

# **China**

## **Legal Provisions**

**Compiled by:**

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### **FOREIGN DIRECT INVESTMENT IN CHINA**

Foreign investments in the People's Republic of China ("China", "PRC") may be divided into direct investment and other means of investment. The direct investment, which is widely adopted, mainly includes Sino-foreign Equity Joint Ventures ("EJV"), Sino-foreign Cooperative Joint Ventures ("CJV"), Wholly Foreign-Owned Enterprises ("WFOE") and some other vehicles for special purposes. The three are generally also referred to as Foreign Invested Enterprises ("FIE").

#### **1.1 Equity Joint Venture**

The key distinguishing feature of an EJV is that profits are distributed and risks allocated in proportion to each party's contribution to the registered capital of the limited liability company. In other words, the risk and profit allocation between the JV partners may not deviate from the proportion set out in the original investment. EJVs are established in the legal form of a limited liability company. In general the capital contribution from the foreign party shall not be lower than 25%.

#### **1.2 Cooperative Joint Venture**

A CJV may either be a "legal person" (PRC terminology) of limited liability, or a non-legal person with unlimited liability in accordance with PRC Civil Law.

The key differentiating features of a CJV compared to a EJV are: a) The parties may allocate profits and losses as they choose rather than in proportion to their respective contributions to the registered capital, b) the foreign party may apply to recover its investment capital during the term of the venture (in some cases before payment of income tax).

The flexibility inherent in the CJV makes it particularly suitable for certain types of investment. The foreign party may apply to recover its investment during the term of the venture with the funds derived from depreciation of fixed assets, amortization of intangible assets, and so on.

#### 1.3 Wholly Foreign Owned Enterprises

The advantages of the WFOE limited liability company (i.e. a 100% subsidiary) are obviously that a Chinese partner is not involved and thus the potential disputes with it can be avoided. Also, when the WFOE is established by a single foreign investor, the 100% management and financial control over the enterprise is guaranteed. In addition, from a practical point of view, a WFOE may be established faster.

#### 1.4 Comparison between JV and WFOE

The major legal reason for opting for a JV structure rather than a WFOE is the desire of the foreign party to be active in a restricted industry or business area where a WFOE is not yet permitted (see further below).

In addition, a JV may have the side advantages that the foreign investor may need to invest less capital and be able to diversify risks and/or costs to its PRC JV partner. Moreover, certain assets of the PRC partner may be valuable to the foreign investor (land-use rights, equipment, infrastructure, trained staff, marketing or distribution channels, etc.) Further, connections from the PRC partner may help securing various licenses, obtaining preferential government treatment or fending off government and administrative interventions.

In addition to the above-mentioned three major types of foreign direct investment, foreign investors may, depending on their business objectives or operation scale, and subject to restrictions and more detailed regulations expected in the future, upgrade the JV or WFOE to a listed foreign invested company limited by shares, to be listed in a PRC stock market.

#### 1.5 Representative Office

Opening a representative office is sometimes reckoned to be the easiest way to establish a commercial presence. However, such representative offices may only be engaged in liaison, marketing or other non-profit-generating activities. Depending on the circumstances, representative offices may be taxed based on their expenses rather than on their income. This principle is not observed in case of representative offices of foreign service providers such as foreign law firms, accounting and tax firms, whose rep offices in China are allowed to conduct profit-generating activities.

#### 1.6 Foreign Investment Company

To create a comprehensive holding vehicle for various types of investment and centralize service functions in the PRC, foreign investors have been given the possibility to establish foreign investment

companies in the PRC. A foreign party seeking to establish a foreign investment company must have good credit standing and either: a minimum asset value of \$400 million (calculated for its corporate group as a whole), plus a total registered capital in existing FIEs of at least \$10 million; or at least \$30 million of registered capital in 10 or more existing FIEs in China. Foreign investment companies may invest up to five or even seven times their registered capital (not less than \$30 million) by means of loans, keep a higher leverage ratio than ordinary FIEs, and possess a more wide-ranging business license, allowing them to act more liberally in many respects compared to ordinary companies. The relevant regulations modified in 2006 expand the scope of services that a foreign invested holding company may provide its affiliates in the PRC with, which may help rationalize the organizational structure and improve the efficiency of its investments in the PRC. The modification has also alleviated the restrictions about the investment methods available to the foreign invested holding companies in that it allows such companies to make strategic investment in domestic listed companies.

#### 1.7 Foreign Invested Partnerships

The Administrative Measures for Establishment of Partnership Enterprises in China by Foreign Enterprises or Individuals (the “Measures”) generally allow a foreign investor to act as a general partner or limited partner of a limited partnership. Special laws or regulations apply where foreign investors are involved.

The Ministry of Commerce and its local bureaus (“MOFCOM”) have been the main approval authority for foreign invested enterprises for decades, but the Measures take a different approach for foreign invested partnerships (“FIP”). An application for the establishment of an FIP shall be submitted to the local administration of industry and commerce as authorized by the State Administration of Industry and Commerce (“AIC”). MOFCOM will only be notified of the registration information upon the establishment of an FIP. An FIP is still subject to foreign investment industrial policies, including the Foreign Investment Industry Catalogue, and the AIC will review an explanation on compliance with foreign investment industrial policies as part of the application process.

#### 1.8 Policies for Foreign Investment Industries

Upon China’s entry into the WTO and in accordance with its WTO commitments, China made significant amendments in laws and regulations and promulgated new regulations related to direct foreign investment, and it continues to open up related restrictions.

The latest Catalogue for the Guidance of Foreign Investment Industries, which is effective from April 10, 2015, for the first time lifts the restrictions in certain service industries such as accounting and auditing (requirement to have a Chinese national as the firm’s main partner), while it encourages foreign investment into R&D in the fields of medicine and technology, architecture design and nursing homes. Under this new Catalogue, restrictions on foreign shareholding requirements and other types of investment restrictions will be removed from more than half of the “encouraged” industries, which

means that foreign investors in these industries can operate their businesses in China through WFOEs. In particular, this relates to the production of biological liquid fuels, e-commerce for technology, media and telecommunications business (value-added TMT excluded), international marine transportation services, as well as construction and operation of urban subways, light railway and other track transports, etc. In addition, the Catalogue removes the limitation of foreign investment in financial companies, trust companies and currency brokerage companies, which were restricted under 2011 Catalogue.

The new Catalogue reflects China's determination and effort to reform the regulation of foreign investment and push more local industries to enter into free market competition.

Furthermore, the Regulations on Foreign Investment in Commercial Areas, which entered into force on 1 June 2004, has substantially lowered the thresholds for foreign investors to establish FIEs in the fields of commission agency, wholesale, retail and franchise.

Within the strategy of development of the Middle and the West of the PRC, the government has also enacted the Advantageous Industries Catalogue for Foreign Investment in Middle and Western Regions to implement preferential policies for foreign investment in the Middle and the Western regions.

