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**HSBC**   
Commercial Banking

# Doing business in China



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The materials contained in this publication were assembled in August 2012 and were based on the law enforceable and information available at that time.

# Executive summary

Economic reforms in China have led to an unprecedented change in the nature of the business environment and the opportunities available for foreign investors and privately owned companies. However, there remain bureaucratic and operational challenges and this guide presents an introduction to some of the key areas that businesses should be aware of when setting up operations and doing business in China.

Some key issues for foreign investors are as follows:

- China joined the World Trade Organisation (WTO) in 2001 and market access has been gradually phased in.
- Despite considerable bureaucracy, the government is making efforts to promote foreign investment.
- Although many industries are largely state-owned, the non-state sector, made of collectively-owned, foreign-owned and private companies, is rapidly gaining importance in the Chinese economy.
- China has been proactive in removing tariff and non-tariff barriers for trade in goods through the negotiation and implementation of regional free trade agreements.
- Certain foreign exchange restrictions are in place.
- Preferential tax treatments such as tax holidays and reduced tax rates for enterprises in Special Economic Zones have been removed with the implementation of a new corporate income law effective from 1 January 2008. Incentives are now available for High-New Technology Enterprises ('HNTEs'), Small and Medium-Sized Enterprises ('SMSEs'), qualified Technology Advanced Service Enterprises ('TASE'), and foreign investments in the central and western regions.
- There are market access and production controls, as well as restrictions on operations.
- Distribution and some service sectors are open to foreign investors.
- China's new anti-monopoly law came into effect on 1 August 2008, and China will join other countries with anti-trust laws that regulate competition.
- Despite the fact that managers and skilled labour are still in short supply, the situation is getting better with the millions of new fresh university graduates coming into the labour market every year.
- Protection of intellectual property is an area of concern.



# Foreword

China has embarked on unprecedented economic growth since its market opened up three decades ago, rising to become the world's second-largest economy today. Thanks to its prudent management under the 12th Five-Year Plan, a new path towards sustainable and balanced development, alongside a focus on boosting domestic consumption, is opening new opportunities in China for continued industrial innovation and business expansion.

Elsewhere, China's 'going out' strategy over the past decade has spurred great promise, with its dynamic enterprises investing overseas while expanding China's economic influence worldwide – one that continues to be a lighthouse for growth in spite of a challenging global environment.

At HSBC, we are ideally positioned to help businesses with interests in and out of China. Having grown to 120 outlets (at June 2012), HSBC is the foreign bank with the largest network of outlets in China and the most comprehensive range of services. From here, we have cultivated our deep-seated local knowledge to help customers achieve their goals, as we leverage our unique global connectivity reaching out to over 80 countries and territories worldwide.

HSBC looks to be your trusted partner while always seeking ways to better support customers. We have produced this booklet – 'Doing Business in China' – in collaboration with PricewaterhouseCoopers, to guide you towards the right business decisions in China.

HSBC and PricewaterhouseCoopers each maintain wide presence across Greater China, well-established to provide the financial services and advice that offer your company the best chance for success in this vibrant region.

On behalf of HSBC, may I wish you a prosperous future in China.



**Helen Wong**  
Group General Manager  
President &  
Chief Executive Officer  
HSBC Bank (China)  
Company Limited



# Introduction

## Doing business in China

### General business climate

China officially joined the World Trade Organisation (WTO) in November 2001, and foreign investment and trade has grown rapidly as a result. Under the WTO, tariffs on agreed products have been reduced, and market access to various regulated industries has been phased in gradually. Industrial sectors opened up in the past years are trade and distribution, including franchising, advertising services, inspection services, freight forwarding agency services, for example. A more open market will attract know-how, technology, services and materials. These imports, together with China's rich manpower, both skilled and unskilled, have turned China into one of the most important manufacturing bases in the world.

China still holds a number of challenging areas for foreign investors. Nevertheless, the government is making efforts to address some of these areas in order to encourage foreign investment. For example, through the amendment of the 'Law on Wholly Foreign-owned Enterprises (WFOEs)', the 'Law on Cooperative Joint Ventures (CJVs)' and the 'Law on Equity Joint Ventures (EJVs)' in 2000 and 2001, China has relaxed its requirements on foreign exchange balancing and raw

materials sourcing for Foreign Investment Enterprises (FIEs). Now, FIEs are no longer required to give priority to the local market when purchasing raw materials, fuels and other materials. Similarly, the requirement for WFOEs and CJVs on balancing foreign exchange incomes and expenditures has been repealed.

Large areas of China's economy are increasingly becoming more market oriented, and a smaller range of sectors and products is now under administrative control. Current industrial policy places emphasis on strengthening basic industries, infrastructure, energy, and transport. Market forces are now playing a more dominant role in China, and the business climate is less subjected to state administrative guidance than before. Foreign participation in investment projects continues to be encouraged by the Chinese authorities, and measures are being taken to make the investment climate more favourable and less bureaucratic. The Chinese government gradually delegated more foreign investment approval authority to local governments. This is considered another step towards reducing bureaucracy. Priority areas for foreign investment remain those where modern technology, environmental protection,

energy and water conservation are required. The coastal areas have experienced a greater degree of industrial development than the inland areas, offering improved infrastructural facilities. In addition, the government has issued a series of laws and regulations intended to encourage foreign investment in the central and western regions of China.

### Climate for foreign investors

#### Incentives for foreign investors

For the purpose of attracting foreign investment, the Chinese government has introduced a number of benefits and incentives towards overseas investors in particular industries, of which we set out a brief list as follows:

- Qualified small and low-profit enterprises and qualified high/new-tech enterprises are subject to reduced income tax rates.
- TASEs, which include information technology outsourcing (ITO), business process outsourcing (BPO), and knowledge process outsourcing (KPO), are subject to income tax benefits: entitled to a preferential Corporate Income Tax (CIT) rate of 15% and a higher education expense deduction cap of 8%. Income derived from the offshore service contracts falling within



the scope of ITO, BPO and KPO are eligible to Business Tax exemption. Meanwhile, qualified equipment obtained by TASE is entitled to bonded treatment.

- Enterprises or projects with a focus on technological development, environmental protection, energy and/or water conservation, production safety, for example, may be entitled to various types of income tax incentives.
- Tax incentives for foreign investment enterprises of a productive nature and most of the 'geography-based' incentives have been removed. A grandfather period is available for certain incentive policies.
- Passive income derived by foreign enterprises from sources in China was previously subjected to a withholding tax of 20%, which has since been reduced to a concessionary rate of 10%. However, an exemption is available under certain circumstances.
- Qualified projects may enjoy certain VAT incentives.
- Technology transfer, technology development and related services are exempt from business tax (BT) subject to technical assessment of certain Science and Technology Commission and approval of related tax authority.

#### **Foreign exchange restrictions**

There are certain restrictions on foreign currency exchange in China. Foreign investment enterprises are required by the State Administration of Foreign Exchange (SAFE) to separate their foreign currency bank accounts into capital accounts and current accounts. For details please refer to section 'Banking in China'.

After years of strong economic growth and waves of foreign direct investment, a substantial foreign currency reserve has been accumulated by the Chinese government. With the sizeable reserve, the relevant foreign exchange restrictions have also been relaxing gradually.

#### **Anti-Trust Law impacts foreign investment**

China has passed an anti-monopoly law which came into effect on 1 August 2008. Foreign investors doing business in China need to consider the immediate impact of this new law on their businesses. Merger and acquisition transactions in China involving foreign parties will be subject to review and can be halted due to anti-trust reasons. Acquisitions of domestic enterprises by foreign investors that may have implications for national security shall be subject to more stringent review.

#### **Local competitor attitude toward foreign investment**

In order to acquire foreign technology, capital and know-how, Chinese domestic enterprises recognise the importance of entering into joint ventures with foreign enterprises. However, there are restrictions on the extent of foreign participation allowed in certain sectors and in some sectors foreign investment is not permitted at all. Such restrictions, however, are gradually being phased out with China's accession to the WTO. In addition to joint ventures, WFOEs are also allowed, provided the sectors in which they operate are not subject to 100% equity restrictions.

#### **Labour attitude toward foreign investment**

The differences between Chinese and western management styles can often prove a problem for foreign joint venture partners due more to cultural differences, language and communications rather than prejudices against foreign management. The situation has improved in recent years as a pool of talented local staff is being developed in major cities through training in modern management techniques and exposure to overseas work experiences.

#### **Key Markets and Trade**

##### **Framework of industry**

State-owned enterprises (SOEs) still maintain an important role in the economy. Notwithstanding this, the non-state sector, made up of collectively-owned, foreign-owned and private companies, is rapidly gaining importance and now accounts for the majority of gross industrial output value.

The private sector has become increasingly important as China transitioned towards a socialist market economy. To enhance the growth of private enterprises which have been dominated by small and medium enterprises (SMEs), the Chinese government has chosen several municipalities in which to launch SME-facilitating policies. SOEs still dominate in some sectors such as oil, power, tobacco, steel, petrochemical, automobile, communication, railway, aviation and financial industries.

Both FIE and domestic enterprises are encouraged to participate in high-tech industries (including software, integrated circuit, R&D, for example).

##### **Overseas trade relations**

##### **Memberships in trade blocs**

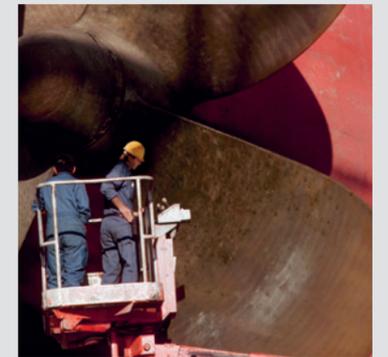
China officially became a member of the WTO in November 2001. As part of

this membership, China has gradually lowered its tariff rates and eliminated non-tariff barriers to trade, including quotas, import licences and unwarranted inspection requirements. However, China still needs to address the issues of legal and regulatory transparency, the protection of intellectual property rights and the opening up of telecommunications, security, and other service industries.

##### **Regional free trade agreements**

At the regional and bilateral level, China has been proactive in removing tariff and non-tariff barriers for trade in goods through the negotiation and implementation of free trade agreements (FTA).

China signed a FTA with ASEAN (Association of South East Asia Nations) in November 2002 which provides for enhanced economic cooperation in the trading of goods, services and in investment. The more important areas and sources of preferential ASEAN market access, in terms of fewer tariff and non-tariff barriers have come into effect at varying times beginning 1 January 2005. The FTA represents a significant opportunity for companies trading between ASEAN and China to reduce supply chain costs and increase overall price competitiveness and profitability.



In addition, China has signed CEPA agreements (Closer Economic Partnership Arrangement) with Hong Kong and Macau which were originally implemented in 2004 and subsequently expanded 8 times up to the end of 2011. In principle, China has agreed to grant zero tariffs to all goods of Hong Kong and Macau origin, other than prohibited imports.

