

CHINA INVESTMENT GUIDE

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大成律师事务所



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I. Introductory Note

This is an informative Guide that aims to provide potential investors with an outline of the legal framework for setting-up a commercial presence in China and conducting business there.

This Guide is an update of the one published in May 2012 that was drafted by a team of Chinese and Portuguese lawyers working together as legal partners in China, Macao and Portugal. These lawyers, from PLMJ Law Firm, Dacheng Law Offices and DSL Lawyers, worked together on this Guide to provide key guidelines for foreign companies and investors entering China as well as warning them about the risks inherent to this developing and complex market.

In this context, and based on the laws and directives currently in force in China in the most relevant areas, this Guide provides a general outline of the structure of the most important types of commercial companies and the different options for investments. The guide also looks at the rules on administrative licences and restricted business areas, tariffs and trade protection instruments as well as the relevant taxation rules. The legal aspects of employment relationships and types of visas for foreigners are also addressed and the Guide also includes a section on protection of intellectual property rights and concludes with an overview of the Chinese judicial system.

This Guide is for general reference only and does not cover all relevant aspects of the legal rules in the areas covered. It cannot, therefore, substitute specific legal advice or be considered as a basis for claiming the existence of any lawyer-client relationship. For advice and legal assistance to carry out specific transactions, interested investors should consult and retain lawyers licenced to practice in China.



II. Commercial Entities and Foreign Investment

COMMERCIAL ENTITIES

INTRODUCTION

The most widely used types of business vehicles in China are the **Limited Liability Company** or **LLC** and the public limited company (**Joint Stock Limited Company** or **JSLC**). Both types are governed by the Company Law of the People's Republic of China, which was revised on 1 March 2014 (the "**Company Law**"). The Company Law establishes the requirements to be met by LLCs and JSLCs in respect of the object of the company, the share capital, the organisational structure, the transfer of shares and dissolution.

(A) LIMITED LIABILITY COMPANY (LLC)

The LLC is a type of company in which shareholders are liable up to the value of the capital they subscribed. The number of shareholders may not exceed 50.

COMPANY NAME

The company name of an LLC must include the phrase *Limited Liability Company* or *Limited Company*.

REGISTERED CAPITAL

The company capital of the LLC is the total amount of equity invested in the company, subscribed by all shareholders and registered with the commercial registry.

The recent amendment of the Company Law established important changes to the requirements of capital contributions of the shareholders, paid capital and minimum registered capital.

The shareholders may pay the capital to be invested in the company in cash or in kind, in the form of assets of which value can be determined in cash or legally transferable rights, such as intellectual property rights, usufruct of land or other intangible assets, excluding the cases specifically provided for by law or administrative provision.

The value of the capital paid in kind must be established and confirmed according to the law and administrative regulations applicable to valuation, if any.

Actually payment of the capital is no longer required in order to register the company. However, it should be noted that shareholders in a limited liability company bear the limited liabilities in accordance with the total amount of their subscribed capital contributions. Thus, to some extent, the size of the registered capital would still reflect a company's financial strength and its capacity to bear civil liabilities.

The higher the registered capital, the more liability each shareholder will bear in relation to their subscribed capital. Accordingly, for shareholders, it is unwise to make subscriptions.

As there is no statutory minimum amount of the registered capital for a limited liability company, one Yuan is enough to register such a company.

Each shareholder must fully and duly pay the capital they subscribed in accordance with the articles of association. Each shareholder must deposit the cash contribution in full in the temporary account of the LLC or legally transfer the contribution in kind by following appropriate transfer process for the assets as prescribed by the law. If a shareholder fails to meet this obligation, that shareholder will remain liable for payment in full to the company and also be liable for his default towards other shareholders who have met their obligations on time. The law also provides that, for each capital contribution made by the shareholders, the company must hold verification from a legitimate capital verification institution.

The truth is that under the recent amendment to the Company Law, the requirement for capital contribution verification has been consigned to history and fees for establishing a company have been reduced greatly (almost no fees other than the registration fee are required).

Shareholders must register their subscribed capital contributions and date of subscription. After all the capital contributions have been paid in accordance with the articles of association, all the shareholders may designate a representative or an agent to apply for registration of the company without capital verification. Procedures are simpler for paying registered capital since there would be no need to open an account or carry out the verification.

Minimum capital requirements for foreign investment in special industries

There are specific Chinese regulations and laws, mainly the Securities Law of the People's Republic of China, the Law of the People's Republic of China on Commercial Banks, and Regulations of the People's Republic of China on Management of International Freight Forwarders, that require a minimum registered capital for incorporation of an LLC in specific industries as follows:

- Foreign capital banks and banks with foreign investments: RMB 1 billion or the same value in a freely convertible equivalent currency and the registered capital must be paid in;
- Insurance companies with foreign investments: RMB 200 million or the same value in a freely convertible equivalent currency and the registered capital must be fully paid up in monetary form. The insurance regulatory authority of the State Council may adjust the amount of the minimum registered capital in accordance with the proposed scope of business and scale of operations. However, the minimum capital may not be less than 200 Million RMB.
- An investment company incorporated by foreign investors: USD 30 million.
- International freight forwarding enterprises with foreign investment: USD 1 million.

In addition to the minimum capital, companies with foreign investments must estimate and indicate their total planned investment amount in their articles of association. The amount of the total investment is made up of the registered capital and financing estimated to be necessary for the foreign investment company to operate productively. The proportion of registered capital and the total amount of investment of the companies with foreign investments must comply with the requirements for LLCs referred to above.¹

¹ According to Article 3 of the "Temporary Regulations of the State Administration for Industry and Commerce on the Proportion of the Registered Capital to the Total Amount of Investment of Sino-foreign Equity Joint Ventures", the proportion of registered capital to the total amount of investment of a Sino-foreign equity joint venture must comply with the following provisions:

SHAREHOLDERS MEETING (GENERAL MEETING)

Unless otherwise provided by law or regulations, or even by the articles of association of the company, the corporate body with the highest level of jurisdiction and authority in the LLC is the general meeting of the shareholders, made up of all shareholders assembled in a general meeting.

The first general meeting must be convened and chaired by the shareholder with the greatest capital investment in the company. The ordinary general meeting of the shareholders is convened and presided over in accordance with the articles of association of the LLC and the extraordinary general meeting is called and held when proposed by:

1. Shareholders holding 10% or more of shares with voting rights, or
2. More than one third (1/3) of the directors, or
3. The supervisory board or the individual supervisor alone if the company does not have a supervisory board.

Major corporate decisions must be approved at the shareholders' meeting by an absolute majority, which means such resolutions must be approved by shareholders representing 2/3 or more of the shares with voting rights. Examples of matters to be decided in this way are a review of the articles of association, an increase or reduction in the company's registered capital, a change in the type of company and the merger, division or dissolution of the company.

To the extent that it is not otherwise provided for in the articles of association, shareholders' voting rights at the shareholders' meeting are proportionate to their stake in the capital of the company.

THE BOARD OF DIRECTORS

The law requires the LLC board of directors to consist of a minimum number of 3 and a maximum of 13 members. However, smaller LLCs or ones with few shareholders may only have a single executive director instead of a board. This executive director may simultaneously act as the manager of the company. The term of office of the directors of the LLC should be stipulated in the articles of association, but each term may not exceed 3 years. Directors have the right to stay in office if they are re-elected for another term.

The rights and duties of the board are, among others established by law, to convene general meetings, to decide on the company's activities and investment plans, to prepare financial budgets, to distribute profits and losses and increase or reduce the company's capital.

1. Where the total amount of investment of a Sino-foreign equity joint venture is less than USD 3 million (inclusive), its registered capital shall be at least 7/10 of the total investment.
2. Where the total amount of investment of a Sino-foreign equity joint venture values from USD 3 million to USD 10 million, the registered capital must be at least 1/2 of the total amount of investment. Where the total amount of investment is less than USD 4.2 million, the registered capital may not be less than USD 2.1 million.
3. Where the total amount of investment of a Sino-foreign equity joint venture is above USD 10 million and up to USD 30 million, the registered capital must be at least 2/5 of the total amount of investment. Where the total amount of investment is less than USD 12.5 million, the registered capital may not be less than USD 5 million.
4. Where the total amount of investment of a Sino-foreign equity joint venture is more than USD 30 million, the registered capital must be at least 1/3 of the total amount of investment. Where the total amount of investment is less than USD 36 million, the registered capital may not be less than USD 12 million.

THE MANAGER

The LLC is permitted to have a manager who can be hired or dismissed at the board's discretion. The manager answers to the board and will be responsible for organising the implementation of annual business plans and investment plans of the company, as well as for developing the internal management structure and other duties imposed by law or by the board.

THE SUPERVISORY BOARD

Among other duties established by law and the articles of association, the supervisory board is responsible for supervising the financial affairs of the company and ensuring that the directors and senior managers carry out their duties. The supervisory board of the LLC must consist of at least 3 members. However, smaller LLCs may have only 1 or 2 supervisors instead of a supervisory board.

The Company Law strictly prohibits any director or senior manager from simultaneously occupying the position of supervisor of the company. The term of office of a supervisor is 3 years and the supervisor has the right to stay on if re-elected for another term. The supervisory board must meet at least once a year and any supervisor may convene extraordinary meetings. Unless otherwise provided by the Company Law, the supervisory board's discussion and voting procedures are established in the articles of association. Resolutions of the supervisory board are approved by a simple majority of its members, which means over half of the supervisors.

TRANSFER OF SHARES

In an LLC, the shares may be transferred between shareholders or to any third party, provided the transfer is made in accordance with the applicable law. Shareholders have a pre-emptive right to acquire the shares of other shareholders. The law gives companies discretion to decide on the methods for the transfer of shares so, if special clauses are included in the articles of association regarding transfer of shares of the company, these special provisions should prevail.

FINANCIAL REPORTS

At the end of each financial year, the company is required to provide a management report and accounts to be audited by an auditing firm. The Chinese financial year begins on 1 January and ends on 31 December. LLCs must submit the financial report for consideration by the shareholders by the deadline established in the articles of association.

DISSOLUTION

An LLC may be dissolved in the following situations: 1) upon expiry of the business term provided for in the articles of association 2) upon the occurrence of any of the situations for dissolution provided for in the articles of association, 3) upon resolution of the shareholders, 4) in the event of merger or division of the company, 5) if the business licence is cancelled, or 6) when its dissolution is ordered by a court.

Shareholders holding 10% or more of shares with voting rights can apply to the courts for dissolution when the company is unable to operate and the continuation of business operation would result in a huge loss to the shareholders.

(B) JOINT STOCK LIMITED COMPANY (JSLC)

The JSLC is a company in which the shareholders are liable in proportion to the shares to which they subscribe. It can be incorporated by two ways: (i) through the subscription of capital by certain promoters, or (ii) through public subscription of shares.

(i) In the former case (promotion), all shares are subscribed by the promoters.

