affairs.

All applicants for a work-type visa in China are split into three categories – A, B and C. The categories are awarded according to a score out of 85, points are awarded according to the different criteria the individual fulfils. Those with a score of 85 become category A, those with a score 60-84 are Category B, and those below 60 are category C. The work visa processes in China are particularly bureaucratic and time consuming especially for category B and C, though the Government is making efforts to improve this.

Most expatriates planning to work in China will first have a Z-visa which has a validity of 30 days. To work in China for more than 30 days expatriate on arrival to China have to apply for a work residence permit which can be valid for nine months or up to five years depending on local requirements.

Different cities and regions in China have slightly different requirements, and it is not unusual for local governments to have some special requirement beyond the state policy. Foreign entrepreneurs and investors including, recently graduated individuals, wanting to work or set up a business in China can benefit from the 2019 visa policies facilitating such individuals to apply for a working visa, and for receiving either a five-year residence permit or a permanent residence permit.

Chinese Court/ IP Protection

China's Judicial System

Under the Constitution of the PRC and the Organic Law of the People's Courts, China has a four-court system and Special Jurisdiction Courts.

The Supreme People's Court (SPC) is based in Beijing, checking that legal procedures are in adherence to the laws and regulations in all the courts underneath it, including Special Jurisdiction Courts. There are six circuit courts outside the capital with the same powers used for resolving cross-provincial cases within their jurisdiction.

The Local People's Courts represent the remaining three levels of the court system composed of the High People's Courts (for Provinces, Autonomous Regions, and Special Municipalities), Intermediate People's Courts (for Prefectures, Autonomous Prefectures, and Municipalities), and Basic People's Courts (for Counties, Town, and Municipal Districts). These courts are courts of first instance and handle criminal and civil cases.

Lastly Courts of Special Jurisdiction operate under the jurisdiction of their respective High Court, and they are composed of Military Court, Railway & Transport Court, Maritime Court, Internet Court, Intellectual Property Court, and Financial Court.

Arbitration

China has established two systems of arbitration one foreign and the other domestic. Foreign arbitration began in the mid-1950s. At that time, according to the relevant decisions of the State Council in 1954 and 1958, the China Council for the Promotion of International Trade (CCPIT) established the Foreign Trade Arbitration Commission in 1956, the Maritime Arbitration Commission in 1959, and formulated corresponding arbitration rules. From the very beginning, China's foreign arbitration has followed the internationally accepted principles of civil arbitration, voluntary arbitration and the final ruling.

Compared with foreign arbitration, the development of domestic arbitration in China is much more complex.

Dispute Resolution

Contractual Disputes between parties one Chinese and the other foreign will have stated the law to be applied in handling the Dispute. If no law is nominated, the law of the country with the closest link to the contract shall be applied.

All contracts relating to Sino-foreign equity joint venture, Sino-foreign cooperative enterprise and Sino-foreign contracts for the cooperative exploitation and development of natural resources in China shall be ruled by the law of the PRC.

Commercial disputes are often resolved via negotiation. However, an increased number of disputes eventually advance to Litigation or Arbitration. Any judgments, arbitral awards or mediation agreements which possess legal effect made by the people's court must be applied.

Lawsuits, or applying for arbitration stemming from an international contract for the sale of goods or a contract for the import and export of technology, must be filed within four years from the date of the infringement.

Trademarks, Patents, and Copyright

Trademarks

China is a first to file jurisdiction, not a first to use, i.e. the rights to a mark go to the first person who has filed with the Trademark Bureau for the relevant category. Normally, before submitting a trademark for registration, a preliminary search is carried out at the China Trademark Office to see if there may be any complete marks that could hinder a registration.

Foreign businesses that want to register a trademark but do not have a permanent address in China must get an Intellectual Property Agent to do the

filing for them, and all documentation submitted must be in Chinese.

There are a total of 42 classes of trademarks in China, which when registering a trademark at least one of the classes must be chosen, but multiple can be selected depending upon the nature of the business that the trademark will cover.

Once the trademark registration has been submitted, the China Trademark Office will look over the documentation to make sure that the trademark is not similar or identical to the existing registered trademarks. After the trademark office has looked over the trademark, it will give a preliminary approval and publish the trademark on the preliminary examination gazette.

Under China's Trademark Law, the trademark at that point can be opposed within a period of three months.

In the optimal situation where there are no oppositions after three months, the trademark will register the trademark and publish the registration in the Trademark Gazette.

Patents

All patents in China are done on a first come first serve basis. Translations are a vital part of the patent application since all patent applications must be made in Chinese. Each translation must be as close to the original patent application as possible as the Chinese translation will prevail over the foreign one.

Inventors or their employers must submit the patent application in Chinese, to the Patent Office of the Chinese State Intellectual Property Office (SIPO) where it will be examined.

Types of patents

Inventions Patent – Innovations in technology which are state-of-the-art and practical to apply. The time for registration completion is three to five years, and patents last 20 years from the filing date.

Utility Model Patent – New technical solutions regarding shape and or

structure of an object. The time for registration completion is one year and patents last 10 years from filing date.

Design patent - Designs relating to shape, pattern, colour or a combination of an object. The time for registration completion is one year and patents last ten years from filing date.

The Patent Rights begin from the date of the publication in the Patent Gazette.

Ways to Submit Patents

Foreign companies without a registered office in China must find a professional local patent attorney to handle the filing of the patent. SIPO will assess both the professional presentation and conduct of both the attorney and the patent application.

It is possible to file a patent application in a foreign country, but it must be a Member State of the Paris Convention, and then submit another patent application in China within 12 months stating the priority date of the first application.

Another method to acquire a patent in China is to submit an international patent application under the Patent Cooperation Treaty (PCT) designating China. Further rules dictate that the applicant has to begin the "National Phase" with the Chinese Patent Office 30 months before the priority date. The Chinese patent application must be in Chinese, which will be used to determine the extent of the protection.

Patent Enforcement

In case of infringement, it is advisable to file an Infringement Complaint with the courts of Beijing, Shanghai or Guangzhou, due to their experience in handling such cases. It is also recommended to hire a local investigation firm as the complaint will have to be proven in court.

The Intellectual Property Office (IPO) can offer assistance for cases where there is a design patent infringement at a trade fair or to mediate between patent disputes.

Copyright

China follows the Berne Convention when it comes to protecting copyright, and protects literary, artistic, oral works, architecture, software, and scientific works. Copyright registration is not obligatory, and Copyright protection usually lasts for 50 years.

Protection of specific works may overlap between copyrights and trademarks, as well as copyrights and patents. Software is an example where it can be protected with a patent and copyright.

PRC's National Copyright Administration (CNAC) is responsible for registering copyrighted works. The procedure requires the submission of a sample of the work to the CNAC and Copyright Protection Centre of China (CPCC) who will examine the application and then issue the certificate if all checks are cleared.

However, the CNAC and CPCC are part of the Central Propaganda Department's Control and will take a closer look at press, media, and publication materials.

Contact us

The information provided in this guide cannot be exhaustive and we recommend anyone considering doing business in China should seek professional advice from our member firms before making any business or investment decision.

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