

# An Introduction to Doing Business in China



I. Establishing and Running a Business

II. Tax and Accounting

III. Human Resources and Payroll

## Preface

China is forging a new identity for itself beyond that of a manufacturing haven. With wage rates rising rapidly, other Southeast Asian countries are stepping up to fill the shoes of “world factory,” while China actively shapes its economic growth in a different direction.

The strategic economic goal-setting of the current 12th Five Year Plan (2011 through 2015) outlines several economic development initiatives, including:

- 51.5 percent urbanization by 2015
- Emerging strategic industries to reach value-added production of 8 percent of GDP
- More foreign investment in agriculture, high-tech and green industries
- Transition of coastal regions from manufacturing hubs to R&D, high-end manufacturing and services hubs

For foreign investors, these changes present great opportunities. With little to no growth in many western nations and the pull of Chinese domestic consumption, the profile of companies investing in China is indeed expanding. China is now experiencing a “second wave” of foreign investment – while the first wave was primarily from big multinationals, the second wave brings with it greater quantities of foreign investment from SMEs.

This publication is designed to introduce the fundamentals of investing in China. It is based on the knowledge of Dezan Shira & Associates, a specialist foreign direct investment practice, providing corporate establishment, business advisory, tax advisory and compliance, accounting, payroll, due diligence and financial review services to multinationals investing in emerging Asia.

Since its establishment in 1992, the firm has grown into one of Asia’s most versatile full-service consultancies with operational offices across China, Hong Kong, India, Singapore and Vietnam as well as liaison offices in Italy and the United States. Dezan Shira & Associates’ experienced business professionals are committed to improving the understanding and transparency of investing in emerging Asia.



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# Establishing and Running a Business



What are my options for investment?  
How do I establish a company?  
How do I make changes to my company?  
What do I need to keep in mind when doing business in China?

## What are my options for investment?

Foreign investment into the People's Republic of China (hereafter "China") can come in several foreign-invested entity (FIE) forms, and choosing the appropriate investment structure depends on a number of factors, including planned activities, industry, investment size, etc.

Here, we discuss:

- a. Representative Offices
- b. Wholly Foreign-Owned Enterprises
- c. Joint Ventures
- d. Other Investment Options

Key points that differentiate investment structures include:

- Business scope

Business scope is the one sentence description of the business activities in which a business will engage. The business scope must be approved early on in the establishment process, as the approved scope will appear on the business license. The business can only conduct the business activities in its business scope and any amendments to the business scope require further application and approval, and can be quite time consuming.

- Registered capital

Registered capital is the initial investment in the company that is required to fund the business operations until it is in a position to fund itself.

In practice, the official requirements for registered capital vary by industry and region. The absolute minimum capital requirements under Chinese law are RMB30,000 for multiple shareholder companies<sup>1</sup> and RMB100,000 for single shareholder companies.

Registered capital contributions can be made in cash or in kind, as a lump sum or in installments. Locally obtained RMB cannot be injected as registered capital - it must be sent in from the overseas investor. The payment schedule of the registered capital needs to be specified in the company's Articles of Association.

After the registered capital has been contributed, this amount cannot be wired

<sup>1</sup> RMB = Chinese currency, renminbi, US\$1 = RMB6.35 on May 30, 2012



*“Choosing an investment structure depends largely on your goals in China. For companies looking to target the Chinese consumer, the foreign-invested commercial enterprise (FICE) is rapidly increasing in popularity.”*

---

Richard Cant  
Regional Director  
Shanghai Office

out again freely. If a company wishes to expand its scope of business later on, there may be a requirement to increase the amount of registered capital.

In addition to the registered capital, a total investment figure also needs to be specified. The total investment quota is the total amount of funds planned to be contributed to the project over its lifespan. The difference between registered capital and total investment represents the debt of the investment and can be made up by loans from the investor or foreign banks.

Mandatory Total Investment – Registered Capital Ratios	
Total Investment (US\$)	Minimum Registered Capital
3 million or below	7/10 of total investment
Above 3 million and below 4.2 million	2.1 million
4.2 million to 10 million	1/2 of total investment
Above 10 million and below 12.5 million	5 million
12.5 million to 30 million	2/5 of total investment
Above 30 million and below 36 million	12 million
36 million or above	1/3 of total investment

- Legal personality liability

A company in China is an enterprise legal person. An enterprise legal person bears civil liability for the operational activities of its legal representatives and other staff. The company is liable for its debts to the extent of its entire property. The shareholders of a company with limited liability status assume liability towards the company to the extent of the capital contributions subscribed by them respectively.

In addition to the options discussed on the following pages, some investors choose to invest in China via mergers and acquisitions (M&A). Acquisition of equity and assets require approval from the local Ministry of Commerce and registration with the local Administrative Bureau of Industry of Commerce. Investors considering M&A should conduct thorough due diligence on their target companies (see chapter 2 for more information on this).

### ***a. Representative Offices***

A representative office (RO) is an attractive way for foreign investors to get a feel for the Chinese market, as it is the easiest type of foreign investment structure to set up and has no registered capital requirements. The defining characteristic of an RO is its limited business scope; an RO is generally forbidden from engaging in any profit-seeking activities and can only legally engage in:

- Market research, display and publicity activities that relate to company product or services; and
- Contact activities that relate to company product sales or service provision and domestic procurement and investment.

An RO has no legal personality, meaning it does not possess the capacity for civil rights and conduct, cannot independently assume civil liability, and is limited in its hiring ability. Local employees can only be hired through government HR agencies and no more than four foreign employees can be hired per RO.

### ***b. Wholly Foreign-Owned Enterprises***

A wholly foreign-owned enterprise (WFOE), the most commonly used foreign investment structure, is a limited liability company wholly owned by foreign investor(s).

Since China joined the World Trade Organization in 2001, WFOEs can do almost any type of business in China. The Foreign Investment Industrial Guidance Catalogue, the most recent version released in 2011, divides industries into three categories: encouraged, restricted and prohibited for foreign investment (industries not listed in the Catalogue are generally permitted). The catalogue also specifies industries in which foreign investment can only be done as part of a joint venture (described next).

A foreign-invested commercial enterprise (FICE), which can be set up either as a WFOE or a joint venture, is a type of company for retailing, franchising or distribution operations. A WFOE or JV can be established exclusively as a FICE, or can combine FICE activities with other business activities, such as manufacturing and services.

*A wholly foreign-owned enterprise (WFOE), the most commonly used foreign investment structure.*

### **c. Joint Ventures**

A joint venture (JV) is a company owned partially by foreign investor(s) and partially by Chinese investor(s). There are two types of JVs in China, which differ primarily in terms of the way in which profits and losses are distributed.