### 1.9 Liberalization of Company Law

The revision of the Company Law in 2013, effective as of March 1, 2014, brought significant changes to the existing company administration system, including abolishment of an all-industry minimum registered capital requirement, of the time limit for capital contribution, of the mandatory ratio of cash contribution and of the capital verification requirement. It also carried out the transformation from the annual inspection system to the annual self-report system, etc. In general, the company establishment procedure has been significantly simplified and the control over companies has been loosened. The reform reflects the trend of turning companies into a more self-responsible and self-disciplined actor in a market economy.

Many further changes for the purpose of alleviating burdens caused by outdated administrative measures have taken place ever since the liberalization of the Company Law. In particular, since 23 June 2015, the three principal corporate certificates: the Business License, the Organizational Code Certificate and the Tax Registration Certificate are consolidated into one integrated Business License with a 9-digits unified social credit code. This means that instead of having to go to various authorities to obtain different certificates after MOFCOM Approval, now the foreign invested companies will only have to visit and go through with incorporation formalities at the AIC. Such change will significantly reduce the time and cost of incorporation for foreign investors. From an administrative point of view, a consolidated business license with a unified social credit code will also enable the administrators to keep a clear and consistent credit record of each company, such record will be essential in other

aspects of the operation of each companies in the market (such as treatment under processing trade discussed in section 2.1.3).

#### 1.10 Future Tendencies

China declares that it will continue to improve the political and legal environment for foreign investment, and to enhance quality and transparency of all administrative levels. China is further expected to continue to improve its legal system, subject to ongoing reforms.

Industry-wise, more and more emphasis has been laid on factors such as optimization of resource efficiency, environment protection and production safety, with a series of relevant laws, regulations and national standards being promulgated to ensure the national industry policy is adhered to.

The new Shanghai Free Trade Zone, which was officially launched in 2013, is an attempt of China to further open its economy. To some extent, it is a response of China to the trend of further economic globalization, led notably by the free-trade talks between the US and the EU and by the negotiations on the TPP (Trans-Pacific Partnership Agreement). The Shanghai Free Trade Zone, built on the four existing Bonded Areas, features the opening of the service industry (a “negative-list” mode has been adopted by which the industries that are not listed will be fully open to foreign investment), the simplification of the company establishment procedure (filing for record, instead of approval by MOFCOM) and reform in financial industry (e.g. free convertibility of Renminbi under the capital account), etc. In an announcement made in December 2014, the Standing Committee of the National People's Congress announced that the Shanghai Free Trade Zone will be expanded to include the Lujiazui financial district, Jinqiao development zone and Zhangjiang hi-tech park. The guiding principle is to build up a free trade zone with international standards, and, with the lessons and experiences from this trial, to extend the reform and opening nationwide. So far, the liberalizations have progressed slower than expected, particularly in the financial sector, and it appears that the Chinese leadership has redirected its focus to broadening the reform trials by opening new free trade zones in other regions of the country, rather than deepening the first reform trial in the Shanghai Free Trade Zone.

The Chinese Ministry of Commerce has released the draft of a proposed new Foreign Investment Law to solicit public opinions on January 19, 2015. The intention of this important move is to standardize and simplify the current regulatory framework for foreign investment. Specifically, there will no longer be a separate legal regime for WFOEs, Equity JVs and Cooperative JVs and foreign invested enterprises in general shall largely be subject to the same legal treatment as domestic companies. The draft expands the definition of foreign investor to include not only domestic enterprises that are established or controlled by a foreign company (e.g. a WFOE), but also its subsidiaries. Furthermore, the proposed law will bring a considerable reduction of legal entry barriers to foreign investment in China. At the same time, however, scrutiny shall be increased in order to assure that foreign investors

do not evade regulations prohibiting investment in restricted industries. The final form of the new Foreign Investment Law and the time of its promulgation are still unclear.

#### 1.11 Responsible Authorities

Generally, the Ministry of Commerce (MOFCOM) is the central government authority that examines and approves the establishment of FIEs with foreign contributions exceeding certain amounts, or engaged in certain restricted business areas, or in businesses subject to quotas and specific licenses. The responsible division within MOFCOM is the Department of Foreign Investment Administration.

After the MOFCOM has issued the relevant approvals necessary, the State Administration of Industry and Commerce ("the SAIC") or its branch offices at the provincial or municipal level ("the AIC") will be in charge of recording and registering the essential information of the established FIE. Subsequently, a business license will be issued to the FIE, indicating the completion of the establishment process. Any further changes of the information recorded and registered are subject to application or filing process with the SAIC or the AIC.

In this context, it is also worth noting that certain foreign investments (1) in encouraged areas where a controlling PRC partner is mandatory and (2) in restricted areas are furthermore subject to confirmation procedure with the PRC State Council or provincial and municipal government, depending on the total volume of such foreign investments.

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### **CUSTOMS AND FOREIGN TRADE SYSTEM**

#### 2.1 PRC Foreign Trade System

##### 2.1.1 Foreign Trade Regulatory Regime

The PRC foreign trade regime rests primarily in the PRC Foreign Trade Law, which has been amended since 1 July 2004 in light of the WTO accession. As the foremost legal basis in the regime of foreign trade in China, it has provided regulations in mainly the following aspects:

- Qualified business operator for foreign trade: any legal person, organization or individual duly registered with the MOFCOM can qualify as such in order to be engaged in the business of foreign trade. This means that an FIE in China could also register to become foreign trade operator without any legal hurdles.
- The different regulatory measures applicable to the import and export of different goods and technologies: for items subject to free import and export, the customs clearance procedure in the following section shall be followed before such goods and technologies could pass the PRC border; for items subject to restrictions, a quota or import/export license shall be obtained before the import/export takes place; for items subject to prohibitions, import/export activities are strictly forbidden. The lists of items under each category are updated and promulgated regularly, usually on an annual basis.
- International service providers are generally granted entrance and national treatment, except under limited situations. However, as the specification of such "limited situations" are broad and general, the State Government still has considerable discretion when it comes to regulating international service providers in China.
- IPR Protection will be provided by the customs, which is discussed in details in section 2.2.

### 2.1.2 Customs Clearance Procedure

The current customs system is based on the PRC Customs Law and regulations on the related Import and Export Tariffs, the latter of which is amended annually to provide a detailed and updated list of tariffs.

The PRC customs duty includes Most-Favored-Nation (MFN) duties, duties subject to territorial trade treaties, special preferential duties, common duties and quota duties, which will apply depending on the status of the country in which the imported goods are produced.

Customs clearance must be applied for to the customs within a certain period of time (generally, within 14 days after the declaration of arrival of the transportation vehicle in China for import customs clearance and within 24 hours before the arrival of goods to be exported in customs supervision area for export customs clearance). While applying for customs clearance, the applicant shall submit a series of documents including import license (if applicable), commercial invoices, bill of lading, packing list or purchase contracts, certificate of origin and commodity inspection certificate etc.

Under certain circumstances, relevant enterprises may, prior to the completion of customs formalities, file an application with the China customs authorities to request for the release of goods earlier than normally required, under the condition that a guarantee is provided.

With regard to trade with Switzerland, the applicable Free Trade Agreement provides various tariff reductions, some of which will enter into force gradually within the next few years.

