

卓纬法律指南 2022

Foreign Direct Investment In China 2022



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1. INTRODUCTION

1.1 WHY INVEST IN CHINA

Territory	9,596,960 sq. km
Population	1.398 billion (2021.7 est.)
GDP (Exchange Rate)	USD 14.28 trillion (2019)
GDP real growth rate	5.95% (2019)
Unemployment Rate	5% (2020 est.)
GNI per capital	USD 10,390 (2019)

(Statistics from the World Bank website and the CIA World Fact Book).

China adopted its “Reform and Opening Up Policy” in 1978 and joined WTO in 2001. Seeing FDI as one of the keys to its economic growth, China has over the past 40 years implemented more flexible FDI policies and attracted more investors. After decades of improvement, China can now proudly offer foreign investors a vast territory with abundant resources and a great number of workforces, supported by world-class infrastructure that is framed in a stable legal system.

1.2 OUR GUIDE

This guide expounds the main legal issues that every foreign company or individual should bear in mind when investing in China. Firstly, it introduces the various sectors open for investment and their different geographic locations. Then, this guide explains the most convenient vehicles for various investments. Finally, this guide deals with other factors foreign investors need to consider including approvals and registration, tax treatment, labor, intellectual property issues, etc.

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2. DECIDING ON AN INVESTMENT

Deciding on an investment in China involves two steps: (1) deciding which sector to invest in; and (2) deciding which region in China to invest in.

2.1 CHOOSING A SECTOR: FOREIGN INVESTMENT LAW OF PRC AND NEGATIVE LIST

The National People’s Congress of China adopted the new Foreign Investment Law (“FIL”) on March 15, 2019, with a view toward unifying and streamlining the foreign investment framework into China. The new-adopted FIL has come into effect on January 1, 2020.

The FIL has been widely promoted as a framework that emphasizes equal national treatment of foreign investment, putting foreign investors on equal footing with domestic investors in the Chinese market and giving them equal protections.

From a high-level perspective, the FIL embodies China’s resolution to continue to modernize its laws to reflect the changing global economy. At the same time, the FIL is more high-level than the FIL (Exposure

Draft) proposed in 2015, which contained more specific provisions but still left questions open regarding its viability in implementation.

The new-adopted FIL establishes a nationwide “pre-establishment national treatment and negative list” management system. The system is intended to create an environment where all foreign investments will be treated the same as domestic investments, other than foreign investments into industries that are listed in the *Special Administrative Measures for Foreign Investment Access (Negative List)* (“Negative List”).

The Negative List is a list of industries into which foreign investment is either prohibited or restricted, and contains restrictions or prohibitions on foreign investment. The Negative List had already been published and in use nationwide since mid-2018 and has been updated in December of 2021. The decrease in the number of restrictive and prohibited business areas provides more options and possibilities for inbound investment, and increases the confidence of foreign investors.

The major lists that specifically guide and regulate foreign investments include: Catalogue of Industries for Encouraging Foreign Investment (“Encouraged Category”) and Negative List.

Compared with the previous year, the number of business sectors included in the 2020 Encouraged Category increased from 1,108 to 1,235, which grants more opportunities for foreign investors. Foreign Invested Enterprises (“FIEs”) in the industries listed in the Encouraged Category shall enjoy favorable custom policy, enjoy lower rate of corporate income tax, and enjoy favorable land transfer consideration if the relevant requirements are fully satisfied.

Compared with the previous year, the number of business sectors included in the 2021 Negative List decreased from 33 to 31, the two sectors removed from the earlier edition of Negative List are automobile manufacturing and satellite television broadcast ground, which is also a positive signal for foreign investors. FIEs in the industries listed in the Negative List are subject to shareholding restrictions, stricter

approval requirements, higher level of governmental scrutiny and, for certain industries, complete prohibition.

Any remaining sectors unlisted in the Negative List are automatically presumed permissible for foreign investment, and are only subject to a record-filing process, which is a significant shift from the case-by-case approval regime. Therefore, if a foreign investor would like to know if their investment falls within the Negative List and requires the approval of Ministry of Commerce of the PRC (“MOFCOM”), the 2021 Negative List would be the best reference.

2.2 LOCATION

As coastal regions were first opened to foreign investment, coastal regions have attracted most of the FDI, which leads to a very uneven distribution of FDI among different regions of China. While coastal regions usually combine better infrastructure and highly qualified personnel with more experienced governmental authorities and has greater possibilities of enforcing the rule of law, the land and labor costs are generally higher in coastal regions. Comparatively, interior regions offer lower land and labor costs, and more political advantages, but they may not have the same levels of infrastructure, transport, skilled employees and legal protection as that offered by coastal regions.

2.2.1 CENTRAL AND WESTERN CHINA

In order to tackle this imbalance, the Encouraged Category includes a sector called the Category of Industries Encouraged for Foreign Investment in the Central and Western Region of China (“The Category of Central and Western China”). The Category of Central and Western China is designed to further encourage foreign investment in interior regions of China, to develop regional open economy and export-oriented industries. In this Category of Central and Western China, foreign investment in several

industries is “encouraged” if invested in locations such as Shanxi, Liaoning and Anhui Provinces, Inner Mongolia and Xinjiang Uygur Autonomous Regions, Chongqing Municipality, among many others.

2.2.2 SPECIAL ZONES

In addition, China offers a number of special zones, where various incentives and benefits are provided to investors. The most important policies of these zones are described in the table below.

Zone Type	Description
Special Economic Zones (“SEZ”)	<ul style="list-style-type: none"> ➤ Tax and business incentives; ➤ Better infrastructure and bureaucratic procedures.
Economic and Technological Development Zones (“ETDZ”)	<ul style="list-style-type: none"> ➤ Emphasize the development of production enterprises, scientific and technological research institutions; ➤ Special treatment is available for production enterprises; ➤ Preferential tax treatment, as well as a higher level of infrastructure and communications.
Hi-Tech Development Zones (“HTDZ”)	<ul style="list-style-type: none"> ➤ Strengthen integration among scientific research, education and production, and promote the development of scientific techniques, society, and the economy; ➤ Preferential tax treatment, as well as a higher level of infrastructure and communications.
Free Trade Zones (“FTZ”)	<ul style="list-style-type: none"> ➤ Goods may be landed, handled, manufactured, or reconfigured, and re-exported without the intervention of the customs authorities; ➤ Only when the goods move to consumers within China do they become subject to the prevailing customs duties; ➤ Preferential tax and currency treatment and a high level of infrastructure such as transport facilities, tele-communications, and energy supply.

Of special note are the FTZs in Shanghai, Tianjin, Fujian, Guangdong, Chongqing, Zhejiang, Hubei, Henan, Sichuan, Shanxi, Liaoning, and Hainan. These FTZs have more liberal economic and social regulations. Of particular importance to foreign investment is the Negative List for such FTZs, i.e., unlike in the rest of China, foreign investors enjoy more favorable policies in the FTZs, and are subject to less limitations.

There are also several other special geographic locations in China, such as bonded zones, bonded logistics parks, bonded ports, export processing zones, cross-border industrial parks, and comprehensive bonded zones, these special geographic locations are subject to special and more favorable custom policies.

3. TYPES OF FOREIGN INVESTMENTS

Once the certain industry and location of the investment have been chosen, the next step is to decide on the type of investment.