#### **1. Equity JV (EJV)**

- Profits and losses are distributed between parties in proportion to their respective equity interests in the EJV
- The foreign partner should hold at least 25 percent of the equity interest in the registered capital of the EJV
- Limited liability as a Chinese legal person

#### **2. Cooperative JV or Contractual JV (CJV)**

- Profits and losses are distributed between parties in accordance with the specific provisions in the CJV contract
- Can operate either as a limited liability company or as a non-legal person

*There are two types of JVs in China, which differ primarily in terms of the way in which profits and losses are distributed.*

### **d. Other Investment Options**

Two other foreign investment options worth mentioning are foreign-invested partnerships (general partnership or limited partnership) and, less common, foreign-invested joint stock companies (or foreign-invested companies limited by shares).

Foreign-invested partnerships, a relatively new type of structure, have some very real benefits not offered by WFOEs, including allowing for domestic and foreign ownership (both individual and corporate) at the same time, setup without registered capital verification, substantial tax savings (pass thru taxation) and the ability to hire foreigners. A disadvantage of this structure is the unlimited liability of the general partner, although this can be overcome by having the general partner as the foreign corporation that initially registers the partnership so that liability stops with the limited liability of the corporate parent.

Foreign-invested joint stock companies are similar to typical Western corporations. This structure offers the advantage of shared ownership by Chinese and foreigners, relative freedom to transfer stock of the company – unlike WFOEs – and even the ability to go public. However, the corporate governance of a foreign-invested joint stock company is more complicated and the initial registered capital requirement is quite high.



Common Purpose(s), Pros and Cons by FIE Structure Type				
FIE Structure Type		Common purpose(s)	Pros	Cons
Representative Office	RO	<ul style="list-style-type: none"> <li>• Market research</li> <li>• Liaise with home country companies</li> </ul>	<ul style="list-style-type: none"> <li>• Easiest foreign investment structure to set up</li> <li>• No registered capital requirement</li> <li>• Paves way for future investment</li> </ul>	<ul style="list-style-type: none"> <li>• Cannot invoice locally in RMB</li> <li>• Must recruit staff from local agency, no more than four foreign employees</li> </ul>
Wholly Foreign-owned Enterprise	WFOE	<ul style="list-style-type: none"> <li>• Manufacturing</li> <li>• Service provision</li> <li>• Trading (if a FICE)</li> </ul>	<ul style="list-style-type: none"> <li>• Greater freedom in business activities than RO</li> <li>• 100% ownership and management control</li> </ul>	<ul style="list-style-type: none"> <li>• Registered capital requirement</li> <li>• Lengthy establishment process</li> </ul>
Joint Venture	JV	<ul style="list-style-type: none"> <li>• Entering industries that by law require a local partner</li> <li>• Leveraging a partner's existing facilities, workforce, sales/distribution channels</li> </ul>	<ul style="list-style-type: none"> <li>• See common purpose(s)</li> </ul>	<ul style="list-style-type: none"> <li>• Split profits</li> <li>• Less management control than a WFOE</li> <li>• Technology transfer/IP risks</li> <li>• Inheriting partner liabilities</li> </ul>
Foreign-invested Partnerships	FIP	<ul style="list-style-type: none"> <li>• Investment vehicle</li> <li>• Service provision</li> </ul>	<ul style="list-style-type: none"> <li>• Allows for domestic and foreign ownership</li> <li>• Easier setup (does not require registered capital verification)</li> <li>• Substantial tax savings</li> </ul>	<ul style="list-style-type: none"> <li>• Unlimited liability of the general partner</li> <li>• Newness of structure (potential challenges with taxation or foreign currency exchanges)</li> </ul>



#### FOR MORE INFORMATION

**China Briefing website articles discuss foreign investment structures in detail**

[www.china-briefing.com](http://www.china-briefing.com)

## How do I establish a company?

When establishing a company in China, seek assistance to guide you through the complex setup process and to help you understand the roles and responsibilities of key positions. This can help set the company up for success and ensure that time-consuming future changes to the company are minimized.

Here, we'll discuss:

- a. Setup Process
- b. Key Positions in Foreign-invested Entities
- c. Intellectual Property

### *a. Setup Process*

Establishing a foreign investment structure in China generally takes between 3 and 6 months and generally involves the following government authorities:

- Ministry of Commerce
- Administration of Industry and Commerce
- State Administration of Foreign Exchange
- State Administration of Taxation
- Customs Office
- Quality and Technical Supervision Bureau
- Statistics Bureau

The establishment process varies based on the foreign investment structures and the planned business scope. For example, manufacturing WFOEs will require an environmental evaluation report, and WFOEs involved in trading will need to undergo customs/commodity inspection registration. Registered capital requirements also differ slightly, with service WFOEs officially requiring >RMB100,000 and FICEs generally requiring >RMB500,000 for value-added tax purposes.

Many companies choose to establish holding companies, or “special purpose vehicles,” in jurisdictions such as Hong Kong or Singapore to hold their Chinese entity. Holding companies allow for an additional layer of distance between the Chinese subsidiary and parent company, and can in certain ways “ring-fence” the investment, protecting it from the potential risks and liabilities of the Chinese subsidiary. In the case that an investor wishes to sell his or her Chinese business, or introduce a third party partner / shareholder into the structure, the administrative changes can also be done at the holding company level, rather than at the China

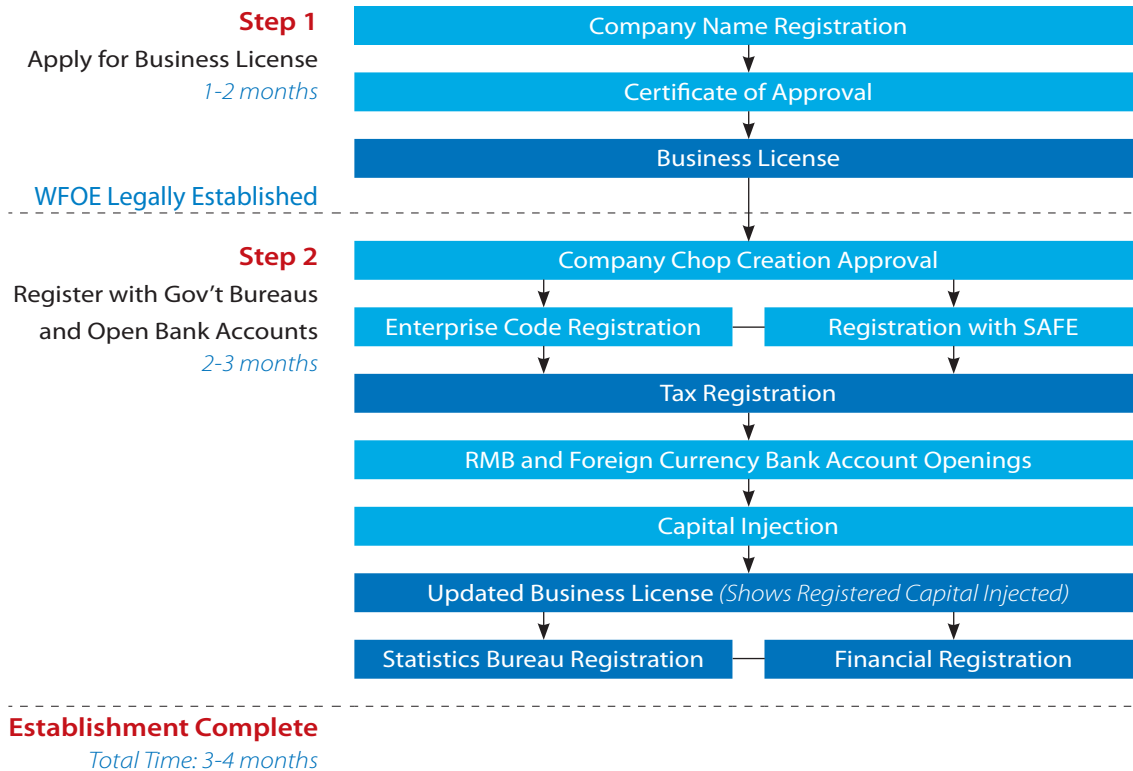


*“The legal representative is the person who really carries responsibility of the company and you need to appoint someone who is really competent. Not just technically competent, but China competent.”*

