



WANG JING & Co.
敬海律师事务所

FDI Guide

INVESTING IN CHINA

Determining and Implementing
Your China Investment Strategy



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1. STRUCTURING YOUR INVESTMENT

Foreign investors can choose one of a number of vehicles to enter the Chinese market. Their choice depends on a number of factors, but the most decisive are the intended activities in China, the commitment in terms of financial and other resources, and whether a partnership with a Chinese company is preferred.

(A) The Representative Office (RO)

If a foreign company wants a presence (e.g. to explore the market) but is wary of committing too much capital, an RO can be established quickly and at relatively low cost. The RO is a registered liaison office of the foreign company that can engage in a number of non-operational activities such as business liaison, market studies and product-sampling. It may not engage in commercial activities (i.e. the buying or selling of goods and services, which should be done directly between the foreign company and its Chinese counterparts), though it can have bank accounts to pay expenses, and can indirectly hire staff through a third-party staff services provider. Note that the RO is not a legal person, and therefore requires no capital commitment beyond cost and liabilities – which will be borne by the foreign company.

(B) The Wholly Foreign-owned Enterprise (WFOE)

The most common vehicle for foreign investment, the WFOE is a subsidiary fully owned and controlled by one or more foreign parties (companies or individuals), without involvement of any Chinese co-investors. It is a China-registered limited liability company, with rights and liabilities similar to Chinese companies. Liability is limited to the registered capital contributed by the investor(s) after the WFOE's business license has been issued (see below).

(C) The Chinese-Foreign Joint Venture (JV)

In the past, foreign investors often established joint ventures with existing Chinese companies either to fulfill requirements under Chinese law or to gain better access to the local market and resources. These can be in the form of an Equity Joint Venture (in which all rights and liabilities are proportioned as per the equity contributed) or a Contractual Joint Venture (in which all rights and liabilities are decided by contract). Similar to the WFOE, the JV is an independent legal person registered in China with limited liability, the only difference being that the JV has at least one Chinese investor (which must be a company).

(D) Branches, Subsidiaries and Liaison Offices

While some industries in the PRC (e.g. banking) allow foreign companies to establish branches directly, in most industries only a Chinese-registered company (WFOEs and JVs

are not allowed) can establish a branch office. Such branches may engage in the same activities as their head office, and may or may not be a legal person. They are relatively easy to establish, and mainly serve to expand a company's geographic coverage.

Chinese-registered companies may also invest in a subsidiary (which will be an independent legal person), or they may open a liaison office. The liaison office is a non-registered office with no legal capacity, and the head company remains fully responsible for all activities including payment, hiring of workers, etc.

2. **PREPARING FOR YOUR INVESTMENT**

After confirming the structure of the investment, a decision must be made on how the invested company is to operate. Issues that deserve particular consideration are the business scope, the registered capital, and the management structure.

(A) Business Scope Restrictions

A company in China may only engage in operational activities as per the business scope approved and/or registered with the competent authorities. Statutory penalties for operating outside the business scope can be severe; therefore considerable effort must be spent on determining exactly what business a newly-invested company will engage in. This will determine whether the company is a manufacturing company, a consulting company, a foreign-invested commercial enterprise (FICE), or foreign-invested real estate enterprise (FIRE). It also settles at what administrative level the company is approved (district, municipal, provincial or national; see below), whether any special licenses are required, and whether restrictions, special requirements or preferential policies may apply.

Different authorities may have different opinions on how general or specific a business scope should be worded, thus it is important to understand their attitude prior to finalizing the application.

(B) Capitalization of Chinese Operations

As ROs do not receive commercial income, they must be capitalized directly by the foreign company, which can remit funds to the ROs bank accounts from time to time to

cover expenses such as rent, salaries and disbursements.

WFOEs, JVs and their branches are capitalized with the investment contributed as registered capital after establishment. The amount, form, and timing of the investment is stated in the Articles of Association, must comply with national law and local policies, and shall be approved by the authorities. While Chinese law maintains certain statutory minimum amounts, companies should above all ensure that the investment is sufficient to capitalize the company's operations. If during operations the WFOE has insufficient capital, it may take out a loan, or increase its registered capital to allow for new non-commercial funds to enter China (see below).

While there are no legal limits to borrowing domestically (i.e. from Chinese institutions), foreign loans (including shareholder loans) are limited to the difference between the registered capital and the total investment, with the maximum total investment being proportionally fixed to the registered capital. Furthermore, to obtain a foreign loan, the foreign-invested company must complete relevant procedures with the State Administration for Foreign Exchange (SAFE).

(C) Decision-making and Management Structure

The RO should have an appointed Chief Representative with overall management responsibility. This Chief Representative may be a foreigner, and if he lives in China (which is compulsory only for certain industries) he can and should obtain a working permit and visa.

In the past, investors of WFOEs and JVs needed to appoint the members of a Board of Directors, which then became the highest organ of the company. Under the amended Company Law effective as of the 1st of January 2006, this remains so for JV's. However, the highest organ of a WFOE is the Shareholder's Meeting, which consists of non-appointed representatives of the shareholders. Under this Shareholder's Meeting, the investor may appoint members to a Board of Directors, or one Executive Director, who often acts as the company's legal representative. These may in their turn appoint senior management to run the company's day-to-day activities.

3. COMPLETING ESTABLISHMENT PROCEDURES

The establishment procedures for ROs are relatively simple, and mainly involve application letters and confirmation of the investor's status. The establishment of a branch is gradually being simplified as well.