China's FIL has come into effect on January 1, 2020, which will replace the PRC Law on Sino-foreign Equity Joint Ventures, the PRC Law on Wholly Foreign-owned Enterprise and the PRC Law on Sino-foreign Cooperative Joint Ventures. Since then, FIEs are no longer classified as "Sino-foreign equity joint ventures", "Sino-foreign cooperative joint ventures" and "wholly foreign-owned enterprises". The organizational structures, forms of organizations, etc. of all FIEs are subject to the provisions of the Company Law of the PRC or the Partnership Law of the PRC. The old FIEs established before the implementation of FIL may retain their original organization forms and other aspects for five years upon the implementation hereof.

A broad comparison of the various types of foreign investments can be found in the table below and described herein.

3.1 COMPANIES

In the PRC, there are only two types of companies: limited liability companies (“LLC”) and joint stock companies (“JSC”, together with LLC, “Companies”). Generally, LLCs are similar to common law private companies limited by shares, and JSCs are similar to common law public companies limited by shares.

An LLC can only have a limited number of shareholders (under PRC laws, no more than 50 shareholders).

In an LLC, shareholders are generally only liable to the extent of their investment in the company.

A JSC shall have no less than two and no more than 200 promoters. In a JSC, shareholders are generally only liable to the extent of the shares it/he has subscribed for.

All companies in China have the traits as follows:

- Business scope – all companies in China must specify its business purpose. Taking part in activities outside the defined scope (ultra vires activity) can lead to significant penalties.
- Organization - the organizational structure of a Company mainly consists of the shareholders' meeting, the board of directors (or an executive director) and the board of supervisors (or a single supervisor). The company is governed by the shareholders' meeting.
- Legal representative – in accordance with the law or the articles of association (“AOA”) of the legal person, the responsible person who acts on behalf of the legal person in exercising its functions and powers shall be its legal representative.
- Company Seal (“Chops”) – under PRC law, the company seal is very important. The company seal takes the place of a signature on behalf of the company. In cases where the company seal appears on a

document, there is an almost insurmountable presumption that the company's legal representative has agreed to it.

3.2 PARTNERSHIPS

Partnerships can, but are not required to, involve a Chinese partner. In either case, the partnership's capital can be contributed in both freely convertible foreign currencies and/or legally acquired Renminbi (RMB).

Partnerships can be: (i) general partnerships comprised of general partners with unlimited joint and several liabilities for the debts of the partnership; or (ii) limited liability partnerships comprised of both general partners and limited liability partners, the latter only bearing liability for debts to the extent of the capital contributions they have subscribed for.

Limited liability partnerships must consist of at least two but no more than 50 partners (unless otherwise specified by the law) and must have at least one general partner. The partners shall appoint one or more managing partner(s) to represent the partnership and execute its affairs. Only general partners can be appointed as managing partners. The other partners are entitled to supervise such appointed managing partners.

3.3 REPRESENTATIVE OFFICES ("REP OFFICES")

Rep Offices can be established in China only for the purpose of liaising on behalf of the parent companies and cannot engage in direct business or profit-making activities. Rep Offices do not constitute separate legal entities independent from its foreign parent companies, so the parent companies will still be liable for the Rep Office's obligations (i.e., tax, labor costs, operative costs, etc.).

Rep Offices can engage in the following activities: (i) market investigation, display, publicity activities in connection with the products or services of foreign enterprises; and (ii) liaison activities in connection with product sales, service provision, domestic procurement and domestic investment.

Rep Offices shall declare and pay corporate income tax for the income attributable to them and value-added tax for their taxable income. Rep Offices must have one chief representative and may have up to three other representatives.

	Company	Partnership	Rep Office
Separate Entity	Yes	Yes	No
Limited Liability	Yes	No	No
Control	Subject to shareholding; Board decisions by majority vote	Depends on the partnership agreement	Complete managerial and operational control
Profit Sharing	As established in the AOA or shareholders' agreement	As established in the partnership agreement (subsidiary proceedings established by law)	N/A (Rep Offices are not entitled to engage in commercial activities)
Capital Recovery	Share net assets upon liquidation; Transfer of shares; Share repurchases; Capital reduction only in special circumstances	Partner retires; Share partnership assets upon liquidation; Contribution reduction only in special circumstances	N/A
Intellectual Property	Controlled	Possibly at risk in Si-no foreign partnerships	N/A

3.4 ORGANIZING THE CORPORATE STRUCTURE

3.4.1 FOREIGN INVESTED INVESTMENT (HOLDING) COMPANIES

Foreign-invested Investment (Holding) Companies (“Holding Company”) are allowed in China to facilitate foreign investors’ investment, and introduce advanced technologies and management expertise from foreign countries. Holding Companies are defined as firms established by foreign companies, enterprises, or economic organizations to engage in direct investments.

In order to establish a Holding Company, the foreign investor must show that it has good credit standing and meets various criteria regarding assets, previously established FIEs, etc.

Holding Companies are limited in the activities they can undertake. They can invest in sectors where foreign investment is allowed, provide certain services to its investees, etc.

3.4.2 MULTINATIONAL COMPANIES’ REGIONAL HEADQUARTERS

Multinational companies may establish their regional headquarters in China through the constitution of an FIE in order to provide management and services to its corporate structure within China and/or other countries. A Holding Company can be recognized as the regional headquarters of a multinational company if it satisfies certain requirements.

Beijing, Guangzhou, Shanghai, Shenzhen, Tianjin, Jiangsu Province, Shandong Province, Shanxi Province and Guangdong Province all have specific regulations regarding the establishment of regional headquarters.

4. ESTABLISHING AN ENTITY

There are various steps that must be taken in order to establish one of the entities described in section 3.

The steps are outlined on the next page and described below.

4.1 PRE-APPROVALS

There are no minimum registered capital requirements for FIEs with scope of business of consulting, trading, retailing, information technology, etc. There are no paid-up capital requirements, either. However, minimum registered capital is still required for some industries, including but not limited to banking, securities, insurances, transportation, etc. For the qualification certificates or authorization documents issued by foreign entities, these shall only be accepted for establishing an FIE upon duly notarization of competent authorities.

Enterprise Name Enterprise names must contain the following parts: administrative area (province, city or county), trade name, trade or business operation characteristics (industry) and organizational form (i.e., LLC). In addition, the enterprise name shall be in Chinese characters and the foreign language name must conform to the Chinese name and also be registered. Enterprise shall submit the name through the online system, or submit the name when go through the offline registry process.

Project Approval If the project involves fixed assets, then the project must be filed with the National Development and Reform Commission (“NDRC”) or a Local Development and Reform Commission (“DRC”). Some projects require approval whereas others need merely to be filed for record. What action needs to be taken depends primarily on the type of the investment and the total investment amount.

Environmental Approval No permission or record-filing for a construction project shall be granted before an environmental impact assessment report is approved by the Ecology and Environment

Department (or its local branch) and the facilities for the prevention and control of pollution are examined. Also, enterprises that discharge waste must register before the Ecology and Environment Department. If they discharge waste in excess of the allowed national or local levels, additional fees must be paid.

Other Approvals Depending on the type of project, pre-establishment approval might need to be obtained from other authorities (e.g., banking, education, etc.)

4.2 COMPANY ESTABLISHMENT

The establishment of an FIE is subject to foreign investment information report system. Foreign investors shall submit investment information to the competent department for commerce concerned through the Enterprise Registration System and the Enterprise Credit Information Publicity System.