The implemented FTAs also include the Asia-Pacific Trade Agreement (APTA), formerly known as the Bangkok Agreement (consisting of members of China, India, South Korea, Sri Lanka, Bangladesh and Laos), the China and Chile Agreement, and the Early Harvest Programme of China and Pakistan Agreement. In April 2008, New Zealand was recognised as the first developed nation to sign an FTA with China.

Meanwhile, China has signed an ECFA agreement (Economic Cooperation Framework Agreement) with Taiwan in June 2010 which aims to promote economic, trade and investment cooperation between the two parties, achieving further trade liberalisation in goods and services, expanding the fields of economic cooperation and building a cooperation mechanism. The signing of ECFA brings cross-strait economic relationship into a new era. At the same time, with Hong Kong serving as the platform

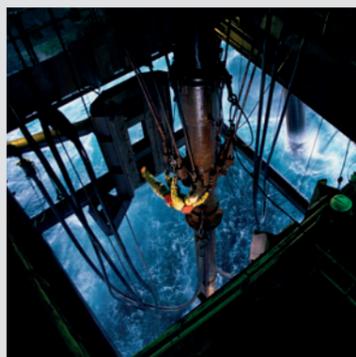
for cooperation between China and Taiwan, ECFA forms a new landscape for the three areas to better cooperate and communicate with each other in achieving mutual development. The ECFA was signed on 29 June, 2010 and went into effect on 12 September, 2010. The first wave of policies went into force on 1 January, 2011.

More FTAs are under negotiation including with Australia, Japan, South Korea, GCC (Gulf Cooperation Council), SACU (The Southern African Customs Union) and Iceland among others.

#### Exports

With the exception of certain items subject to state export restrictions, most products exported by foreign investment enterprises are exempt from export duties. The general rate for value-added tax (VAT) is 17%. By law, except for certain special products, exports are zero-rated, i.e. no VAT will be levied on exports, and input VAT will be refunded.

With the pressure of persistent trade surpluses with major foreign trading partners and with concerns about resource preservation and environmental protection, there have been adjustments (i.e. lowered or eliminated) to the export VAT refund rate since 2004, which increase exporters' operating costs.



# Conducting business in China

## Forms of business

The principal forms of business open to foreign investors in China are classified under the following headings:

### Equity joint ventures

An equity joint venture is a separate legal entity and takes the form of a limited liability company registered in China. The partners have joint management of the company and profit sharing is according to the ratio of each partner's capital contribution.

### Cooperative joint ventures

The parties to cooperative joint ventures may apply for approval to have the company structured as a separate legal entity with limited liability. Profit sharing is defined in the contract and can vary over the contract terms. In addition, there is a form of unincorporated cooperative joint venture which is not a legal entity. Income and expenses are shared amongst partners based on the contract terms. Income tax might be imposed on the individual joint venture parties

instead of the unincorporated cooperative joint venture. The tax authorities in charge, i.e. the relevant state or provincial tax authority, of the unincorporated cooperative joint venture would determine how it or its partners are being taxed.

### Wholly foreign-owned Enterprises

WFOEs are established exclusively with the foreign investor's capital. They are limited liability companies.

### Joint stock companies

Joint stock companies, also known as companies limited by shares, are established primarily in order to be able to list on Chinese or foreign stock markets. The capital stock of a joint stock company is made up of equal value shares. Contributions are made by both domestic and foreign shareholders.

### Foreign enterprises

In general, foreign enterprises are enterprises (other than foreign investment

enterprises in China) that have establishments or places of business in China and engage in production or business operations. Foreign enterprises that do not have establishments or places of business in China but derive certain China-source income are also included in this category.

Foreign enterprises include representative offices, sites for the exploitation of natural resources, contracted project sites, and companies providing labour services or employing business agents.

### Branches of foreign enterprises

Under the Company Law of the People's Republic of China, a foreign company may establish branches in China. A branch does not have the status of a Chinese legal person, and the foreign company assumes the civil liabilities of its branches in China. However, in practice, only foreign banks and insurance companies have been granted licences to open branches.

## Setting up a business

### Equity joint ventures

#### Formation procedures

- Equity joint ventures are governed by the Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment that was promulgated in 1979. The latest amendments to the law were made in 2001.
- The Ministry of Commerce (MOFCOM) has overall responsibility for approving joint ventures and for issuing the approval certificates. The local MOFCOM authorities generally undertake the examination and approval procedures.
- Once the approval certificate has been received, the venture has to register within one month with the administrative bureau of industry and commerce in the relevant locality to obtain a business licence. Thirty days after the business licence is issued, the joint venture must register with the local tax authorities.

#### Capital structure

- The equity joint venture law requires that the foreign partner to the venture contribute generally at least 25% of the registered capital. No upper limit on the foreign partner's contributions has been set, except in some special

industries where regulations require the Chinese partner's share to give them dominant control.

- Capital contributions of an equity joint venture can take the form of cash, capital goods, industrial property rights and other assets. In general, the Chinese partner will contribute cash, land development or clearance fees and land use rights, while the foreign partner will contribute cash, construction materials, equipment and machinery. All joint venture contracts should contain a schedule for capital contributions. If the capital contribution is to be a single payment, all partners must pay the full amount within 6 months of the date the business licence is issued. A temporary business licence can be issued during the period in which capital contributions are to be made. If the partners do not make their contribution within the stipulated time frame, the temporary business licence will not be renewed. All capital contributions must be certified in a report from a Chinese registered CPA (Certified Public Accountant) firm (this may be either an international accounting firm acting through a Sino-foreign joint venture or a Chinese CPA firm) as confirmation that the contributions listed in the contract have been received.

- During the life of an equity joint venture, the foreign partner's equity contribution should normally not be repaid. However, once the venture has been liquidated, the net assets (if any) are distributed according to the partners' shareholdings.

#### Relationship of shareholders, directors and officers

- The partners of an equity joint venture share joint management of the venture. The board of directors has the authority to make all major decisions concerning the financial position of the venture. The joint venture partners are responsible for appointing the board members, and representation generally matches the proportion of ownership interest in the venture. Also, the law requires that a meeting of the board be held at least once each year. The board of directors is required to engage a general manager and deputy managers. The general manager is responsible for carrying out board decisions and is in charge of the daily management of the venture.
- The profits and losses of an equity joint venture are distributed according to the ratio of each partner's investment. After the payment of taxes and before the distribution of profits, the joint venture

is required to make allocations to three funds, namely, a staff bonus and welfare fund, an enterprise expansion fund and a general reserve fund. The amount contributed to the three funds by the venture may be designated in the joint venture contract or decided by the board of directors. All the previous years' losses must be cleared before the current year's profits can be distributed.

### Cooperative joint ventures

#### Formation procedures

- Cooperative joint ventures are governed by the Law of the People's Republic of China on Chinese-Foreign Cooperative Joint Ventures, promulgated in April 1988 and revised in 2000. The law provides that the venture can operate as a 'legal person', which means that a limited liability company can be formed. Under the limited liability structure the company would own all of the venture's assets, but the liabilities of the investors would be limited to their investment contributions.
- To establish a cooperative venture the Chinese and foreign partner(s) must submit documents such as a project proposal, the signed agreement, contract, and articles of association to the Department of Commerce or the relevant local government



authority for examination and approval. If approval is granted, the partners have 30 days in which to apply to the administrative authorities of industry and commerce for registration and a business licence. The date on which the business licence is issued is the date of the establishment of the venture. The venture then has 30 days in which to register with the tax authorities.

#### Capital structure

- Capital contributed to the venture by the two parties may be in cash or in kind. Land use rights, industrial property rights, and other property rights are included as capital contributions. The cooperative joint venture law requires that both parties fulfil their investment and cooperation requirements as set out in the joint venture contract. Failure to do so within the prescribed time limit will result in another time limit being set by the relevant authorities, and further failure will be handled in accordance with the relevant state provisions.
- Capital contributions by both parties must be verified by a Chinese-registered CPA firm (this may be either a Chinese CPA firm or a Sino-foreign joint venture accounting firm), which will provide a verification certificate.

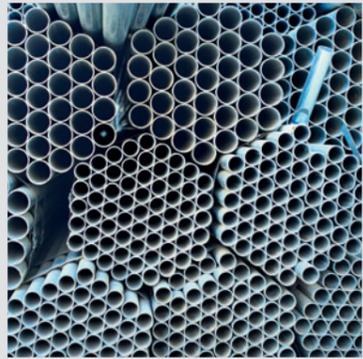
#### Relationship of shareholders, directors and officers

- As with an equity joint venture, a cooperative joint venture operating as a limited liability company is required to appoint a board of directors or a joint managerial committee that will make all major decisions and oversee the management of the company.
- The profits and losses of a cooperative joint venture would normally be distributed according to the ratio established in the contract, which may vary over the contract terms. While the total amount provided for the three reserve funds (staff welfare and bonus fund, general reserve fund and enterprise expansion fund) by an equity joint venture is expressed as a percentage of the after-tax profit, the total amount provided for these funds by a cooperative joint venture is expressed as a percentage of pre-tax profit.

#### Wholly foreign-owned enterprises

#### Formation procedures

- WFOEs are governed by the Law of the People's Republic of China on Enterprises Operating Exclusively with Foreign Capital. Although this law came into force in 1986, it was subsequently amended in 2000. A WFOE is a limited liability company.



- The law and regulations prohibit or restrict the establishment of WFOEs in certain industries.
- MOFCOM is responsible for the examination and approval of WFOEs. Local governments are also authorised to approve these enterprises, provided certain conditions are met.
- Before applying to establish a WFOE, the investor must submit a report, which must include specific information requested under the regulations, to the relevant government authority in the location in which the enterprise is to be established. The investor will receive a written response within 30 days of submitting the report.
- The investor must apply for registration and obtain a business licence within 30 days of receiving approval, or the approval certificate will automatically become void. The date the business licence is issued will be the date of the establishment of the enterprise. Tax registration must be performed within 30 days of establishment.

#### Capital structure

- The amount of registered capital of a WFOE should be consistent with the scale of intended operations. The registered capital cannot be reduced during the term of operation unless special approval is received, and

increases must receive prior approval from the authorities.

- Foreign investors may contribute capital in the form of freely convertible foreign currencies or certified RMB profits from other FIEs. Subject to certain requirements set out in the regulations, such items as machinery, equipment, industrial property and proprietary technology may be capitalised according to their monetary value.
  - The time limit within which the capital contributions are to be made must be specified in the application and articles of association. The contributions can be made in instalments. The first instalment representing no less than 15% of the total registered capital must be made within 90 days and the last instalment within three years of the issuance of the business licence. Other contributions must be made pursuant to the published schedule.
  - After all the capital contributions have been made, a Chinese-registered accountant must be engaged to verify the contributions and issue an investment verification report.
- Relationship of shareholders, directors and officers**
- WFOEs are required to make

allocations to a reserve fund and a bonus and welfare fund for its employees from its after-tax profits. The reserve fund allocations must be not less than 10% of the after-tax profits. Profits may not be distributed until the prior years' losses have been cleared.

