Investing in China
中国投资指南
Summary

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China has experienced strong economic growth over the last few decades. Its gross domestic product (GDP) has reached CNY74.4 trillion in 2016\(^1\), rising from CNY406.26 billion in 1979\(^2\) when the country implemented its economic reform. Since 2008, China has been ranked among the world’s top three destinations for foreign investment\(^3\).

There is no doubt that one of the world’s largest emerging economies - China - was, and is, among the most active countries in opening up various industries to overseas investors.

According to the Ministry of Commerce (MOFCOM), from January to December 2016, newly approved foreign-invested enterprises (FIE) amounted to 27,900, up by 5% year on year; and the actual use of foreign investment reached CNY813.22 billion (USD126 billion), up by 4.1% year on year.\(^4\)

Since the operation of the “opening-up” policy as part of its economic reform, China has welcomed

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1. The Government work report, [http://www.gov.cn/premier/2017-03/16/content_5177940.htm](http://www.gov.cn/premier/2017-03/16/content_5177940.htm), accessed on 27 March 2017
foreign direct investment (FDI) in a range of industries including automotive, chemical, financial services, real estate. On 17 January 2017, the State Council issued the Circular on Certain Measures for Expanding Opening-up and Actively Using Foreign Investment (Guo Fa [2017] No.5) (the Circular). The Circular clearly prompts current and future Chinese foreign investment policy. It is foreseeable that the Chinese government will launch a new round of high-level opening-up by advocating foreign investment and accelerating liberalization in industries including service, energy and infrastructure development.

China has been ranked among the world’s top three destinations for foreign investment

By creating a more competitive environment, China will further demonstrate its competitiveness for industries, upgrade its industrial structure, and join the process of national, regional and international market integration as a socialist market economy making the successful transition. And such series of “opening-up” policy also make it much easier for foreign investors to gain access to the ever-growing Chinese market.
China has promulgated a series of laws, regulations and policies for the legal and regulatory protection and encouragement of FDI. They included, for example, the *Sino-foreign Equity Joint Venture Enterprise Law*, the *Sino-foreign Cooperative Joint Venture Enterprise Law* and the *Wholly Foreign-invested Enterprise Law* (collectively, the “Three FIE Laws”), *Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors*, *Provisions on Directing Foreign Investment (Order of the State Council [2002] No.346)*, the *Catalogue for the Guidance of Foreign Investment Industries (Revised in 2015)*, the *Catalogue of Advantageous Sectors for Foreign Investment in Central and Western Regions 2017 (Revised)*.

Furthermore, China strives to create a more stable, transparent and foreseeable legal environment for foreign investment. In this light, Chinese legislators hope to formulate a fundamental law on foreign investment that complies with the economic development of China and adapts to the requirements of internationally prevailing rules. On 19 January 2015, the MOFCOM published the *Foreign Investment Law of the People’s Republic of China (Draft for Comments)* (the “Foreign Investment Law (Draft for Comments)”) to seek feedback from the general public. This marks the end of the Three FIE Laws governing foreign investment in China. Foreign investment will be regulated by a unified “Foreign Investment Law” in the future. Once the Foreign Investment Law comes into effect, it will exert positive influence on foreign investment activities and foreign investment enterprises.

Moreover, China has concluded bilateral investment agreements with many countries/regions and is the member of some of the most important investment protection organizations such as the International Center for...
the Settlement of Investment Disputes (ICSID) and Multilateral Investment Guarantee Agency (MIGA). Those domestic laws and international treaties constitute the legal framework and safeguard for foreign investment in China.

Market access

Since China accessed to the World Trade Organization (WTO) in 1995, more and more sectors have been opened to foreign investment. In 1995, China published its first Catalogue for the Guidance of Foreign Investment Industries. This catalogue has been constantly revised to allow and encourage foreign investments in a wide range of industrial sectors.

More industrial sectors welcome foreign investment

The currently effective version is the Catalogue of Industries for the Guidance of Foreign Investments (Revised in 2015) (the "2015 revised Catalogue"). The 2015 revised Catalogue further opens up the general manufacturing industry to foreign investments.
Foreign investors are also encouraged to invest in areas including modern agriculture, high technology, advanced manufacturing, energy conservation and environmental protection, new energy, and the modern service industry.

The 2015 revised Catalogue reduces the number of restricted areas for foreign investments from 79 to 38 by delisting areas such as energy conservation, environment protection, technology, safety. The 2015 revised Catalogue further increases policy transparency and removes the restriction concerning the ratio of foreign to domestic shares placed on the permitted areas for foreign investments.