With the recent amendments to the law, the amount of 2 RMB can meet the requirement to establish a joint stock limited company with less than 2 but not more than 200 promoters. Therefore, when a joint stock limited company is established by promotion, promoters should consider the possibility of subsequent financing.

Before all the initial agreed capital is paid, no stock may be offered to others for subscription, namely, no new shareholder can be introduced. The shareholders must subscribe to the full amount of the agreed shares provided in the articles of association. Otherwise, they will be liable for other shareholders who have already made their capital contributions.

(ii) As to the latter option – a JSLC with open capital – the shares issued by the company are subscribed by the promoters together with the general public, or by a particular group of people.

To establish a JSLC in either way, the number of promoters cannot be more than 200 and at least half of the promoters must be domiciled in China.

In conclusion, the main difference between a limited liability company and a joint stock limited company, after the amendments to the law, is the maximum number of promoters and the forms of establishment.

COMPANY NAME

The company name of the JSLC should include words such as “Joint Stock Limited Company” or “Joint Stock Company” to indicate the type of company.

THE COMPANY CAPITAL

The new revision of the Company Law determines no statutory minimum amount of registered capital to set up a JSLC, without prejudice to specific conditions imposed by law for certain situations. For example, the minimum capital of a JSLC with foreign capital is RMB 30 million (about USD 4.4 million). The capital of a JSLC is divided into shares carrying the same nominal value. The certificate of ownership of the shares must be issued by the JSLC to prove ownership of the shares subscribed.

If the JSLC is set up by promoters, the capital at registration should be the total capital of the shares subscribed by the promoters at the Registry of Companies. Shares may not be offered to third parties for subscription until the set up capital has been paid.

If the JSLC is incorporated with open capital, its capital will consist of any such amount which has actually been paid, corresponding to shares registered with the Registry of Companies.

GENERAL MEETING

The General Meeting is the supreme corporate body in a JSLC and is made up of all the shareholders. The ordinary general meeting of shareholders must be held once a year. However, extraordinary general meetings may be called with two months' prior notice in the following circumstances (among others provided for in the articles of association): if the number of directors is less than 2/3 of the required number, if the company's losses exceed 1/3 of the capital, when the board of directors or supervisory board deem it to be necessary, and by any shareholder or group of shareholders holding at least 10% of the shares. The shareholders present at the meeting are entitled to one vote for each share they hold in the company. However, the shares held by the company do not confer voting rights.

Resolutions of the general meeting must be approved by simple majority of the votes of the shareholders attending the meeting. However, issues of greater relevance such as changing the articles of association, increasing or reducing the share capital, changing the company type, merger, division or dissolution of the company, must be approved by 2/3 or more of the votes of shareholders attending the meeting.

BOARD OF DIRECTORS

The JSLC must establish a board of directors, which must be made up of at least 5 and no more than 19 directors. The term of office and the powers held by the board are the same as those described above for LLCs. The board must meet twice a year and extraordinary meetings must be held when proposed by: 1) shareholders representing 1/10 or more of the voting shares, 2) at least 1/3 of the directors, or 3) the supervisory board. The meeting of the board can only take place if more than half of the directors are present. Any decision of the board of directors must be approved by more than half of all directors. Each director has one vote only.

THE MANAGER

JSLCs must have a manager who is hired and dismissed by the directors. The term of office and powers assigned to the manager are the same as those described above for LLCs.

SUPERVISORY BOARD

Unlike LLCs, the supervisory board of the JSLC is made up of at least 3 members. They meet regularly once every 6 months or whenever proposed by a supervisor. The term of office of its members, functions, discussion methods and voting procedures of the board are the same as that for the LLC, as described above.

TRANSFER OF SHARES

There are two types of shares in a JSLC, namely, registered/nominative stock and unregistered/bearer shares. Registered or nominative shares may be transferred by endorsement or other ways provided for by relevant laws or administrative regulations and unregistered shares or bearer shares are transferred by simply handing them over to the transferee. Shares issued to promoters or legal entities must be registered shares and may only be registered in the name of those promoters or legal entities. The Chinese Company Law imposes restrictions on the term and value of shares held by promoters, directors, supervisors and senior managers in JSLCs, when they transfer such shares.

ANNUAL REPORTS AND ACCOUNTING

At the end of each financial year, the company is required to produce a report on its financial situation prepared by a legitimate auditing firm. In China, the financial year begins on 1 January and ends on 31 December. The report and accounts must be submitted to the shareholders for consideration in the 20 days preceding the annual meeting of shareholders. If the JSLC is a listed company, it should make its management report and accounts public.

The documents, books, balance sheets, reports and other accounting documents must be prepared in accordance with the unified accounting rules laid down by the Accounting Law of People's Republic of China as revised in 1999.

ARTICLES OF ASSOCIATION

The articles of association contain the rules that govern the operation of the company. In both LLCs and JSLCs, the articles of association must state the company name, the object of the company, the registered office, the registered capital and the capital subscribed by each shareholder, the directors and the rights and obligations of the shareholders, among other issues.

FOREIGN INVESTMENT

INTRODUCTION

The most important decision to be made by investors in China is the choice of the most suitable investment vehicle. Typically, the most popular forms of foreign investment in China are:

- The Wholly Foreign-Owned Enterprise (WFOE外商独资企业) - a company fully established by foreign capital.
- Joint Ventures (合资企业) divided into Equity Joint Ventures (EJVs) and Cooperative Joint Ventures (CJVs). Joint ventures are formed on the basis of foreign and Chinese joint investments.
- The Representative Office (Rep. Office 代表处).

Foreign investors can also opt for more specific forms of investment such as:

- Build-Operate-Transfer (BOT).
- Compensation Trade (CT 补偿贸易).
- Processing & Assembly (PA 来料加工装配贸易).
- International Leasing (IL 国际融资租赁).

1. LEADING SOLUTIONS FOR INVESTMENT

(A) THE WHOLLY FOREIGN-OWNED ENTERPRISE (WFOE)

A WFOE is a Chinese limited liability company composed entirely of foreign capital owned by one or more foreign investors, excluding branches set up in China by foreign enterprises and other foreign economic organisations. China encourages the establishment of WFOEs with the capacity to export their products or that are equipped with innovative technology.

Typically, there is only one investor behind a WFOE, but this is not always the case. Two individuals or two or more foreign legal entities that wish to invest jointly in China may, for example, set up a holding company in a country or jurisdiction they are familiar with and then set up a WFOE and invest in China through this controlling company (holding).

The WFOE must conduct its activities and its business under the precise category for which the commercial licence granted. In order to comply with Chinese law, it should retain formal and independent accountants, keep organised and independent accounting records, approve and register its balance sheets and financial statements and be ready for any kind of supervision by the Chinese regulatory and financial authorities.

There are three common types of WFOEs in China:

- Manufacturing WFOEs (生产类外商独资企业)
- Consulting WFOEs (咨询类外商独资企业)
- Commercial WFOEs (贸易类外商独资企业)

In China, WFOEs were originally designed to encourage manufacturing activities aimed at exporting or introducing innovative technology to China. However, after China's accession to the WTO in 2001, such policies on WFOEs have changed. WFOEs are now increasingly used as a means of investment in services such as management consulting or software development and trading. The Ministry of Commerce of People's Republic of China (商务部) issued five supplementary provisions to the 'Measures for the Administration of Foreign Investment in Commercial Fields' (外商投资商业领域管理办法), whereby foreign investors were allowed to establish Commercial WFOEs with 100% foreign capital, destined for wholesale or retail sales and franchises in China.

Some of the advantages of a WFOE:

- It has all the functionality of an independent legal entity, with the power to enter into contracts, issue invoices, hire and fire employees, make payments and receive payment in RMB;
- It allows full management powers and total control by the management board;
- It has the independence to implement strategies of a global dimension made by the affiliated companies without having to consider the involvement of Chinese shareholders;
- It can convert profits earned in RMB (or, CNY) to USD if it intends to distribute them to an associated company located outside China;
- It benefits from more effective protection for its intellectual property, know-how and technology;
- It has greater efficiency in its operation, administration and future development.

(B) THE JOINT VENTURE (合资企业)

The Joint Venture (JV) is another popular vehicle for investment in China. This investment solution always combines the market knowledge, the favourable market treatment and the manufacturing capacity of the Chinese partner, with the technology, know-how and market experience of the foreign partner.

The JV is usually formed as a limited liability company, taking the form of an equity joint venture (the "EJV" 合资经营) or a cooperative joint venture (the "CJV" 合作经营). While the EJV is more strictly regulated and operates more closely to the corporate model, the CJV allows its shareholders greater flexibility when setting out contractual provisions that regulate, for example, distribution of profit, management and registered capital.

CJVs and EJVs resemble each other and, in many respects, work in the same way. Aspects in which they are similar include their general management structure, the process of getting governmental approval and their relations with authorities to which they must submit requests for approval. They also share similar contractual formats, tax exemptions, legal status and applicable legal provisions as well as the authorities to which they may resort to settle potential commercial disputes.

(C) EQUITY JOINT VENTURE (合资经营)

The EJV is a partnership between a Chinese company and a foreign company in China, through which shareholders can share the profits, risks and losses in proportion to their respective shares in the capital of the company. The foreign investors, in general, must contribute no less than 25% of the total investment. Any transfer of capital to the EJV by any investor requires authorisation from the other shareholders and should be made by consensus. It should also be approved by the supervisory authority with jurisdiction to grant approval and must follow the procedures for changes with the registration and administration office. Partners of EJV have pre-emptive rights to acquire other partners' shares. EJV are limited liability companies and their investors or shareholders are not personally liable for the debts which the company may incur. As a company, the EJV is able to acquire property, hire employees independently, execute works, etc.

The investment by foreign investors and Chinese investors in an EJV can take the form of cash, intellectual property rights, technology, real estate or other assets, such as equipment. However, only advanced technology and equipment that meet Chinese needs can be treated as foreign joint venture investment. Chinese regulations specify the proportion of the capital that must be submitted for registration in face of the total amount invested in the EJV. They also specify the minimum registered capital when the foreign investment concerns certain industrial activities regarded as special, as referred to above.

The management of the EJV is under the control of a board consists of at least 3 directors. The term of office for directors is 4 years and may be renewed with the consent of the investors in the joint venture. The usual period of operation for an EJV is between 10 and 30 years.²

(D) CONTRACTUAL JOINT VENTURE (CJV合作经营)

The CJV is an enterprise established by a Chinese company and a foreign company. Unlike the EJV, which is subject to tighter legal regulation, the CJV is based on a contract for a cooperative joint venture (partnership) that regulates issues such as the duration of the enterprise and the sharing of profits and risks, as well as the division of losses at the end of the CJV. Profits from a CJV are divided in accordance with the clauses of the agreements rather than simply following the investment proportion of each partner as in the EJV. Furthermore, the way in which profits can be shared is more flexible.