#### 2.1.3 Processing Trade

Goods imported for processing trade (i.e. which will be re-exported after being transformed in the PRC) are not subject to customs duties. However, FIEs which intend to be engaged in processing trade shall handle the procedures of record keeping at the customs and obtain a registration manual for processing trade.

In recent years, especially in the year 2015, the Government has frequently updated the Prohibition and Restriction Lists of Commodities for Processing Trade. As goods listed on the prohibition list can only be imported under the general trade customs category, companies active in processing trade are not allowed to import them, even if they are willing to pay customs duty and import VAT. The various updates are one of many steps taken by the Chinese Government to curb the part of the processing industry that engages in labor intensive, low value added processing trade and shift the industry towards the processing of higher technology goods. Furthermore, companies with different credit records are subject to differentiated treatment when it comes to importing restricted items for processing trade. In the long run, it is a positive step towards an integrated management regime that is more flexible and adaptable based on the capability and credential of each individual company in play.

#### 2.1.4 Bonded Zones

In principle, goods shipped into bonded zones are not subject to import customs duty and import VAT, as they are not deemed imported. These import customs duty and VAT will become payable only when the goods are transported into areas that are within the PRC but outside of the bonded zones. Furthermore, products that are manufactured in the bonded zones are exempt from export duty when they are exported. Consequently, bonded zones are used mainly for foreign trade, logistics, warehousing and processing trade. In Shanghai, the above is applicable on the recently established Shanghai Free Trade Zone, which unifies the four former bonded zones.

#### 2.1.5 VAT Refund

FIEs that export goods manufactured in China can apply for VAT refund on a monthly basis at the respective customs. However, to qualify as a VAT tax payer and VAT refund, local approval authorities in charge of foreign direct investment may set certain requirements for the registered capital of the FIEs. Note that VAT refunds in the PRC can be subject to considerable time-lags.

China has implemented the Agreement on Customs Valuation under the WTO by enacting the Measures of the Customs of the People's Republic of China for the Assessment and Determination of Dutiable Value of Import and Export Goods in 2006, which was further amended in 2013.

## 2.2 IPR Protection

China's system for IP customs protection was established with the promulgation of the Regulations on Customs' Protection of Intellectual Property Rights (1995), which was renewed in 2003 and further strengthened with a 2010 amendment. The implementing rules were published in 2004 and further amended in 2009.

At present, the IP rights subject to customs protection include the following:

- Registered trademarks as verified and approved by the China Trademark Office (except service trademarks);
- Trademarks registered internationally with the World Intellectual Property Organization (WIPO) and extended to China (except service trademarks);
- Patents for invention, for utility model and for design as granted by China's State Intellectual Property Office (SIPO);
- Copyright and related rights as held by citizens or organizations of the member states under the Berne Convention for the Protection of Literary and Artistic Works.

The first consideration that IPR owners should make is whether to record their IPR with the General Administration of Customs (GAC). The recording of trademarks, patents and copyrights serves as a notification on the conditions of an IPR, with details on who to contact in case of suspected infringement, and a picture or sample of the products and its packaging. While recording is not a precondition for customs protection, it makes it more likely that the customs authorities will actively look for fake items being exported out of China and alert the IP holders of the infringement. For owners of trademarks and design patents, recording is inexpensive, will last for an extendable ten years and will ensure that an owner can use customs protection should the occasion arise. For invention and utility model patent rights, recording is less relevant since customs will unlikely detect infringements during their daily supervision of imported and exported goods. However, for active protection, such recording may still be useful.

Customs protection falls into two distinct categories: passive protection, which relates to customs taking measures in response to an IPR owner's request; and active protection, in which customs investigates and disposes of infringing goods on their own initiative. Most cases until now still fall into the first category, but customs are now becoming more inclined to actively investigate infringements. If more active investigations are taken, IPR owners will be expected to have fewer challenges to overcome.

## 2.3 Future Tendencies

China's tariff reduction commitment which was made when it became a member of WTO in 2001 was fully performed in 2010. In 2016, 9 tariff items were added and the currently taxable tariff items amount to 8294. The general tariff level is left unchanged at 9.8 percent, the same as the previous seven years.

#### 2.4 Responsible Authorities

The General Administration of Quality Supervision, Inspection and Quarantine of the People's Republic of China is responsible for the inspection of imported goods whereas the Customs General Administration is the competent authority for supervision and control over import and export and collection of customs duties, and the State Administration of Taxation is responsible for the import VAT (State Administration of Taxation contact information please refer to Chapter 4).

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### **TAXATION**

#### 3.1 Major PRC Taxes Affecting Foreign Investors

##### 3.1.1 Business Tax and Value Added Tax ("VAT")

The Business Tax is a local tax on business activities which includes only services not covered by VAT and the transfer of immovable or intangible property within China. The tax rates vary from 3% to 5%, except for the entertainment business where rates may be as high as 20%. No credit is allowed of VAT against Business Tax. A Business Tax of 5% was imposed on representative offices of foreign enterprises in certain industries such as law firms, accounting firms, tax consulting firms, cost-plus basis representative offices, etc.

VAT currently applies to all individuals and enterprises engaged in supplying goods or rendering specified services or in importing goods (not services), under the limited scope explained above.

Since 1 January 2012, the trial of transition from Business Tax to VAT for transportation and certain modern service industries was implemented in Shanghai and then expanded to Beijing and seven other provinces and municipalities. On 1 May 2016, the transition from Business Tax to VAT for all industries has been completed.)

Since such reform has been carried out, the general VAT rate is 6%, with the following exception: the VAT rate for the provision of services such as transportation, postal services, basic telecommunication, construction services, leasing of immovables, sale of immovables and transfer of land use right is 11%; the rate for the provision of leasing services of tangible movables is 17%; and the rate is 0% for cross-border taxable transactions. Goods sold or services provided by certain small-scale taxpayers are taxed at a special VAT rate of 3%. Qualified tax payer as stipulated in the law may apply for the simple tax computation method to be subject to lower VAT rates.

### 3.1.2 Foreign Enterprise Income Tax

The 2008 reform of the Chinese Enterprise Income Tax Law has unified the tax rates for FIEs and domestic enterprises. Since then, the general unified tax rate of enterprise income is 25%. Small enterprises with small profits enjoy a rate of 20% and high-tech enterprises encouraged by the State enjoy a preferential rate of 15%.

Enterprise income tax adopts the classical system whereby profits distributed by a company in the form of dividends will then also be subject to individual income tax in the hands of individual shareholders.

Income derived in the PRC (e.g. dividend, interests or royalties) by a foreign company with domicile outside the PRC may be subject to Enterprise Income Tax. Reductions may apply in case of bilateral treaties (from usually 10% withholding tax to as low as 5%).

### 3.1.3 Individual Income Tax

There is no system of personal deductions, though a standard monthly deduction is allowed for some income (such as employment income) and specified deductions may be made for some types of income. Each individual is considered to be a separate taxable person, and there is no aggregation of the income of, or joint taxation of, spouses.