**The special administrative measures on access of foreign investments (the negative list)**

Recently, the National Development and Reform Commission (NDRC) and the MOFCOM have drafted a revision of the *Catalogue for the Guidance of Foreign Investment Industries (Revised Draft)* (the "Revised Draft") for public comments.

The Revised Draft states that China continues to open to the outside world, as the number of restrictive measures stipulated in 2015 revised Catalogue is reduced from 93 to 62. The Revised Draft integrates the encouraged items subject to limitations on ownership of shares, restricted items and prohibited items into special administrative measures on access of foreign investments (the negative list) and clarifies the restrictive measures in a unified manner.
Types of FDI

The two major forms of vehicle foreign investors uses are FIEs and representative offices (RO). With the market opening up to foreign investors and the limited allowable activities of ROs in China, FIE is a much more popular choice these days. We shall focus our discussion below on FIEs. The forms of a FIE may fall into:

Sino-foreign equity joint ventures (EJVs)

- EJVs are limited liability companies with joint China and foreign ownership. The share of results is proportional to the equity contribution of each party.

Sino-foreign cooperative joint ventures (CJVs)

- CJVs are based on contracts between venture partners. CJVs are typically formed to develop projects that have a limited duration and a specific objective, such as the development of a building, hotel or service project. CJVs offer greater flexibility in structuring capital contributions, profit and loss sharing and investment recovery.

Wholly foreign-owned enterprises (WFOEs)

- WFOEs are legal entities in China and are wholly owned by one or more foreign investors. The foreign investor has full autonomy over the management and operation of the company. A WFOE is the preferred vehicle for foreign investors if there is no compelling business reason for having a Chinese partner.

There are other forms of FDI which can meet the various needs of foreign investors such as foreign-invested company limited by shares, holding companies, and strategic investments in domestic listed companies, etc.
Establishment procedure

When establishing a business in China, it is crucial to obtain approval and complete all required registration processes with various Chinese authorities.

Approval from the NDRC

The Administrative Measures for Approval and Record-filing of Foreign Investment Projects (Order of the NDRC of the People's Republic of China No.12), effective as of 17 June 2014, stated that the total investment size and the categories set in the Catalogue for the Guidance of Foreign Investment Industries are the main basis for the examination and approval of relevant authorities.

In order to implement the requirements of the Circular of the State Council on Promulgating the Catalog of Investment Projects Subject to Government Approval (2016 Version) (Guo Fa [2016] No.72) and further improve the administration of the approval and record-filing of foreign investments, the NDRC released the Circular on Effectively Implementing Foreign Capital-related Work in the Catalog of Investment Projects Subject to Governmental Approval (2016 Version), effective as of 14 January 2017, to clarify that:

I. The foreign investment projects set forth in the following shall be subject to examination and approval:

1. any project of the restricted category with a total investment (including capital increase) amounting to USD300 million or above as included in the Catalog for the Guidance of Foreign Investment Industries shall be approved by the NDRC, and it shall be submitted to the State Council for the record-filing provided that the total investment (including capital increase) amounts to USD2 billion or above;
2. any project of the restricted category with a total investment (including capital increase) of less than USD300 million as included in the Catalog for the Guidance of Foreign Investment Industries shall be approved by the provincial government; and

3. the foreign investment projects other than those set out in the above two items but listed in items 1 to 10 of the Catalog of Investment Projects Subject to Governmental Approval (2016 Version) shall be approved in accordance with the provisions in items 1 to 10 of the Catalog of Investment Projects Subject to Governmental Approval (2016 Version).

II. The foreign investment projects beyond the scope of projects subject to examination and approval and not in the prohibited category as provided in the Catalog for the Guidance of Foreign Investment Industries shall be presented to local development and reform commissions for the record-filing.

Approval from the MOFCOM or Local Commission of Commerce (COC)

Whilst the establishment and modification of FIEs subject to the special administration measures in China shall still be subject to examination and approval by the MOFCOM or Local COC, China administers the establishment and modification of FIEs not subject to the special administration measures by record-filing instead of examination and approval in order to simplify formalities and facilitate foreign investments. FIEs or investors may fill up and submit record-filing information through the online record-filing system. The competent authorities of commerce shall complete the record-filing process within three working days and release the results through the record-filing system.
The establishment of FIEs shall be filed before obtaining the Business License or within 30 days as of the date issuing the Business License, modification of FIEs shall be filed within 30 days after the modification has been made. Record-filing is not the prerequisite of the industry and commerce registration.