#### Joint stock companies

Joint stock companies, also known as companies limited by shares, are governed by the 'Company Law of the People's Republic of China' issued in December 1993 and amended in October 2005. In addition to the Company Law, joint stock companies are governed by the provisional regulations regarding certain issues relating to the establishment of a foreign investment company limited by shares, promulgated on 10 January 1995. The provisional regulations add certain requirements for the formation of a joint stock company, including requiring a minimum of 25% of the capital to be invested by foreign investors and a minimum capital requirement of RMB30 million.

#### Partnerships

Partnerships have traditionally not been commonly used in China. The first version of the Partnership Enterprise Law came into effect on 1 August 1997. In August 2006, the law was revised, coming

into effect on 1 June 2007. According to the 2006 version of the Partnership Enterprise Law, a partnership in China is a general partnership enterprise or a limited partnership enterprise established by natural persons, legal persons and/or other organisations within China. The profit distribution or loss allocation of the partnership enterprise is made according to the partnership agreement or as regulated by the Partnership Enterprise Law.

In November 2009, the Administrative Measures for Foreign Corporations and Individuals to Establish Partnership in China ('Measures') was released, coming into effect on 1 March 2010. The Measures set forth the administrative rules and procedures for foreign investors to establish partnerships in China which provided a new form for foreign investors to make their investments in China.

#### Representative offices

- Foreign enterprises (including enterprises in Hong Kong, Macao and Taiwan) are permitted to open representative offices in China. Legally, these are to be established purely for liaison purposes, and their activities are limited to the provision of services that do not give rise to any earnings. The permissible activities of

representative offices include the following:

- *Investigating and collecting market information;*
- *Providing introductory services to potential buyers and sellers, such as setting up meetings and passing on price and technical information to Chinese customers;*
- *Assisting in making arrangements for trade visits to China;*
- *Coordinating with the parent company and other associated companies or affiliates.*

- In practice, many representative offices provide services that are outside this legal scope. Local branches of the State Administration of Industry and Commerce (SAIC) are empowered to penalise the representative office for operating without a business licence, if the representative office should be regarded as engaging in operating activities and collecting funds through various means..

- With the circular issued by the State Council in May 2004, representative offices do not need to be approved by MOFCOM or other relevant authorities except for representative offices whose head offices are engaging in some special industries. Representative offices are required to register with the SAIC. Upon approval of the representative office, the

chief representative should visit the office in person to receive the business registration certificate and complete some additional forms to formalise the registration.

- The representative office is required to submit the annual report to the SAIC during the period of 1 March to 30 June annually.
- The immediate head office of the representative office must have been established for at least two years before the application.
- The number of representatives (including Chief Representative) is limited to 4. Representative offices with more than 4 existing representatives may only apply for de-registration representatives, but not add new ones.
- The company is required to register with the local tax authorities within 30 days of receiving the business registration certificate.
- The registration certificate is valid for one year only, which is subject to annual renewal.
- Local branches of SAIC are required to inspect the office premises of a representative office within 3 months of issue of the registration certificate.

# Taxation in China

## Key messages

- Starting from 1 January 2008, a unified CIT system is applicable to foreign investment enterprises and foreign enterprises, as well as domestic enterprises.
- Tax resident enterprises in China are taxed on their worldwide income. Non-tax resident enterprises are taxed on China sourced income.
- CIT is at a flat rate of 25%.
- Starting from 1 September 2011, amended China individual income tax law will take effect.
- Individuals domiciled in China are subject to IIT on their worldwide income.
- Foreign individuals who are not domiciled in China and have not resided in China for more than five years may reduce their IIT liabilities on employment income under certain conditions. Employment income is subject to the progressive rates from 3% to 45% (effective 1 September 2011). Individuals carrying out sole-proprietary business in China are subject to IIT at progressive rates from 5% to 35%. Other incomes received by individuals are subject to IIT at a flat rate of 20%.
- Double taxation relief is offered through credit, exemption or reduction provided under national statutes and tax treaties.

## Principal taxes

The main applicable taxes when doing business in China are as follows:

1. Taxes on income:
  - CIT
  - IIT
2. Taxes on transactions – turnover tax system:
  - Value-added tax (VAT)
  - Business tax (BT)
  - Consumption tax (CT)
3. Other taxes:
  - Customs duties
  - Stamp tax
  - Vehicle and vessel tax
  - Motor vehicle acquisition tax
  - Deed tax
  - Land appreciation tax
  - Real estate tax
  - Urban and township land-use tax
  - Resources tax
  - Urban Construction and Maintenance Fee and Education Surtax
  - Other surtaxes and levies

## Corporate income tax

### Key messages

- Tax resident enterprises, which include enterprises incorporated in China and foreign enterprises whose effective management is located in China, are liable to CIT on their worldwide income.
- Accelerated depreciation is acceptable under certain circumstances.

- Amortisation of intangible assets is allowed.
- In principle, the accrual method of accounting is required.
- Income tax is levied at a flat rate of 25%.
- Dividends paid between qualified tax resident enterprises are exempt from CIT. However, non-tax resident enterprises are subject to a 10% withholding CIT (unless reduced under a tax treaty) on dividend income derived from China.
- Foreign tax credits are available.
- Qualifying high and new technology enterprises are eligible for a reduced tax rate of 15%. Other forms of tax incentives, which are in the forms of tax holidays, reduced tax rate, reduction of revenue, investment tax credit, etc. are also available for enterprises that are engaged in encouraged industries or which invest in research and development and specific equipment.
- Qualifying advanced technology service enterprises are able to enjoy certain preferential tax treatment and other support. In certain areas, various local financial subsidies are available for foreign investment.
- Arm's length prices must be used for transactions conducted between related parties.





## Corporate income tax system

### Residence concept

Enterprises incorporated in China are automatically tax resident enterprises. A foreign enterprise with its effective management located in China is also regarded as a tax resident enterprise. The effective management refers to the place where the overall management and control over the business and production, personnel, accounting, properties, etc, of an enterprise is, in substance, exercised. Tax resident enterprises are subject to CIT on worldwide income.

A non-tax resident enterprise, which has an establishment or place of business in China, is subject to CIT on the income derived by the establishment or place of business.

For a non-tax resident enterprise that has no establishment or place of business in China, or that has an establishment or place of business in China but the income derived from there is not effectively connected with the establishment or place of business, is subject to withholding CIT on China source income (generally includes passive income, such as, dividends, interest, royalties, rental income, capital gains, etc.).

To avoid double taxation of foreign sourced income, a foreign tax credit is allowed for income taxes paid to other countries on foreign-sourced income.

### Gross income

- **Inter-company transactions**

In principle, the CIT law requires an enterprise to conduct business transactions with its related parties in accordance with the arm's length principle. If a related-party transaction is not conducted at arm's length and there is a reduction of gross income or taxable income, the Chinese tax authorities are authorised to make the appropriate tax adjustment under general anti-avoidance rules.

- **Capital gains, interest, royalties and dividends**

Capital gains, interest and royalty income derived by a tax resident enterprise are taxable as ordinary income. The aforementioned capital gains refers to the gains from the disposal of property, including residential property, buildings, structures, and attached facilities located in China, and from the assignment of land-use rights and the direct or indirect transfer of the equity interests in Chinese enterprises. For any gain derived from the transfer of land-use rights, buildings and premises and related

facilities attached thereto, a land appreciation tax is also levied. Dividends paid between qualified tax resident enterprises are CIT exempt under the CIT law.

- **Service fees**

Service fees generated from consultation, management, training and other labour services by a tax resident enterprise are taxable as part of worldwide income, irrespective of the locality in which the services are performed.

- **Exchange gains and losses**

Exchange gains and losses incurred during business transactions and year-end translation in respect of monetary assets and liabilities denominated in foreign currencies should generally be accounted for in the current year and are taxed or deducted accordingly.

- **Donation and debt release**

Unless otherwise prescribed in the tax regulations, tax resident enterprises should include donations received and releases from debt as taxable income.

- **Non-taxable income**

Fiscal appropriation, governmental administration charges and governmental funds that are collected and administered as treasury management of the state are non-taxable income under the CIT law.

- **Tax-exempt income**

Tax-exempt income includes: interest on state treasury bonds; dividends paid between qualified tax resident enterprises; after-tax profit distributions derived by a non-tax resident enterprise which has an establishment or place of business in China from a tax resident enterprise and the said dividends are effectively connected with the establishment or place of business; income derived by qualified non-profit-seeking organisations; and financial subsidies, approved by the State Council and received by the enterprises, which are to be used for specific purposes.

### Deductions

- **Business expenses**

In principle, unless specifically excluded under the CIT law and other tax regulations, reasonable business expenditures including costs, expenses, taxes and losses, that are actually incurred by a tax resident enterprise and relevant to the generation of income, are deductible.

- **Depreciation**

The straight-line method of depreciation has to be followed and there is a minimum depreciation period for different types of fixed assets. Certain fixed assets, for example

fixed asset replacements due to advancement of technology or fixed assets that are subject to constant vibration or severe corrosion may be depreciated over a shorter period or under accelerated depreciation methods.

- **Leasing agreements**

Leased fixed assets are generally consistent with the accounting treatments under China Accounting Standards 2006.

- **Interest**

Interest on loans is generally deductible. On borrowings from non-financial institutions by a non-financial institution, the deductible interest expense cannot exceed commercial interest rate. Interest related to capital expenditure on assets before they are put into use should be capitalised, while interest incurred subsequently is deductible in the current period. However, the deduction of interest paid to related parties is subject to the thin capitalisation rule under the CIT Law. The thin capitalisation ratio for the financial industry is 5:1 and for other industries is 2:1.

- **Royalties and service fees**

Royalties and service fees paid by tax resident enterprises are generally allowed as a deduction, provided they are of a reasonable amount.

- **Employee remuneration**

Actual paid remuneration for employees of a reasonable amount can generally be deducted as an expense.

- **Staff welfare expenses**

Expenses incurred for basic social security contributions, supplementary pension insurance and supplementary medical insurance for local Chinese staff are deductible, subject to caps stipulated by the government.

Other staff welfare expenditure is deductible subject to wage bill cap of 14% of the total wage bill of an enterprise.

- **Insurance premiums**

Premiums paid for commercial insurance for investors or employees are generally not deductible, with a few exceptions.

- **Inter-company charges**

Reasonable inter-company charges that represent specific and active services provided by affiliated companies for the day-to-day operations of an enterprise in China are generally deductible, but subject to certain restrictions.

- **Other deductions**

- *Business entertainment expenses*  
Only 60% of actual incurred

business entertainment expenses are deductible. In addition, the total amount is capped at 0.05% of the total sales (business) revenue of the subject tax year.

- *Bad or doubtful debts*

Enterprises other than commercial banks are not allowed to deduct bad debt provisions for CIT purpose. Financial institutions can deduct bad debt provisions up to 1% of the incremental loan assets during the year for CIT purposes. Bad debt losses are deductible only when the loss is actually incurred and approved by the in-charge tax bureau.