Income is taxed at different rates depending on the nature of the income. Whereas wage income, business income, and management fees are subject to progressive taxation, some other types of income such as remuneration for professional services and rent, royalties, interest and dividends are taxed at a flat rate.

With regard to the employment income, residents of the countries or regions having concluded bilateral treaties with China will generally only be taxed in China for China-related income, as long as they stay in China for less than 183 days and the income is not paid by a permanent establishment of a foreign enterprise in China.

**3.1.4 Urban Maintenance and Construction Tax (the “UMCT”) and Education Surcharges (the “ES”)**  
Since 1 December 2010, UMCT and ES are imposed on foreigners who are obliged to pay any one of the “Three Taxes”: VAT, Consumption tax, or Business Tax. The UMCT and ES are a sort of surcharge calculated based on the total amount of the Three Taxes actually paid by foreigners.

With regard to the taxation rates, the rates for UMCT on the total amount of the Three Taxes actually paid are as follows: 7% for taxpayers located in urban areas, 5% for taxpayers located in counties or townships and 1% for taxpayers located in areas other than urban area, counties and townships.

The education surcharges shall be collected at the rate of 3% of the total amount of the Three Taxes actually paid.

### **3.1.5 Main Other Taxes**

Consumption tax, agriculture tax, stamp duty, deed tax, land appreciation tax, urban property tax, vehicle and vessel use tax, slaughter tax, tax on tonnages of ships, vehicle purchase tax and resource tax.

## **3.2 Tax Incentives for Foreign Direct Investment**

Tax incentives are mainly available for enterprise income tax, import duty and VAT (in particular, imported equipments of qualified FIEs within the range of their total investment may be exempted). Since the entry into force of the new Chinese Enterprise Income Tax Law in 2008, tax incentives for FDIs are no more based on who invests and where the investment takes place, but rather on which industry the investment flows in, regardless of the origin of the capital. In other words, preferential treatments in enterprise income tax treatments are granted to the important industries and projects the development of which are supported and encouraged by the state.

Major tax incentives provided by the Chinese Enterprise Income Tax Law are as follows:

- The enterprise income tax on enterprises with small profits which meet certain conditions shall be levied at a reduced tax rate of 20%.
- The enterprise income tax on important high- and new-tech enterprises supported by the state shall be levied at the reduced tax rate of 15%.
- Taxes on incomes incurred from projects of agriculture, forestry, husbandry and fishery, from business operations of important public infrastructure investment projects supported by the state, from the projects of environmental protection, energy and water saving, from the transfer of technologies, may be exempted or reduced.

### 3.3 Tax Authorities

The State Administration of Taxation (“SAT”) is a Ministry-level department under the direct leadership of the State Council, which is responsible for implementing the tax law and collecting taxes assigned to the central government. It is situated in Beijing and has many branch offices throughout the country. In addition to SATs, there are local tax authorities responsible for collecting and managing local taxes.

With regard to the major tax categories, SAT is primarily responsible for the levy of corporate income tax, VAT and consumption tax whereas local tax administrations are mainly responsible for the levy of urban maintenance and construction tax, education surcharges and individual income tax. However, for the sake of efficiency, they may also collect each other's taxes upon mutual request.

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## CAPITAL MARKETS

### 4.1 Overview

Since their opening around 20 years ago, China's capital markets are now best described as emerging. The WTO also opened the door to foreign participation in China's capital markets. A number of new regulations issued since 2002 have made it possible for foreign firms to establish joint-venture fund management companies as well as securities companies. In addition, a Qualified Foreign Institutional Investor (“QFII”) scheme was introduced to permit major foreign financial institutions to invest directly in the domestic bond and equities markets. In 2014, the State Council has issued a roadmap for the ongoing reforms of the capital market, which outlines goals such as further loosening restrictions on shareholding of foreign investors in listed companies, increasing the allowance for foreign investors' participation in the securities and futures industry, and steadily opening the domestic capital markets in order to allow foreign individuals to directly invest in the Chinese capital market while also promoting investment in overseas capital markets by domestic individuals. In November 2014, the Shanghai-Hong Kong Stock Connect program was launched. Under the program, investors in Hong Kong and Mainland China can trade and settle shares listed on the other market via the exchange and clearing house in their home market. However, this program still has a quota system in place to control the initial pace and size of cross-boundary fund flows.

### 4.2 Fund Management Companies

According to Article 10 of the Measures for the Administration of Securities Investment Fund Management Companies, the cumulative proportion of capital contribution of or cumulative proportion

of rights and interests owned (directly and indirectly) by the foreign party of a Sino-foreign joint venture fund management company may not exceed those in the commitment made by the state on securities industry for opening to the outside world. Under the Catalogue for the Guidance of Foreign Investment Industries (revised in 2015), the current limit to foreign participation in fund management companies is a maximum investment of 49%. By April of 2016, 45 Sino-foreign joint-venture fund management companies have been established in China.

In 2012, the China Securities Regulatory Commission (“CSRC”) released the Interim Provisions on the Administration of Subsidiary Companies of Securities Investment Fund Management Companies, Trial Measures for Asset Management Business for Specific Clients of Fund Management Companies and Provisions on Issues concerning the Implementation of the “Trial Measures for Asset Management Business for Specific Clients of Fund Management Companies” to further lower qualification thresholds and expand the investment scopes, as well as strengthen supervision and loosen control in the capital market.

#### 4.3 Securities Companies

Regulations limit foreign participation in the domestic securities industry to joint ventures, with a maximum foreign shareholding of 49% of the registered capital. According to the Catalogue for the Guidance of Foreign Investment Industries, which is mostly in line with China's WTO commitments in this aspect, Sino-foreign joint venture securities companies may, subject to approval by the government authority, engage in the underwriting and sponsorship of RMB-denominated A-shares, foreign-currency denominated B- and H-shares, government bonds and corporate bonds, the brokerage of B- and H-shares, and the brokerage and proprietary trading of treasury bonds and corporate bonds upon establishment, and may apply for expanding their business scope two years after establishment if they satisfy relevant conditions. By the end of January 2012, 13 Sino-foreign joint venture securities companies had been established in China.

#### 4.4 Qualified Foreign Institutional Investors (QFII)

In December 2002, QFII regulations were enacted, allowing foreign institutions to invest in the domestic stock and bond markets. As of February 27, 2015, 265 qualified foreign financial institutions have been granted a total investment amount of 69.723 billion dollars by the State Administrate of Foreign Exchange (SAFE).

The Measures on the Administration of Domestic Securities Investment by Qualified Foreign Institutional Investors (QFII) came into force as of September 2006. The Measures provide a better legal environment for QFII investing in the Chinese market, and they are therefore considered to be propitious to QFII to actively participate in the reform and development process of the Chinese capital market. The Measures are also in favor of dispersing financial risks. In 2012, CSRC promulgated the Implementation of the Measures, which allows more institutions to gain QFII status and to facilitate the execution of their investments. In 2016, SAFE issued the new Provisions on Foreign Exchange

Control for Securities Investments in China by Qualified Foreign Institutional Investors, which broadens the limitation of investment quota of a QFII.