### Establishment and modification of FIEs not subject to the negative list

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<td>Within 30 days after the resolution or decision is made by the highest authority of the FIEs</td>
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<td><strong>Applicants</strong></td>
<td>Representatives or agents of all investors (or founders of foreign-invested joint stock company, hereinafter founders) Representatives or agents of the FIEs</td>
<td>Representatives or agents of the FIEs</td>
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<tr>
<td><strong>Scope of application</strong></td>
<td>Wholly foreign-owned enterprises, Sino-foreign equity joint venture companies,</td>
<td>Any change to the FIE’s basic information Any change to the</td>
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| Application documents | Sino-foreign cooperative enterprises  
|-----------------------|--------------------------------------------------------------------------------|
|                       | ▶ Foreign invested investment companies, foreign invested venture capital companies and foreign invested equity investment companies (deemed as foreign investors)  
|                       | ▶ Enterprises established by investors from Hong Kong Special Administrative Region (HKSAR), Macau Special Administrative Region (Macau SAR) and Taiwan area  
|                       | ▶ Pre-verification approval of the company name or business license of the FIE  
|                       | ▶ Declaration Form on Record-filing for Establishment of FIE signed by all the investors (or founders) or their authorized representatives, or Declaration Form on Record-filing for Change
| investor’s basic information | ▶ Any change to the shareholding (shares) or cooperative interests including pledge of equity  
|                       | ▶ Any merger, division or termination of the FIE  
|                       | ▶ Any mortgage, or transfer of the property rights of the FIEs  
|                       | ▶ Any early recovery of investment by foreign investors of a Sino-cooperative joint venture enterprise  
|                       | ▶ Any appointment of a third party to manage and operate a Sino-cooperative joint venture enterprise |
| Record-filing authorities | The competent department of Commerce of the State Council, the administrative department of Commerce of all provinces, autonomous regions and municipalities directly under the central government, and Xinjiang production and Construction Corps, deputy provincial city and relevant departments of free trade zones, the state-level economic and technological development zones |
| Way of handling | Applying and submitting documents on line, examining the completeness and correctness of the submission |
| Handling timeline | Within three working days |
| Non-compliance of record-filing | If the information is incomplete or Where the change involves |
incorrect or the business scope needs to be further explained, the record-filing authorities shall inform the applicants in one instance and grant 15 days to supplement the documents on-line. The special administrative measures (the negative list), the examination and approval administration shall apply.

| Collection of record-filing receipt | After receiving a notice, FIEs or investors may present their company name pre-verification approval (copy) or business license (copy) to collect the Receipt of Record-filing for Establishment of FIEs or the Receipt of Record-filing for Modification of FIEs from the record-filing authorities |

Registration with the State Administration for Industry and Commerce (SAIC) or the local Administration for Industry and Commerce (AICs) for the issuance of Business License

According to the administration regulations of China, FIEs shall register with the SAIC or the local AICs to obtain Business License to legally start operation in China.
As a worldwide practice, cross-border M&As have gradually replaced direct investment as a major form of investment adopted by many multinational corporations.

Regarding the M&As in China, the following points are worthwhile to be noted:

- That acquisition of equity/shares and acquisition of assets are two ways of M&As.

- A foreign investor is allowed to use the public listed shares over which it has the right of disposal or the Renminbi-denominated assets legally owned by it as means of payment.

- Foreign investors may participate in the re-organization of state-owned enterprises (SOEs) by acquiring all or part of the ownership, equity, debt or assets of SOEs.
Tax

The taxing regimes in China are complex and the tax practice varies from location to location. The major China tax issues to be considered are highlighted below. The information provides it general in nature and should not be relied upon as professional advice.

Income tax

Enterprises incorporated in China and foreign enterprises with effective management located in China are treated as tax resident enterprises (TREs).

The statutory CIT rate is 25%. The withholding tax rate on passive income (such as dividends, interest, royalties and capital gains) of non-TREs is generally taxed at 10% with relief depending on the double taxation agreement/arrangement.

Foreign tax credit is allowable for income taxes paid in other countries/regions, with a cap at the China income tax payable on the same income.

Tax losses sustained by TREs can be carried forward and utilized against the succeeding five years’ taxable income. Tax loss carry-back is not allowed.

VAT in lieu of BT

Upon approval of the State Council, the pilot program of the collection of value-added tax in lieu of business tax ("VAT in lieu of BT") has been promoted nationwide in a comprehensive manner as of 1 May 2016, and all taxpayers of business tax engaged in the building industry, the real estate industry, the financial industry and the life service industry shall be included in the scope of the pilot program with regard to payment of
value-added tax (VAT) instead of business tax (BT).

VAT payers are classified into general VAT payers and small-scale VAT payers. For a general VAT taxpayer, input VAT paid can generally be recovered by crediting against output VAT.

VAT rates under Article 15 of the Circular on Comprehensively Promoting the Pilot Program of the Collection of Value-added Tax in Lieu of Business Tax states that:

1. Any taxable activities of taxpayers shall be subject to a tax rate of 6%, except as specified in items 2, 3 and 4 of this Article.