- *Amortisation of intangible assets*

The straight-line method is allowed with a minimum amortisation period of not less than 10 years, or pursuant to the useful life prescribed in the laws or agreed in the contracts.

- *Advertising and promotional expenses*

The deduction is limited to 15% of the annual sales revenue. The cap is raised to 30% for certain specified industries. The remaining expenses can then be carried forward and deducted in future years.





- *Research and development (R&D)*  
Subject to approval, a tax resident enterprise that incurs qualifying R&D expenses for the development of new techniques, new products and new craftsmanship is entitled to an extra 50% deduction of the R&D spending.

- *Donation*  
Donation to qualifying charitable institutions is deductible up to 12% of the annual profit.

- *Commission fee and handling charges*  
The typical deductible rate is up to 5% of the corresponding income. Insurance companies are subject to higher deduction caps.

- *Pre-operating expenses*  
These could be deducted for CIT purpose at the start-up of the business.

#### **Non-deductible items**

The CIT law states that the items listed below are non-deductible in calculating the taxable income of a tax resident enterprise:

1. Payments in the nature of equity investment returns to investors such as dividends
2. CIT payments
3. Tax surcharges
4. Penalties, fines and losses due to the confiscation of property

5. Donations to institutions other than qualified charitable institutions
6. Sponsorship expenditures
7. Provisions
8. Other expenditure that is irrelevant to the generation of income

#### **Losses**

• **Tax loss**  
Tax losses sustained by a tax resident enterprise could be carried forward and deducted from the succeeding five years' taxable income. Tax loss carry-backs are not allowed.

• **Asset loss**  
Asset losses incurred by enterprises shall be deductible before tax after being declared with the in-charge tax authority in accordance with the prescribed procedures and requirements. Any losses which are not declared shall not be deducted before tax.

#### **Withholding CIT**

Non-tax resident enterprises that do not have an establishment or place of business in China, or those that have a permanent establishment or place of business but earn China sourced income such as dividends, interest, rent and royalties, that are not effectively connected

with that establishment or place of business, will be subject to withholding CIT at a concessionary rate of 10% (though the statutory standard rate is 20%) on such income sourced in China unless reduced under a tax treaty. Nevertheless, dividends distributed by a foreign investment enterprise out of its pre-2008 profit are still exempted from withholding tax.

The non-tax resident enterprises that are eligible to enjoy favourable income tax treatment under Double Tax Treaties agreed by China with the countries/regions where the foreign enterprises are tax resident, are required to follow certain formalities to claim the treaty treatments.

#### **Tax computation**

**Taxable income**  
Taxable income is defined as the amount from the gross income in a tax year after deduction of non-taxable income, tax exempt income, various deductions and allowable losses brought forward from previous years.

Taxable income in foreign currency should be converted into RMB to arrive at the taxable income.

#### **Tax rates**

The standard CIT rate is a flat rate of 25% for all tax resident enterprises and non-tax resident enterprises, which derive income effectively connected with their establishments or places of business in China.

#### **Foreign Tax credits**

A tax resident enterprise that generates foreign source income, may deduct the foreign income tax paid from the amount of CIT payable. However, the deductible amount may not exceed the amount of CIT otherwise payable in respect of the foreign source income. If the foreign tax paid exceeds the limit, the unrelieved balance of the foreign tax paid may be offset against the tax payable in subsequent years, up to a maximum of five years. An enterprise applying for a foreign tax credit must submit the original tax receipts to support its claim for a foreign tax credit.

#### **Consolidation**

A tax resident enterprise should make combined CIT filings for its branches. Except for rules otherwise prescribed by the State Council, affiliated companies are not permitted to file consolidated returns on a group basis.

#### **Tax reporting**

##### **Tax returns**

The tax year for enterprises is the calendar year. Tax resident enterprises are required to file their annual income tax returns and annual financial statements within five months after the end of a tax year, together with an audit report issued by a Chinese-registered CPA firm, or a verification report issued by a Chinese registered CTA firm. Generally, non-tax resident enterprises with their establishment or place of business in China shall file the annual CIT documents within five months after the end of the calendar year. There are exceptions such that certain non-tax resident enterprises may not need to perform the annual CIT filings.

There is a late payment surcharge of 0.05% of the unpaid tax balance for each day the income tax is in arrears. If the taxpayer fails to file a return or pay the tax due, an additional fine may be assessed.

As withholding agents, the payers who make payments of dividends, interest, rent, royalties or other income to non-tax resident enterprises are required to file a withholding tax return,

withhold the proper tax and remit the tax to the tax authorities once payments to non-tax resident enterprises are made or accrued as deductible expenses in the account of the payers for CIT purposes. Under certain circumstances, if the withholding agent has failed to fulfil the withholding obligation, the non-resident enterprises are required to perform the withholding tax procedure by themselves.

##### **Assessments**

Enterprises are required to make provisional assessments and file CIT returns on a monthly or quarterly basis. The returns are generally prepared on a self-assessment basis and the provisional payments are reconciled after the year-end in an annual return for final tax settlement. Any tax discrepancy shall be paid within five months after the year-end and any tax overpayment may be refunded upon approval by the tax authorities.

## Personal Income Tax

### The scope of Chinese individual income tax (IIT)

The basic rules governing expatriate taxation in the People's Republic of China (PRC) are set out in the 'Individual Income Tax Law of the PRC' and in the 'Detailed Regulations for the Implementation of the Individual Income Tax Law of the PRC'. These rules are supplemented by various administrative rulings of the Ministry of Finance and the State Administration of Taxation which, although not codified, do have the force of law.

International assignees coming to work in the PRC are generally liable to Chinese income tax on employment or self-employed income related to their work in the PRC. They are also liable to IIT on any interest and rental income earned in the PRC. Capital gains derived from the sale of property in the PRC are also liable to IIT. There is currently no inheritance or wealth tax.

### Taxable income

Individual income is categorised as follows:

- Wages and salaries;
- Production or business income derived from individual industrial or commercial enterprise;
- Income from sub-contracted operations;

- Compensation for personal services;
- Income from authorship;
- Royalties;
- Interest and dividends;
- Income from the lease of property;
- Income from the transfer of property;
- Incidental income; and
- Other kinds of income specified by the Ministry of Finance.

### Taxation of employment income

Foreign individuals are liable to PRC IIT on employment income based on:

- Residence status – the term 'residence' is generally interpreted as 'physical stay' or 'temporary stay';
- The source of their income; and
- Whether or not they are connected to a PRC employer.

The source of employment income is normally determined by the location where the service is provided.

Taxable employment income under this 'wages and salaries' category includes basic wage/salaries, awards, bonuses,

hardship and foreign service allowance, and insurance, etc. Taxable income can be in the form of cash, in-kind benefits, marketable securities and any other forms of economic benefits. Reimbursements of business-related expenses to employees and certain non-taxable fringe benefits provided to foreign individuals, if the amount is reasonable and supported by valid receipts, are not taxable.

### Liability to tax: Less than 90 days (or 183 days for treaty countries)

In general, non-domiciled individuals (e.g. foreign individuals) who derive income from work and services performed in the PRC are subject to PRC IIT unless they are present in the PRC for not more than 90 days in the calendar year concerned and their income is not paid or borne by any PRC entity/establishment.

The term 'domiciled' normally refers to the place where the individual habitually resides by reason of household registration, family or economic benefits.

If the foreign individual is a tax resident of a country/region which has entered into an income tax treaty/agreement with the PRC, the said 90-day threshold may be extended to 183 days within the base period as specified in the income tax treaty/agreement.



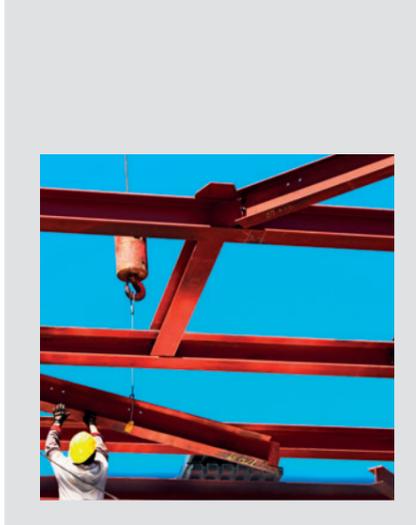
In other words, the individual will generally be exempted from PRC IIT if his/her cumulative stay in the PRC does not exceed 183 days in a calendar year concerned or in any 12-month period (this base period varies from one treaty to another) and his/her remuneration is not paid for by any PRC enterprise or a permanent establishment.

Individual treaties may differ and a review of the relevant treaty is therefore recommended. [Note: For the purpose of counting the 90/183-day threshold, any part of a day in the PRC is counted as one day in the PRC.]

To enjoy 183 days treaty exemption, foreign individuals are required to make record-filing. Treaty benefits are not granted automatically unless proper record-filing is accepted by local tax bureaus.

### Liability to tax: More than 90 days (or 183 days for treaty countries) but less than one full year

For a foreign individual who has resided in the PRC for a period or periods exceeding in the aggregate 90 days (or 183 days where a tax treaty applies) but less than one full year, his China sourced income will be subject to PRC IIT regardless of whether the salary is borne by a PRC or foreign entity. However, his non-China sourced income will not be liable to PRC IIT.



A 'full year' of residence in the PRC means individuals having stayed in the PRC in a calendar year with temporary absences from the PRC for not more than 30 consecutive days or 90 days in total.

For example, an individual with one 35-day trip outside the PRC during the year will not be considered as having a full year of residence for that calendar year. Similarly, an individual with cumulative absences of 100 days during the year (even if any single trip is for less than 30 days) will also not be considered as having a full year of residence for that calendar year.

**Liability to tax: More than 1 year but less than 5 consecutive full years**

A foreign individual who has resided in the PRC for one full year or more but not more than five consecutive full years is subject to PRC IIT regardless of whether the salary is borne by a PRC or foreign entity. In addition, his non-China sourced income will also be subject to PRC IIT but only to the extent that such income is borne by a PRC entity.

**Liability to tax: More than 5 consecutive full years**

A foreign individual who has resided in the PRC for more than five consecutive full years

will be subject to the PRC IIT on his worldwide income for every subsequent full year of residence in the PRC.

However, regardless of the length of the stay in the PRC and the location of the payment, the PRC sourced income (see examples below) is taxable according to the PRC IIT law and regulations:

- Bank interest derived from deposits in a bank located in the PRC (effective from 15 September 2008 onwards, bank interest income is exempted from PRC IIT until further notice);
- Fees for the use of proprietary rights within the PRC;
- Rental income related to the lease of property within the PRC; and
- Interest paid by the Chinese government or enterprises in the PRC.

**Double-taxation relief**

A foreign individual who is subject to PRC IIT on his/her worldwide income may claim a foreign tax credit on non-PRC sourced income that is subject to tax in another tax jurisdiction. The amount of the credit is, however, limited to the amount of PRC IIT payable on the same income. Excess credits may be carried forward for not more than five years.