In a CJV, Chinese companies usually provide the workforce, land and manufacturing infrastructures, whereas the foreign companies normally provide technology, equipment and capital.

² Article 100 in "Regulations for Implementation of the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures" says the duration of a joint venture must be decided through consultation among all the parties to the joint venture according to the actual conditions of the particular lines of business and projects. The duration of a joint venture engaged in an ordinary project will, in principle, be between 10 to 30 years. Duration for those engaged in projects requiring large amounts of investment, long construction cycles and low profit rates on the capital, or in projects producing highly sophisticated products or products selling well on the international market, with advanced technology or key technology offered by the foreign parties to the joint ventures, may have their duration extended to 50 years. The duration of a joint venture may be longer than 50 years, if specially approved by the State Council.

(E) REPRESENTATIVE OFFICE (REP. OFFICE 代表处)

Another common form of foreign investment is through the setting up of a representative office (Rep. Office), which is not an independent company and is, therefore, considered as an extension of its parent company. A Rep. Office normally serves as a commercial link between the holding company and local companies in China. It is also used to conduct market surveys and product promotions, to establish contacts with potential consumers, to structure and organise the travel of representatives of the holding company to China and to conduct other not-for-profit activities. A Rep. Office is unable to engage in any activity that generates income, except in the cases where there are intergovernmental agreements for that purpose.

The Rep. Office is less demanding in terms of procedure and takes less time to set up. Normally, the activities of a Rep. Office are restricted and it may NOT:

- Engage directly in business activities aimed at making a profit;
- Issue invoices;
- Accept payments in RMB;
- Open bank accounts, use letters of credit or benefit from other financial services;
- Employ local employees directly (but it may hire local employees through a duly registered human resources agency).

2. OTHER FORMS OF INVESTMENT

(F) BUILD-OPERATE-TRANSFER (BOT 建设-经营- 转让)

Foreign investors who carry out industrial and infrastructure projects in China have the option of investing through a BOT. This form of investment usually requires investors to finance, design, build and conduct the business for a certain period of time, after which, upon the expiry of the contract, the ownership of the project is transferred to the Chinese government.

(G) BUSINESS OF COMPENSATION (补偿贸易)

In the compensation business, essentially, the Chinese companies produce goods with the use of machinery, equipment, raw materials and technology which are provided by foreign investors directly or on a credits basis. Foreign investors receive their compensation through capital obtained from other manufactured products, negotiated by both parties. This form of investment involves technology transfer, trade in raw materials and is financing by foreign investors and by their Chinese partner.

(H) PROCESSING & ASSEMBLY (来料加工)

This kind of investment is based on a processing and assembly contract to be established between a Chinese company and a foreign company, allowing foreign investors to benefit from manufacturing products in China without the need to form a company with this sole object. This form of investment is very popular in Southern China.

The foreign investor usually provides the raw material, parts and components required for the manufacturing process, while the Chinese partner provides manufacturing and industry facilities and the workforce. The Chinese company operates under the directions of its foreign partner and then exports the final product to the foreign partner.

(I) INTERNATIONAL LEASING (国际租赁)

International leasing involves the leasing of equipment to the lessee in China and, under the contract terms, receiving the income arising from that lease. During the period of the lease, the lessee has the right to use the equipment, while ownership of the equipment remains with the lessor. In the lease, the lessor and lessee normally agree on what will happen to the equipment at the end of the lease agreement. The lessor can choose between taking back the equipment and selling it to the lessee for a fixed price.

3. ADDITIONAL CONSIDERATIONS ON FINANCIAL INSTITUTIONS AND INVESTMENT COMPANIES INCORPORATED WITH FOREIGN CAPITAL

(A) FINANCIAL INSTITUTIONS INCORPORATED WITH FOREIGN CAPITAL

Financial institutions incorporated with foreign capital registered in China include banks, financial companies and the manufacturers and distributors of credit cards, which are financed entirely by foreign capital or through a partnership known as a Sino-Foreign Equity Joint Venture.

A financial institution funded with foreign capital may opt to set up a representative office (Rep. Office) in China to undertake non-commercial activities such as consulting, networking and market research. Under no circumstances can the representative office enter into an agreement with any individual or legal person with a view to making a profit for the financial institution represented, or engage in any commercial and operational activities.

The incorporation of banks funded with foreign capital is dependent on compliance with statutory requirements and regulations. The minimum registered capital of the bank is RMB 1 Billion (approx. USD 0.15 Billion) or the equivalent in other freely convertible currencies and this capital must be fully paid up.

Under the Regulation of the People's Republic of China on Administration of Foreign-Funded Banks (《中华人民共和国外资银行管理条例》), in force since 2006, banks funded by foreign capital in China have been allowed to accept deposits from the general public. Foreign financial institutions are also subject to the Chinese Anti-Money Laundering Law (《中华人民共和国反洗钱法》), in force since 2007. Financial institutions are required to establish internal anti-money laundering control systems including customer identification and records preserving the details of their customers and transactions carried out. They must also have alert systems for amounts that are large or suspicious for any reason.

(B) INVESTMENT COMPANIES FINANCED BY FOREIGN INVESTORS

The regulations on the establishment of investment companies by foreign investors in China are contained in the Provisions of the Ministry of Commerce on the Establishment of Investment Companies by Foreign Investors (《商务部关于外商投资举办投资性公司的规定》) enacted in 2003, revised twice in 2004 and supplemented by the Supplementary Provisions on the Establishment of Investment Companies by Foreign Investors in 2006.

An investment company established by foreign investors is a company with limited liability entirely controlled by foreign capital or a mixed joint venture company, designed for direct investments. To incorporate an investment company, the investor must previously have had at least ten companies incorporated with foreign capital in China. The minimum share capital for this type of company is USD 30 million, which must be fully paid up. This kind of investment company is often encouraged for industry, agriculture, infrastructure and energy projects.

(C) RESTRICTIONS ON FOREIGN INVESTMENT

Investment projects in China are legally classified as encouraged, permitted, restricted or forbidden under the Provisions Guiding the Orientation of Foreign Investment (指导外商投资方向规定). If the project does not fit into the Foreign Investment Industrial Guidance Catalogue (2011 Revision) (外商投资产业指导目录) or the Catalogue of Foreign-Funded Dominant Industries of the Mid-west Region (2013 Revision) (中西部地区外商投资优势产业目录), it may be classified as permitted and, therefore, will not be subject to any favourable treatment or restriction. These regulations are constantly updated to reflect the foreign investment policies of the country.

APPROVAL AUTHORITY - MOFCOM

The establishment of a Foreign Investment Enterprise (FIE) in China is subject to approval by the Ministry of Commerce of China (MOFCOM) or by one its departments for different areas, depending on the volume of the investment and the classification code of the activity. In 2009, MOFCOM issued two new circulars: Circular of the Ministry of Commerce on Further Enhancement of the Approval Scheme for Foreign Investment (商务部关于进一步改进外商投资审批工作的通知) (Shang Zi Han No. 7 (2009) ("Circular 7"), in force since 5 March 2009 and Circular of the Ministry of Commerce on Delegation of Approval Authority on the Establishment of Foreign Investment Holding Companies (商务部关于下放外商投资举办投资性公司审批权限的通知) (Shang Zi Han No. 8 (2009) ("Circular" 8), in force since 6 March 2009.

ACTIVITIES WHERE FOREIGN INVESTMENT IS PROHIBITED

Foreign investment is generally prohibited in the following areas of business or in activities with the following characteristics/consequences:

- State security and/or public interest activities;
- Environmental pollution, damage to natural resources or human health;
- Threat to security and use of exclusive military areas;
- Excessive occupation of farmland adverse to the protection and development of natural resources;
- Exclusive use of Chinese resources in the production of goods.

RESTRICTED FOREIGN INVESTMENT

Restricted foreign investment is subject to approval and special assessment. The applicable legislation also controls the form of investment in the case of activities restricted to “EJVs and CJVs”, in which the Chinese partner’s investment and control will be greater than that of the foreign investor.

Activities in which foreign investment is restricted:

Exploitation of specific types of mineral resources the use of which is limited by the State;

- Activities harmful to natural resources and environmental protection;
- Activities using obsolete technologies;
- Previously prohibited industries which the State is gradually liberalising.

The activities in which foreign investment is restricted are updated regularly by the State. Pursuant to Article 7 of the Catalogue for the Guidance of Foreign Investment Industries (Revised in 2011), on the Catalogue of Restricted Foreign Investment Industries, the restricted activities are the followings:

- Finance

1. Banks, finance companies and currency brokers
2. Insurance companies (foreign investment ratio of life insurance companies may not exceed 50%)
3. Financial leasing companies and securities companies (limited to the underwriters in A-shares and B-shares and H-shares, as well as government and corporate bond underwriting and trading, foreign capital ratio of not more than 1/3), securities investment fund management companies (foreign ratio may not exceed 49%)
4. Insurance brokerage companies
5. Futures companies (Chinese partner must hold the majority of shares)

ACTIVITIES WHERE FOREIGN INVESTMENT IS ENCOURAGED

Activities where foreign investment is encouraged are:

- High and new technologies or advanced application technologies which can improve the performance of products, increase the technological and economic efficiency of companies, or create new equipment and materials which are beyond the capacity of domestic production;
- New technologies for agriculture, comprehensive development of agriculture, energy, transportation and the raw materials mining industry;
- Energy saving and raw materials and environmental protection;
- Product improvement and development of new markets or increasing the international competitiveness of products;
- Currently, foreign investment is principally encouraged in the areas of modern logistics, international economy consulting services, science, technology, environmental protection, outsourcing for financial intermediation services, human resources services, software development offshore call centre services, data processing and the operation of sports events.

4. SETTING UP A COMPANY THROUGH INVESTMENT BY A FOREIGN COMPANY

(A) ESTABLISHMENT OF A REPRESENTATIVE OFFICE (REP. OFFICE)

Foreign companies planning to set up a Rep. Office in China have to complete the registration with the competent authorities. Prior approval is required for a company to operate in an area where foreign investment is restricted. The registration request must include:

- The Application Form;
- Certificate of registration of foreign company;
- Letter proving credit;
- Appointment of legal representative;
- CV and identification of the legal representative;
- Tenancy agreement for the Rep. Office premises.

(B) INCORPORATION OF FOREIGN INVESTMENT ENTERPRISE (FIE)

The following steps are required in connection with the incorporation of an FIE:

1. Due diligence

Finding appropriate premises for the headquarters of the FIE or choosing a partner are examples of tasks to be performed in advance.

2. Pre-approval of the company name

Prior to registration, the name of the company has to be pre-approved by the commercial registry of companies – the local Administrative Bureau for Industry and Commerce (工商行政管理局).

3. Approval of the articles of association and contracts

These documents must be submitted for review and further approval to either MOFCOM or to one of its departments located in any of the different provinces. The approval is granted through the issue of a certificate for the FIE.