#### 4.5 Second Board

After 10 years of preparation, China launched ChiNext on October 30, 2009, otherwise known as “Growth Enterprise Market” or “Second Board” in Shenzhen. This Nasdaq-style board aims to nurture small and medium-sized growth companies in the country and provide them financing channels. Applicants for the second board listings are required to have at least RMB 30 million worth of stock capital, which is much lower than the minimum RMB 50 million needed to list on Shenzhen’s SME board or Shanghai Stock Exchange. Likewise, second board applicants shall have been profitable for two years prior to listing, with accumulated net profits of at least RMB 10 million during these two years, or the issuer shall be profitable for the past year, and its operating income shall not be less than RMB 50 million in the latest year. On the SME board, the requirements are three years and profits of at least RMB 30 million.

The opening of ChiNext has had clearly positive effect on the development of China’s small and medium-sized enterprises (SMEs), which are often overlooked when it comes to domestic funding routes.

#### 4.6 Foreign Strategic Investments in Listed Companies

As per the Measures for the Administration of Foreign Strategic Investment to Listed Companies of December 31st, 2005, a foreign investor may, by way of subscribing to a private placement of A shares or entering in a share transfer agreement with shareholders, make a “strategic investment” in a listed company.

#### 4.7 Acquisition of Domestic Enterprises and FIEs

The Provisions on Acquisition of Domestic Enterprises by Foreign Investors which was latest revised on June 22, 2009 defined the approaches and procedures to acquire the equity or assets of domestic enterprises. All acquisitions are subject to review by the Ministry of Commerce (MOFCOM) or the competent branch thereof. The Provisions for the first time explicitly allow payments in the way of stock swaps.

If the acquisition reaches the threshold set forth in the Anti-Trust Law and in its implementation measures for anti-trust notification, it shall be submitted to MOFCOM for notification. MOFCOM may conduct an in-depth anti-trust scrutiny if it considers that there is a risk of eliminating or reducing competition by the acquisition. Besides, for an industry or brand that might involve national security, a national-security examination shall be gone through before the acquisition can proceed. Pursuant to the Provisions of the Ministry of Commerce on Imposing Additional Restrictive Conditions on the Concentration of Business Operators (for Trial Implementation), issued on December 4, 2014, MOFCOM may impose three types of restrictive conditions to reduce potential adverse impacts on competition:

- (1) Structural conditions requiring the disinvestment of tangible assets, intellectual property rights ("IPR") and other intangible assets, or relevant rights and interests, etc.;
- (2) Conditions requiring certain actions to be taken, such as open networks or platforms and other infrastructure, licensing key technologies (including patents, proprietary technologies or other IPRs), termination of exclusive agreements, etc.; and
- (3) Comprehensive conditions that combine structural conditions with conditions requiring actions to be taken.

#### 4.8 Future Tendencies

The state authorities constantly follow a policy of opening the capital market, though they maintain many restrictions considered to be crucial for a sound development in this area. A circular of the CSRC calls on domestic listed companies to reveal information actively which could be interesting for direct investment by FIEs in these companies. Listed companies are asked to create an account of their business activities that can attract attention of FIEs and promote a better mutual understanding. In doing so listed companies are supposed to regard especially the needs of small and middle sized investors.

China is currently continuing a share structure reform of state owned enterprises for the purpose of allowing shares to float on the market. But the state will hold a controlling position as a shareholder in enterprises considered to be of crucial interest for the national economic development.

Furthermore, a law released in 2005 regulates management buy-outs of small and middle sized current state owned enterprises. This law stipulates that managers of these enterprises shall stand a fair competition with private bidders. However, big state owned enterprises remain excluded from management buy-outs.

Note that the launch of the international board in Shanghai Stock Exchange, which would allow overseas companies to list in the A-share market, has been put aside and postponed temporarily. This international board is expected to attract big multinational companies and a return of 'red chips' to Shanghai - companies registered and listed overseas but controlled by Chinese entities.

#### 4.9 Governing Authorities

The China Securities Regulatory Commission (CSRC) is the dominating regulatory body over China's capital market. A draft for the 2nd revision of the securities law envisions to give more rights to the CSRC in order to supervise the capital market but also limits its power to guarantee a fair and lawful use of its rights. The amendments may be deliberated and approved by the end of 2016.

CSRC

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## **FOREIGN INVESTED BANKS**

### 5.1 Overview

Starting from December 11, 2006, foreign invested banks began to enjoy national treatment in offering their services in China. In November 2014, China published its updated Administrative Regulations for Foreign Invested Banks (“Regulations”) effective as of January 1, 2015, in order to further open access to the market by foreign banks.

Shortly after the establishment of the Shanghai Pilot Free Trade Zone (“FTZ”), the People’s Bank of China promulgated Opinions concerning the cross-border business of banks located in the FTZ. These new rules facilitate cross-border direct investment and expand the cross-border Use of RMB, etc. Various foreign banks have taken advantage of the facilitated access by opening branches in the FTZ.

### 5.2 Legal Forms of Foreign Invested Banks

The following choices are available for a foreign bank in establishing a business presence in China: (1) representative offices; (2) bank branch; (3) wholly foreign owned subsidiary banks; and 4) joint ventures with Chinese banks.

Previously, the presence of a representative office was the prerequisite for any foreign bank to apply for the opening of a branch or subsidiary, or entering into a joint venture with a Chinese bank. Also, a foreign bank was required to have operated a representative office in China for at least two years before setting up its first branch in China.

Since the revised Regulations have come into effect, the representative office is no longer required as a precondition to establish a foreign invested bank or branch.

Subsidiary banks may provide the full range of banking services like local banks. However, a foreign bank’s branch (unincorporated) is not allowed to offer RMB services to Chinese natural person customers - except receiving deposits each with a value of no less than RMB 1 million (roughly USD 160'000). The Capital requirements for a subsidiary bank are RMB 1 billion.

Another alternative is a joint venture with a local bank, which is usually implemented by acquiring shares in a Chinese bank; one of the advantages of such a strategy is that the existing networks of

the Chinese bank can be utilized. However, according to the 2015 Catalogue for the Guidance of Foreign Investment Industries, the shareholding allowed to be held by a foreign financial institution (including its affiliates) where it acts as a promoter or strategic investor in a Chinese-funded commercial bank is limited to 20%. The aggregate shareholding that could be held by several foreign financial institutions (as promoters or strategic investors) in a Chinese-funded commercial bank shall be subject to a ceiling of 25%. This is consistent with the Implementing Measures on Administrative Approvals for Chinese-invested Commercial Banks issued by the CSRC in 2013. In addition, only foreign banking financial institutions may invest in rural commercial banks. Joint ventures may provide the full range of banking services, including service to Chinese natural persons.

### 5.3 Approval Procedures

The establishment of any of the aforesaid business presences has to be first approved by CBRC, the supervisory authority over the banking sector in China.