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Fabian Knopf  
Business Development  
Suzhou Office

## Establishing a WFOE



level where the regulatory environment is tougher and procedures more time-consuming.

Given that the banking and legal systems in both Hong Kong and Singapore are relatively stable and sophisticated, a holding company can also provide a good solution for foreign companies wishing to hold their China-earned profits offshore. In this way, the profits can be re-invested into China if the need arises, or used to further expand operations in Asia. Subject to the parent country's anti-avoidance tax rules, this method is often used as a tax deferral mechanism for foreign companies who do not want to remit their China profits immediately back to the home country.

In addition, Hong Kong and Singapore holding companies present a number of tax advantages, including reduced withholding tax rates on the repatriation of profits and limiting tax exposure on capital gains.



### FOR MORE INFORMATION

**China Briefing magazine**

*Hong Kong and Singapore Holding Companies*  
May issue, 2012

[www.asiabriefingmedia.com/bookstore](http://www.asiabriefingmedia.com/bookstore)

## b. Key Positions in Foreign-Invested Entities

The key positions in China foreign-invested entities vary by entity structure and size.

ROs should designate a chief representative to sign documents on behalf of the company. In addition to a chief representative, an RO can also nominate multiple general representatives.

For WFOEs and JVs, key positions include shareholders, executive director (or board of directors), supervisor(s), general manager and legal representative.

- Shareholders and executive director (or board of directors)

For a WFOE, the shareholder(s) are the highest authority of the company. In a WFOE, there can be an executive director or board of directors. The executive director (or board of directors) sets the agenda of the company's operations according to shareholder decisions.

For a JV, the board of directors is the highest authority. The board of directors should have no fewer than three directors appointed by the parties of the JV, with the ratio between Chinese and foreign-appointed directors determined through consultation between the two parties.

- Supervisor(s)

WFOEs and JVs must also have at least one supervisor to supervise the execution of company duties by the directors and senior management personnel. To ensure that there are no conflicts of interest, directors and senior management personnel cannot concurrently serve as supervisors. Where a company has a relatively small number of shareholders and is relatively small in scale, it can have one or two supervisors. For larger companies, a board of supervisors composed of no less than three members is required.

- General manager

Both WFOEs and JVs need a general manager who is responsible for day-to-day company operations. The executive director or a member of the board of directors can concurrently serve as the general manager. For JVs, several deputy general managers can also be appointed; this group is collectively referred to as the management office.

A director of the board can concurrently hold the post of general manager, deputy general manager, or any other senior management position, which also includes CFO, and any other personnel designated as such in the company's articles of association.

Legal Representative Candidates		
	WFOE	JV
Executive Director	✓	
Chairman of the Board of Directors	✓	✓
General Manager	✓	✓



- Legal representative

Every business established in China, foreign or domestic, is required to designate a legal representative, i.e. the responsible person who performs the duties and power on behalf of a company. The legal representative is, by definition of his or her role, one of the most powerful people in a foreign-invested entity. Yet this power comes with heavy responsibility and if a single individual in a foreign-invested entity is to be held accountable for company actions, that person is more likely than not the legal representative.

The people eligible to fill the role of legal representative vary by FIE type, as shown in the accompanying table.



#### FOR MORE INFORMATION

**China Briefing magazine**

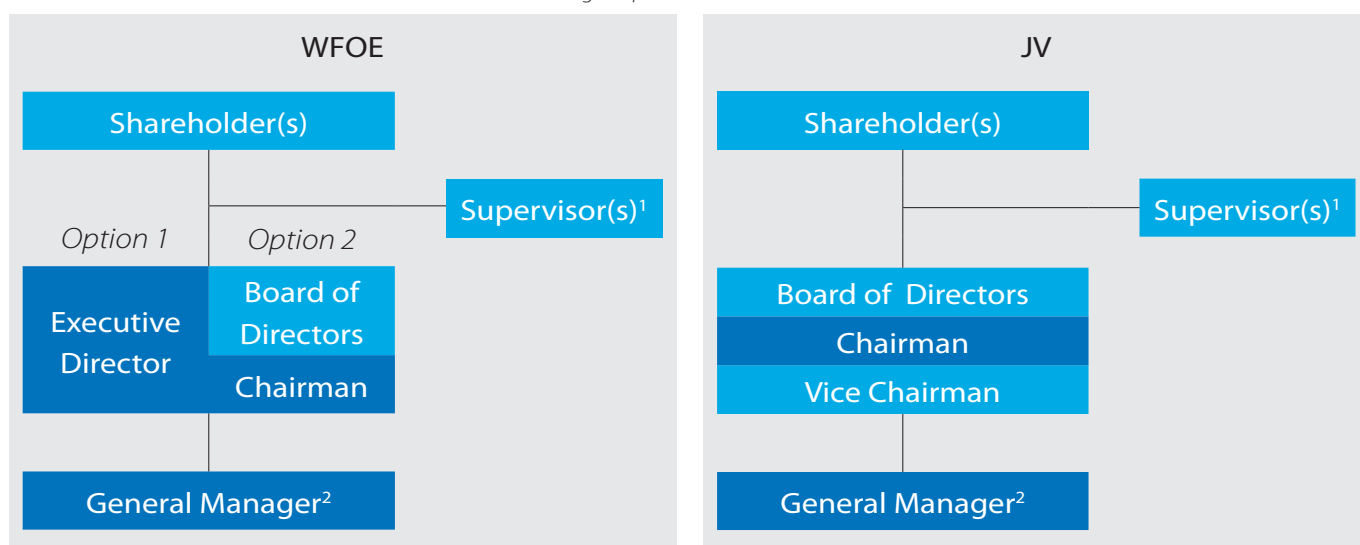
*The China Manager's Handbook*

*April issue, 2012*

[www.asiabriefingmedia.com/bookstore](http://www.asiabriefingmedia.com/bookstore)

## Key Positions in WFOEs and JVs

■ Legal representative candidate



<sup>1</sup> A supervisor or member of the board of supervisors cannot be director or senior management personnel. Larger companies require a board of supervisors composed of representatives of the shareholders and representatives of staff/workers.