4. Business licence

Within 30 days of the issue of the certificate of approval, the foreign investor must register the FIE and apply for a commercial licence from the local commercial registry. The date of the commercial licence granted to the FIE is also the date when the company is deemed to have been incorporated, after which it may begin its activity under the terms of its commercial licence.

5. Other formalities

The company must take the following steps within 30 days of the issue of the commercial licence:

- i) obtain approval to acquire a corporate seal from the police department;
- ii) obtain the organisational code from the Bureau of Quality and Technical Supervision (质量技术监督局);
- iii) apply for registration with the local administration for the foreign currency exchange;
- iv) open a foreign currency bank account in the name of the company and transfer the registered capital to that account;
- v) register with the local Statistics Bureau (统计局);
- vi) register with the Tax Bureau (税务局), at the local and state levels;
- vii) apply for authorisation to print or purchase financial invoices/receipts;
- viii) register with the Social Security Bureau;
- ix) if the company is involved in the import/export business, it must also register with Customs Authorities.

6. Registration of foreign capital

Once issued, the Foreign Currency Exchange Registration Certificate is valid for one year and reviewed annually. If the company changes its name, address, nature of business, transfers shares, increases capital or merges then, after carrying out the statutory changes and the commercial registration of the same, the FIE should apply for the replacement of the Foreign Exchange Registration Certificate.

The FIE must open a foreign currency exchange bank account with a bank which is certified to provide such service before the expiry of validity of the FIE's Foreign Currency Exchange Registration Certificate, within the deadline required by the local government.

7. Employee Registration

Within 30 days of its formation, the newly incorporated company must register its employees and social welfare contributions with the local Social Security Bureau, as required by the 1999 Interim Measures on the Management of Social Insurance Registration (社会保险登记管理暂行办法 1999) and upon doing so, it will be granted its social security registration card.

(C) INCORPORATION OF A MANUFACTURING COMPANY

In addition to meeting the general procedure described above, the following specific steps are to be taken for setting up a foreign capital manufacturing company in China.

1. Letter of Intent or Investment Agreement

After selecting the primary site in China where the investment will be located, foreign investors are advised to sign a Letter of Intent or Investment Agreement with the local government (this document is not legally enforceable).

The Letter of Intent or Investment Agreement should address the following matters:

- Project description;
- Amount of investment;
- Project schedule;
- Demarcation of land (including details such as location, size and the price of land);
- Preferential treatment offered by the local government;
- Support to be offered by the local government during the approval process.

2. Land use

There are two types of land (real property) in China: (a) collectively-owned land or (b) State-owned land.

(a) Public land - usually rural farmland and rarely an investment option for foreign investors. If a foreign investor intends to invest in this type of land, it is advisable to first seek appropriate professional support.

(b) State-owned land – subdivided into two subtypes: i) allocated land and ii) granted land.

i) the use of allocated land is granted to the entity by the Chinese government with a particular purpose. Allocated land cannot be freely transferred, mortgaged or sold without the approval of the local authority and the payment of an allocation fee. Normally, this right is not limited in time.

ii) granted land, on the other hand, is paid for and can be used for commercial and industrial purposes. Moreover, the right to use this type of land – usufruct – can be transferred, mortgaged and leased freely.

The usufruct right over the land is acquired further to the conclusion of a contract granting land tenure with the competent authority for land administration. For the grant of the land tenure, the company must pay the government a special fee. Provided the applicable requirements are met, the government will pass the Land Use Certificate to the company. Pursuant to Chinese land law, the usufruct is valid for a maximum fixed term of 50 years for industrial projects. Once the term expires, the holder is granted a period in which to apply for an extension of the contract against payment of a fee for land use.

3. Project Feasibility Report

A Project Feasibility Report should be submitted to the National Development and Reform Commission, at state or local level, to request approval. The report should address matters such as name, term and target of the project, qualification of the investor, fundamental information on the project, adopted technologies, the selected area, environmental assessment, sales, purchases and consumption of raw materials, registered capital and investment capital proportion, etc. The feasibility report is not a compulsory document and no longer has to be approved by the authorities.

4. Environmental Impact Report

The environmental impact report for the establishment of an industrial unit must be submitted to the local government. The report usually covers matters such as types and volume of pollution involved in the project, the impact on environment, pollution controlling measures and a technical flow chart. The environmental impact report must be prepared by a technical expert. The environmental authority will assess the project, which can only proceed upon its written approval.



III. Foreign Trade Policy 三、外贸政策

(A) TARIFF MEASURES

Import tariffs

China import tariffs are calculated on the basis of the Harmonisation System of Classification Codes (*HS-Code*) and the rates vary according to the type, composition and final destination of these products. Similarly to other jurisdictions, China provides a favourable tariff for imports from countries with whom it has a convention or an agreement and/or with WTO members.

Partial repayment of Export Taxes

The partial refund of taxes on exports is aimed at achieving competitiveness of exports and an increase in the quality of export goods. It consists of the recovery of part of the amount already paid as taxes on production and circulation of goods, whenever such goods are for export.

The Chinese Government has repeatedly extended the percentage of refund of taxes on exports of various products, mainly for textiles and clothing, iron, non-ferrous metals, petrochemicals, information technology and energy. The current value of tax deduction can be easily found on the website of the State Administration of Taxation <http://www.chinatax.gov.cn/>.

(B) NON-TARIFF MEASURES

(i) CLASSIFICATION OF IMPORTS

Imported goods are subject to different requirements and are divided into the following categories:

- prohibited goods - weapons, poisons and chemicals of a toxic nature;
- restricted circulation goods - the ones that require an import licence or are subject to limitation by quota;
- free circulation goods - class that comprises the vast majority of imports.

More detailed information about categories of goods, their restrictions and relevant policies involving each type may be obtained on the English language web site of the Ministry of Commerce of China: <http://english.mofcom.gov.cn>.

(ii) IMPORT LICENCE

The Chinese Government has recently implemented a system of "import licences (进口许可证)" that allows a more stringent control of certain imported goods of restricted circulation. For example, on 1 April 2007, the Chinese Government waived import licences on 338 different categories of products. With the new "licensing system of importation", Chinese importers may request an "automatic import licence" (自动进口许可证).

Import licences are granted by the Chinese Ministry of Commerce (商务部) and the General Administration of Customs (海关总署). The latest list of catalogues of goods subject to automatic import licence in 2014 is included in Announcement No. 98 (2013) of the Ministry of Commerce and the General Administration of Customs (商务部、海关总署公告2013年第98号 - 2014年《自动进口许可管理货物目录》公告).

(iii) IMPORT QUOTAS

Import quotas are used as a form of protection of local producers of goods in the domestic market economy. Since China joined the WTO in 2001, it has been cancelling its import quotas for various types of products.

Import quotas are regulated and determined by the National Commission on Reform and Development and by the Ministry of Commerce.

(iv) ANTI-DUMPING AND ANTI-SUBSIDY

(A) REGULATIONS

China currently adopts extensive regulations that deal with the anti-dumping measures, providing and addressing possible breaches. Some examples of regulations are: the Anti-dumping Regulation of the PRC (revised in 2004) (中华人民共和国反倾销条例), the Provisions on Anti-dumping cases concerning Exported Products (2006) (出口产品反倾销案件应诉规定), the Provisions on the Antidumping Investigation of Industry Injury (2003) (反倾销产业损害调查规定), the Interim Rules on the Access to Non-Confidential Information in Anti-dumping Investigations (2002) (反倾销调查公开信息查阅暂行规则), the Interim Rules on Price Commitments in Antidumping Investigations (2002) (反倾销价格承诺暂行规则), etc.

The Tariff and Classification Committee of State Council and the Ministry of Commerce are the bodies responsible for setting the anti-dumping and anti-subsidy regulations and directives.

(B) MEASURES TO PROTECT ANTI-DUMPING AND ANTI-SUBSIDY

As anti-dumping measures that may be imposed in China, there are (i) provisional anti-dumping measures (deposits in guarantee, letters of guarantee, etc.), (ii) obligations (they may take the form of guarantee given by the exporter on price changes or on ceasing any imports at prices deemed below market price, or even guarantees about the elimination or limitation of granted subsidies).

The Ministry of Commerce has the final say on the acceptability of such guarantees and/or anti-dumping measures (required when a dumping or subsidy situation is ruled, by final and irrevocable decision, as harmful to the domestic market - the entities responsible for the payment of tariffs will be the importers of the dumping products and/ or the subsidised products).

(C) ANTI-DUMPING AND ANTI-SUBSIDY AUTHORITIES

Ministry of Commerce (MOFCOM)

- Bureau of Fair Trade for Imports and Exports of the Ministry of Commerce (商务部进出口公平贸易局) - responsible for the admission of applications, filing of cases, goal-setting for products, providing of information and notification of the parties involved in situations of dumping or granting of subsidies. It is also responsible for the investigation procedure in relation to offences and for setting the minimum margin below which the product is considered under market value, and for supervising the implementation of agreed prices (<http://wms2.mofcom.gov.cn/>). Furthermore, it is also responsible for conducting and coordinating cases involving situations considered as dumping and public subsidy initiated by third party countries dealing with exported Chinese products.
- Bureau of Industry Injury Investigation of the Ministry of Commerce (商务部产业损害调查局) - responsible for reviewing issues, conducting investigations and determining possible damage to the domestic industry, as well as for the investigation and determination of damage to the agricultural industry. It also works directly with the Ministry of Agriculture in conjunction with the Ministry of Commerce.
- Bureau of Industry Injury Investigation of the Ministry of Commerce (商务部产业损害调查局) - responsible for the investigation and analysis of possible damage to the domestic industry. The investigation and determination of damage to agriculture will also have the direct involvement of the Ministry of Agriculture in conjunction with the Ministry of Commerce.
- The Customs Tariff Commission of the State Council (国务院关税税则委员会), under the supervision of the State Council, is responsible for collection of anti-dumping and anti-subsidy payments, according to the determination of the Ministry of Commerce, which will subsequently make them public.

(D) ANTI-DUMPING CASES IN CHINA

China frequently faces claims of anti-dumping filed by foreign countries. For further information about these cases, please see the website of Bureau of Fair Trade for Imports and Exports of the Ministry of Commerce at: (<http://gpj.mofcom.gov.cn>)



IV. Taxation

The Chinese tax system is regulated by sparse laws, administrative regulations and tax rules issued by various authorities at different levels. The authorities involved are the National People's Congress (全国人民代表大会) and its Standing Committee (常务委员会), the State Council (国务院), the Ministry of Finance (财政部), the State Administration of Taxation (SAT) (税务总局), the Tariff and Classification Committee of the State Council (国务院关税税则委员会) and the State General Administration of Customs (海关总署).