A two-stage process is imposed by CBRC on any application for opening a bank branch and subsidiary banks in China. The Establishment Application shall be first filed and CBRC will decide whether it approves or not within 6 months. Upon physical establishment, the bank should file its Operation Application and CBRC will decide whether to give operation license or not within 2 months.

### 5.4 Governing Authorities

The China Banking Regulatory Commission (CBRC) is the dominating regulatory body over China's banking sector.

CBRC

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## FOREIGN EXCHANGE

### 6.1 Overview

PRC authorities removed most restrictions on foreign exchanges under current accounts in 1997 so that PRC individuals and enterprises can easily purchase and make payment in foreign currencies whenever necessary. However, restrictions under capital accounts remain to a large extent as they were.

Foreign investors, however, are treated somehow differently. The profits derived from their investments in China (i.e. FIEs), after due taxation, can be freely changed into foreign currencies and remitted abroad. Foreign currencies brought in by foreigners can either be kept by them or be sold to or deposited with designated banks.

Since 2005 the RMB is no longer pegged to the US Dollar but is free to float according to market supply and demand. From that time the People's Bank of China announces the closing price for each foreign currency traded against the RMB at the end of each working day. This price will be the central parity for trading on the following working day. Since March 17, 2014, the RMB is allowed to float to the US Dollar within a band of 2% around the central parity published by the People's Bank of China and shall be adjusted in relation to a basket of major foreign currencies.

## 6.2 Anti-money Laundering

The promulgation of the Law of the People's Republic of China on Anti-money Laundering indicates the government's stand to attack money laundering and safeguard its foreign exchange order. The definition of "money laundering" mentioned therein mainly includes money obtained by means of illegal drug trafficking, organized crime, terrorist crimes, smuggling, corruption, bribe taking, violating financial management regulations and financial fraud, etc. Thus this law has widened the definition of money-laundering considerably.

According to this law, all financial and non-financial institutions incorporated within the territory of China shall be responsible for establishing procedures and systems to attack money laundering. The Law also stipulates that information, such as commercial secrets gained from attacking money-laundering, shall only be used for legal investigation and litigation.

The China Anti-Money Laundering Monitoring & Analysis Center, with offices in Beijing, has been established as per the requirements of the Law, and the responsibilities of such center are to receive information and analyze suspicious trading and trades involving big amounts.

Where new financial institutions or new branches of existing financial institutions are established, an internal system of anti-money-laundering procedures and systems shall be established. Actual and effective identity information about clients has to be recorded.

## 6.3 Individual Foreign Exchange

As for individual foreign exchange, according to the Detailed Rules for Implementing the Measures for the Administration on Individual Foreign Exchange, each person may convert the total annual amount of USD 50,000 every year, and the State Administration of Foreign Exchanges (SAFE) may make adjustments on the total annual amount in light of the national payment balance.

Foreign exchange purchased by an individual may be remitted abroad, deposited into his or her foreign exchange savings accounts or carried out of the territory of China in line with the related provisions. Personal foreign exchange income and expenditure under the current account may be divided into business foreign exchange income and expenditure and non-business foreign exchange income and expenditure.

#### 6.4 Foreign Exchange Administration Regulations

The revised Foreign Exchange Administration Regulations of the People's Republic of China ("FX Regulations") promulgated in 2008. have removed the mandatory requirements for the transfer and settlement of foreign exchange. Under the FX Regulations, the foreign exchange income of a domestic institution or individual may be transferred back into China (either to be reserved in a foreign exchange account or sold to qualified financial institutions), or deposited overseas.

A distinct shift of supervision focus can be seen in the clauses on the new penalty imposed on illegal collection and settlement of foreign exchange. Unauthorized collection and settlement of foreign exchange (such as so called "hot money", i.e. money transferred into China without due approval or filing) is subject to the same penalty as unauthorized purchase of foreign exchange and remittance offshore: The fine is up to 30% of the amount of violation, in serious cases, a fine ranging from 30% to 100% thereof may be imposed. To verify the legality of such cross-border foreign exchange transactions, the supervision authority applies a test about the authenticity and lawfulness of underlying transactions. The new law also strengthens the control over the use of settled foreign exchange, which should be strictly in line with the purpose as approved by the foreign exchange administration authority or by a qualified financial institution.

The Regulations specify that in certain emergencies, such as a serious unbalance of international payments or an economic crisis, the government may take the necessary protection or control measures. In addition, the Regulations open a door for domestic financial institutions to provide commercial loans to off-shore entities.

On 13 February 2015, SAFE issued a Circular on Further Simplifying and Improving the Foreign Exchange Administration for Domestic and Overseas Direct Investment, which simplifies and improves the foreign exchange administration procedures for domestic and overseas direct investments, in particular by outsourcing certain tasks to banks. According to such Circular, the administrative approval procedure relating to foreign exchange registration was cancelled, the administrative procedures relating to equity purchases and capital contributions were simplified, and the annual inspection by SAFE has been replaced by a reporting system.

#### 6.5 Responsible Authority

The State Administration of Foreign Exchanges (SAFE) is responsible for the supervision and regulation of foreign exchange related affairs.

SAFE

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## **INTELLECTUAL PROPERTY RIGHTS**

### **7.1 Overview**

Foreign investors are often concerned about the protection of their intellectual property rights (IP rights) in China. The IP protection regime of China consists mainly of the Trademark Law, the Patent Law, the Copyright Law and the Unfair Competition Law. A set of implementation rules and legal interpretations have also been promulgated to strengthen the protection in this area.

### **7.2 Trademarks**

By virtue of a series of international conventions, of which China is a signing party, trademarks from the other signing parties of these conventions may be registered in China and by virtue of such registration enjoy the same protection as a trademark registered by a Chinese applicant. In addition, a foreign trademark applicant from a signing country of the Paris Convention has the priority right to file for trademark protection in the PRC within six months after its filing proper application in its home jurisdiction. A foreign trademark from a signing country of the Madrid Agreement or Protocol can extend the protection of its IP rights to China by means of an international registration in Geneva and a separate request of extension.

Except for the applications through the Madrid channel, applications for trademark registration by foreign entities must be made to the Trademark Office of the State Administration for Industry and Commerce (SAIC) through one of the officially designated trademark agents authorized to deal with PRC trade-mark application. A registration is valid for 10 years and may be renewed.

Trademark applications can be lodged for both goods and services. Trademark assignment shall be approved by, and license agreements shall be registered at, the Trademark Office of the respective SAIC.

Once the trademark has been registered, exclusive rights to use a registered trademark are limited to the approved registered trademark and the commodities for which the trademark is approved for use. There are certain circumstances regulated by the law deemed as infringement of exclusive rights; some may even constitute unfair competition. Trademark license contracts must be registered with the Trademark Office of the State Administration for Industry and Commerce ("CTMO"). A trademark license contract which has not be registered is legally valid, but it cannot be used to oppose third parties acting in good faith (e.g. in the case of an exclusive license).

China grants protection to well-known trademarks under particular conditions.