<sup>2</sup> The general manager can also be a director or executive director. For JVs, in addition to the general manager, several deputy general managers can also be appointed, collectively referred to as a "management office."

### *c. Intellectual Property*

A lot of companies in China have graduated from a manufacturing focus to a model where their real business value is in their intellectual property. A company must register its patents and trademarks with the appropriate Chinese agencies and authorities for those rights to be enforceable in China.

- Copyrights  
Copyrighted works do not require registration for protection. Nonetheless, entities should consider registering their works with the National Copyright Administration, since this provides evidence of ownership.
- Patents  
Patents are territorial rights, meaning that a patent in another country has no effect in China. Companies should file applications for both their core and fringe technologies and make sure that their patents are properly translated. China follows a “first to file” system for patents, which means patents are granted to those that file first even if the filers are not the original inventors. A foreign patent application filed by a person or firm without a business office in China must be through an authorized patent agent. Patents are filed with China’s State Intellectual Property Office in Beijing.
- Trademarks  
China has a “first-to-register” system for trademarks, meaning that the first party to file for the registration of a particular trademark will be granted the rights of that trademark. Companies should register their brands’ English and Chinese names as well as their marks and/or logos with the Trademark Office, carefully choose the product categories and sub-categories in which to file, and check similar trademarks that have already been filed.

The International Classification of Goods and Services, which is also the standard in China, sets out 45 classes of goods and services. The owner must apply separately for registration in each class for which protection is sought. When registering a trademark in China, it is highly recommended to also register it in Chinese characters. A trademark application is filed with the Trademark Office of the State Administration for Industry and Commerce in Beijing. Any foreign person or foreign enterprise intending to apply for the registration of a trademark or for any other matter concerning a trademark in China needs to hire a trademark agency that is authorized by the state to act as an agent. A list of trademark agencies can be found at <http://www.saic.gov.cn/>.

*China has a “first-to register” system for trademarks, meaning that the first party to file for the registration of a particular trademark will be granted the rights of that trademark.*

## How do I make changes to my company?

Making changes to a Chinese entity after establishment – such as what the entity does and how or where it does it – can be challenging and time consuming, as can closing the entity all together.

Here, we'll discuss:

- a. Changing business scope
- b. Increasing registered capital
- c. RO-WFOE "conversion"
- d. Liquidation
- e. Relocation or expansion

### *a. Changing Business Scope*

Changing business scope is a time consuming process that involves working with most of the government authorities involved in the entity's setup. If such a change is approved, which it may not be, it will likely take at minimum two months.

Generally, when an enterprise intends to change its business scope, it has to submit an amended Articles of Association (or an amendment to the existing AOA) and Board Resolution (or Shareholder Resolution), among other documents, to the relevant approving authority. Following the issuance of the approval certificate to change the business scope, the changes have to be filed with the Administration for Industry and Commerce within 30 days. Subsequently, the company's tax certificate, financial certificate and foreign exchange registration certificate, etc. have to be changed.

If the new business scope diverges significantly from the original business of the company, the company name should be changed as well, since the company's name should generally reflect the main business of the company. The application for a new name should be undertaken with the local Administration for Industry and Commerce prior to applying for approval.



*“Setting your business up right from the start can save a lot of hassle in the long run. Any changes to your business are likely to take at least another 2-3 months.”*

---

Cory Lam  
Business Development  
Shanghai Office

### ***b. Increasing Registered Capital***

Similar to changing a company's business scope, increasing registered capital is a time consuming process that involves working with most of the government authorities involved in the entity's setup. An application to increase registered capital should be submitted to the original approval authority. Upon approval, an application to transfer funds into China should be made to the State Administration of Foreign Exchange. Following the fund transfer, a local CPA firm should be engaged to issue a capital verification report. The business license and other relevant certificates should also be updated to reflect the increased capital.

*While the steps for deregistering an RO are few, the difficulty of tax deregistration should not be underestimated.*

### ***c. RO-WFOE "Conversion"***

Deregistering an RO and establishing a new WFOE are two separate procedures that can be done in any sequence. As an RO is not a legal personality, the term "deregistration" is used instead of "liquidation," though the process is in many ways a liquidation. RO deregistration begins at the tax bureau (for which the RO must conduct an audit and clear tax liabilities) and proceeds to all other relevant authorities, which may vary by region. While the steps for deregistering an RO are few, the difficulty of tax deregistration should not be underestimated. ROs that have not fulfilled all previous tax obligations will run into particular difficulty in this regard. RO deregistration can take 6 months to more than two years, depending largely on the period of time required for deregistration at the tax bureau. The new WFOE can be established while the RO deregistration process is underway.

### ***d. Liquidation***

The procedures for closing a company can be more time-consuming and less predictable than setting up such a company. For example, the entire liquidation process for a WFOE normally takes between 12 to 14 months to complete.

Following approval for termination, the company should carry out liquidation procedures, including the establishment of a liquidation committee and completion of a liquidation audit report by a certified CPA firm. FIEs in China undergoing liquidation will need to deal with both outstanding tax liabilities and new tax liabilities that arise during liquidation. All foreign investors should anticipate an "exit tax" of some sort, be it an unpaid stamp tax or unpaid individual income tax for expats, both of which are very commonly found outstanding during tax audits.

Following liquidation procedures, the company should be deregistered with all relevant authorities (essentially those contacted during the setup process).



### ***e. Relocation or Expansion***

When possible, relocation should be avoided to prevent the loss of time and money. Relocating within a tax district is a relatively simple process, but cross-tax district relocations (transfers coordinated between governmental bureaus in two different districts) are significantly more involved, requiring several months for full completion.

The challenges in relocation are largely related to taxation, which is largely decentralized in China. Taxes are managed directly by the local tax bureau and transferring to a new tax district requires the foreign investor to actively coordinate between bureaus in both tax districts. These bureaus are often in competition with each other and no tax officer wants to lose your company's revenue by letting you relocate to another tax district.

If relocation is not possible, or to avoid interruptions in business operations, establishing an entirely new company and then closing the old company is a "default" option for relocation. Opening a branch office in the destination location is also a possibility. Branches are easier to set up and maintain, but limited in many ways, such as not being able to expand beyond their parent WFOE's business scope.



#### **FOR MORE INFORMATION**

**China Briefing magazine**

*Relocating or Expanding Your China Business*

*June issue, 2012*

[www.asiabriefingmedia.com/bookstore](http://www.asiabriefingmedia.com/bookstore)

Branch Office (BO)		
Common purpose(s)	Pros	Cons
<ul style="list-style-type: none"><li>• Geographic expansion</li><li>• Alternative to relocation</li></ul>	<ul style="list-style-type: none"><li>• Simple establishment</li><li>• No registered capital requirement</li><li>• Easy maintenance (only branches that wish to invoice must declare taxable items from locally produced invoices)</li></ul>	<ul style="list-style-type: none"><li>• Limited business scope (must be within that of the parent WFOE, cannot import or export)</li><li>• Not a legal entity (all liabilities are born by the parent company)</li></ul>



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## What do I need to keep in mind when doing business in China?