Foreign investors shall not invest in fields for which investment is prohibited by the Negative List. If the FIE falls within the scope of one of the industries which is restricted by the Negative List, the establishment shall comply with the restrictive admission special administrative measures such as equity requirements, senior management personnel requirements, etc. stipulated by the Negative List. Foreign investments outside the scope of Negative List will be subject to the principle of consistency for domestic and foreign investment.

4.2.1 PROCEDURES FOR EXAMINATION (NEGATIVE LIST FIES)

When applying for FIE establishment or modification registration, the investor needs to give an undertaking on whether it complies with the requirements of the foreign investment admission special administrative measures of Negative List, and tick the industry/field in the Negative List in accordance with the actual circumstances. The registration authorities (i.e., market regulatory authorities) will conduct formal examination of the relevant application materials. If the FIE complies with the foreign investment

admission special administrative measures of Negative List, the market regulatory authorities will grant the registration. In the case of the FIE which is subject to license according to law, the relevant administrative authorities will not process licensing for proposed investments by foreign investors if the FIE does not comply with the foreign investment admission special administrative measures of Negative List. In the case of the FIE which is subject to approval for fixed asset investment projects, the NDRC will not process the relevant approval if the FIE does not comply with the foreign investment admission special administrative measures of Negative List.

4.2.2 PROCEDURES FOR FOREIGN INVESTMENT INFORMATION REPORT (FOR BOTH NEGATIVE LIST AND NON-NEGATIVE LIST FIES)

Both the Negative List and non-negative list FIEs need to submit foreign investment information report to MOFCOM or other commerce administrative authorities through the Enterprise Registration System and the Enterprise Credit Information Publicity System.

In the case that the foreign investors establish an FIE in China, an initial report will be submitted through the Enterprise Registration System at the time of applying for the establishment registration for the foreign investment enterprise; in the case that the foreign investors undertake a merger and acquisition of a non-foreign investment enterprise in China, an initial report will be submitted through the Enterprise Registration System at the time of applying for the modification registration for the target enterprise. The market regulatory authorities will promptly forward the investment information submitted by foreign investors and FIEs to MOFCOM or other commerce administrative authorities.

Submission of a foreign investment information report is not a condition precedent for establishment registration of FIEs. The market regulatory authorities need not examine the foreign investment information report. After the submission of an application for enterprise registration, the applicant may continue to fill in information of foreign investment information report.

The initial report contains basic information of the enterprise, the information of investors and their actual controlling party and investment transaction information, etc.

The investment information submitted by a foreign investor or an FIE will be announced to the public through the National Enterprise Credit Information Publicity System and the foreign investment information reporting system if the FIE agrees to announce to the public. In the case that any information is not declared, wrongly declared or omitted in the foreign investment information report by a foreign investor or an FIE, MOFCOM or other commerce administrative authorities will notify the foreign investor or the FIE to make supplementation or correction within 20 working days.

4.2.3 LEGAL LIABILITY

Where a foreign investor or an FIE fails to submit foreign investment information report; conceals true information or provides misleading or false information in the process of making information report; commit reporting error of significant information such as the industry it is in, whether it is subject to foreign investment admission special administrative measures, the enterprise's investors and their actual controlling party etc. or a foreign investor or an FIE is subject to any other serious circumstances determined by the commerce administrative authorities, administrative penalties shall be imposed.

4.3 COMPANY REGISTRATION

In China, State Administrative for Market Regulation (“SAMR”) is the registration authority of enterprises, companies and other economic organizations. The establishment documents of FIEs shall be submitted to the local branch of SAMR for the initial report of entity information.

Upon approval of the registration, the local branch of SAMR shall issue the FIE’s business license. FIEs exist and have independent legal personality from the moment they obtain their business license. Before

their business license is issued, FIEs are not allowed to engage in business operations or enter into binding contracts.

Partnerships: For partnerships, registration is directly required by the local branch of SAMR. However, if the scope of operation of the partnership enterprise includes industries that need to be approved before registration, the approval documents must be submitted.

The local branch of SAMR shall decide whether or not to approve the partnership registration within 20 days from the date of acceptance of the application, and if the application materials need to be replenished, the authority that accepted the application shall inform the list of materials all at once.

Rep Offices: Direct registration with SAMR or its local branch is sufficient to establish a Rep Office of a foreign company whose business scope includes but not limited to advertising, pharmaceutical, trading, manufacturing, freight forwarding, contracting, consultancy, leasing, or railway transportation company. However, prior approval granted by the competent industrial regulator is still required to establish a Rep Office in specific sectors. For example, if a banking institution intends to establish its Rep Office in China, it shall firstly obtain the approval of the People's Bank of China.

4.4 POST-REGISTRATION APPROVALS

Once the business license is obtained, the FIE must apply for the following post-registration approvals (which may vary depending on the specific business scope of each FIE):

- Company seal registration: Public Security Bureau;
- Registration of organizational code: Administration for Organizations Code Allocation;
- National and local taxation registration: State Administration of Taxation and Local Taxation Bureau, respectively;

- Foreign exchange registration: State Administration of Foreign Exchange (“SAFE”);
- Statistical registration: Bureau of Statistics;
- Public security registration: Public Security Bureau;
- Finance registration: Finance Bureau or its district or county level;
- Import and/or export: Local Customs Bureau;
- Products inspection and quarantine registration: Inspection and Quarantine Bureau; and
- Labor registration: Local Labor Bureau.

4.5 ADMINISTRATIVE MEASURES FOR MODIFICATION OF FIES

The designated representatives or entrusted agents of FIEs shall file a modification report within 20 days upon the occurrence of the following changes via the online registration system, and if the modification needs to be filed for records, the modification report shall be submitted when the offline modification documents are submitted for registration and filing.

For these following changes of investment information, the report shall be duly submitted:

- Change of basic information of FIE, including: name, registered address, type of business, operating period, investment industry, operation scope, whether or not it falls within the scope of tax exemption, registered capital, total investment, organizational structure, legal representative, and contact information of legal representatives;
- Change of basic information of investors of FIE, including: name, nationality/ registered address (place of registration or registered address), license type and number, registered capital, type of investment, investment period, source of funds, changes of type of investor.
- Changes in equity (shares) or cooperation interest;

- Merger, division or termination; and
- Mortgaging of FIE property or rights and interests to others.

4.6 SUPERVISION AND MANAGEMENT

Competent commerce departments are legally responsible for supervising and inspecting the implementation of these measures by FIEs and their investors. Specifically, competent departments have a variety of methods for checking, including the spot check and conducting examinations according to reports, etc. As for the contents of supervision and inspection, the following lists should be included:

- Whether the reporting procedure is legitimately handled;
- Whether the reporting information is filed authentically, correct and complete by FIEs or their investors;
- Whether the investment falls within forbidden investment sectors;
- Whether circumstances that trigger national safety inspection exist; and
- Whether they have been subject to any administrative penalty decision.

5. CAPITAL AND FUNDING

The 2013 Amendments to the *Company Law* removed the general minimum registered capital requirements. Nonetheless, other laws and regulations do specify minimum registered capital requirements for companies in particular industries or that engage in particular businesses.

5.1 REGISTERED CAPITAL

5.1.1 TYPES OF CAPITAL CONTRIBUTIONS

Shareholders may make capital contribution in cash or in kind such as, intellectual property rights, land use rights and other non-cash properties which can be valued and transferred in accordance with the applicable law of PRC. However, shareholders shall not make capital contribution in the form of appraised value of services, credit, name of natural person, goodwill, franchise rights or properties on which security interests are created, which are prohibited by laws and administrative regulations to be used for capital contribution.