**Tax rates and calculation of tax liability**

The PRC IIT rates vary depending on the category of income. For salaries and wages (i.e. employment income), the applicable IIT rate is based on a progressive scale ranging from 3% to 45% (effective 1 September 2011). Although the standard monthly deduction (i.e., taxable income threshold) is increased from RMB2,000 to RMB3,500 for Chinese individuals effective from

Amended tax rates and brackets		
Grade	Monthly taxable income** (RMB)	Tax rate (%)
1	1,500 or less	3
2	The part > 1,500 and ≤ 4,500	10
3	The part > 4,500 and ≤ 9,000	20
4	The part > 9,000 and ≤ 35,000	25
5	The part > 35,000 and ≤ 55,000	30
6	The part > 55,000 and ≤ 80,000	35
7	The part > 80,000	45

\*\* The monthly taxable income from wages and salaries shall be the balance after the standard deduction (local Chinese [RMB3,500] / foreigner [RMB4,800]) from the monthly income

1 September 2011, the standard monthly deduction for foreigners remains at RMB4,800. The new tax rate table effective from 1 September 2011 is set out as opposite.

**Other income**

Income other than employment income is generally taxed differently depending on the income category.

**Administration of the regime**

The PRC tax year runs from 1 January to 31 December.

The tax filing is administered on a monthly basis.

**Registration with the Chinese tax authorities**

Subject to the practice of the competent local tax bureaus, foreign individuals who are liable to PRC IIT may be required to register with the local tax authorities. Registration should be made with the local tax bureau in the location where the individual usually works.

Registration, if required, usually takes place upon arrival in the PRC for employees of foreign investment enterprises and for resident representatives of representative offices of foreign companies. Other individuals should register at such time as they become liable to tax (i.e. an employee of a foreign employer

on work-related assignments in the PRC for more than 90 days or 183 days for a tax resident of a treaty country in a year) provided his/her income is not paid/borne by any PRC entity/establishment.

A fine of up to RMB2,000 may be imposed on an individual who fails to perform the tax registration. Further fines may be imposed if the taxpayer fails to remedy the situation within prescribed time limits.

**Tax filing frequency**

Monthly tax returns are normally due on the 15th of the following month and the tax is normally payable upon submission of the monthly tax returns. In practice, the tax filing due date varies from one location to another and there are also circumstances where the tax filing is done on an annual basis instead. Also, except for certain circumstances as stipulated by the law, the employing entity in the PRC is the statutory tax withholding agent for the employees/ assignees. In addition, starting from the calendar year 2006, individuals whose annual income exceeds RMB120,000, or US\$19,113 converted at the exchange rate of 6.2787, (except for foreign individuals who are physically away from the PRC for more than 30 days in a single trip or for more than 90 days in total in the calendar year concerned) are required to file annual tax returns to declare their personal income from all sorts (e.g. income from

employment, consultancy, interest and dividend, gain of disposal of property etc.). This annual tax return should be filed within 3 months after the end of the tax year (i.e. 31 March).

**Tax filing**

If your tax has been remitted or withheld by your employer who files monthly withholding tax returns for you, you do not need to file monthly income tax returns again unless you have other categories of income earned during the month. Annual tax returns should also be filed by certain individuals.

The regular due date for filing a monthly individual income tax return in the PRC and payment of tax due is the fifteenth day of the following month. The said due date may be different depending on the local practice. Annual tax returns, if required, should normally be filed within 3 months after the end of the tax year.

Your local tax authority will verify the correctness of your returns. Evidence of the salary and other remuneration details (e.g. confirmation letter issued by the employer) may be required. This document, sometimes referred to as an 'income certificate', is also required for tax registration and whenever there is a change in the remuneration details. In the case of tax audits, a copy of the employment contract or copies of tax returns filed in the home

country may also be required. A consolidated tax receipt will normally be issued by the tax authority to the withholding agent, i.e., the employer, for total tax withheld and paid by all its employees after the monthly withholding tax return has been filed and verified. A tax payment certificate may be issued by the tax bureau to the individual taxpayer on an annual basis or upon request.

### Extensions

Extensions for monthly tax filing and tax settlement may be granted only upon application and approval by your local tax authority. In practice, it would be very difficult to secure the approval from the tax authority for such extension.

### Penalties and surcharges

Late payment surcharge computed at the rate of 0.05% per day will be imposed on the amount of tax in arrears. A penalty of up to RMB2,000 may be imposed for failure to file a return and pay tax within the prescribed time limits. A further fine of RMB2,000 to RMB10,000 may be imposed if the taxpayer or withholding agent fails to remedy the situation. In addition, in the case of tax evasion, tax authorities can impose a penalty ranging from 0.5 to 5 times the amount of tax overdue on the taxpayer or the withholding agent.

### Tax de-registration

When you leave the PRC, you may need to de-register with the local tax bureau for tax purposes.

### Social security

The long-awaited PRC Social Security Law ('the Law') has been taken effect from 1 July 2011. The Law will have implications to Chinese individuals as well as foreigners working in the PRC.

The Ministry of Human Resources and Social Security in China has invited comments from the public on its draft interim measures for the participation of foreigners employed in China ('Draft Interim Measure') in the Chinese social security system. The salient points in the Draft Interim Measures are as follows:

- The draft rules are applicable to foreigners (including residents of Hong Kong, Macau and Taiwan) lawfully working in China and holding appropriate work permits. They may be locally employed or employed overseas and on secondment to work in China.
- Similar to Chinese national, foreigners working in mainland China should contribute to the following social security insurance:
  - Basic pension fund
  - Basic medical insurance
  - Work-related injury insurance
  - Unemployment insurance
  - Maternity insurance
- If foreigners leave China before the mandated date for drawing pensions, their accounts can either be maintained, as they may return to work in China, or terminated. If terminated, the amount accumulated in the account may be withdrawn in a lump sum upon approval by the relevant authority.
- Foreigners holding citizenship of countries with which mainland China has entered into bilateral or multi-lateral Totalization Agreements could be exempted from contribution to specific types of social security in accordance with the relevant agreements.

On 2 December 2011, the Ministry of Human Resources and Social Security issued circular Renshetingfa [2011] No 113 to further clarify some points of concern/uncertainty

arising from the aforementioned regulations that affected foreigners participating in the social security scheme. Following this, some cities, such as Beijing, Tianjin, and Guangzhou, have released the local implementation/practice details.

## Turnover Taxes

### Key messages

- Nearly all transactions in China are subject to a turnover tax, either value added tax (VAT) or business tax (BT). Certain categories of consumable goods are also subject to consumption tax (CT).
- The standard rate of VAT is 17%. Reduced rates and exemptions are available.
- BT rates range from 3% to 20%.

### Value-added tax (VAT)

- **Scope**  
The sale of taxable goods and the provision of labour services in relation to the processing of goods and of repair and replacement services within China are subject to VAT. 'Taxable goods' refers to tangible goods as well as certain utilities such as electricity, thermal power and gas, but the term excludes real estate properties. VAT is also levied on the import of taxable goods into China unless the imports are specifically exempt under special rules.
- **Registration**  
Enterprises that make sales taxable for VAT purposes in China should voluntarily register for VAT with the local tax authority. VAT payers are generally classified into two categories: general VAT payer and small-scale VAT payer.

- **Rates**  
General VAT payers are subject to the standard rate of 17% which applies to most taxable goods and services and the lower rate of 13% which applies to certain goods. Small-scale VAT payers are levied at the rate of 3%. The sale of certain goods is exempted from VAT.
- **Basis of taxation**  
VAT is levied and collected on the basis of the value added to the taxable goods or services at each stage of a production chain, i.e. from the acquisition of raw materials by producers to the purchase of finished goods or services by consumers. At each stage, VAT on sales (output tax) is collected by the seller from the purchaser. With the support of a valid VAT invoice, the general VAT payer can usually deduct the VAT that has been paid on the purchase of goods (including fixed assets) that are used for the taxable sales (input tax) and account for the difference to the authorities.
- **VAT on exports**  
Exporters of goods from China may be entitled to a refund of input VAT incurred on the exported goods. As the refund rates ranges from 0% to 17%, exporters may not be able to enjoy the full refund of input VAT incurred and suffer a certain degree of VAT costs on exports.
- **VAT Reform Pilot Program**  
China is transforming the BT regime to VAT regime with an aim to repeal BT over a period of time. A VAT Reform Pilot Program was introduced on 16 November 2011. Shanghai is the first city to participate in the VAT Reform Pilot Program and Beijing will be the next city to join the program in 2012.  
  
The current VAT Reform Pilot Program in Shanghai only covers

Transportation and certain 'Modern Service Industry'. 'Modern Service Industry' includes the business activities of providing technology or expertise-based services for the manufacturing industry, cultural industry and modern logistics industry, including research, development and technological services, information technology services, cultural innovation services, logistics supports, lease of corporeal movables, attestation and consulting.

The VAT Reform Pilot Program may extend to other industries such as the financial services industry when the circumstances warrant it.

In addition to the existing VAT rates of 13% and 17%, the VAT Reform Pilot Program introduced two additional VAT rates of 11% and 6%. The transportation industry and Modern Service industry are covered by the VAT Pilot Reform Program are subject to 11% and 6% respectively.

Foreign enterprises which fall within the scope of 'Modern Service Industry' receiving payments from enterprises located in Shanghai should be subject to 6% withholding VAT instead of the 5% BT. The payers in China should be the withholding agents.

### Business tax (BT)

- **Scope**  
Service income shall be taxable for BT purpose, regardless of whether the services are rendered onshore or offshore China (excluding processing services and repair and replacement services, which are taxed under the VAT regime). In addition, certain specified services in culture and sport industry, entertainment industry, other special services etc rendered offshore are exempt from BT.

It also applies to the transfer of intangible assets such as goodwill, patents and the sale of real estate properties in China. BT and VAT are mutually exclusive. However, some lines of certain industries may be exempt from the BT.

- **Rates**  
BT rates are 3% or 5%, except for the leisure and entertainment industry which may attract a rate of up to 20%. For qualified foreign institutional investors, an exemption to BT is granted on their income derived from securities trading through domestic securities companies. It is not recoverable but may be deductible for income tax purpose.
- **Registration**  
Enterprises that provide services or sell intangible assets or properties within the scope of BT should voluntarily register for business tax with the local tax authority.
- **Basis of taxation**  
Unlike VAT, business tax is not a creditable tax and is generally levied on the gross income. Business taxpayers in certain specified industries are allowed to compute BT liabilities on a net basis.
- **Tax reporting**  
As withholding agents, the payers who make service fee payments to non-resident enterprises are required to withhold BT before the outbound remittance could be made.

### Consumption tax (CT)

CT is imposed on 14 categories of goods, including cigarettes, alcoholic beverages, certain luxury and environmentally harmful items. It is not recoverable but is deductible as expenses for income tax purposes. CT is computed based on the sales amount and/or the sales volume depending on the goods concerned.