Day-to-day operations in China, often thousands of miles away from a foreign company's headquarters, are shielded by a thick language barrier, as well as a business culture that accepts less than transparent transactions and places little value on contracts. Widespread allegations of accounting, financial and operational irregularities/fraud against Chinese companies have recently received a lot of media attention, encouraging those conducting any business transactions with Chinese companies (including those with FIEs) to take a closer look at the way these companies are being run.

For those considering M&A or other investments in Chinese companies, thorough due diligence on target companies is in order. For those with Chinese FIEs, thorough due diligence on potential suppliers/distributors/other partners and effective, internal control systems with routine internal audits are the best tools for minimizing opportunities for fraud. Western approaches to due diligence and internal control often are not comprehensive in China – these processes must be tailored to the Chinese business context.

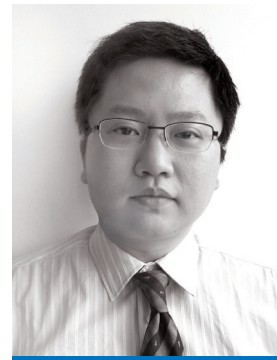
Here, we discuss:

- a. Due Diligence
- b. Internal Control and Audit

### *a. Due Diligence*

Broadly speaking, due diligence is a thorough review of a company so as to uncover any fraud, lack of compliance or other issues. Due diligence procedures, which can vary widely based on the intended business transaction and the industry of companies involved, are often split into legal, financial and operational due diligence. A due diligence checklist in China is generally quite similar to those used elsewhere, likely including a review of:

- Legal documents for company establishment and any additional government approvals and licenses
- Financial documents, including annual audits, tax returns, current financial statements and loans



*“We typically recommend one of two types of assurance to our clients: a ‘health check’ or a ‘full scope.’ In a health check, we run through a general internal control checklist and try to gauge whether an organization is under control risk.”*

---

Ronin Lin  
Manager, Audit  
Shanghai Office

- Documentation for real estate and land use rights (in China, the land is owned by the state, an individual can merely purchase land use rights)
- Documentation for intellectual property and hard assets
- Major contracts, distribution records, etc
- Litigation history and outstanding litigation (if any)
- HR administration documents

Due diligence can uncover a wide variety of issues, from a company completely misrepresenting itself to more minor accounting issues.

One of the key differentiating aspects of due diligence in China is the variety of issues commonly discovered in accounting books, from a company completely misrepresenting its financial situation to minor accounting errors that may come from a misguided actions to help the company (i.e. by avoiding tax) or lack of knowledge. Some very common points to pay attention to in financial due diligence investigations in China include:

- Two or more sets of financial accounts  
Many companies keep two or more sets of financial accounts so as to avoid tax, but this practice can also be used to cover up inappropriate financial behavior.
- Revenue received “off the books”  
Underreporting of accounts receivable is often used to hide sales and reduce taxable income.
- Employees paid “off the books”  
Employees are sometimes paid “off the books” so as to increase expenses and avoid paying taxes on labor salaries. This can result in high liabilities related to IIT and social security.
- Phantom assets and contracts  
The assets list on the books are often an overstatement or understatement of assets actually held. Assets are sometimes “mixed” with those of shareholders.

**Linked in.**

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*Discuss due diligence and other timely topics about doing business in China.*

## ***b. Internal Control and Audit***

Strong internal control systems and periodic internal control audits are essential to prevent fraud when running a company in China. Common types of fraud in China-based enterprises (including foreign-invested entities with less than adequate internal controls systems) that can be found across departments, include:

### Payroll

- Discrepancy between contract salary and payroll payments
- Deliberate over-accrual/unauthorized use of welfare benefits
- Ghost employees (non-existent employees, whose salary is often sent to the bank account of another employee)

### Supply Chain

- Purchasing of overpriced raw materials due to relationship/inappropriate agreement between staff and supplier
- Improper disposal of scrap
- Fake VAT invoices
- Poor inventory control

### Sales

- Sales of goods at/below cost due to relationship/inappropriate agreement between sales staff and purchaser
- Payment of unauthorized sales commissions to employees or friends
- Lack of competitive bidding process

A key aspect of the Chinese legal environment is the use of official company seals, or “chops,” to legally authorize documentation (often in place of a signature). This presents great opportunity for fraud, so chops should not all be held by one person and steps should be taken to ensure that chops are not misused. Depending on the business scope, a company may hold any number of chops, all for a different purpose and used on different types of official documentation, including company chop, financial chop, contract chop, customs chop, invoice chop, etc.

An internal audit ordered directly by company headquarters is the best way to evaluate the effectiveness of internal control systems and prevent fraud in a China-based entity. This is because an internal audit engaged by the China-based entity itself reports only to that entity, and if fraud is discovered at a local level, it may not be reported directly to company headquarters.



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# Tax and Accounting



What are China's major taxes?  
What are some of the key compliance requirements?

## What are China's major taxes?

Tax planning is a complicated matter as China levies different taxes at different tax rates depending on your location and your scope of business. When structuring your investment, detailed attention needs to be paid to turnover and income taxes.

Here, we discuss:

- a. Corporate income tax
- b. Business Tax
- c. Value-added Tax
- d. Withholding tax
- e. Other taxes
- f. Customs duties

### ***a. Corporate Income Tax***

The new Corporate Income Tax Law, which took effect in 2008, unified the tax rates for foreign and domestic enterprises. The income tax rate for all companies in China today, both foreign and domestic, is 25 percent.

Corporate income tax (CIT) is calculated against the net income in a financial year after deducting reasonable business costs and losses - in other words it is effectively a tax on profits. CIT is settled on an annual basis but is often paid quarterly with adjustments either refunded or carried forward to the next year. The final calculation is based on the year-end audit.

### ***b. Business Tax***

Business tax (BT) is a tax payable against turnover by all enterprises and individuals undertaking the following businesses:

- Providing taxable services, including communications, transport, construction, finance and insurance, telecommunications, culture, entertainment and service industries;
- Transferring intangible assets; and
- Selling real estate.

Rates of BT vary from 3-20 percent, depending on the industry. BT applies to services performed where either the service provider or the service recipient is located in China, without regard to where the service is actually being rendered. BT is usually calculated, filed and paid to the local tax bureau every month. As part of the current



*“Making changes to your business can be complex and time consuming, so it is strongly recommended to plan ahead and utilize the most tax efficient structure from the start.”*

Sisi Xu

Senior Manager, Corporate Accounting Services  
Shenzhen Office

Five Year Plan, VAT will replace BT, a transition that is already underway with VAT pilot programs (see below).

### **c. Value-Added Tax**

Enterprises and individuals engaged in the following are required to pay VAT:

- Sale of goods,
- Provision of processing, repairs and replacement services, and
- Import of goods in China

VAT taxpayers are divided into general taxpayers and small-scale taxpayers. Taxpayers with an annual sales value exceeding the annual sales threshold for small-scale taxpayers must apply to the tax department to be recognized as general taxpayers. The VAT rate for general taxpayers is generally 17 percent, or 13 percent for some goods. VAT payable relies on two figures: output VAT and input VAT. Output VAT is that payable on the services and goods sold by a company.