If the capital contribution is made in cash, foreign investors are encouraged to invest with convertible currencies, and if the foreign investors intend to make the contribution in RMB, such investment shall be the profits generated by other FIEs or the legitimate offshore RMB and the foreign investors shall present their profit contribution certificate and tax exemption or reduction certificate to MOFCOM for examination and approval. In the case of establishing a JSC through public share offering, the shares subscribed by the sponsors shall be no less than 35% of the total shares of the company. In accordance with *Company Law*, the number of sponsors required for the establishment of a JSC shall be more than 2 but less than 200, and more than half of which shall have a domicile in China.

If non-cash properties are contributed as company capital, they shall be valued and verified by a qualified institution and shall not be overvalued or undervalued. Where the applicable law and administrative regulations have specific provisions on property valuation, such provisions shall prevail.

5.1.2 SCHEDULE OF CAPITAL CONTRIBUTION

The shareholders can arrange the schedule for the contribution of the registered capital based on negotiation and consensus. The schedule for capital contribution must be specified in the application for establishment of the FIE and its AOA. The shareholders shall make their respective capital contribution in accordance with the amount of their capital subscription and the agreed schedule. Shareholders who fail to fulfill their obligation in terms of capital contribution shall, in addition to making the capital contribution in full, bear default liability towards observant shareholders.

5.2 EQUITY FUNDING

Although the *Company Law* no longer specifies minimum registered capital requirements, there are still requirements for FIEs that a certain percent of the total investment amount shall be registered capital. Considering that the *Interim Provisions on the ratio between Registered Capital and the Total Investment Amount of Chinese-foreign Equity Joint Ventures* is still valid, even if the FIE does not provide for the total investment amount, it is still recommended that the FIE comply with applicable provisions related to the total investment amount.

The registered capital of FIE shall be appropriate for the scale and scope of its business and operation, the ratio between registered capital and the total investment amount shall comply with the following requirements.

Total Investment Amount (equity funding + loans)	Minimum percent of the total investment required to be registered capital
Less than USD 3 million (3 million inclusive)	70%

Total Investment Amount (equity funding + loans)	Minimum percent of the total investment required to be registered capital
USD 3 – 10 million (10 million inclusive)	50% (where the total investment amount is less than USD 4.2 million, the registered capital shall not be less than USD 2.1 million)
USD 10 – 30 million (30 million inclusive)	40% (where the total investment amount is less than USD 12.5 million, the registered capital shall not be less than USD 5 million)
More than USD 30 million	1/3 (where the total investment amount is less than USD 36 million, the registered capital shall not be less than USD 12 million)

5.3 LOANS

FIEs can borrow loans in either RMB or foreign currency without any prior approval. However, foreign currency loan agreements must be registered with the SAFE.

In general, the total debt incurred by an FIE can never exceed the balance between their total investment amount and registered capital. However, in the specific case of investment companies, the incurred debt must comply with the following requirements:

Registered capital (USD)	Maximum amount of loans
Not less than USD 30 million	Four times the paid amount of registered capital
Not less than USD 100 million	Six times the paid amount of registered capital

If the amount of loans of an FIE exceeds the above limitations and shall be necessary for its business operation, such loans shall be reported to MOFCOM for approval. If the approval is not granted by MOFCOM, the FIE must reduce its incurred debt or increase its registered capital (see next section).

5.4 INCREASE OR DECREASE IN REGISTERED CAPITAL

Increasing the registered capital of an FIE requires record filing with MOFCOM and subsequent modification registration before the SAMR. On the other hand, registered capital decrease requires a public announcement to all of the creditors and potential creditors and it will take much longer time compared to capital increase.

If the FIEs capital is increased or decreased, the AOA (and, in the case of Partnerships, the partnership agreement) need to be amended to reflect such modifications.

5.5 FOREIGN EXCHANGE

The FIE shall, after receiving the business license, go through the basic information registration at the bank where the FIE is registered. The bank shall, upon the review of submitted materials, issue the registration certificate, after which the FIE will be entitled to open and maintain the foreign exchange accounts in Chinese banks allowed to engage in foreign exchange business. If the FIE intends to open a foreign exchange account outside China, prior approval from SAFE's is required.

As the RMB is still not fully convertible, the *Provisions for the Administration of Domestic Foreign Exchange Accounts* issued by the People's Bank of China on October 1997 makes it necessary to distinguish between "current account" items and "capital account" items.

5.6 FINANCIAL AND ACCOUNTING ISSUES

The accounting years shall be from January 1st to December 31st each year.

In accordance with the *Company Law*, the profits must be distributed in the following order: (i) payment of taxes; (ii) make-up of previous accounting years' losses; (iii) withdrawal of funds; and (iv) distribution to the investors. Undistributed profits from previous accounting years can be distributed in current accounting years.

In accordance with the *Partnership Law*, the profits shall be distributed in accordance with their partnership agreement.

6. LABOR

6.1 THE LABOR RELATIONSHIP

The establishment of a labor relationship requires a written labor contract to be concluded. In the absence of a written contract, the employer shall be liable for monetary compensation or shall be subject to a labor contract with a non-fixed term, as described below:

Time	Action
Within the first month of the date on which the he/she is employed	Must conclude a written labor contract
From the end of the first month to the end of the first year	The employer must pay the employee twice his/her monthly salary and conclude a written labor contract.

Time	Action
Over or equal to one year	A labor contract with a non-fixed term is deemed to have been concluded and a written contract shall be concluded with the employee forthwith

However, if the employer notifies the employee in writing of the need to conclude a written contract but the employee fails to conclude a written employment contract with the employer within one month of the date on which he/she is employed, the employer is entitled to terminate the labor relationship and notify the employee in writing without paying any monetary compensation.

There are three types of labor contracts:

- i.Contract with a fixed term (with a specific expiry date of labor relationship);
- ii.Contract with a non-fixed term (with no specific expiry date of labor relationship); and
- iii.Contract which shall expire upon the completion of specific work.

Employers are entitled to require their employees to go through a probationary period during which the employer can pay the employee a lower amount (subject to limits) of monthly salary and may terminate the employment contract where the employee is proven to be disqualified for the position upon the sending of a written notice. The maximum term of the probationary period is six months, and the employers are entitled to stipulate a probationary period in accordance with the term of the contract.

Term of Labor Contract	Maximum Probationary Period
Over three months but less than one year	One month
Over one year but less than three years	Two months

Term of Labor Contract	Maximum Probationary Period
More than three years	Six months

In general, the employer can only terminate the employment contract under certain circumstances (e.g., where the employee and employer reach an agreement; where the employer is not competent for employment, where the contract cannot be performed due to major changes of objective conditions; and where the employer business operation is in serious difficulties.) and must give the employee 30 days' prior written notice or pays the employee an extra month's wages. However, the termination with notice or extra wage shall not be given to the employees under these circumstances, e.g., where the employee suffers from a work-related disease or injury and has been confirmed as being totally or partially unable to work; where the employee is receiving medical treatment and where a female employee is in pregnancy, perinatal or lactation. Termination without notice can only be given in certain, enumerated, serious circumstances (e.g., where the employee is proved unqualified for employment during the probationary period, where the employee seriously violates labor discipline or the employer's rules and regulations, where the employee causes great damage to the interest of the employer due to his/her misconduct and where the employee is subject to criminal liability).