# Audit and accountancy

## General accounting principles and regulations

In 2006, the Ministry of Finance issued new Chinese Accounting Standards (CAS 2006). It is expected that these new accounting standards may become a requirement for FIEs in the next few years. In general, these new standards reflect all IFRS principles, although several differences exist to reflect unique circumstances in China.

CAS 2006 is effective from 1 January 2007 for all listed companies; other companies are encouraged to adopt CAS 2006, but they still have other alternatives.

The Ministry of Finance in late 2011 issued the Accounting Standards for Smaller Business Enterprise with a view to simplifying and standardizing the accounting standards for smaller business enterprises. The Accounting Standards for Smaller Business Enterprises are supplement to CAS 2006. This will become effective from 1 January 2013 for companies that fall within the category of 'small business enterprise'.

According to CAS 2006, basic financial statements such as balance sheet, income statement (profit and loss account), statement of changes in equity, cash flow statement, and notes to financial statements are all required according to CAS 2006.

An enterprise shall adopt the accrual basis of accounting in performing recognition, measurement and reporting for accounting purposes. All income realised and expenses incurred or attributable to the current period should be recognised as income or expenses in the current period regardless of when the income is received or expenses are paid.

An enterprise shall disclose the following information related to its parent and subsidiaries in the notes, irrespective of whether there have been transactions with those related parties:

- Names of the enterprise's parent and subsidiaries.
- Nature of business of the subsidiaries, place of registration and registered capital (or paid-in capital or share capital) and changes therein.
- Proportion of shareholdings and voting power of the parent over the enterprise, and that of the enterprise over the subsidiaries.
- Where there have been related-party transactions between an enterprise and its related parties, the enterprise shall disclose the nature of the related-party relationships, the types of transactions and the essential elements of the transactions in the notes.

## Books and records

The accounting year of an enterprise shall start on 1 January and end on 31 December.

The accountancy law stipulates that companies must keep three kinds of primary accounting records: journals, a general ledger and subsidiary ledgers, as well as appropriate supplementary memorandum records. Computerised accounting systems, if utilised, can be regarded as the venture's accounting records.

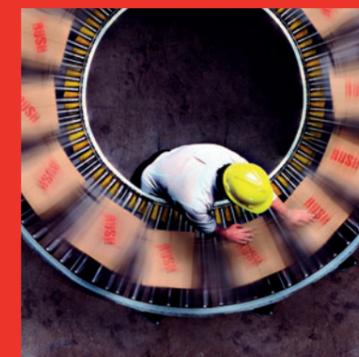
All accounting documents, books and statements prepared by a FIE must be written in Chinese, however, they may also be written concurrently in a foreign language.

Books and records should be recorded in renminbi (RMB), unless agreed otherwise by relevant authorities and partners. If a foreign currency is used, the financial statements must be converted into RMB at year-end for the preparation and auditing of the annual financial statements. Typically, most foreign-invested enterprises choose to record their books in RMB because their income and expenses are largely denominated in the local currency.

## Audited financial statements

FIEs are required to engage a Chinese-registered CPA firm (including an approved Sino-foreign joint venture CPA firm) to audit their statutory annual financial statements. It is generally the duty of the board of directors of a FIE to appoint the auditor. A foreign CPA firm may also be engaged alongside a local CPA firm in performing auditing or related work, but the Chinese-registered CPA firm must issue the report.

Audits are required under company law, accounting regulations and income tax laws in China, and audited financial statements should be filed with the tax authorities, together with the annual income tax returns. FIEs are required to provide the auditors with all the enterprise's documents, books and reports. The accounting statements to be submitted for an annual audit include the balance sheet, income statement, statement of cash flows and relevant supporting notes. The audited financial statements must be submitted to a number of government authorities, including the local offices of the SAIC, SAT, the local Finance Bureau and the SAFE. Audited financial statements must be submitted to the relevant authorities within four to six months of the year end, depending on local government requirements.



# Human Resources and Employment Law

## Contracts and Unions

### Legal environment

Effective from 1 January 2008, a new Labour Contract Law was enforced in China. This Labour Contract Law is formulated with the purpose of governing the establishment of employment relationships, and the conclusion, performance, amendment and termination of labour contracts between the employer and the employee.

This Law encourages employers to enter into long-term or non-fixed term employment contracts with employees, and sets more strict regulations for the termination of employment, stipulating conditions of termination and increasing any relevant costs. It also increases the penalties for violation of the Labour Contract Law and other related regulations.

### Recruitment

Recruitment methods differ for FIEs and representative offices (ROs) of foreign companies in China.

FIEs, for instance, joint ventures and WFOEs, are able to employ staff from the local workforce directly. Joint ventures normally do so through recommendations from their

Chinese partner or the local authorities. Staff from the original manufacturing plant of the Chinese partner will often be employed by the joint venture. WFOEs normally have a free hand in recruiting staff locally. However, due to a lack of local networking, they will often need to rely on professional firms, mass media, or other methods to recruit managerial level staff.

Recruiting local staff is different for ROs, which are required to hire staff through an authorised labour agency. There are several available authorised labour agencies in China, such as the Foreign Enterprise Service Corporation (FESCO) and China International Intellectech Corporation (CIIC). The labour agency is the legal employer of the staff and seconded them to the representative office to provide agreed services. In practice, representative offices need to establish a contractual relationship with the labour agency and pay the required service fee. As the staff working for representative offices are the employees of the agency, many representative offices in China choose to enter into a separate agreement with the staff stipulating the terms and conditions of the engagement.

### Termination of employment

Unlike practices in many other countries, 'employment at will' is not permitted in China. Employers have to follow certain procedures and conditions to terminate the employment with the staff, e.g. upon contract expiration, or where the employee is proved to be unqualified, violates the enterprise's rules and regulations or discloses criminal convictions. In addition, staff may be made redundant as a result of production or technical changes. However, it is not permitted to dismiss staff who undergo stipulated medical treatment, who lose their ability to work due to an occupational disease or a work-related injury, or who are on pregnancy or maternity leave or who are breast-feeding their children. To terminate an employment relationship with staff, enterprises may need to give a statutory termination notice and provide required severance payment. By law, the severance payment is calculated based on the actual service years and the salary level of the staff.

In China, ROs are also able to terminate their staff. As they do not have an employment relationship with the seconded staff, representative offices may terminate the service of these staff through their engaged agency.



The service agreement between representative offices and the labour agency serves as the guidance of the termination.

### **Employer/employee relations**

The Chinese government is now enforcing the Trade Union Law. According to the Trade Union Law, companies are required to support employees to set up a trade union and provide funds equivalent to 2% of the company's total salary costs for the activities of the trade union. For activities related to employees, for example, re-organisations and layoffs, the company shall notify the trade union and heed its comments before taking action.

## **Immigration Rules**

### **Visas**

As an international assignee coming to the PRC to take up an employment, one is required to apply for a work visa; i.e., single entry 'Z' visa. Within 30 days after arrival, an international assignee is required to apply for a foreign resident permit (formerly known as 'multi-entry 'Z' visa') with the local Public Security Bureau. Chinese visas may be obtained from a Chinese embassy or consulate in any foreign country with which the PRC has diplomatic relations. 'Z' visa holders are allowed

to take up employment in the PRC. An initial 'Z' visa cannot be issued within the PRC. International assignees who have entered into the PRC with visas other than 'Z' visas must leave the PRC to apply for 'Z' visas and then re-enter into the PRC again. To take up employment in the PRC, an international assignee must apply for employment permit and residence permit.

To obtain an initial 'Z' visa, one would normally be required to submit an 'invitation letter' issued by a sponsoring entity in the PRC. Other required documents may vary depending upon the type of visa to apply. An employment licence is required to apply for Z visa 'invitation letter' from the duly authorised unit in PRC.

### **Working Card**

Registered representatives of a representative office need to apply for a Working Card with the local Administration for Industry and Commerce. Foreign employees who are not registered under a representative office are not required to apply for a Working Card, but instead they will need to apply for an employment permit with the local Labour Bureau. In light of China immigration criteria, the limitation of non-local hiring under one representative office is 4 (take Shanghai for instance), including foreigner and Hong Kong/Macau/Taiwan residents. In other words, if your

representative office has already hired 4 expatriates, it is not allowable to hire more.

### **Employment Licence**

An entity in the PRC which employs a foreign individual is required to obtain an Employment Licence from the local Labour Bureau.

### **Employment Permit**

All international assignees are required to obtain an Employment Permit from the local Labour Bureau.

### **Registration with the Public Security Bureau/Foreigner Residence Permit**

If you are an international assignee working in the PRC, you and each of your accompanying family members over 18 years old must first obtain a health certificate from the local International Travel and Health Care Centre. After the certificate has been obtained, you can register with the Public Security Bureau and apply for a Foreigner Residence Permit to be affixed on your passport. The following documents are normally needed when applying for a foreigner residence permit:

- 'Z' visa;
- Copy of business licence or business registration certificate of your employer;
- Passport;

- Working Card/ Employment Licence;
- Employment Permit;
- Photographs;
- Physical examination report for anyone over 18 years old;
- A Registration form of Temporary Residence is required for all non-Chinese residents which should be applied for within 24 hours after arrival – you may get it from hotel/serviced apartment after your check-in; and
- Marriage certificate or birth certificate for accompanying family members.

## **Working conditions**

### **Wages and salaries**

In China, enterprises have the right to set their own remuneration package, including compensation and benefits. Pursuant to PRC Labour Contract Law, the wages of staff shall not be lower than the minimum wage in the location where the company is registered.

In addition to compensation, enterprises may also implement effective incentive programmes, e.g. sales incentives, performance bonuses, stock options, and the like, in order to attract talent. This is of great importance for positions in management and sales, which are often the driving force behind company performance.

In terms of payroll, salary shall be disbursed to the staff at least once a month in local currency. The date of disbursement can be decided through an agreement between the company and staff. The wage paid to staff shall not be deducted or delayed without justification. Delayed payroll disbursement may lead to a financial penalty. In addition, the company is responsible for withholding PRC individual income tax that is payable from staff gross compensation.

### **Fringe benefits**

In China, employers and employees are required to participate in a social benefits system. As a result, they are obliged to make contributions to the statutory social insurance programmes based on the schemes for different locations. For a majority of the workforce, whose salary level falls within the local social insurance contribution base, the social insurance contribution could be between 35-40% of their salary cost. The social insurance programmes cover the following social insurance and funds:

- Pensions;
- Medical insurance;
- Unemployment insurance;
- Work-related injury insurance;
- Maternity insurance; and
- Housing fund.

To participate in social insurance programmes, enterprises need to register with the relevant labour bureau, set up an account with a social insurance management authority and pay the required insurance premiums on a monthly basis. Apart from employer premiums, companies shall withhold the premiums of employees from their monthly salary and make the payment to the relevant authority. For representative offices, because they are not legal entities, premiums should be paid via the authorised labour agency.