### 7.3 Patents

The third revision of the Patent Law of China became effective on October 1, 2009. This law brought many aspects of Chinese patent law further into line with current practice in major countries, and also reflects the need to build up an “innovative society”, by, for example, strengthening the standards for granting patents.

Patents in the PRC include invention patents, utility models and design patents. The Patent Law allows foreign applicants wanting to file a Chinese patent application to do so through any legally established patent agent firm, rather than having to file through a designated patent agent firm as was required under the former law.

Patent applications are governed by the first-to-file principle. Since China is a member of the Paris Convention, for an application for an invention or utility model patent filed in another country that is a member of the Convention within 12 months prior to the filing of an application in China, the prior filing date in the other country will be deemed to be the filing date in China. For design patents the prior application must be made within 6 months prior to the application in China to enjoy the priority.

For the inventions completed in China, a secrecy examination procedure shall be gone through before any patent filing is submitted to a foreign country (the requirement that the patent shall be filed in China first was abolished in the 3rd revision). Failure to go through the secrecy examination will cause the patent not to be granted in China.

The substantive standards for granting a patent in China are not significantly different from those in most western countries, being “novelty”, “inventive step”, and “practical applicability” (one of the most important changes made in the 3rd revision of the Patent Law is the raise of the standard for novelty from “relative novelty” to “absolute novelty”, including the prior publications in a foreign country into the scope of “prior art”, against which the novelty of the technology or design is judged).

The procedures for examining the applications for invention patents on the one hand, and those for utility model patents and designs on the other hand, are different. For the applications for invention patents, a substantive examination as to the qualification of the invention will be carried out. For the applications for utility model patents and design patents, only a formal procedure as to the completeness of the application documents is to be gone through.

The term of protection of patents for invention is twenty years, subject to an annual fee, whereas the terms of protection for utility models and designs is ten years. As patent law systems of other countries, the patents granted in China are also subject to certain limitations, including mainly fair use and compulsory license.

Patent-related contracts (e.g. license agreements) shall be registered at the respective Patent Offices within three months after its entering into force.

#### 7.4 Copyrights and Software

Work produced by foreign persons and which is published first in China is protected by copyright. If the work is first published outside China, copyright protection is granted only under bilateral or multilateral agreements.

Furthermore, and unlike Switzerland, copyrights can be registered in China and a corresponding certificate of copyrights can be obtained. The same applies to computer software. The advantage of such registration is that once a dispute arises or escalates into litigation, the registered copyrights and computer software are strong evidences for IP rights that could be effectively applied during the litigations. The revision of the Copyright Law in 2010, as the only substantive change made, established that the pledge of copyright may and shall be registered with the copyright administration department of the State Council.

For something to qualify as a “work” (capable of being protected by copyright) it must be an intellectual creation that can be reproduced in tangible form in domains of literature, art and science and it must have originality.

The term of protection for copyrights is usually the author's life plus fifty years.

If the author is a legal person, e.g. a company, or the original copyright is otherwise granted to a legal person, the term of protection is fifty years after the work is first published. Besides, if the work has not been published within fifty years after the completion of such work, the related copyright can no longer be protected by law.

Since May 2005, a liability of the net service providers for violation of copyrights by users has been stipulated by law. Owners of copyrights can claim providers to remove such content violating lawful rights of the owner. Providers who refuse to do so or know about unlawful content will be charged with fines. In January 2013, the Supreme People's Court further published interpretations to offer more detailed guidance to the courts how to assess net service provider's liability.

The responsible authority for copyrights related issues is the State Copyright Administration.

#### 7.5 Competent Authorities

Trademark Office of SAIC  
No. 8 Sanlihedonglu, Xicheng District,  
Beijing, 100820

Tel: +86 10 8865 0000

Web: [www.saic.gov.cn](http://www.saic.gov.cn)

National Copyright Administration  
No. 40 Xuanwumenwaidajie, Xuanwu District  
Beijing, 100052  
Web: [www.ncac.gov.cn](http://www.ncac.gov.cn)

State Intellectual Property Office (Patent)  
No. 6 Jimengqiao Xituchenglu, Haidian District, Beijing, 100088  
Tel: +86 10 6208 3114  
Web: [www.sipo.gov.cn](http://www.sipo.gov.cn)

## **LAND USE RIGHTS**

### **8.1 Overview**

In China, the ownership of land belongs to either the state or collectives (of farmers). The law prohibits the transfer of the ownership of land between individuals or entities, with the exception that the state may, in accordance with certain rules and procedures, expropriate collective-owned land (which again is subject to adequate compensation for the farmers).

However, the right to use land (Land Use Right or LUR) is transferable. Investors may acquire LURs either by applying for such right directly from the government (LUR Assignment) upon payment of assignment price, or purchase the right from a non-governmental entity (LUR Transfer). Both Assignment and Transfer are on a paid basis, which are the main and most usual way to acquire LURs. Free LURs are granted (LUR Allocation) in some exceptional cases, such as building of government offices, hospitals, military facilities and other infrastructure and public welfare facilities.

The term of Assignment LUR lasts from 40-70 years. The maximum terms of Assignment LUR for industrial land have a validity of 50 years.

Foreign individuals and organizations are basically allowed to purchase real estate in China. However, the procedure is still complex and many limitations exist, for instance the real estate must be used for the pre-determined purpose.

### **8.2 The State Policy to Tighten the Control over Land**

In August 2006, the State Council promulgated the Policy to Tighten the Control over Land. According to this policy, the assignment of all industrial purpose land must be subject to public sales such as bidding, auction or listing on LUR market. And the assignment price must not be below the "Bottom Price" of that in the specific area. This "Bottom Price" is fixed according to certain calculation formula.

The reiteration by the State Council of strengthening the administration of LUR assignment procedures and the implementation of local “Bottom Prices” indicates the central government’s determination to ensure that the LURs are assigned in an adequately paid way instead of in a de facto for free as quite a lot of local governments have been practicing.

#### 8.3 Land Use Tax

The Provisional Regulations of the People’s Republic of China on Land Use Tax in Cities and Towns (the “Regulations”) have been lastly revised and published on 7 December 2013. These Regulations are formulated to rationalize the use of land in cities and towns, to regulate the income differential on land, to improve efficiency of the land use and to strengthen management of land. Units (“danwei”) and individuals which use land within the boundaries of cities, counties, towns and industrial and mining districts shall be the obligatory tax payers for the land used within cities and towns and shall pay land use tax in accordance with provisions of these Regulations. The term of “Units” (“danwei”) herein shall also refer to foreign invested enterprises and foreign enterprises. The calculation of the land use tax shall be based on the actual area of land used by the taxpayer and shall be levied in accordance with the stipulated tax rate.

#### 8.4 The Classification of Land

According to the Circular of the Ministry of Land and Resources Regarding the Promulgation and Implementation of the State Criterion on Minimum Assignment Price of Industry Use Land, the land of the whole country has been classified into 15 categories, from Class I to Class XV, and the minimum assignment price of Class I land is RMB 840 per square meter, and the minimum assignment price of Class XV land is RMB 60 per square meter.

#### 8.5 Governing Authority

The related governing authority is the Ministry of Land and Resources.