For the circumstance where the termination is given with prior written notice or extra wage, the employee is entitled to one month of compensation (the calculation of which is subject to the relevant regulations, and might be subject to an upper limit) for each year he/she has worked for the employer. The employer, if fails to fulfill the obligation of giving the foresaid monetary compensation, shall be subject to a punitive damage, which shall be twice of the compensation.

Employees can resign with 30 days' notice but can dispense with the notice requirement under certain serious circumstances (e.g., if the employer fails to pay the entire salary on time).

Part-time employment, at most four hours per day and twenty hours per week, is not subject to the rules regarding written labor contracts, probationary periods, or termination.

In addition, foreign investors should be aware of the following labor-relative issues:

- With some exceptions, the employment of minors under the age of 16 is strictly forbidden.
- Unless otherwise approved by the competent labor department, employees shall not work more than eight hours a day and forty-four hours per week and must be given one day off a week.
- Overtime work requires consultation with the labor union and is subject to certain limits (generally one hour a day but can be longer if there are special circumstances). In addition, overtime pay ranges from 150% to 300%.
- Employees are entitled to a minimum amount of paid leave, the amount of which depends on how long the employee has been employed.
- Governments of the provinces, autonomous regions or municipalities set minimum wage requirements.
- Labor disputes are settled through mediation and/or arbitration, the results of which can be challenged in court.
- Social insurance payments must be made by both the employer and the companies.

- Employees have the right to organize and participate in trade unions, to represent and safeguard their rights and interests. The trade union can enter into collective bargaining agreements with the company.

6.2 FOREIGN EMPLOYEES

In general, labor relationships with foreign employees are governed by the same laws and regulations as those with local employees. However, there are certain additional requirements for the hiring of a foreign employee.

Generally, foreigners can be hired for positions where special skills are required and local employees are temporarily unavailable. To be hired in China, foreigners need to satisfy the following requirements:

- i. 18 years of age or older and in good health;
- ii. with professional skills and job experience required for the intended position;
- iii. have no criminal record;
- iv. have a specific employer; and
- v. hold a valid passport or other international document that is equivalent to passport (hereinafter referred to as “passport substitute”).

In order to hire a foreign employee, the following steps must be taken:

- The domestic employer shall file in the application form for the employment of foreigners and submit relevant materials to the competent authority for approval. After being approved, the employer will be issued with an employment license. For FIEs, the approval procedure is not required. FIEs shall receive the license after the submission of relevant documents.

- The foreigner intends to work in China shall apply for and acquire the Z visa for entry (where there is an agreement on visa exemption, such agreement shall apply) and can be employed only after obtaining valid employment certificate and residential document for foreigner.
- The employer must, within 15 days after the entry of the employed foreigner, apply for the employment certificate for the foreigner with competent authority, the employer shall bring forth the employment license, the signed labor contract and the valid passport or passport substitutes.
- Finally, the foreigner who has obtained the employment certificate must apply for a residential document for foreigner with a public security authority within 30 days of his/her entry.

The term of labor contracts concluded with foreigners cannot exceed five years, the period of validity of the employment certificate shall be the same of the term of contract. If the employer and employee intend to renew the contract, the employer shall file the application for employment certification extension with competent authority 30 days prior to the expiration of the original contract.

6.3 DISPATCH OF FOREIGN EMPLOYEES TO CHINESE SUBSIDIARIES

Senior management employees or senior technical officers of multinationals companies are often dispatched to China to work for Chinese subsidiaries. If they have entered into employment contracts with the overseas holding company, but have not entered into employment contracts with the Chinese subsidiaries, they will be treated as having established labor contractual relationship with the overseas employer rather than with the Chinese enterprise where they perform their job.

However, if a foreign employee has worked in China for more than 3 months, his/her employment in the Chinese subsidiary shall also be regulated by PRC laws and regulations and the foreign employee must apply for the employment certificate and residential document for foreigner. Meanwhile, such

foreign employees will be entitled to Chinese welfare and benefits stipulated by PRC laws and regulations, e.g., rest and vacations.

According to the relevant rules of State Administration of Taxation of PRC on individual income tax (IIT) declaration, a foreign employee working in China under the dispatching arrangement, whose remunerations are paid by the offshore employer rather than the Chinese subsidiaries, does not need to file an IIT declaration and pay IIT as long as he/she stays for no more than 90 consecutive or cumulative days in China within a tax-paying year (or 183 days for employees from countries that have specific treaties with China). Otherwise, the foreign employee must file IIT declaration and pay IIT.

7. MERGERS AND ACQUISITIONS

Foreign investors are allowed to conduct M&A of domestic enterprises in the following forms:

- Any foreign investor purchases the equities of a domestic non-FIE or subscribes to the increase of capital of a domestic enterprise to change it into an FIE;
- Any foreign investor purchases the equities of any Chinese shareholder of an FIE or subscribes to the increase of capital of an FIE;
- Any foreign investor establishes an FIE and through which, it purchases the assets of a domestic enterprise by agreement and operate them accordingly, or purchases the equities of a domestic enterprise;
- Any foreign investor directly purchases the assets of a domestic enterprise and use them to invest and establish an FIE which will operate asset.

In all the above circumstances, foreign investment regulations regarding the available sectors for foreign investment (for example, the 2021 Negative List) and capital requirements must be respected and complied with.

7.1 ACQUISITIONS

Acquisitions can be (1) direct; or (2) offshore/indirect. The methods and approval requirements are as follows:

	Direct	Offshore/Indirect
Methods	Direct purchase of the equity or assets of the target company or subscription of its increased capital.	Offshore purchase of shares of the target's foreign parent company or companies
Required Approvals	MOFCOM or its competent local branch Modification of the registration before the SAMR.	Anti-Monopoly review may be needed. (Note: other reviews might be required by the other jurisdictions.)

In addition, acquisitions can be (1) equity acquisitions; or (2) asset acquisitions. For equity acquisitions, FIEs that incorporated as LLC or JSC shall be subject to different limitations in terms of the equity transfer:

LLC	The consent of more than half of all the non-selling shareholders is required. Once obtained, the non-selling shareholders have the right of first refusal and may acquire the shares under the same condition. And where the provisions in the AOA of the target company provide otherwise, such provisions shall prevail.
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JSC	The shares held by promoters shall not be transferred within one year from the date of incorporation of the company. And the shares issued by the company before public offering shall not be transferred within one year from the date on which the shares of the company are listed on a stock exchange.
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When the target company of M&A is a listed company, the foreign investors are subject to the disclosure obligation imposed by China Securities Regulatory Commission, and the procedural requirements shall be strictly complied with.

Asset acquisition is subject to strict regulatory restrictions and must always be approved by local authorities. Due to the variety of assets and liabilities that may be involved, the acquisition of assets may be more complex and the closing of transaction might take longer time.

Special regulations govern foreign investors' acquisitions of state-owned enterprises and private corporations with state-owned interests.

7.2 MERGERS

Mergers in China are possible as onshore transactions between FIEs and FIEs or between FIEs and domestic companies. However, the merger of an FIE must always result in the establishment of a new FIE.

The approval mechanisms for mergers of FIEs depend upon whether the merging of FIEs is subject to the Negative List. Only the merging of FIEs, which falls into the scope of the Negative List requires formal approval by MOFCOM or the competent local government. All other mergers of FIEs are subject to recording-filing of the incorporation and change of FIE.

7.2.1 PROCEDURES FOR FORMAL APPROVAL (ADMINISTRATIVE MEASURES OF ACCESS)

The formal approval should be examined and approved by MOFCOM or the competent local government. It shall then go to the registration departments (SAMR) for registration of establishment, modification or cancellation.