For WFOEs and JVs the main documents that are necessary in establishment, besides various application and appointment letters, are the investor's business registration certificate (which in some cases needs to be notarized and legalized in the investor's country of origin), a credit certification by the investor's bank, the project's Feasibility Study Report and the invested company's intended Articles of Association (and Joint Venture Contract if a JV). Local authorities may have different requirements for the preparation of these documents.

Submission documents must be stamped and signed by the investor and its legal representative. Beyond this, the presence of the investor is not required, and an agent (such as a law firm) can complete the procedures for establishment of a WFOE or JV.

(A) Name pre-approval

The Chinese name of a company usually consists of the brand name, the place of investment, and the industry in which the company is operating. After a check of whether the suggested name is available and can be registered, the Administration of Industry and Commerce (AIC) at the municipal level (or sometimes at the provincial or national level) will give pre-approval, reserving the company's use of that name.

(B) BOFTEC Approval

For most projects, the first stage of approval involves the district and/or municipal level department of the Ministry of Commerce (MOFCOM), referred to as the Bureau's of Foreign Trade and Economic Cooperation (BOFTEC). After confirming the project's legal and commercial feasibility, and reviewing the required documents, the BOFTEC may issue its approval notice. For companies engaging in certain activities (most notably wholesale or retail trading), the application must then be submitted to the provincial level authority, the Department of Foreign Trade and Economic Cooperation (DOFTEC), while in some cases the MOFCOM will make the final decision on approval.

(C) Special approvals

For some large or sensitive projects, approval for the project must first be given by the National Development and Reform Commission (NDRC, either at district, municipal, provincial, or national level). For certain activities or industries, authorities for the environment, urban planning, quality supervision, and others, will need to be involved. Such approvals and licenses take time, and will influence the time needed to implement the project, so a careful mapping out of the required procedures will allow the investor to choose the most efficient strategy.

(D) Company registration

The registration authority for foreign-invested enterprises (as well as for RO's and branches) is the Administration for Industry and Commerce (AIC), either at municipal,

provincial or national level. The official establishment of the company, office, or branch is marked with the issuance of the Business License. The company's file will be kept by the competent AIC.

4. POST-REGISTRATION PROCEDURES

After the foreign-invested company has been officially established, a number of procedures need to be completed to make the company operational. These procedures are usually completed either by the same agent or by the invested company's employees. For certain items, such as the opening of the bank account, the invested company's legal representative must be present in China, though in some cases the bank can waive this requirement. The primary steps to make the company operational are the following:

- (i) Making stamps (for company, financial, contract, legal representative etc.)
- (ii) Registration with the Quality and Technology Supervision (QTS) department
- (iii) Registration with the State Administration for Foreign Exchange (SAFE)
- (iv) National and local taxation registration
- (v) Finance registration
- (vi) Registration as a Foreign Trade Operator (not required in some districts)
- (vii) Opening of bank accounts
- (viii) Registration with customs authorities

Many companies will want to apply for VAT general tax payer status, which can lessen the burden of value added tax. Normal procedures include an on-sight visit and interview with the invested company's legal representative.

After opening of the bank account, the investors can contribute some or all of their capital, and after such contribution has been verified by an accountant, the money can be used for operational purposes.

5. AMENDMENT OF REGISTRATIONS

As companies develop their business in China, and as China opens up more sectors to foreign investment, many more foreign-invested companies will need to amend their registrations to meet their changing business practices and future goals. If such an amendment involves a change to the company's Articles of Association, a company will

have to follow many of the same procedures as required when establishing a new company, including post-registration procedures.

Some of the most frequent amendments include:

- (i) Expansion of the business scope – e.g. to include trading activities, or the manufacturing of different products.
- (ii) Increase of registered capital – to ensure sufficient capitalization (either under the existing or an expanded business scope).
- (iii) Transfer of shares – e.g. when buying out the Chinese joint venture partner
- (iv) Change of address – following the company's relocation, either within or outside the same district / municipality
- (v) Resignation and appointment of members to the Board of Directors.

Some of these amendments may require a lot of time to complete, therefore advance planning is crucial.

WANG JING & Co.'s SCOPE OF SERVICES

This “FDI Guide: Investing in China” is designed to help you decide whether or not, and how to plan, implement and maintain your subsidiary, representative office or branch in China. However you are strongly advised to retain a law firm or consultancy, established in China with experience and a good reputation, to guide you through this process. Wang Jing & Co. offers Clients a full range of services relating to foreign direct investment in China, and has supported Clients from all over the world with strategic advice, the establishment of subsidiaries, and the amendment of registrations.

The specific advantages that Wang Jing & Co.'s FDI Department has to offer its Clients include:

- ◆ Extensive experience in establishing companies all over southern China, which operate across a broad variety of industries;
- ◆ Strong familiarity with the laws and procedures for establishment and amendment of WFOEs, JVs, Branches and ROs;
- ◆ Close relations and effective communication channels with competent authorities across the region;
- ◆ Standardized internal procedures to handle your project in an efficient, effective and transparent way;

Wang Jing & Co. may be retained to implement the whole project, from strategic advice up to issuance of the business license and completion of post-registration procedures, or to deal with only part of such a project in support of the investor's own employees or other advisors.

Wang Jing & Co.'s FDI Department is supported by the firm's lawyers specialized in other fields, such as general corporate and commercial transactions, employment, real estate, and intellectual property rights protection and enforcement.

Contact Details

If you wish to receive more information on foreign direct investment issues, please contact the following persons of Wang Jing & Co., FDI Department or your usual contact at Wang Jing & Co.

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