2. To provide services related to transportation, postal services, basic telecommunications, construction, leasing of real property, sell any real property, or transfer any land use rights, the tax rate is 11%.

3. To provide leasing services of tangible personal property, the tax rate is 17%.

4. For any cross-border taxable activity conducted by an entity or individual within the territory, the tax rate is zero. The specific scope shall be prescribed separately by the Ministry of Finance and the State Administration of Taxation.

**Customs**

Customs duties are imposed on certain goods imported and most exported goods are exempted from custom duties.

**Other taxes**

Other taxes in China include individual income tax, resource tax, land appreciation tax, real estate tax, stamp duty, deed tax, vehicle and vessel tax, land usage tax, motor vehicle acquisition tax, and city construction tax.
Labor and employment

Employee recruitment

An FIE can hire local personnel directly or indirectly through qualified labor dispatch agencies. The recruitment of employees from other countries and jurisdictions, including Hong Kong SAR, Taiwan and Macao SAR, shall be approved by the local labor department; and related procedures like the employment permits shall be carried out in accordance with relevant regulations of the state.

Salary

FIEs shall be in line with the national and local minimum salary standards. The payroll is determined by the board of directors or through collective negotiation of the enterprise.

Insurance and welfare

FIEs shall participate in the social insurance systems of pension, unemployment, medical care, work injury and childbirth through regular and adequate payment to the insurance agencies in accordance with the standards prescribed by the local government as required by relevant Chinese regulations. In addition, there are other welfare such as housing fund, professional training, stipends and statutory holidays.

Working hour

FIEs shall observe China's current working hour system – no more than eight hours per day and on average no more than 40 hours per week. Where the enterprises cannot operate on the standard working hours due to the nature of their production, the enterprises can operate on a non-standard working hour system upon approval by the labor department.
To assist overseas investors with their application and approval efficiency, we provide a diversified service including, but not limited to, the following areas:

- seeking Chinese partners if required
- drafting business proposals, feasibility studies, letters of intent, EJV and CJV contracts, merger and acquisition agreements, articles of association and all other related documents required by our clients
- assisting with all matters relating to application, examination and approval of the FIE
- locating offices including drafting, negotiating, finalizing and registering office lease agreements
- enterprise registration including applying for Business Licenses
- assisting in matters of construction, design and planning, obtaining land use rights, environmental protection and all other property related matters
- advising in relation to employment related matters including employee recruitment and employment considerations when investing in existing enterprises (such as SOEs) within China
- other professional services and advice if required
About EY Chen & Co. Law Firm

EY Chen & Co. Law Firm

Founded in 1998, EY Chen & Co. Law Firm is registered to practice the laws of the People's Republic of China in mainland China and Hong Kong. With more than 130 professionals in our Shanghai head office and Beijing and Hong Kong offices, EY Chen & Co. Law Firm is widely recognized as an outstanding commercial law firm in China, uniquely positioned to provide multi-disciplinary, comprehensive and one-stop legal services to our clients.

As a member firm of Ernst & Young Global Limited, we work closely with EY legal practices in other countries to provide integrated, commercially-focused advice that addresses our clients' needs and helps enable them to thrive in different markets, with the aim of reducing legal and other risks.

Practice areas

EY Chen & Co. Law Firm is a PRC law firm specializing in commercial law, experienced in capital market, investment, mergers and acquisitions (M&As), anti-trust, banking, trusts, funds and compliance legal services.

Our clients include many leading multinational companies, as well as numerous well-respected state owned, publicly listed, and privately held companies, government entities, and many other parties with or representing diverse commercial or financial interests and we are experienced in advising clients from all sectors especially in banking and finance, life science and health care, automotive, technology, media & telecommunication (TMT), real estate and infrastructure and retail
products.

With extensive legal experiences and a practical understanding of Chinese business, we strive to deliver comprehensive and pragmatic solutions to the business questions and needs of our clients.

Our professionals

Our professionals closely follow and understand political and commercial environment and emerging trends in their respective practice areas as corporate law, securities, tax and investment. Equipped with multi-language skills, extensive cross-border legal expertise, and understanding of diversified culture backgrounds, our professionals act as outstanding legal counsel for your business success.
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About EY Chen & Co. Law Firm

EY Chen & Co. Law Firm is a Chinese law firm, experienced in capital market, investment, merger & acquisition, anti-trust, banking, trust, fund and compliance legal services. Our Law practitioners work closely with EY Assurance, Tax, Transactions and Advisory professionals to provide integrated, commercially focused advice that addresses your needs and helps your businesses to thrive in different markets, with the aim of reducing legal and other risks.

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