The formal approval procedure for mergers requires:

- Approval: The applicant should submit a series of necessary documents to MOFCOM or the competent local government for examination and approval. The examination and approval authorities shall decide on approval or non-approval pursuant to the applicable law within 30 days from the date of receipt of all documents required to be submitted. Where the approval is granted, the examination and approval authority shall issue an approval certificate.
- For assets acquisition by a foreign investor, the investor shall apply for incorporation registration with competent authorities within 30 days from the date of receipt of the approval certificate and acquire a business license for FIEs; for equity acquisition by a foreign investor, the acquired domestic company shall apply for modification registration with competent authorities and acquire a business license for FIEs.
- Foreign investors shall submit an initial report through the Enterprise Registration System at the time of applying for establishment registration or modification registration. The initial report shall include the basic information of the FIE, the investors and their actual controlling party, and the transaction or investment etc.

7.2.2 PROCEDURES FOR RECORD-FILING OF MODIFICATION OF FIES (NON-SPECIAL ADMINISTRATIVE MEASURES OF ACCESS)

Alternatively, FIEs that do not fall within the scope of the Negative List must file for modification by submitting a modification report through the Enterprise Registration System.

In the case of any modification of the information in the initial report, which involves the enterprise's modification registration, the FIE shall submit the modification report through the Enterprise Registration System when undergoing the enterprise's modification registration.

Where the enterprise's modification registration is not involved, the FIE shall submit a modification report through the Enterprise Registration System within 20 working days after the occurrence of the modification. If an enterprise makes a resolution on the modification according to its bylaws, the time when it makes the resolution shall be taken as the time of occurrence of the modification; and if it is otherwise prescribed in the laws and regulations with respect to the conditions for the entry into force of any modification, the time when the corresponding requirements are met shall be the time of occurrence of the modification.

A listed foreign-funded company and a company quoted in the National Equities Exchange and Quotations may, when the change of foreign investors' shareholding ratio accumulatively exceeds 5% or the foreign party's controlling or relatively controlling status changes, report the information on the modification of investors and the shares held by them.

A modification report shall include the basic information of the enterprise, information on investors and their actual controllers, investment trading information and other information.

7.3 ANTI-MONOPOLY REVIEW

In accordance with the regulations of FIL and the Anti-Monopoly Law of PRC (“AML”), M&A transactions shall be subject to the review of concentration of undertakings by the SAMR if:

- i. The transaction constitutes “concentration of undertakings”; or
- ii. The concentration of undertakings reaches the thresholds of review stipulated by relevant regulations.

The term “concentration of undertakings” is defined as:

- i. Merger of undertakings;
- ii. Acquisition of control over other undertakings through acquisition of equity or assets; or
- iii. Acquisition of control or capacity to impose decisive influence over other undertakings by way of contract or any other means.

Where a concentration of undertakings reaches any of the following thresholds, the undertaking(s) concerned shall file a prior notification, and no such concentration may be implemented without the clearance of prior notification:

The combined worldwide turnover of all the undertakings concerned in the preceding financial year is more than RMB 10 billion;	OR	The combined nationwide turnover within China of all the undertakings concerned in the preceding financial year is more than RMB 2 billion;
AND		
The nationwide turnover within China of each of at least two of the undertakings concerned in the preceding financial year is more than RMB 400 million.		
“Turnover”: The turnover of an undertaker involved in a concentration shall be the combined turnover of the undertaker and each undertaker directly or indirectly controlling or controlled by the undertaker at the time of notification, excluding the turnover from transactions between the aforementioned undertakers.		

Where a concentration of undertakings does not reach any of the foresaid thresholds, but facts and evidence indicate that such transaction has, or may have the effect to restrict or eliminate the competition, SAMR shall initiate the investigation against the transaction.

If the SAMR concludes that the M&A transaction might eliminate or restrict competition, the involved undertakings may submit a commitment proposal with attached restrictive condition to reduce the adverse effects of the transaction. If the proposal is deemed to be effective, SAMR shall make a conditional approval, otherwise, the transaction shall be prohibited. If the SAMR considers that the proposal for commitments is insufficient to reduce the adverse effect of the concentration on competition, it may negotiate with the undertakers involved in the concentration on the restrictions and require them to give another proposal for commitments within a reasonable period.

7.4. SECURITY REVIEW

To guide the orderly development of M&A and safeguard national security, China has established a Security Review System for M&A of domestic enterprises by foreign investors. M&A under this sector shall include the new establishment of entities, stock or asset purchases of domestic entities and other foreign investments. The scope of security review of M&A is as follows:

- Foreign investors invest in military industry, military-support industry and other sectors that are related to national security and invest in the surrounding areas of military facilities.
- Foreign investors invest in major agricultural products, energy and resources, large equipment manufacturing, important infrastructure, transportation services, cultural products and services, information technology, Internet products and services, financial services, key technologies and other important sectors, and shall obtain the actual control of the project or entity.

- The above-mentioned obtaining the actual control shall include these following circumstances: (i) the foreign investors obtain more than 50% of the shares of the invested entity; (ii) the foreign investors, though do not obtain more than 50% of the shares of the invested entity, but shall be eligible to have critical influence on the resolution of the board of directors and shareholder meetings; and (iii) other circumstances in which foreign investors shall be eligible to have critical influence on the management, employment, finance and technologies.

The security review includes general review and special review, and no investment shall be implemented by foreign investors till the review process has been duly finalized.

Any foreign investor shall file an application for M&A of one domestic enterprise to the MOFCOM and for the M&A within the scope of security review, the joint conference shall be requested to conduct the review. The application shall firstly go through the general review and if the conference deems that the M&A may affect the national security, the procedure for special review shall be initiated.

During the security review procedure, the applicant may file an application for amendments to the plan for M&A or cancellation of M&A.

Where the M&A has seriously affected or probably affects the national security, the joint conference shall request the MOFCOM and relevant departments to terminate the act of the party concerned, or take the measures of transferring related equities, assets or others to eliminate the effect of M&A on national security.

8. TAX

8.1 CORPORATE INCOME TAX (CIT)

Enterprises are classified into resident and non-resident enterprises.

A resident enterprise refers to (i) an enterprise established in China (Including all FIEs); or (ii) an enterprise established according to foreign laws but with its actual management institution located in China. A resident enterprise is subject to a CIT rate of 25% on its worldwide income (with some tax breaks in certain industries).

A non-resident foreign enterprise shall refer to an enterprise established in accordance with the laws of a foreign country and whose actual management institution is not in China, but (i) it has established an institution or place of business in China; or (ii) it has incomes derived from China although it does not have an institution or place of business in China. Non-resident foreign enterprises are subject to a CIT rate of 20% for incomes originating within China and income originating outside the territory of China but which is actually connected with the said institution or place of business within China.

8.2 INDIVIDUAL INCOME TAX (IIT)

An important amendment to IIT Law, which became effective on 1 January, 2019, is that the taxpayers in China are divided into resident individuals and non-resident individuals: (i) resident individuals: any individual who has a domicile in China or who has no domicile but has resided in China for an aggregate of 183 days or longer in a single tax year shall be deemed as a resident individual, and a resident individual shall pay individual income tax for their worldwide income according to the provisions of the IIT Law; (ii) non-resident individuals: any individual who has no domicile and has not resided in China or who does not have a domicile but has resided in China for less than 183 days in aggregate shall be deemed as a non-resident individual, who shall pay individual income tax for any China-source income according to the provisions of the IIT Law.