Tax laws are approved by the supreme legislative authority, the National People's Congress, e.g. the Law of the People's Republic of China on Individual Income Tax (中华人民共和国个人所得税法) or its Standing Committee, for example the Law of the People's Republic of China on the Administration of Taxation Collection (中华人民共和国税收征收管理法). The regulations and administrative rules are drafted by the State Council, for example, the Detailed Regulations for the Implementation of the Law of the People's Republic of China on the Administration of Tax Collection (中华人民共和国税收征收管理法实施细则) or the State Council under the authorisation of the National People's Congress and its Standing Committee, such as the Provisional Regulations of the People's Republic of China on Value Added Tax (中华人民共和国增值税暂行条例). The tax rules of the different tax departments are approved by the Ministry of Finance, the State Administration of Taxation, the Tariff and Classification Committee of the State Council and the State General Administration of Customs, for example, the Detailed Rules for the Implementation of the Provisional Regulations of the People's Republic of China on Business Tax (中华人民共和国营业税暂行条例实施细则).

The government authority responsible for collecting taxes is the State Administration of Taxation. The State General Administration of Customs and its offices are responsible for collecting tariffs. Hong Kong SAR and Macau SAR have independent tax systems and double taxation agreements with China, meaning that the Central Government cannot levy any tax in these two special administrative regions.

(A) TYPES OF TAXES

Taxes in China can be divided into various categories, according to their nature and function:

- Taxes on turnover: the collection of this category is normally based on the taxpayers' turnover or sales in the sectors of manufacturing and the distribution or services, and include value added tax, consumer tax and transactions tax.
- Taxes on income: these taxes are assessed on profits earned by producers or traders or income earned by individuals, such as the Enterprise Income Tax and Individual Income Tax.
- Taxes on natural resources:³ these taxes are assessed by the usage of natural resources in the territory of the People's Republic of China and apply to investors involved in holdings of natural resources.
- Taxes for specific purposes: these taxes are collected for specific regulatory reasons, including tax on construction and city maintenance, tax on the occupation of cultivation land, the regulating tax on investment in fixed assets, land value added tax, and the tax on the acquisition of motor vehicles.
- Property tax: this category is based on the properties held by individuals or legal entities, including the tax on residential property and the urban property tax.
- Taxes on conduct: This category of taxes is based on specific conduct, including but not limited to tax on vehicles and ships, stamp duty, the tax on contracts.
- Customs duties: taxes or customs charges are charged on goods and articles that are exported from China.

(B) TAXATION OF INDIVIDUALS

In accordance with the provisions of article 1 of the Individual Income Tax Law of the People's Republic of China (6th Revision, 2011) (《中华人民共和国个人所得税法》), all individuals who reside or who are domiciled in China or, not being under these conditions, who remain in China for over one year, must pay tax on personal income applicable to any income obtained from both inside and outside China.

Any income earned in China by individuals who reside abroad or are not resident in China, although they remain in Chinese territory for less than one year, will also be subject to taxation in China.

³ According to Article 1 of the Interim Regulations of the People's Republic of China on Resources Tax, entities and individuals that engage in mineral exploitation or salt production provided herein within the territory and territorial waters of the People's Republic of China (hereinafter referred to as "exploitation or production of taxable products") will be taxpayers subject to the resource tax and must pay resource tax in accordance with these Regulations.

INDIVIDUAL INCOME IN CHINA

The individual income in China is charged on the following:

- (i) Income derived from retainers and salaries;
- (ii) Income from private or domestic industries, namely income deriving from production and private trade.
- (iii) Income deriving from sales of commercial enterprises or leases to companies and institutions;
- (iv) Income from services rendered;
- (v) Income from copyright;
- (vi) Income from royalties;
- (vii) Interest, dividends and bonuses;
- (viii) Rent;
- (ix) Income from transfer of property;
- (x) Other occasional earnings; and
- (xi) Other taxable income specified by the tax departments of the State Council.

TAX RATES ON PERSONAL INCOME

The main tax rates of personal income in China are (i) the progressive rate and (ii) fixed rate, depending on the types of income.

(i) The progressive tax is applicable to the following income:

- Salaries: the rate varies between 3% and 45%. The amount of income subject to taxation is the remaining monthly income after deduction of RMB 3,500. For foreigners, the amount of the deduction is RMB 4,800 per month.
- Income from private or domestic industries, namely arising from private production and trade and income from the assignment or leasing of companies to other companies and institutions: the rate varies between 5% and 35%, the tax base being the annual income obtained, after deduction of costs, expenses and losses.

(ii) The flat rate applies to the following income:

- Tax on authorship rights: the tax rate on this one off income is 20%, to which a 30% tax reduction must be made.
- Taxes on services: the tax rate is 20%. An additional amount may be charged on extremely high remuneration.

In the remaining cases, the tax rate is always 20%, namely on royalties, income from interest, dividends and premiums, rent, income derived from transfer of property, occasional earnings and other income.

EXEMPTIONS OF INDIVIDUAL INCOME TAX

Certain types of income are exempt from taxation in accordance with the provisions of Article 4 of the Individual Income Tax Law of the People's Republic of China (2nd Revision, 2007). As an example, some subsidies and/or scholarships for science, education, technology, health, etc., interest derived from Public Treasury bonds or income of diplomatic representatives and their employees are exempt under law and international conventions applicable in China.

(C) TAXATION OF LEGAL ENTITIES (COMPANIES)

The main taxes applying to legal entities in China are: (i) Enterprise Income Tax, (ii) Value Added Tax, (iii) Consumption Tax, (iv) Business Tax and (v) Customs Duties.

(i) EIT - ENTERPRISE INCOME TAX

According to the Law of the People's Republic of China on Enterprise Income Tax, effective since 1 January 2008, companies and other organisations earning income in China are subject to this tax. Individual entrepreneurs or business partnerships are not subject to EIT, but rather to individual income tax.

Tax base

The law distinguishes between “resident companies for taxation purposes” and “non-resident company for taxation purposes”, applying a different tax in each case.

A company based in China or based in a foreign country but with its main administrative organisation established in China, is generally considered as a “resident company for taxation purposes” and should pay EIT to the Chinese government for all the income earned worldwide.

For companies that are established in foreign countries but with an establishment in China, or that have no establishment in China, but have a source of income there, are generally deemed to be “non-resident company for taxation purposes” and should pay EIT only on the income obtained, directly or indirectly, from China.

Rates and tax assessment

The amount of EIT to be paid by a “resident enterprise for taxation purposes” is typically calculated by reference to income subject to taxation, at the applicable rate of 25%. The EIT rate for “non-resident companies for taxation purposes” is 20% on their income generated in China.

Since 1 January 2008, foreign investment companies and other foreign companies benefit from the same tax treatment and must observe the same tax rules as Chinese companies. Presently, favourable treatment is granted to small companies and businesses with small profits, which pay 20%, while companies whose business is focused on cutting-edge technology pay 15%.⁴

⁴ According to Article 28 of the Law of the People's Republic of China on Enterprise Income Tax:
With respect to a qualified small enterprise earning low profits, the tax charged on its income will be reduced to a rate of 20 per cent. With respect to a high and new technology enterprise that needs key support by the State, the tax levied on its income shall be reduced at a rate of 15 per cent.

Major exemptions and tax deductions

Income exempt from tax:

- (i) income derived from treasury bonds;
- (ii) dividends, premiums, etc. distributed among private investment companies that are resident for taxation purposes;
- (iii) income derived from investment, such as dividends, bonuses, etc. obtained by non-resident companies for taxation purposes with establishment in China, paid by companies resident for taxation purposes, provided that such income is actually connected with the said establishment;
- (iv) income of a non-profit organisation (which meets all the criteria) may be exempted from EIT.

Tax exemptions or tax reductions may be granted to companies or projects whose income comes from projects in agriculture, forestry and aquaculture; investment projects in basic infrastructure strongly supported by the government; environmental protection, renewable energy and hydro conservation that meet all the conditions imposed; projects involving the transfer of technology, etc.

Payment of EIT and tax statements

The EIT owed by a company can be paid in advance every month or every quarter. The company must submit its self-assessed EIT returns and pay by bank deposit to the authorities in the last 15 days of each month or quarter. In the 5 months prior to the end of the year, the company must file the annual statement of EIT with the tax authority and calculate the tax payable and the refundable tax.

(ii) VAT (VALUE ADDED TAX)

Under the Interim Regulation of the People's Republic of China on Value Added Tax (2008 Revision) (中华人民共和国增值税暂行条例), revised on 10 November 2008 and effective as from 1 January 2009, any company, entity or individual that engages in sales or import of goods, the provision of services of processing, repair and distribution ("taxable services") is subject to VAT tax in China.

Taxable goods and tax rates

- 0% - for export goods (excluding those stipulated by the State);
- 13% - for the following goods: i) cereals, vegetable cooking oil; ii) water, central heating, air conditioning and hot water equipment, domestic gas, liquid oil gas, natural gas, methane and coal for domestic use; iii) books, newspapers and magazines; iv) animal feed, chemical fertilizers, pesticides, agriculture machinery, film components; and v) other merchandise specified by the State Council from time to time; and
- 17% - for all goods not mentioned above and for manufacturing services, repair and replacement.

Payment of tax due

Taxpayers subject to VAT are divided into (i) small-scale taxpayers and (ii) general taxpayers, and the calculation of the tax payable is different in each case.

(i) Currently, small-scale taxpayers are enterprises whose annual revenues from sales are less than RMB 500,000, and relating to companies in the manufacturing industry and companies that provide services subject to taxation, retail companies and other companies with less than RMB 800,000 in annual revenue. These pay VAT at a rate of 3%.

(ii) The remaining taxpayers, other than small-scale taxpayers, must register with the tax authorities under the general taxation regime. To determine the amount of VAT to be charged, these companies must separately calculate the tax already borne by the company and the tax that is levied by the State. The difference between the tax paid and the tax collected will be the current amount of VAT to be paid.

Imported goods

Imported goods are taxed on the basis of the estimated final price by, applying the relevant tax rate.

VAT refund to exporters

Exporters can apply for a refund of VAT paid on export goods.

VAT exemptions

Exempted items include: agricultural products sold directly by producers; contraceptive products; antique books; instruments and equipment imported to serve scientific research and education directly; offers of goods and equipment donated freely by foreign governments or international organisations; articles of specific use for the disabled that are imported directly by charitable or social organisations and second hand items.

(iii) CONSUMPTION TAX

Anyone involved in the production, import or selling of consumption products taxable in China must pay Consumption Tax.⁵ Taxable consumption products exported by taxpayers are exempt from consumption tax, unless they are restricted by the state of export.

Taxable items

Tobacco; spirits and alcohols; cosmetics; valuable jewellery, precious stones and jades; firework materials; refined oil products; motor vehicle tyres; motorcycles; motor vehicles; golf balls and equipment; luxury watches; yachts; wooden disposable chopsticks; and wood floors.