In addition to statutory social insurance, enterprises in China also provide supplementary benefit schemes to their employees as a way to attract and retain local talent.

### **Working hours**

The working hours per week were reduced from 48 to 44 hours in March 1994, then further reduced to 40 hours in May 1995 by the State Council. In general, overtime is not encouraged, though permissible under special circumstances.

Overtime pay is higher than that for normal working hours, ranging from 150% up to 300% of normal wages, depending on whether the overtime is during weekdays, rest days or statutory holidays.

# Trade

## Key messages

- China's accession to the WTO had a great impact on regulations and practices in terms of customs and trade laws.
- Approved foreign-invested enterprises, for example, can now import and export directly and in their own name, without the use of a local import/export agent or a trade corporation.
- Many imports are regulated through a licensing system and by commodity inspection.
- Some items are restricted by the Chinese government.
- Most imported goods are subject to customs duty and import VAT.
- Various exemptions and reductions from customs duty and import VAT are available.

## Customs procedures

The Customs Law of the People's Republic of China was first issued in July 1987. Amendments were approved by the National People's Congress Standing Committee on 8 July 2000 and it took effect on 1 January 2001. The revisions aim to empower Customs with more administrative authority, promote the transparency of customs procedures, and make customs practices more consistent with international best practices, as embodied in the Revised Kyoto Convention for the Simplification

and Harmonisation of Customs Procedures.

Under the Customs Law of the PRC, importers and exporters must register with Customs before filing customs declarations. Importers should file declarations to Customs at the port of entry within 14 days of the goods' arrival. Exporters should file the declaration within 24 hours before the goods are loaded. Customs will review the documents submitted and will randomly perform examinations of the goods. The maximum period for examination on imports should be around 48 hours. The majority of goods are cleared within 48 hours. However, in practice, it may take longer for importers to clear goods from the port due to restrictions in Customs resources.

Customs duty must be paid to a designated Customs bank account within 15 days after the duty memo is issued. Surcharges will be imposed for late payments, which will be calculated at the rate of 0.05% per day on the total amount of customs duty and import VAT due.

## Tariff rates

Tariff rates shall be determined per the tariff codes, which are known as the Harmonised Commodity Description and Coding System (HS), and the origin of the goods. China adopted the HS coding system with effect from 1 January 1992. China adopted the 2007 version of the HS on 1 January 2007. Imported and exported goods should be classified according to the corresponding HS codes.

Since WTO accession, China has lowered the tariff rate gradually. By 2007, all of China's multilateral WTO tariff reduction commitments had been fulfilled. Further unilateral tariff reductions are unlikely.

The PRC tariff book sets out different types of tariff rates: most-favoured-nation tariff rates, preferential tariff rates, general tariff rates and interim tariff rates.

The most-favoured-nation tariff rate is applicable to imported goods whose place of origin is a member country of the WTO.

The preferential tariff rate is applicable to imported goods whose place of origin is a country or region that has concluded a bilateral or regional free trade agreement. Currently, prominent examples include the

Asia-Pacific Trade Agreement, China-Pakistan Free Trade Agreement, China-Chile Free Trade Agreement, China-ASEAN Free Trade Agreement, the Closer Economic Partnership Arrangement with the Hong Kong and the Macau special administrative regions and Economic Cooperation Framework Agreement with Taiwan. The list of countries in which a preferential tariff rate is applicable will continue to grow, as China is actively negotiating free trade agreements with several trading partners.

The general tariff rate is the highest tariff rate and it is applicable to imported goods whose place of origin is unknown. In practice, the place of origin is usually known. This means that the MFN tariff will be applicable, unless a lower preferential or interim tariff can be used.

The interim tariff rate is applicable to selected imported goods and it is reviewed annually by the Tariff Committee under the State Council. An interim tariff rate is normally 0%, 1% or 3% and is set to support the country's industry policy. For example, most commodities and aviation parts are subject to an interim tariff rate of either 0% or 1%.

China has applied a 0% tariff rate since 2003 for goods

covered by the Information Technology Agreement (ITA).

## Duty exemption and duty reduction

China has issued various regulations to stimulate foreign investment and development of certain sectors of the economy.

Exemptions from customs duty and import VAT are granted for machinery and equipment imported by an enterprise if the project is recognised as encouraged industry per the Foreign Investment Industry Guidance Catalogue and the Most Encouraging Industry, Products and Technology Catalogue. The Catalogue has been updated several times. The latest Foreign Investment Industry Guidance Catalogue was issued in 2007 by the National Development and Reform Commission (NDRC) and the Ministry of Commerce. The latest Most Encouraging Industry, Products and Technology Catalogue was issued in 2005.

There are other restrictions around this preferential policy, namely the machinery and equipment to be imported shall be within the total investment or the self-generated funds of the importer, restricted for 'self-use', and the equipment should not fall into the Catalogue of Goods of Non-Exemption

for Foreign Investments or the Catalogue of Goods of Non-Exemption for Domestic Investments.

Equipment and machinery imported but exempt from customs duty and import VAT is under the supervision of Customs for a period of 5 years from the date of importation. During the supervision period, the equipment and machinery should not be transferred, sold or otherwise disposed of without the pre-approval from Customs.

## Anti-dumping

China will utilise trade remedy measures, i.e. levying an anti-dumping duty, countervailing duty or safeguard duty, to protect the domestic industry from material injury or the threat of material injury. Of these three trade remedy measures, anti-dumping is most frequently used.

According to Chinese regulations, anti-dumping complaints may be brought to the MOFCOM in writing by any natural person, legal person or organisation from the domestic industry or on behalf of the domestic industry.

The application should contain details such as the full description of the products, the volume and price of domestic production of the product.



The volume and price of the imports and the impact of the imports on the domestic industry should also be stated. Evidence should be presented to justify the existence of dumping, the damage caused to the domestic industry, and the causal link between the dumping and the injury.

MOFCOM is responsible for investigating and determining dumping and injury. Investigations should be completed within 12 months from the date that the case is established. The period can be extended by six months in special cases.

Anti-dumping duty rates can be imposed for a period as long as five years, unless the period is extended for special reasons.

#### **Customs valuation**

The customs value is determined following the customs valuation methodologies as set out in PRC Customs Valuation Measures. These measures essentially implement the Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994.

The value for customs duty calculation purposes is the CIF (Carriage, Insurance and Freight) price.

The primary valuation method is the Transaction Value method and this is applied over 95% of the time. Where the Transaction Value method cannot be used, the customs value shall be assessed by applying the alternative methods sequentially.

China has applied the provisions of the decision on the treatment of interest charges for customs valuation purposes and the decision on the valuation of Carrier Media Bearing Software for Data Processing Equipment (G/VAL/5).

Valuation remains one of the more complex areas of customs law. Since implementation of the WTO-based customs valuation rules in 2001, this area remains one of the most controversial from an importer's perspective. It is an area of focus for Customs, and re-assessments in the declared value result in additional customs duty and import VAT liabilities.

For example, royalty and licence fees, which are related to imported goods and paid as a condition of the import sale, are dutiable for customs valuation purposes.

#### **Customs bonded zones**

There is now an increasing number and variety of bonded zones throughout China. These bonded zones allow different types of activities to be performed and carry different conditions from a customs, tax and foreign exchange point of view. These special bonded zones are routinely available to foreign-invested enterprises. The special bonded zones are summarised below. Bonded warehouses have been established for a long time and can be used to temporarily store imported and exported goods. Bonded warehouses can be 'public' or 'private' in nature.

Free Trade Zones (FTZ) have also been established for a long time, and can be used for bonded manufacturing as well as other operations, such as a bonded regional distribution centre.

Export Processing Zones (EPZ) are well established, and have been historically used for bonded manufacturing for export. The allowable business activity in an EPZ is now being expanded to include activities like research and development, testing and repair.

Bonded Logistics Parks (BLP) were newly introduced in 2004 and 2005 to promote the logistics industry, and feature bonded stored and

similar processing only (fully fledged manufacturing is not allowed). There are eight BLP located in selected coastal cities, generally adjacent to the port areas. BLP are also favourable for export VAT refund purposes.

Bonded Logistic Centres (BLC) are also another newly-introduced bonded zone. The most prominent public BLC is located in Suzhou. It is expected that new public and private BLC will be introduced throughout China in the years ahead.

The Zhuhai Cross-Border Industrial Park is another newly-introduced facility, which consolidates the bonded logistics, bonded manufacturing and international trade functions. This bonded zone also allows repair and CEPA privileges.

Export Supervision Warehouses (ESW) are also new and are designed for the temporary storage of exported goods. Pilot programmes are being carried out for selected ESW in Shenzhen and Xiamen. Exporters can claim an export VAT refund upon exporting into the ESW.

For all bonded zones, customs duties and import VAT will not be levied on imported goods that enter the facility. If imported goods are sold on the domestic market, they will

then become subject to both customs duty and import VAT. The cost of bonded storage can be included in the customs value for duty assessment purposes.

#### **RMB Trade**

The Pilot RMB Trade Settlement Scheme was announced in April 2009, coming into effect in July 2009. The trial locations in the PRC may opt to use RMB settlement when conducting cross-border trade with overseas companies. Cross-border RMB settlement and clearance can be done through designated banks in certain area.

# Banking in China

## Types of Accounts

Depending on its structure, a company needs to set up different types of accounts. Joint Ventures and Wholly foreign-owned Enterprises must have certain book accounts, including FCY Accounts, RMB Basic Accounts, and RMB General Accounts. General Accounts cannot be opened with the same bank that hold the basic accounts. Banks can open both RMB and foreign currency accounts, depending on the usage.

### RMB corporate accounts

- Basic account: used to handle daily fund transfers, payment of employee salaries and bonuses as well as cash deposits and withdrawals.
- General account: for customer cash management needs, mainly used to deposit loan proceeds, repay loan and other settlements. Cash withdrawal is not allowed.
- Special account: for special purposes, such as infrastructure construction, reconstruction, agency business, credit cards, etc. Cannot settle sales income or withdraw cash.
- Temporary account: for temporary need such as establishment of temporary institutions, temporary business activities in different places or verification of injected RMB capital. It can be used to make account transfers or to withdraw cash in accordance with relevant regulations. Generally, this kind

of account cannot issue checks. Only one RMB basic account is allowed per customer across banks in China, however, there is no restriction on the number of General accounts a corporate can operate. The banks need to report customers' account openings to People's Bank of China in a timely fashion.

### Foreign currency accounts

Companies need to open different foreign currency accounts for different purposes and uses. Upon the requirement of State Administrative of Foreign Exchange (SAFE), the foreign currency bank accounts should be separated into capital accounts and current accounts. The capital accounts (including capital account and foreign debt account, etc.) hold the capital funds or shareholder's loan etc. injected by an enterprise's foreign investors. The current accounts hold foreign exchange used by the enterprise for regular day-to-day operating items. After the separation of the capital account and the current account, RMB transactions under the current account are freely convertible (subject to certain procedural controls) as long as the transactions are considered commercially legitimate. However, in the case of capital accounts, the convertibility of the currency is still subject to the

verification of processing banks on a transaction-by-transaction basis. Foreign currency capital accounts are subject to SAFE's approval. All foreign currency inflows and outflows must go through the specific related accounts. Funds cannot be freely transferred between any capital item account and the settlement account.