Although subject to numerous rules and exceptions, in general the IIT rate for income from wages, salaries, remuneration and royalties ranges from 3% to 45%. For income gained by business operations,

the tax rates range from 5% to 35%. The IIT rate for interest, dividend and bonus income, property lease income, property conveyance income and contingent income are subject to a proportional tax rate of 20%.

8.3 VALUE-ADDED TAX (VAT)

Entities and individuals who sell goods, provide labor services of processing, repairs or maintenance services, sell services, intangible assets or real property, or import goods to China, shall be identified as taxpayers of VAT, and shall pay VAT under the VAT Regulations.

The tax payable shall be:

$$\text{Tax Payable} = \text{Taxable Amount} * \text{VAT Rate (The VAT rate can range from 0\% to 17\%.)}$$

The formula for the taxable amount is:

$$\text{Taxable Amount} = \text{Output Tax in the Current Period} - \text{Input Tax in the Current Period}$$

8.4 M&A TRANSACTION TAXES

All M&A transactions are fraught with complex tax issues that require dedicated expert attention. A few notable points are listed below:

- Regarding CIT, when undergoing restructuring, gains or losses arising from the transfer of assets should be recognized at the time when the transaction occurs, and the tax base for the relevant assets shall be re-determined according to the transaction price.
- Regarding VAT, the transfer of fixed assets and inventories shall be subject to VAT based on their fair values. However, transfer of all or part of physical assets and related creditor's rights, liabilities and labor to other organizations and individuals in the course of asset restructuring by a taxpayer

through merger, division, sale or replacement etc. shall not fall under the scope of levying of VAT and transfer of goods involved therein shall not be subject to VAT.

- In an asset transaction, gains from the transfer of state-owned land use rights, buildings and their attached installations are subject to a land value-added tax based on the amount of appreciation.¹The rates range from 30% to 60%.
- A stamp tax rate of 0.05% based on the share transfer price and 0.03% based on the asset transfer price shall be imposed on both sellers and buyers.

9. INTELLECTUAL PROPERTY (IP)

It is highly recommended that all IP applications be filed locally in China even if the IP holder's rights extend to China through an international system. Filing in China, and in Chinese, will significantly increase the likelihood that the holder will win in the case of any disputes.

9.1 PATENTS

The duration of patent protection is

Invention Patents	20 years
Utility Model Patents	10 years
Design Patents	15 years

In all cases, the protection period begins from the filing date of the patent application.

¹ An amount of a surplus received by the taxpayers from the transfer of real estate after excluding the deductibles.

In order to file an application, local patent attorneys must be entrusted if a foreigner, foreign enterprise or any other foreign organization does not have any habitual residence or business office in China. There are three ways to file a patent application in China:

- i. direct filing in China;
- ii. filing first in another country which is a member of the Paris Convention and then filing in China within 12 months from the date of the first application (6 months for designs); and
- iii. filing an international patent application under the provisions of the Patent Cooperation Treaty (“PCT”) and naming China as the designated state.

9.2 TRADEMARKS

The Chinese trademark regulation is based on the “first-to-file” rather than the “first-to-use” system, thus the rights of unregistered trademarks cannot be fully protected.

Holders of well-known trademarks should not rely exclusively on the protection granted by Article 6b in the Paris Convention on “well-known” trademarks. The Chinese regulation system for the protection of well-known trademarks:

- i. is decided case-by-case;
- ii. is passive (i.e., no protection until a request is filed);
- iii. has an exceedingly high threshold. (Typical examples of such trademarks are McDonalds, Jaguar and Hugo Boss.)

Although a trademark holder can file under the Madrid Protocol through World Intellectual Property Organization (WIPO), it is highly recommended that the holder also files under the Chinese national system and obtain a Chinese certificate.

9.3 COPYRIGHTS

The *Copyright Law* provides copyright protection for works that foreign entities first published in China and also protects works published outside China within the scope of international copyright conventions and bilateral agreements. However, it is highly recommended that foreign investors register their copyrights with the National Copyright Administration as material evidence of the copyright ownership in the event of a dispute.

In order to own the copyright of a work in China, the interested party must be either the creator of the work or the employer of the creator. Copyrights can be also acquired through succession, donation, assignment or other contractual arrangement. Normally, the copyright protection will cover the life of the author plus the subsequent 50 years. But if the vested copyright owner is an enterprise, the copyright protection will be of 50 years from the date of its first publication.

9.4 OTHER ISSUES

There are other issues to consider regarding IP. A few of them are listed below.

- Computer software is protected against unauthorized online distribution.
- One can apply for IP rights with the General Administration of Customs (GAC) which allows them to prevent counterfeit versions of their products from being imported and exported.
- The AML is applicable to the business operators who eliminate or restrict market competition by abusing their intellectual property rights.

10. ANTI-MONOPOLY LAW

Since 2018, the State Council established the SAMR, and the existing anti-monopoly functions of China's anti-monopoly enforcement agencies, the NDRC, the State Administration for Industry and Commerce, and the MOFCOM, were unified and integrated into the SAMR. SAMR is responsible for the enforcement of the fair competition on the market of China, including but not limited to issues covering non-price anti-competitive behavior, price related matters and conducting antitrust review of concentrations between undertakings.

Since August 2020, the *Guidelines for Operator Antitrust Compliance*, *Guidelines on Antitrust in the Field of Platform Economy* and other regulations have been released, which have put forward more specific and clear requirements for compliance and enforcement in the field of anti-monopoly.

According to the AML, “monopolistic practices” include:

- i. Conclusion of monopoly agreements between business operators;
- ii. Abuse of dominant market position by business operators; and
- iii. Concentration of undertakings which may have the effect of eliminating or restricting market competition.

In addition, it is a violation of the AML for an administrative organ or organization empowered by a law or administrative regulation to “abuse of administrative power to eliminate or restrict competition.”

In accordance with the AML, monopolistic practices restricting or with the potential to restrict competition in China will be subject to administrative investigation, even if conducted outside China.

10.1 MONOPOLY AGREEMENTS

For the purposes of the AML, “monopoly agreements” refer to agreements, decisions or other concerted actions, which eliminate or restrict competition. Agreements that are either horizontal (between competitors on the same level of the distribution chain) or vertical (between upstream and downstream undertakings) might contain provisions potentially restricting competition.

Exemptions are provided for agreements which create benefits for economic development or public interest, such as the improvement of technology, product quality, cost reductions and operational efficiency among others. Provided that none of these exemptions significantly impede effective competition in the relevant market and can enable the consumers to share the benefits from the agreement.

10.2 ABUSE OF DOMINANT MARKET POSITION

Various factors, such as the market share or ability to control the market, are used to determine if a business operator has a “dominant market position”.

If a business operator does have a dominant market position, certain practices are prohibited. For example, such business operator is prohibited to buy/sell commodities at an unfairly low/high price, refuse to trade with a trading partner without a justifiable reason, etc.

10.3 CONCENTRATION OF UNDERTAKINGS

Please see section 7.3.

11. EXITING CHINA

Dissolution and liquidation regulations as well as insolvency proceedings must be considered when investing in China. Simply abandoning the FIE is not a recommended option because of the business risks related to branding and IP issues.

Also, foreign investors or the FIE shall submit the information regarding the exiting to competent commerce departments through the Enterprise Registration System and the Enterprise Credit Information Publicity System.

Liquidation proceedings are divided into non-bankruptcy and bankruptcy proceedings.