Input VAT is that payable on the goods and services a company buys from another supplier. The input VAT is used as a credit against the output tax levied on selling the goods. The VAT payable is the output VAT for the period, after deducting the input VAT for the period, i.e.  $\text{VAT payable} = \text{output VAT} - \text{input VAT}$ .

The current VAT rate for small scale taxpayers is 3 percent. Taxpayers cannot deduct input VAT, the formula is as follows:  $\text{VAT payable} = \text{sales value} * \text{tax rate}$  (i.e. 3 percent)

To resolve the issue of duplicate taxation on goods and services and support the development of the modern service industry, a pilot project has been launched to replace BT with VAT in the transport and certain modern service sectors. Shanghai was the first location to implement the pilot project in January 2012. It is expected to be expanded to Beijing in July 2012. Nine other cities and provinces have officially applied to participate in the VAT reform pilot scheme so far, including Chongqing, Shenzhen, Tianjin, Xiamen, as well as Anhui, Fujian, Hainan, Hunan and Jiangsu provinces.

Under Shanghai's current pilot scheme, VAT is applied at an 11 percent rate to transport services and at a 6 percent rate to modern services excluding tangible movable property leasing services.

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*Stay up to date on VAT Reform and other regulatory and legal updates.*

#### ***d. Withholding Tax***

Withholding tax is a PRC tax levied on passive income (i.e., dividends, bonuses, other equity investment gains, interests, rentals, royalties, transfer of property) received by non-resident enterprises from China. The withholding income tax rate is currently 10 percent. If a foreign party is a tax resident of a country or jurisdiction that has entered into a double tax treaty with China that includes reduced withholding tax, the foreign party can enjoy these reduced rates upon approval from the designated tax bureau. The China enterprise remitting the fund overseas should be the withholding agent.

*If the headquarters (HQ) is a tax resident of a country or jurisdiction that has entered into a double tax treaty with China, it is eligible to enjoy reduced withholding tax rates.*

#### ***e. Other Taxes***

Consumption tax applies whenever certain luxury or other goods are manufactured, processed or imported. Tax rates vary considerably depending on the product, for example, a rate of 36 percent is imposed against cigars, and 3 percent on motor vehicle tires. The tax paid is generally computed directly as a cost and cannot be refunded. If you are processing taxable goods for others, you are liable to withhold and pay consumption tax based on the value of the raw material and your processing fee. Consumption tax should be filed and paid monthly.

In addition, stamp taxes are levied on contracts with regard to purchases and sales, processing contracting, construction and engineering projects, asset leasing, transportation of goods, storage and warehousing, loans, asset insurance, technology contract, transfer of property rights, accounting ledger and royalty license. The tax rates vary between 0.005 percent and 0.1 percent.

#### ***f. Customs Duties***

Tariffs include import duty rates and export duty rates. Import duty rates fall into two categories - general tariff rates and preferential tariff rates. The general tariff rates apply to the imports originating in the countries with which China has not concluded "most favored nation" trade agreements, while the preferential tariff rates apply to imports originating in the countries with which China has concluded such agreements. Customs duties are computed either on an ad valorem basis (based on value) by applying an applicable rate, or on a quantity basis by applying an amount of duty per unit.



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## What are some of the key compliance requirements?

There are a number of legally mandated requirements with which FIEs in China must comply, failure of which will jeopardize the ability of the FIE to continue operating in China. The procedures and requirements may be different from what the FIEs are accustomed to in their home countries. Investors should therefore be sure to familiarize themselves with these requirements as well as seek professional advice

Here, we discuss:

- a. Accounting and bookkeeping
- b. Annual compliance
- c. Transfer pricing

### *a. Accounting and Bookkeeping*

China's current basic accounting standards, issued by the Ministry of Finance in 2006, are broadly in line with the International Financial Reporting Standards.

All FIEs in China are required to prepare annual financial statements, including balance sheets and income statements for their annual Chinese audit (conducted by a CPA registered in China). RMB is the base currency for ledgers and financial reports. For enterprises using currencies other than RMB in their business transactions, the foreign currency can be used as the bookkeeping base currency. However, the financial reports are required to be shown in RMB. Furthermore, accounting records have to be maintained in Chinese. FIEs can choose to use only Chinese or a combination of Chinese and a foreign language.

Enterprises in China should adopt the accrual basis of accounting in performing recognition, measurement and reporting for accounting purposes. FIEs, including their legally responsible persons, must take full responsibility for the truthfulness, legitimacy and completeness of financial statements. These statements will be used for computing the FIEs taxable and distributable profit. Books and records have to be retained for at least 15 years under Chinese law.

By law, any business transactions carried out in mainland China require a fapiao. More than just an official receipt with a distinctive red oval seal ("chop"), a fapiao is a tax invoice designed to ensure the government receives tax payment. A significant



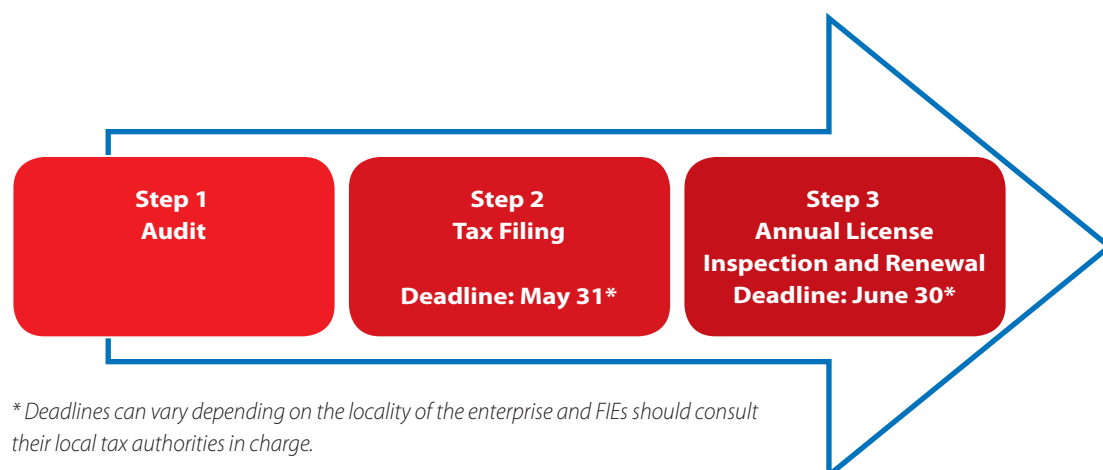
*“Many foreign companies are surprised to learn that for a Chinese entity to make foreign exchange payments, it must first obtain approval from the State Administration of Foreign Exchange.”*

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Jenny Zhang  
Manager, Corporate Accounting Services  
Shanghai Office

portion of small to medium-sized companies conduct certain sales under the table and remain reluctant to part with their fapiaos, since every sale that they make in which a fapiao is issued, tax will be payable on the profit from that transaction. This is the way the tax bureau ensures that taxpayers fulfill their tax obligations. For those purchasing goods and services, fapiaos are essential for claiming VAT refunds and lowering tax liability.