### Documents needed

The documents required to open a bank account may vary depending on each banks' rules. Nonetheless, some basic documents are commonly required:

1. Approval Certificate issued by government bodies authorised by the State Council, i.e., Ministry of Commerce or the relevant provincial or municipal people's government.
2. Legal Person Business Licence issued by the State Administration for Industry and Commerce.
3. Certificate of Legal Personal Code and Organisation issued by the State Bureau of Quality and Technical Supervision.
4. Valid foreign-invested Enterprise Foreign Currency Account Opening Approval Documents (if applicable) and Foreign Exchange Registration IC Card issued by the State Administration for Foreign Exchange.
5. Identification documents of the legal representative,

6. Company seal/chop and special seal/chop for finance.
7. Account application and other relevant documents provided by the bank.
8. State and Local Tax Registration Certificate (original)
9. Memorandum/Articles of Association and amending supplements
10. List of directors (with the company's official chop or signature/chop of the legal representative)
11. Completed mandate/board resolution
12. An organization chart showing shareholding percentage of each entity and each stage in the ownership chain of the corporate structure.
13. Basic information for enterprises issued by State Administration for Foreign Exchange with company's official chop (for the enterprise required to conduct Balance of Payment reporting)

Beside the required documents, most banks require authorised signatories to be present when opening an account. Some banks, however, have alternative rules dealing with the absence of the authorised signatories.

When opening different offices in different cities, each office needs to open accounts within the registered city according to

local regulations. Same users can be set up for accounts in different cities.

## Local financing

### Foreign Debt

Foreign investment enterprises ('FIE') can borrow foreign loan with due foreign debt registration with SAFE. However, FIE should follow the ratio of registered capital to total investment ('D-E ratio') requirements in structuring their initial total investment. The total amount of investment includes the registered capital as well as loans borrowed by the FIE. According to Provisional Rule on the Management of Foreign Debt, the accumulated balance of long- and medium-term foreign debt plus short-term foreign debt borrowed by an FIE should not exceed the difference between the FIE's approved total investment and the registered capital. If there is any excess, the total investment amount should be re-approved by the original approval authority.

Besides, the gap between total investment and registered capital will be the allowable borrowing limit for foreign debt even if the FIE also borrows certain domestic debts denominated either in renminbi or in foreign currency within China.

### Entrusted Loan

Direct inter-company lending is prohibited in China. Companies are only allowed to carry out entrusted loan activities, in which a bank acts as an intermediary in the lending/borrowing arrangement.

The State Administrative of Foreign Exchange also issued the Circular which allows the fund flow within qualified Multinational Companies ('MNC') in China and with their member companies abroad. The initiative aims to decrease MNCs' financing costs and facilitate companies to better use and allocate their capital. In which case, bank (trustee) acting as agent between the cash surplus group company (lender, entrustor) and the cash deficit group company (borrower).

## Restriction on outbound remittance

Repatriation of cash is strictly controlled. The only way a company can transfer profits out of the country is to pay an annual dividend. Supporting documents must be submitted to banks for cross-border profits transfers. Meanwhile, for payment amounts exceeding US\$30,000 or equivalent, tax clearance certificates should also be presented for remittance purpose.

1. As at May 2012.  
 2. Figures represent ownership of Hang Seng Bank in Hong Kong, which is 62.14% owned by Hongkong and Shanghai Banking Corporation Limited.

# HSBC in China

As one of the first foreign banks locally incorporated in China, HSBC Bank (China) Company Limited started operations on 2 April 2007. Local incorporation marks an historic milestone for HSBC in China, enabling the bank to further expand its network and service range, in particular its RMB financing ability for the benefit of its customers.

## Network

As of June 2012, HSBC China has 120 outlets (26 branches, 94 sub-branches) in 33 cities across 19 provinces/municipalities, the largest network among foreign banks in China. There are over 5,000 staff members of which 98% are local hire.

HSBC also serves its customers through a huge ATM network in all cities where HSBC China has a presence.

## Overview

- City of incorporation: Shanghai
- Relationship with parent: 100% subsidiary of the Hong Kong and Shanghai Banking Corporation Limited.
- Registered Capital: RMB10.8 billion
- Moody's Rating: A1 (Outlook is stable)

## Largest foreign bank investor in mainland China

HSBC's investments in China	% Ownership	Outlets
<b>HSBC Operated Business</b>		
HSBC Bank (China) Company Limited	100.0%	120
HSBC Jintrust Fund Management Company Limited	49.0%	1
HSBC Life Insurance Company Limited	50.0%	2 customer service centres, 230 sales agents and bancassurance products offered via partners*
HSBC Rural Banks	100.0%	12
Hang Seng Bank (China) Limited	100.0% (via Hang Seng Bank)	43
<b>Strategic Investment in China</b>		
Bank of Communications	19.0%	2,600+
Ping An Insurance	15.57%	486,900+ sales agents and 62,000+ bancassurance outlets
Bank of Shanghai	8.0%	230+
Industrial Bank	12.8% (via Hang Seng Bank)w	640+
Yantai Bank	20.0% (via Hang Seng Bank)	70+

\*HSBC Life Insurance Company's partners are HSBC Bank (China), Hang Seng Bank (China) and Bank of Communications

## HSBC milestones in mainland China

### 1865

Founded in Hong Kong and Shanghai.

### Since 1865

Has had a continuous presence in mainland China.

### 1980

The first foreign bank to open a representative office in Beijing following the Open Door policy.

### Dec 2001

The first foreign commercial bank to acquire an 8% stake in a Mainland bank – Bank of Shanghai.

### Feb 2004

The first foreign bank to conduct RMB business to local companies in mainland China.

### Dec 2006

The first foreign bank to offer time deposit service to local citizens for amounts no less than RMB1 million in nine cities of Beijing, Dalian, Guangzhou, Qingdao, Shanghai, Shenzhen, Tianjin, Wuhan and Xiamen.

### Apr 2007

HSBC Bank (China) Company Limited started operations on 2 April 2007 as a wholly-foreign-owned bank solely owned by The Hongkong and Shanghai Banking Corporation Limited. HSBC is among the first batch of foreign banks to locally incorporate in mainland China.

### Dec 2007

Hubei Suizhou Cengdu HSBC Rural Bank Company Limited (HSBC Rural Bank), a wholly-owned subsidiary of The Hongkong and Shanghai Banking Corporation Limited, opened for business, marking the first entry by an international bank into China's rural market.

### Nov 2008

HSBC China launched debit cards in 17 mainland Chinese cities on 17 November. The cards can link with RMB and foreign-currency accounts, a feature unparalleled among the debit cards offered by foreign banks in mainland China.

### Jun 2010

HSBC launched its China new head office building, HSBC Building, in Shanghai Pudong's Lujiazui financial district and opened the 100th HSBC-branded service outlet in Shanghai.

### Jul 2011

The first foreign bank to be granted access to China's gold futures market.

### Nov 2011

The Hongkong and Shanghai Banking Corporation Limited paid in RMB2.8 billion to boost HSBC China's registered capital to RMB10.8 billion, which enables HSBC China to hold the largest capital base among all foreign banks in the mainland.



## Corporate Sustainability

For HSBC, Corporate Sustainability is about bringing social and environmental issues together with financial performance to maintain and grow a successful business for the benefit of our stakeholders.

- We apply clear policies and processes to manage potential social and environmental risk in our lending and other financial activities in sensitive sectors.
- We help our clients to seize the opportunities presented by the shift to a low-carbon economy.
- We try to reduce our own environmental footprint and share good practice on this with our clients and other stakeholders.
- We focus our community investment (philanthropic activities) on education and the environment.

Our education programmes help to lift people out of poverty, build financial literacy and promote environmental awareness.

Our environmental programme focuses on the HSBC Climate Partnership – a five-year environmental programme to reduce the impact of climate change on people, forests, freshwater and cities.

HSBC's programme partners are carrying out original scientific research, developing demonstration projects, creating working models, and proving clear solutions so that governments can enact legislation for the adoption of low-carbon policies.

In China, cooperation with Tongji University has included the Tongji-HSBC Leadership programme: Environment for Sustainable Development and a three-year research project on carbon dioxide emission reduction in the Yangtze river delta region. HSBC China was first locally incorporated bank to publish its CSR report and launch the Consumer Education programme to provide consumers with commercial-free financial knowledge.



## Awards for Excellence in China

**Best Foreign Commercial Bank in China**  
FinanceAsia  
2001-06, 2008-11

**Best Foreign Retail Bank in China**  
2009-2012

**Best Domestic Cash Management Bank in China**  
Euromoney  
2011

**Best Trade Finance Provider in China**  
Euromoney  
2011

**Best International Trade Bank in China**  
Trade Finance  
2008-09 & 2011

**Best Risk Management Bank in China**  
Treasury Management International  
2010-11

**Rated China's No.1 Leading Clients Top-rated Agent Bank**  
Global Custodian  
2009-2011

**Best Foreign Private Bank in China**  
Private Banker  
2011

# Country overview

<i>Capital city</i>	Beijing
<i>Area and population</i>	Area of 9,600,000 sq km and population size of 1,371 million as of 2011
<i>Language</i>	Putonghua (or Mandarin), based on the Beijing dialect
<i>Currency</i>	RMB
<i>International dialling code</i>	+86

<i>National Holidays</i>	Scheduled Public Holidays for 2013	
	<i>New Year's Day</i>	1 January
	<i>Chinese New Year (3 days)</i>	9-11 February*
	<i>Qing Ming (Tomb Sweeping) Festival</i>	4 April*
	<i>Labour Day</i>	1 May
	<i>Dragon Boat Festival</i>	12 June*
	<i>Mid-Autumn Festival</i>	19 September*
	<i>National Day</i>	1-3 October
	*Depending on the lunar calendar. Note that in addition to the holidays listed above, individual provinces may observe provincial holidays.	

<i>Business and banking hours</i>	In most cities in China, businesses and government offices are usually open Monday through Friday from 8:00am to noon and from about 1:00pm to 5:00pm, although this can vary depending on the organisation. China has a five-day working week consisting of 40 hours. Banks are generally open Monday through Friday from 9:00am to 5:00pm. Shops are generally open every day. Most of China's business world slows down considerably during the spring festival in late January and early February. Business visitors would be wise to avoid this two to three week holiday period.
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<i>Stock exchanges</i>	Shanghai Stock Exchange/Shenzhen Stock Exchange
<i>Political structure</i>	The National People's Congress System

Source – Office of National Statistics [www.ons.co.uk](http://www.ons.co.uk)



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