Ministry of Land and Resources  
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Beijing, 100812  
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Web: <http://www.mlr.gov.cn>

### **LABOR & SOCIAL SECURITY**

#### 9.1 Labor Contract

The Chinese Labor Contract Law became effective on 1 January 2008 and was revised in 2012. According to this law, three types of labor contracts exist: labor contracts with a fixed period, labor contracts with an open period, and labor contracts for completing certain works. Any employer must

conclude a written labor contract with the employee within one month after the commencement of employment. Non-compliance with this requirement will lead to substantial punishment on the employer. If a labor contract is concluded with a period of more than three months but less than one year, the probation period thereof shall not be more than one month. Where the term of a labor contract is above one year but less than three years, the probation period thereof shall not exceed two months. With respect to a labor contract with a fixed period of above three years or with an open period, the probation term thereof shall not exceed six months.

If an employee dissolves the labor contract in violation of the law, or if he is in violation of relevant stipulations of the labor contract concerning the confidentiality obligation or limitation of competition, he or she shall bear liability if the employer suffers losses through these actions.

Employers in China can only terminate an employee under particular circumstances, for example if the employee has seriously violated labour discipline or rules and regulations of the employing unit or if the employee turns out to be incompetent for his or her position, even after he or she has undergone an additional education or has been transferred to a new position. Unless serious circumstances exist, the employer must pay to the employee a compensation calculated on the basis of his or her years of employment and average salary of the last 12 months (basically one month's salary for each year of employment, but maximum 12 salaries). In the case of employees with high income, the compensation is limited to a multiple of the local official average salary. If it turns out that the termination is not justified by the reasons stipulated in the law, the employer can be obligated to pay a double compensation. Thus, the termination of an employee must be approached with great caution in China (the sending of a warning letter in the case of violation of duties is a must).

Employees with whom an employer may agree on a (post-employment) non-competition obligation are limited to employees in a position of a senior manager, senior technician and a position which is otherwise reasonable to be subject to confidentiality obligation. The non-competition clause shall stipulate the geographical range, business fields involved, scope and time limit of the non-competition obligation. However, the maximum time a non-competition obligation can be agreed on is two years.

According to article 2 of the Labour Law of the PRC, a contractual labour relationship taking place in China shall be governed by Chinese law. Thus, the choice of a foreign law is not tolerated.

## 9.2 Representative Offices

The employment of PRC nationals by a representative office of foreign company must be arranged through a government-designated labor service company (such as FESCO). The rep office will enter into a service contract with the service company and the service company will provide PRC employees to work for the office. Thus, the representative office only has a contractual relationship with the service company and not with the PRC staff. A supplementary contract may, however, be

entered into by and between the foreign company and the PRC employee in order to regulate certain specific items such as salary amount, vacation, confidentiality, non-competition clauses and so on.

### 9.3 FIE Recruitment

In principle, FIEs may recruit any PRC individual directly without going through a service company. FIEs must conclude an individual labor contract with each employee.

### 9.4 Employment of Expatriate Staff

Every foreigner who plans to work in China is required to first obtain a Foreigner Work Permit Certificate, Work Visa, Work Certificate, and Residence Permit.

### 9.5 Welfare and Social Insurances

The mandatory social security to be subscribed for employees are (1) pension; (2) unemployment insurance; (3) medical insurance; (4) occupational insurance (5) birth insurance and (6) housing fund, which should be borne by both employer and employee respectively at a certain percentage. The contributions for these types of social security must be deducted and paid directly by the employer.

### 9.6 Labor Dispute Resolution

Labor disputes may be settled by mediation or labor-dispute arbitration, and may only be brought to the court after having gone through the labor-dispute arbitration. According to the Law on Labor Dispute Mediation and Arbitration, the statutory period to file an arbitration application in labor disputes is one year starting from the date the applying party actually became aware of or should have become aware of the fact that his or her right had been infringed, except for that the one-year period shall start from the dissolution of the employment relationship, if the dispute is concerning the default in payment of labor remuneration.

An arbitration award must be made within 45 days (could be extended to 60 days in certain circumstances) from the date of receipt of the application. Parties unsatisfied with the award may bring a lawsuit to a people's court within 15 days from the date of receipt of the written award.

### 9.7 Governing Authority

The related governing authority is the Ministry of Human Resources and Social Security.

Ministry of Human Resources and Social Security  
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Beijing, 100716  
Tel: +86 10 8420 1114  
Web: <http://www.mohrss.gov.cn>

## **PROPERTY RIGHTS**

In general, the alteration, transfer and extinguishment of the property rights of movables are subject to and take effect upon the delivery of the property; the change of property rights of immovable is subject to registration with relevant authorities to be effective. Natural resources owned by the state are not subject to registration. Property rights determined by court judgments etc. and the acquisition of property rights out of succession and factual conducts take effect from the time of the judgment, succession or conduct.

### **10.1 Ownership**

Three different types of ownership, namely: state ownership, collective ownership and private ownership exist. For specific properties, only the state can enjoy their ownership. Those properties include: some urban land, minerals, rivers, maritime areas, etc. Except for the object of ownership, the Property Law does not have differentiated protection for state ownership, collective ownership and private ownership. The Distinguishable Ownership of Building (also named as "Ownership of Apartment House"), neighborhood relation, joint ownership and special regulations about the acquisition of ownership are also provided for in the Property Law of the People's Republic of China.

### **10.2 Usufructuary Rights**

Usufructuary Rights govern the relation in the utilization of properties. The major types of usufructuary rights are: land use rights, water rights, exploration rights, mining rights, fishery rights, contracted land management rights, easements. Although the Law admits both movables and immovable as the object of usufructuary rights, all the explicitly established usufructuary rights are related to immovable property.

### **10.3 Property Rights for Security**

Four types of Real Rights for Security exist under Chinese Law, namely: mortgage, pledge, lien and guarantee. The object of mortgage can be either movables or immovables and the institution of a mortgage does not require the delivery of the property; the object of a pledge can be either a movable or certain types of rights (such as bills, bonds, equity interests, intellectual properties, receivables), and the institution of a pledge is subject to the delivery of the object or the corresponding pledge registration; the object of lien can only be movables, and the prior possession of the property by the lienor is indispensable for the right; and the guarantee is only provided by the third party to creditor for the debtor.

### **10.4 Possession**

The fact of possession, whether authorized or unauthorized, is offered protection by the Property Law. The possessor is entitled to remedies such as the right to claim the restitution of the property or the elimination of obstacle or danger to the property when his possession of the property is prevented in some way, and the right to claim for damages incurred by such prevention.

## 10.5 Purchase of Real Estate by Foreigners

Since issuance of new legislation in 2006, foreign individuals who work or study for more than one year in China as well as foreign institutions or companies who established a branch office or a representative office in China are allowed to purchase commercial or residential buildings (i.e. built by real estate development companies; this excludes self-built real estate), but for their own use only (rental is thus excluded). Purchase of real estate by foreigners are also subject to the regulations of the local government which may stipulate further restrictions.

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