### ***b. Annual Compliance***



Prior to distributing and repatriating profits, FIEs must complete annual compliance, involving three steps: audit, tax filing and annual license inspection and renewal. These procedures are not only required by law, but are also a good opportunity to conduct an internal financial health check. Annual compliance procedures and key considerations vary slightly by region and entity type, with annual compliance for ROs different from those for JVs and WFOEs.

First, the audits required by the region in which the FIE is based should be conducted. These may include a financial audit, foreign exchange audit and tax verification audit. Second, all FIEs need to submit the annual taxation reporting package to the tax bureau by the end of May each year. This reporting package verifies all the taxes payable, including CIT, VAT, BT, consumption tax and other taxes on the basis of the audit result.

Should the audited tax figure be lower than the figure paid, the FIE would need to apply for a tax adjustment for the fiscal year in question. Should the audited tax figure be higher than the paid tax, the FIE will need to pay the balance due to the tax bureau upon submitting the report.

Following audit and tax filing is the annual license inspection and renewal, or “annual cooperative examination,” jointly conducted by all relevant government departments, including the local office of the Ministry of Commerce, the Finance Bureau, the Administration of Industry and Commerce, the Tax Bureau, Customs, the State Administration of Foreign Exchange and the Statistics Bureau to ensure that FIEs conduct business in compliance with legal requirements.

Third, following inspection, FIEs shall submit a signed annual cooperative examination report and other prescribed financial information, including the report, the audited financial statements and other materials (all signed and stamped), to the governing administrative body by the end of June.

Following the annual audit and completion of tax payment, a net profit figure can be derived. Your planning for declaration of dividends for repatriation and/or reinvestment of profits will depend on the current situation of your Chinese company and its parent company abroad. Repatriation of profits may be preferable if your organization requires the funds for re-investment abroad or to be returned to shareholders.

Not all profit can be repatriated or reinvested. A portion of the profit (at least 10 percent for WFOEs) must be placed in a reserve fund account. This is treated as part of owner’s equity on the balance sheet. This account is capped when the amount of reserve funds equals 50 percent of the registered capital of the company. In addition, the investor may choose to allocate some of the remainder to a staff bonus welfare fund or an expansion fund, although these are not mandatory for WFOEs.

The remaining net profit is available for redistribution. Following a resolution of the board of directors, an application form for the repatriation of funds can be submitted to the tax bureau to authorize the bank to disperse funds.

*Not all profit can be repatriated or reinvested. A portion of the profit (at least 10 percent for WFOEs) must be placed in a reserve fund account.*

### *c. Transfer Pricing*

Transfer pricing concerns the prices charged between associated enterprises established in different tax jurisdictions for their intercompany transactions. The transfer pricing regime in China is generally consistent with the OECD Guidelines and has developed rapidly over the past few years.

The relationship threshold for transfer pricing rules to apply between parties is low in China compared to other countries. China requires taxpayers to prepare and retain detailed transfer pricing documentation to support the arm's length nature of their related party transactions. All transactions between the HQ and WFOE should be conducted based on the arm's length principle, as the HQ and WFOE are related parties according to Chinese tax laws.

When filing annual tax returns, enterprises for which the annual amount of related party tangible goods transactions is below RMB200 million and the amount of related party intangible goods transactions is below RMB40 million should submit the "Enterprise Annual Reporting Forms for Related Party Transactions of the People's Republic of China" which includes nine forms: Related Parties, Related Party Transactions, Sales and Purchases, Services, Transfer of Intangible Assets, Transfer of Fixed Assets, Financing, Outbound Investment and Outbound Payments. These forms should be submitted in Chinese by the same deadline as annual tax returns, which is 31 May of the following year.

Enterprises exceeding this transaction threshold (except those that are covered by an advance pricing agreement or that have foreign shareholding below 50 percent and only transact with domestic related parties) should submit a contemporaneous transfer pricing documentation package.

The tax authorities can make transfer pricing adjustments and levy additional tax and penalties to include years when documentation may not have been strictly required. The limitation period is up to 10 years, and the interest and penalties will not be capable of correlative relief under any double tax treaties.

*Conduct all transactions between the HQ and WFOE based on the arm's length principle, as the HQ and WFOE are related parties according to Chinese tax laws.*



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# Human Resources and Payroll



How do I hire staff/workers?

What major legal obligations does a company have for its staff/workers?

## How do I hire staff/workers?

China's Labor Law is very protective of employee rights – as can be seen in strict stipulations on contract types, probation periods, termination and social insurance contributions (discussed in the next section).

Here, we discuss:

- a. Visas for Foreigners
- b. Contracts
- c. Compensation

### *a. Visas for Foreigners*

The two primary visas for business and work in China are the F visa and the Z visa.

The F visa is commonly referred to as a business visa. It is used by foreign business people who come to China on business but are not employed at a Chinese entity (either domestic or foreign-invested). In order to receive an F visa, the foreigner must be invited by a company that is established in mainland China.

There are several variations of the F visa. It can be single-entry, double-entry, or multiple-entry. The main inconvenience of an F visa is the maximum period of time the holder may spend inside China on any one visit. This period may be as short as one month or as long as six months, but it is hard to guarantee which kind of F visa the Chinese visa office may be prepared to issue to an individual.

The Z visa is usually referred to as a working visa. It is used by foreigners who are employed by a company that has been incorporated in China (either domestic or foreign-invested) to enter the country, after which the employee must submit a passport with a Z visa and a work permit to obtain a residence permit and legally work in China.

The residence permit allows the foreigner an unlimited number of trips into and out of China during the term, which is usually one year. The process for obtaining a residence permit can include special requirements of the candidate, such as a medical exam, and presenting evidence of two years prior work experience and a college degree. While in the past it was common for F visas to be converted into employment and residence permits, currently most cities require an applicant to obtain their Z Visa from their country of residence (their home nation or country where they possess legal residency).



*“Outsourcing payroll processing allows for greater transparency, efficiency, accuracy, confidentiality, and continuity, as well as cost savings and ensured compliance with all laws and regulations.”*

---

Helen Kong  
Corporate Accounting Services  
Dalian Office



## ***b. Contracts***

The vast majority of employees hired in the private sector in China are given fixed-term contracts. A fixed-term contract can be of any length of time (with the legally permissible probation period depending on length of time), but can only be renewed once; on the occasion of the second renewal the contract effectively becomes an open-term contract, which is very difficult to terminate. Other types of contracts include job contracts and part-time contracts, which can only be used in limited circumstances.

Dispatch of staff, or “secondment,” when the employer pays an employment agency to dispatch one of their own employees, is another hiring option. ROs do not have the ability to hire staff directly, so Chinese staff can be outsourced or can be “seconded” from an employment agency. The most commonly referenced term to describe secondment agencies is FESCO (Foreign Enterprise Service Company Organization), which is not actually a company but a generic term used by dozens of local HR companies around the country.