(iv) BUSINESS TAX

Anyone who provide the services stated by law, intangible assets or who sells real estate is subject Business Tax according to *Interim Regulation of the People's Republic of China on Business Tax* (中华人民共和国营业税暂行条例), revised on 10 November 2008 and in effect as from 1 January 2009.

Taxable goods and tax rates

- - 3% - communications and transport; construction; post and telecommunications; culture and sports;
- - 5% - financial transactions and insurance; services; sale of real estate; transfers of intangible assets;
- - 5% - 20% - entertainment.

⁵. According to Article 1 of Interim Regulations of the People's Republic of China on Consumption Tax, any institution and individual that produces, subcontracts the processing of, or imports consumer goods specified in these Regulations and other institutions or individuals that are recognised by the State Council and sell the consumer goods specified in these Regulations will be taxpayers of consumption tax and must pay consumption tax in accordance with these Regulations.

Tax settlement

Taxpayers who provide taxable services or intangible assets or sell real estate must calculate the tax payable according to the gross revenue of the business and the specific tax rates.

Major exemptions

Exemptions from Business Tax exist: (i) for care services provided by nurseries, kindergartens, nursing homes, old people's homes and charity institutions for the disabled, as well as funeral and marriage services; (ii) for services provided by the disabled, according to their capabilities, (iii) for medical services provided by hospitals, clinics and other health institutions; (iv) for educational services provided by schools and other educational institutions and services provided by students in student-worker programmes, (v) for agricultural tractor cultivation, irrigation and drainage, prevention and control of plant diseases and elimination of pests, in plant protection, agro-pastoral insurance and in related technical training, and also in the breeding, prevention and control of diseases of poultry, livestock and fish farms; (vi) for income derived from admission fees related to or collected by memorials, museums, cultural centres, administrative organisations for the protection of cultural relics, art galleries, exhibition halls for painting and calligraphy as well as libraries, (vii) for income derived from admission fees for cultural and religious institutions; and (viii) insurance provided by domestic insurance companies linked to exports of goods.

(v) CUSTOMS DUTIES

The consignees of imported goods, the consignors of exported goods and owners of imported goods are subject to Customs Duties.

Fees

Fees include import and export tariffs. Import tariffs are divided into six categories: the "most favoured nation" tariff, the conventional tariff, the preferential tariff, the normal tariff, the quota tariff and the temporary tariff. The "most favoured nation" tariff is applicable to imports from countries or regions with which China has bilateral or multilateral trade agreements containing a 'most favoured nation clause'. The conventional tariff and preferential tariff are respectively applicable to imports from countries with which China has already signed trade agreements containing preferential or special preferential duty clauses. The normal rate applies to the import of goods from other countries.

Settlement of charges

Customs duties are payable or paid in accordance with the ad valorem principle or according to the quantities. The taxable price of goods for import and export should be defined by the customs authorities based on their transfer prices. If the price of the transaction cannot be determined, the customs authorities can estimate the taxable price in accordance with the law. The price will usually include the value of goods, freight, insurance, etc.

Main reductions and exemptions from customs duties

The following goods may be exempted from customs duties if approved by customs authorities:

- a) goods donated by international organisations or foreign governments⁶ ; when the value contained in a single billing document is lower than RMB 50, goods used for advertising or non-commercial samples;
- b) goods or products that are specified in international trade agreements or contracts to which China is a party;
- c) raw materials, parts and accessory components, components and materials for packaging imported for processing, assembly or production aimed at exportation of products actually completed and exported; or
- d) imported products which are subsequently exported.

(vi) TAX ON REPRESENTATIVE OFFICES (REP. OFFICE)

Representative offices are subject to tax in China, even if they do not enter into local transactions or conduct any profit generating activities locally. Transfers of funds from the foreign company to its representative for funding of the Rep. Office's costs are deemed to be income of the Rep. Office.

Rep. Offices are, therefore, subject to the following taxes:

- (i) trade tax applicable to monthly administrative expenses, and
- (ii) tax on the income of the company.

There are two major methods for tax assessment in relation to the Rep. Office:

- (i) the effective yield method - applicable to representative offices of law and accountancy firms.
- (ii) the cost-plus method - taxable income of the Rep. Office will be calculated according to the expenses incurred in the taxation period. The majority of the representative offices use this method.

Exemption

Rep. Offices that only engage in preliminary or subsidiary activities for the information and support of the main company; Rep. Offices established by foreign governments, non-profit organisations and non-governmental organisations (NGOs) may be exempted from payment of the above tax upon approval from the competent authorities.

AGREEMENTS TO AVOID DOUBLE TAXATION IN FORCE IN CHINA

Up to the end of June 2013, China had entered into 99 Double Taxation Avoidance Agreements with various regions and countries all around world, 96 of which have been put into effect, and has three tax arrangements with Portugal and China's Special Administrative Regions of Macau and Hong Kong.

⁶ According to the Regulations of the People's Republic of China on Import and Export Duties, Article 45, "The duties on goods damaged prior to customs release may be deducted in accordance with the degree of damage confirmed by the customs."



V. Labour Relations

LABOUR LAWS IN CHINA

Labour in China is governed by a set of comprehensive laws that have been subject to several revisions to strengthen the protection of workers' rights. The main labour laws include:

- Labour Law of the People's Republic of China (1994) ("Labour Law") 中华人民共和国劳动法; (in force from 1 January 1995)
- Employment Contract Law of the People's Republic of China (Revised 2012) 中华人民共和国劳动合同法 (in force from 1 July 2013);
- Labour Arbitration and Dispute Resolution of the People's Republic of China (2007) 中华人民共和国劳动争议调解仲裁法 (in force from 1 May 2008), and
- Labour Unions Law of the People's Republic of China (2009 Revision) 中华人民共和国工会法

The Labour Laws listed above have been successively complemented by a number of national and local laws, regulations, measures and circulars.

HIRING EMPLOYEES

Duration

As in most jurisdictions, in China working schedules are divided into (A) part-time and (B) full-time.

(A) Part-time – involves the provision of normally no more than 4 hours per day and no more than 24 hours per week.

(B) Full time – full time work is divided into three types of contract, as follows:

- (i) fixed-term: date of expiry pre-agreed;
- (ii) open / no fixed-term: there is no term date specified;
- (iii) by project / task – for completion of a defined task.

FORMS OF CONTRACT

The employment contract must be executed in writing. If the employment relationship was established without a written contract, the contract should be completed within 1 (one) month from the date on which the employee began work.

If an employment contract is not completed within 1 (one) month after the beginning of employment, the employer will be subject to payment of double wages during the period without completion of the employment contract in writing. If 1 (one) year passes without a written contract, the employer is not only subject to payment of double the wages for that 1 (one) year period but will be bound in relation to the employee by an open-ended employment contract.

STATUTORY REFERENCES

Pursuant to the Law on Employment Contracts, the following must always be stated in an employment contract:

- (i) name and address of the employer and its legal representative or the main responsible person;
- (ii) name, address and ID card number or any other valid identification document of the employee;
- (iii) duration of the employment contract (term / no-term);
- (iv) job functions/ category and workplace;
- (v) working hours, rest and leave days;
- (vi) remuneration;
- (vii) social security;
- (viii) labour protection, working conditions and prevention against accidents at work.

Regarding the probation period, the Labour Law provides a maximum probation period of 1 month if the contract term is between 3 months and 1 year. If the term is of 1 to 3 years, the probationary period may not exceed 2 months. For a term contract over 3 years or a no-term contract, the probation period should not exceed 6 months. There can be no more than one probation period.

MINIMUM WAGES

According to the Provisions on Minimum Wages (2004) (最低工资规定), the employer must pay the employee the minimum wage set by law, subject to the condition that the employee has worked within normal working hours, as defined in the employment contract and in accordance with the law.

WORKING HOURS

The normal working hours in China correspond to 8 hours a day, 5 days a week for a maximum period of 40 hours, with 2 rest days (typically on Saturday and Sunday). Article 36 of the Labour Law of the People's Republic of China provides that "The State shall use a working hour system under which employees work for no more than eight hours a day and no more than 44 hours a week on average". Article 38 of the same law provides that, "The employer shall guarantee that its staff and workers have at least one day off in a week."

Any additional hours of work required by the employer should be compensated according to the standard below indicated:

- Working days: 150% of the standard remuneration;
- Rest days: 200% of the standard remuneration, and
- Public holidays: 300% of the standard remuneration.

Currently, public holidays in china include New Year's Day (1 day), Spring Festival (3 days), 1 May (1 day), National Day holiday – 1 October (3 days), Qing Ming Day (1 day), Dragon Boat Festival (1 day) and Full Moon Festival (1 day).

PAID LEAVE

Apart from the public holidays established by law, according to the Regulation on Annual Paid Leaves to Employees (职工带薪年休假条例), those who have worked continuously for 1 (one) year or more are entitled to a period of paid annual leave, as follows:

- 5 days - employees who have worked for 1-10 years;
- 10 days - employees who have worked for 10-20 years;
- 15 days - employees who have worked for 20 years or more.

If an employer does observe the employee's right to annual leave, the employee is entitled to the proportionate payment of three times his or her daily remuneration for each day of leave not taken.

SOCIAL SECURITY

Employers in China must grant the following benefits and social security payments to its employees, known as "Five insurances, One Fund":

- Basic pension insurance;
- Unemployment insurance;
- Medical insurance;
- Maternity insurance;
- Insurance against accidents at work; and
- Housing Fund.

The employee and employer contribute together to the first 3 types of insurance (basic pension, unemployment insurance, medical insurance) and to the housing fund, while the employer is the sole contributor to the last 2 types of insurance (maternity insurance and insurance for accidents at work). The rates vary by geographic location.

The maximum percentage of Social Security for each employee to pay may not exceed 40% of their wages. Employees do not need to pay to the remainder of the highest proportion.

MATERNITY PROTECTION

The law in China grants mothers security of employment from the time they inform the employer of the pregnancy until 1 year after the child's birth. The female employee is also entitled to a maternity leave of 90 days, to be granted during the period closer to birth (usually 15 days before and 75 days after birth). In addition, first time mothers over 24 years old can get additional leave days, which vary depending on the different regional jurisdictions (for example, in Shanghai it is 30 days). The employee's remuneration during the pregnancy period is paid by the Social Security Fund.

NON-COMPETITION AND CONFIDENTIALITY

The Law on the Employment Contract specifies that an employment contract between employer and employee may include provisions on non-competition and confidentiality. The obligation relating to confidentiality normally requires that the employee maintains confidentiality about business secrets and intellectual property of the employer. The non-competition obligation after termination of employment requires the payment of compensation in order to be valid.

The obligations of non-competition are not applicable to all employees and apply only to management, senior staff and employees with access to trade secrets of the employer.

Any non-competition agreement must be in writing, in a separate document but forming part of the employment contract and it must define the term, scope, radius of geographical application and compensation for the period of non-competition, etc. The term of non-competition cannot be longer than 2 (two) years.