11.1 NON-BANKRUPTCY LIQUIDATION

FIEs can be dissolved for a number of reasons including the expiration of its term, being unable to continue with its operation, etc. In addition, the AOA, shareholders' agreement, and/or partnership agreement can specify additional criteria for dissolution. Additionally, a partnership must be dissolved when the number of partners fails to meet the legally required number of partners for 30 days or more.

As for Companies, generally, the shareholders' meeting must resolve to dissolve the company. A company may be dissolved where (i) the company's term expires or any dissolution event as prescribed in the AOA occurs; (ii) the shareholders' meeting or the general meeting of shareholders resolves to dissolve the company; (iii) its business license is revoked or it is ordered to close down or be resolved or the people's court makes an order for dissolution. If the company is dissolved for one of the reasons set forth above, a liquidation committee must be established within 15 days. If the company is dissolved due to any combination or division to which the company is a party, the claims and debts of the parties to such combination or division shall be succeeded by the company that survive the combination, or by the newly-established company.

The members of the liquidation committee shall be the shareholders (for an LLC) or the directors or other individuals appointed by the shareholders' meeting (for a JSC). The committee must prepare a liquidation report which shall be presented to the shareholders' meeting and to the people's court for confirmation. The liquidation committee's powers include convening creditors' meetings, recovering creditors' rights, claiming credits and paying off debts, etc.

For partnerships, upon consent of more than half of the partners, one or several partners or third persons may, after the occurrence of the cause for the dissolution of the partnership, be designated or entrusted to act as liquidators.

The liquidators shall prepare an inventory of the partnership's property and a statement of its assets and liabilities, manage the partnership affairs related to the liquidation proceedings, etc. After paying off the liquidation expenses, wages of employees, social insurance premiums and legal indemnities, the outstanding taxes and the debts with the properties of the partnership, the remaining assets shall be distributed to the partners. If the assets are not enough to cover these amounts, the general partners are liable for them.

11.2 BANKRUPTCY PROCEEDINGS

Bankruptcy could occur when: (i) an enterprise cannot pay its due debts and its assets are not enough to pay the totality of the debts; or (ii) the enterprise apparently lacks the capacity to pay off its debts.

When bankruptcy occurs:

- The enterprise can apply for its reorganization, compromise or bankrupt liquidation;
- Creditors may apply for the enterprise's reorganization or bankrupt liquidation;

- The person liable for liquidation shall apply with people's court for the enterprise's bankruptcy, if the enterprise has already been dissolved while has not initiate liquidation or the liquidation has not been completed and the assets are not enough to pay off its debts.

11.2.1 BANKRUPTCY

The People's Court will specify the time limit for creditors to declare their claims after accepting the application for bankruptcy, though creditors can still declare claims after the expiry of such time period (so long as they do so before the final distribution of the enterprise's insolvent assets).

A bankruptcy administrator must be appointed by the People's Court. The administrator must prepare a conversion plan and submit it to the creditors' meeting for discussion. The insolvent assets must be subject to monetary distribution through auction (unless otherwise decided by the creditors' meeting or provided by specific regulations).

Secured creditors are paid with the guarantee property and then, after repaying the expenses of administering the bankruptcy case and other debts incurred for the common good of all the creditors in priority, the bankruptcy property is distributed in the following order:

- The wages and subsidies for medical treatment and disability, comfort and compensatory expenses due to the employees, the fundamental old-age insurance premiums, fundamental medical insurance premiums that shall have been transferred to the employees' personal account as well as the compensation payable to the employees as prescribed by applicable laws and administrative regulations;
- The social insurance premiums and tax fees as defaulted by the bankrupt other than those as prescribed by the aforesaid provisions;

- The common credit of bankruptcy.

11.2.2 REORGANIZATION

Alternatively, the enterprise or its creditors may directly apply for reorganization instead of bankruptcy. If bankruptcy has already been accepted by the People's Court after the request made by a creditor, the enterprise or its partners/shareholders representing one-tenth or more of the registered capital may still apply for reorganization. The enterprise or its administrator must submit a draft plan to both the people's court and the creditors' meeting within six months from the date of the approval of the reorganization application (the period may be extended for another three months, if upon request of any debtor or the bankruptcy administrator and on a justifiable ground). If the enterprise or its administrator fails to submit the plan on time, the people's court shall rule to terminate the reorganization proceedings and announce the bankruptcy of the debtor.

11.2.3 COMPOSITION

The enterprise may directly apply for composition with the people's court after the application of bankruptcy is accepted but before the declaration of bankruptcy. A draft composition agreement must be jointly submitted with the application.

If the people's court deems upon examination that the application complies with the law, it shall rule on a composition, announce it and a creditors' meeting shall be held to discuss the draft of a composition agreement. A resolution regarding the composition must be adopted by half or more of the creditors with voting rights who are present in the meeting, and the amount of their credits shall account for two-thirds or more of the total amount of unsecured claims. the secured creditors can exercise their rights once the court rules in favor of the composition).

11.3 DEREGISTRATION

11.3.1 FIE DEREGISTRATION

For FIEs, the liquidation committee must file an application for deregistration before the local branch of SAMR after the liquidation is completed (the application should be filed within 15 days after the completion of the liquidation proceedings in the case of partnerships). The enterprise shall be formally terminated after completion of the formalities before the local branch of SAMR.

11.3.2 REP OFFICE DEREGISTRATION

Rep Offices must apply for deregistration within 60 days upon the occurrence of any of the following circumstances:

- i. its term of residence expires and the Rep Office stops business activities;
- ii. A Rep Office is cancelled of approval or ordered to be closed according to law;
- iii. the foreign enterprise revokes the Rep Office; or
- iv. the foreign enterprise is dissolved.

In order to deregister a Rep Office, proof of deregistration from the tax, customs and foreign exchange authorities must first be obtained. To this end, all tax due must be paid off, and after which deregistration may be requested with the local branch of SAMR.

12. LIST OF ABBREVIATIONS

Abbreviation	Full Name
AOA	Article of Association
AML	Anti-Monopoly Law of the PRC
CIT	Corporate Income Tax
DRC	Local Development and Reform Commission
ETDZ	Economic and Technological Development Zone
FDI	Foreign Direct Investment
FIE	Foreign Invested Enterprises
FTZ	Free Trade Zones
GAC	General Administration of Customs
GDP	Gross Domestic Product
GNI	Gross Natural Income
HTDZ	High Technology Development Zone
IIT	Individual Income Tax
IP	Intellectual Property
IPR	Intellectual Property Rights
JSC	Joint Stock Company
LLC	Limited Liability Company
M&A	Merger and Acquisition
MOFCOM	Ministry of Commerce of the PRC
NDRC	National Development and Reform Commission
PCT	Patent Cooperation Treaty
PRC	People's Republic of China
Rep Office	Representative Office

Abbreviation	Full Name
RMB	Renminbi
SAMR	State Administration for Market Regulation
SAFE	State Administration of Foreign Exchange
SEZ	Special Economic Zones
USD	US Dollar
VAT	Value Added Tax
WFOE	Wholly Foreign Owned Enterprise
WIPO	World Intellectual Property Organization
WTO	World Trade Organization

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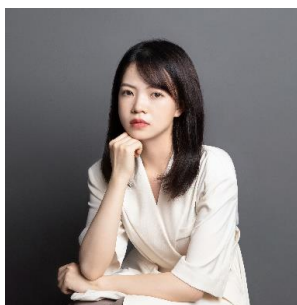


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