TERMINATION OF EMPLOYMENT

(i) TERMINATION BY MUTUAL AGREEMENT

The employment contract may be terminated by mutual agreement between the employer and employee. It should be noted that if the employer is proposing to terminate the work contract, even if the employee agrees, the employer has to pay termination compensation to the employee.

(ii) TERMINATION BY THE EMPLOYEE

The employee may terminate the contract of employment, giving 30 (thirty) days' written notice to the employer. During the probationary period, the employee must give 3 (three) days' notice.

If there is just cause of termination, the employee may terminate without prior notice to the employer. For example, there will be just cause for termination by the employee if the employer does not provide the working conditions agreed in the employment contract or if the employer does not pay the remuneration in full, among others.

(iii) TERMINATION BY THE EMPLOYER

Prior to terminating an employment contract, the employer is advised to pay special attention to the causes and legal requirements applicable, and in some cases it may be necessary to pay compensation. The legal termination of employment contracts in China is divided into two categories: (a) termination without notice and (b) termination with notice.

(a) The employer may terminate the employment contract without giving any notice to the employee if the latter fails to comply with the company's internal rules or the rules of general labour law, if convicted of a crime, or causing damage to the employer by abandoning his or her work post, or for violation of the exclusivity obligation (when applicable).

During the probation period, the employer may also terminate the employment contract without notice.

(b) There are several other circumstances under which the employer may terminate the employment contract, by giving the employee 30 days' notice or payment in lieu. The Employment Contract Law provides an exhaustive list of situations based upon which the employment contract may be terminated, such as when it is deemed that the employee does not have appropriate skills for the job, even after professional training, or cannot work due to suffering from a disease unrelated to the employment.

(iv) PROHIBITION ON TERMINATION

Under Chinese labour law, unilateral termination is clearly prohibited under the following circumstances:

- (i) Whenever the employee is suspected of or has been medically confirmed to have developed an occupational disease, or is exposed to occupational hazards and has not undergone a medical examination, or is under the period of diagnosis; before leaving his or her position, the employee must go through a health check-up;
- (ii) When confirmed that the employee has fully or partially lost his or her capacity to work as a result of an illness or injury related with his employment;
- (iii) When the employee has contracted an illness or injury unrelated to his or her employment and is still within the period of medical treatment;
- (iv) When the employee is pregnant (having communicated such pregnancy to the employer), and up to 1 (one) year after the child is born;
- (v) When the employee has worked for a period of at least 15 years and will retire in less than 5 years.

(v) LAYOFFS FOR ECONOMIC REASONS

If the employer needs to dismiss its employees for economic reasons, it should follow a series of special regulations. The economic reasons may be justified by a restructuring process, bankruptcy, insolvency or serious difficulties in the production or the management of the business operations, and others stipulated by law.

If at least 20 employees or 10% of the workforce (whichever is less) has to be laid off, the employer must follow these procedures:

- (i) issue a notice 30 days before the layoff;
- (ii) explain the situation clearly and consult employees and trade unions representing them; and
- (iii) report the reduction/layoff plan to the local labour authorities and provide justification for it.

In its decision, the employer shall give priority to maintaining employees with long term employment contracts as well as those who provide for the main sustenance of their families and those who have elderly or small children under their care. These employees must be notified and given priority in any recruitment by the employer within 6 months.

(vi) COMPENSATION FOR TERMINATION OF EMPLOYMENT CONTRACT

For termination of employment under certain conditions, the employer has to pay the employee compensation for termination.

If a fixed term contract expires and is not renewed, compensation for termination is mandatory in China.

Compensation for termination of an employment contract is also imposed in all circumstances set out above for notice of termination and layoffs for economic reasons. If the employer has the right to terminate the contract of employment without notice under the circumstances described, compensation for termination of employment contract is not mandatory.

In general, compensation should be paid to the employee based on the number of years of work at the rate of a monthly salary for each full year of work. For periods between 6 to 12 months, the compensation should be one month's salary. For periods less than 6 months, the compensation should be half of one month's salary. "A monthly salary" is usually set by Chinese labour law as the average monthly salary over a period of 12 months of work prior to termination.

WORK RULES FOR FOREIGN EMPLOYEES

The main law regulating foreign employees in China is the Regulation on the Administration of Employment of Foreigners in China (2010 Revision) (外国人在中国就业管理规定), in force since 12 November 2010. .

To hire a foreigner, the employer in China firstly has to qualify for the “Certificate of the People’s Republic of China Permitting the Employment of Foreigners (中华人民共和国外国人就业许可书” - “Certificate of Permission for Hiring”.

In order to seek employment in China, a foreigner must meet the following qualifications:

- be 18 years of age and in good health;
- have professional skills and work experience for the position to be filled;
- have no criminal record;
- receive an employment offer from a Chinese employer;
- Hold a valid passport or other international travel documents equivalent to a passport

Foreigners who fail to obtain a certificate of residence (with F, L, C, and G type visas) and those under study programmes in China should not work without prior approval by the competent authorities.

The term of employment contracts between an employer and a foreign employee may not exceed 5 years and renewal is subject to approval by the labour authorities in China.

Foreign employees working in China need authorisation to change jobs, or otherwise the work in the new (unauthorised) position will be deemed illegal.

CHINA VISAS

A foreigner wishing to enter, exit or transit through Chinese territory must apply for a visa. Generally, the issuing of a visa and the type of visa to be granted by the Chinese authorities will be determined by the nationality of the foreigner, the reason for his or her visit to China and the type of passport (in China, there are three types of passports: civil passport, business passport and official passport).

The Chinese authorities responsible for granting visas are authorised to operate through the Ministry of Foreign Affairs of China, such as embassies, consulates, agencies and specialised departments established abroad.

TYPES OF VISAS

There are four types of visa in China: diplomatic visa; courtesy visa; official visa and ordinary visa. In general, there are eight different types of ordinary visas that may be requested by the interested foreigner, such as:

- work visa (Z-type);
- residency visa (D-type);
- student visa (X-type);
- visiting visa (business or academic reasons) (F-type);
- tourist visa (L-type);
- transit visa (G-type);
- visa to foreign correspondents (journalists) (J-1 or J-2-type); and
- visa for international transportation employees (train, ships and aircraft) (C -type).

More detailed information on this matter may be obtained from immigration lawyers, by consulting of the official Chinese websites or from Chinese embassies around the world

(see also <http://www.china.org.cn/english/Life/34355.htm>).



VI. Intellectual Property

After China's accession to the WTO, the country is now required to make greater efforts to guarantee the protection of intellectual property, especially regarding its legislation. At present, China has laws and regulations that govern the protection of patents, trademarks, design of electronic circuits, franchises, software, copyright, etc.

The Trademark Office (商标局), under the direct supervision of the State Administration for Industry & Commerce (国家工商行政管理总局), is the body responsible for registering and control of trademarks in the country. **The State Intellectual Property Office (SIPO) (国家知识产权局)**, which acts under the control of the State Council, is the body responsible for promoting and coordinating the protection of the rights inherent to patents in the country.

(A) PATENT RIGHTS

Patent rights cover inventions (发明), utility models (实用新型) and their designs (外观设计). An invention or any utility model, to which the patent is awarded, should be innovative, i.e., resulting from a technical study that enabled the invention and its practical application. A design, to which the patent is awarded, should have distinctive features and not be identical or similar to any publicly known design at domestic or foreign levels, and it should not conflict with lawful rights that were obtained by any other entity before the date of filing.

The term of the patent is 20 years and the duration of a patent for utility models or design is 10 years, both counted from the date of application.

The Patent Law stipulates that no patent will be granted for an invention that is contrary to law or to social morality, harms the public interest or is based on genetics, if proven that access or use violates the laws or applicable administrative regulations. Moreover, the Patent Law of China states clearly that no patent rights may be granted for certain scientific discoveries, rules and methods that involve mental processes, diagnosis or methods for the treatment of diseases, varieties of animals and plants, excluding scientific methods used to achieve a particular variety of plant or animal; substances obtained from nuclear transformations, or designs used to identify patterns, colours or the combination of both.

Any foreigner, foreign company or any other type of foreign organisation without residence or a business office in China, that intends to apply for a patent or deal with matters related to patents in China, must hire one of the Patent Agencies duly constituted and certified to represent its interests before the authorities. Patent rights in China also respect priority rights over patents.

(B) TRADEMARK

The *Trademark Law of China* was amended on 30 August 2013 and came into force on 1 May 2014.

This Law provides 4 types of trademarks, including commodities trademarks (商品商标), service trademarks (服务商标), collective trademarks (集体商标) and certification trademarks (证明商标).

The validity period of the registered trademark is 10 years from the date the registration is approved, renewable for successive periods of 10 years. An application for renewal must be made within twelve months prior to expiration, and only one extension period of six months will be granted if the registering person or entity fails to request the renewal in due time.

With the exception of a few other limitations, any visible mark distinguishing one type of goods from another is subject to registration of the mark, if easily identified and not conflicting with any other rights that have been acquired by those who hold a priority right. These brands include any word, device, letter, number, three-dimensional sign, colour combination, sound and combination thereof.

Chinese trademark law clearly stipulates which trademarks may not be registered. These include trademarks identical to names, flags or state symbols of countries or international organisations, without prior approval, or even marks which lack features that distinguish them from others, as well as the brands that encourage discrimination, exaggeration and falsehood.

The Trademark Law of China also establishes the conditions of the priority right. Moreover, if a trademark is recognised as “well-known”, it may enjoy other protections. In addition to the Trademark Law of China, “well-known” marks also benefit from protection under the Provisions for the Determination and Protection of Well-known Trademarks (驰名商标认定和保护规定), in force since 1 June 2003.

(C) TECHNOLOGY AND TECHNICAL AND SCIENTIFIC SERVICES

The Regulation on the Protection of Integrated Circuit Design (Integrated Circuit Layout Design) (集成电路布局设计保护条例) of 2001 provides for the protection of intellectual property rights relating to the design of integrated circuits.

The design of integrated circuits includes a three-dimensional display of the integrated circuit composed of two or more components (one being the active component), the circuits being interconnected or set in three-dimensions, in part or in their entirety, intending for their manufacture. The protection of the designs thus conferred does not apply to ideas, data processing systems, operation methods or mathematical concepts.

The validity of the exclusive right of protection for designs of integrated circuits is 10 years from the date of the first request for protection or the date on which the design in question is made available for the first time for commercial use, anywhere in the world. However, after 15 years from the date of creation of the design in question, whether registered or made available for commercial use, the right to protection and exclusivity ceases to exist.

(D) COPYRIGHT

The works protected by the Law of Copyright in China are intellectual creations in the fields of literature, art, natural sciences, social sciences, technology engineering and other areas more likely to be published in a tangible form, for example, oral and written works, musical works, paintings, sculptures, maps, etc.

Copyright includes the rights of publication, authorship, alteration, integrity, reproduction, payment, distribution, location, exposure, performance, exhibition, broadcast, translation, compilation of words, etc. They may be partially transferred by the holder, but the rights of publication, authorship, alteration and integrity cannot be transferred.

Copyrights are valid from the day the work to be protected is in its final form. The protection of the rights of authorship, alteration and integrity are not limited by time, while the other copyright rights are limited to specific protection periods. These time-limited copyrights lapse 50 years after the death of the work's creator (in works of joint authorship works the copyright will lapse after the death of the last surviving co-author). In some special works, including cinematographic works or those created in a way similar to cinematography, as well as those where the holder of the copyright is a legal entity, the 50-year term will be calculated from the date of the first publication of the work. When a work created by a foreign person is published in China within 30 days after it was first published outside the country, it is deemed to have been published in China simultaneously.

The Chinese Law on Copyrights also establishes the cases in which the work can be used without the approval of the owner or without payment of remuneration to the holder.

(E) FRANCHISE

Franchises are regulated by the Regulation on the Administration of Commercial Franchises (商业特许经营管理条例), in force since 1 May 2007. The term "commercial franchise" (hereinafter referred to as "franchise") as mentioned in this Regulation refers to business operations by which an enterprise owning a registered trademark, enterprise mark, patent, know-how or any other business resource (hereinafter referred to as "franchiser") confers the right to use the said business resource on any other business operator (hereinafter referred to as "franchisee") by means of contract, and the franchisee undertakes business operations using the uniform business model as stipulated by the contract and pays franchising fees to the franchiser.

To engage in franchising activities, a franchiser must have a mature business model and the ability to provide long-term business guidance, technical support, business training and other services to the franchisee. The franchiser must also have at least two direct sales stores and have undertaken the business for more than a year.

A franchise contract must include the following main contents: term of the franchise, type, amount and payment method for the franchising fees, etc.

The franchise term stipulated in the franchise contract may not be less than three years, unless it is otherwise agreed by the franchisee. This provision does not apply when the franchiser and the franchisee renew the franchise contract.

Within 15 days of concluded a franchise contract for the first time, the franchiser must report it to the commercial administrative department for archival filing according to this Regulation.

(F) SOFTWARE

Computer software includes computer programs and related documentation. To enjoy protection in accordance with the Regulation of China on the Protection of Computer Software (Revised in 2013) (《计算机软件保护条例》(2013年修订)) (which came into force on 1 March 2013) the software should be developed independently by its creator and must already exist physically. Pursuant to regulations on software copyright, the available protection does not cover ideas, processing courses, operating methods, mathematical concepts applied to the development of that software, etc.

Holders of software copyright enjoy protection on publication rights, authorship, review, duplication, distribution, leasing, network dissemination of information, in addition to the right of translation, among others.

The protection of software is similar to the protection of other author rights and begins to run from the date on which the software is in its final form, i.e., fully developed.



VII. Judicial System

(A) JUDICIAL SYSTEM – COURT HIERARCHY

The judicial system in China has four levels of hierarchy, which are divided as follows:

- a) The People's Supreme Court, which is the highest authority; (最高人民法院)
- b) The People's Superior Courts; (高级人民法院)
- c) The People's Intermediate Courts; (中级人民法院)
- d) The People's District Courts, the first instance courts of the Chinese justice system. (基层人民法院)

In addition to the four different levels in the common Chinese judicial system, there are also special courts that deal with specific matters, such as military (军事法院), maritime (海事法院) and railway (铁路法院) matters.

All cases have the right to a second trial and the decision issued pursuant to the second analysis is considered final and not subject to appeal.

(B) ARBITRATION

Arbitration is regarded as a common and very important form of dispute resolution in China, especially in relation to trade disputes and related investments. The Arbitration Act of the People's Republic of China was adopted on 31 August 1994, by the People's National Congress, China's legislative body. It came into force on 1 September 1995 and was slightly revised on 27 August 2009⁷ (CAA 2009). The CAA 2009 applies to arbitration cases involving domestic or international issues. This law includes modern concepts and current information on arbitration and describes the basic principles by which arbitration is governed in China.

ARBITRATION AUTHORITIES

(1) Board of Arbitration

The board of arbitration is the authority to be appointed by the parties to the arbitration agreement. If no board of arbitration is appointed in the agreement, the two parties must make a complementary agreement to choose one. If the two parties fail to reach a complementary agreement, the arbitration agreement will be invalid.

(2) China International Economic and Trade Arbitration Commission (CIETAC - 中国国际经济贸易仲裁委员会) - It is considered the most important body in permanent operation. Since 2000, the CIETAC has also been known as the Court of Arbitration of the International Chamber of Commerce of China (CACICC, 中国国际商会仲裁院). The headquarters of CIETAC are currently located in Beijing, and there are two sub-commissions in the cities of Shanghai and Shenzhen, called respectively CIETAC (Shanghai Subcommittee) and CIETAC (Subcommittee of South China). To promote and encourage arbitration, the CIETAC set up 19 affiliated offices in various localities with specific business departments provide the best possible to those seeking to resort to arbitration.

⁷. Based on the "Decision of the Standing Committee of the National People's Congress on Amending Certain Laws" Article 95.

Matters that can be the subject of an arbitration award by the CIETAC are not limited to commercial disputes or merely based on the origin of the parties involved. Matters arising from economic and commercial transactions, whether contractual or not, may also be submitted to arbitration. These subject matters may include:

- International disputes themselves or disputes that involve international relations;
- Disputes originating from the Special Administrative Regions of Hong Kong, Macau or from Taiwan; and
- Internal disputes.

ARBITRATION AGREEMENT

A valid arbitration agreement is the basis of arbitration. It is a pre-requisite that the arbitration board accepts cases brought before it and disregards the jurisdiction of the courts.

However, even after the arbitration agreement has been signed by the parties, the courts may intervene if and when:

- a) the arbitration agreement is considered invalid or its validity has expired; and/or
- b) if a party resolves to take the dispute before the State Courts and the other party agrees.

CIETAC provides a Model Arbitration Clause (quote):

“Any dispute arising from or in connection with this Contract shall be submitted to the China International Economic and Trade Arbitration Commission for arbitration which shall be conducted in accordance with the Commission’s arbitration rules in effect at the time of applying for arbitration. The arbitral award is final and binding upon both parties.” (凡因本合同引起的或与本合同有关的任何争议，均应提交中国国际经济贸易仲裁委员会，按照申请仲裁时该会现行有效的仲裁规则进行仲裁。仲裁裁决是终局的，对双方均有约束力)

EFFECTS OF THE AWARD

The final arbitration award issued binds the parties with immediate effect, without the possibility of appeal. Nevertheless, the unsatisfied party has the right to seek review before the judicial courts, which may hold the Arbitration Award to be invalid if it finds evidence that any of the conditions laid down in the Arbitration Law has been infringed, such as disregard for the regulations and directives in force and the consequent (proven) violation of these regulations, among others.

RECOGNITION AND ENFORCEMENT OF FOREIGN ARBITRAL AWARDS

China has been a signatory country to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (“1958 New York Convention”) since 22 April 1987, and its accession to the Convention is subject to trade restrictions and reciprocity.

Due to the applicability of that Convention, it is possible for parties to certain legal relationships to recognise and enforce Arbitral Awards which are issued in the State where the debtor has assets, provided that such State is also a signatory country to the New York Convention. According to the UN Committee on the International Trade Law (UNCITRAL), so far 149 countries are signatories to the Convention. For further details, please check the website of UNCITRAL at: http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention_status.html



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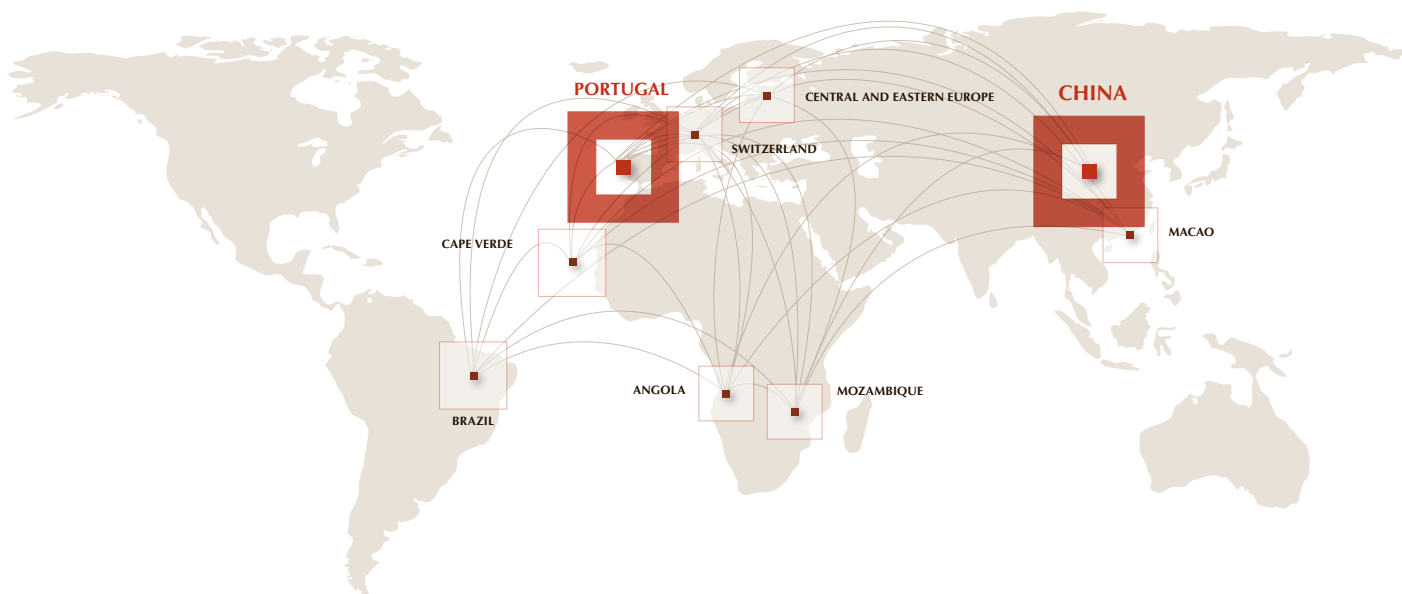


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PLMJ INTERNATIONAL LEGAL NETWORK

PLMJ International Legal Network brings together leading firms from each country while maintaining the full legal and financial independence of all members through a deep respect for local requirements and rules of professional ethics, and ensuring a standard culture of quality service to the client.

This Guide was prepared by a multidisciplinary team made up of lawyers from PLMJ Law Firm and by lawyers from Dacheng Law Firm and DSL Lawyers, working under an international cooperation agreement and membership of PLMJ International Legal Network. The information in this document is not intended to be exhaustive or to substitute the support and assistance of a Lawyer or Legal Consultant for its practical use on a case by case basis, being solely intended to allow its readers to have a better understanding of the Chinese legal system and background.



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