In addition to labor contracts, the employee handbook is a critical piece of documentation explaining the rules of the company and the degree of severity of various infringements. For it to be an effective tool for the company, employees should be asked to sign it to prove that they have received it.

## ***c. Compensation***

Historically cheap costs for China’s huge labor force are rising rapidly. Furthermore, the labor supply of certain types of workers, such as skilled labor in interior provinces, and worker retention are also major issues facing employers in China today.

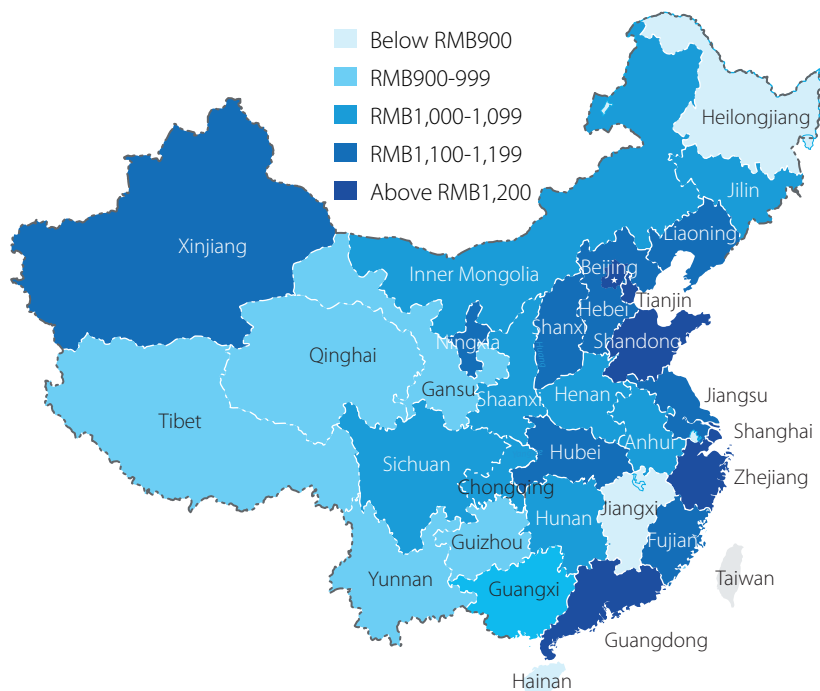
Minimum wages vary by province/municipality, city and district class. Shenzhen has the highest monthly minimum wage (RMB1500/month), while Beijing has the highest hourly minimum wage (RMB14/hour).

The standard work week in China is 40 hours and overtime payments in China can be quite steep – 150 percent of basic hourly salary for weekdays, 200 percent for weekends and 300 percent for public holidays under the standard work hour system. A comprehensive work hour system (in which working hours are calculated on a set period over which the average is approximately that of the standard work hour system) and a non-fixed work hour system are also available, but both require special government approval.

*As an annual bonus of sorts, many companies in China pay 13 months of salary, adding an extra month of salary around Chinese New Year (January/February).*

## Minimum Wages Across China

(Values based on current minimum wage levels within each provincial capital)



Source: China's Ministry of Human Resources and Social Security, [http://news.xinhuanet.com/politics/2012-04/27/c\\_123045244.htm](http://news.xinhuanet.com/politics/2012-04/27/c_123045244.htm)  
Accurate to April 25, 2012

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Discover the latest minimum wage increases and other practical business news in China.

As an annual bonus of sorts, many companies in China pay 13 months of salary, adding an extra month of salary around Chinese New Year (January/February). In addition, personal allowances, such as a monthly cell phone allowance, are common.

## What major legal obligations does a company have for its staff/workers?

Under Chinese law, a company is required to withhold and pay individual income tax (IIT) and make monthly contributions to social insurance funds on behalf of its employees. In addition, a company is required to hold an employee's personnel file and file employment/termination with government authorities. These are obligations that can be outsourced to a human resources administration services provider.

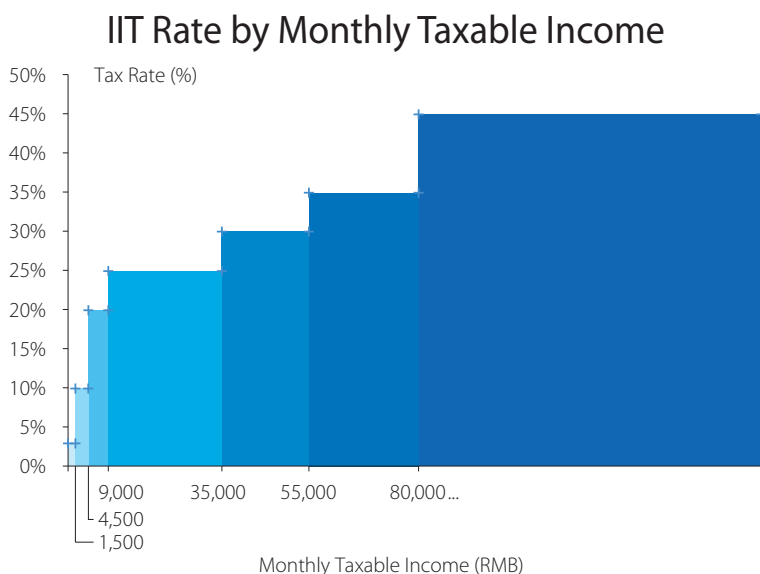
Here, we discuss:

- a. Withholding and paying individual income tax
- c. Contributing to social insurance funds

### *a. Withholding and Paying Individual Income Tax*

IIT is normally withheld by the employer from wages or salaries by employers and paid to the tax authorities on a monthly basis (within 15 days of the end of each month). At the end of the year, an annual IIT declaration should be submitted to tax authorities within three months of the end of the previous calendar year.

Income from wages and salaries is taxed according to progressive rates, ranging from 3 percent to 45 percent of monthly taxable income.



*“Most people are aware of the importance of an employment contract, but many foreign investors ignore the value of the employee handbook/confidentiality agreement.”*

Adam Livermore  
Manager, Payroll  
Dalian Office



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Monthly taxable income is calculated after a standard monthly deduction of RMB3,500 for local employees. For foreign individuals working in China (including residents of Hong Kong, Taiwan and Macau), the standard monthly deduction is RMB4,800. Money paid into Chinese social insurance can also be added to your pretax deduction.

Individual Income Tax Rates and Deductions		
Monthly Taxable Income (RMB)	Tax Rate	Deduction (RMB)
1,500 or less	3%	0
1,500 < TI ≤ 4,500	10%	105
4,500 < TI ≤ 9,000	20%	555
9,000 < TI ≤ 35,000	25%	1,005
35,000 < TI ≤ 55,000	30%	2,755
55,000 < TI ≤ 80,000	35%	5,505
> 80,000	45%	13,505

Tax Payable = Taxable Income x Applicable Tax Rate - Quick Calculation Deduction

Expatriates who are employed by a foreign-invested entity in China are liable for individual income tax (IIT) from the first day they arrive in China.

Annual IIT declarations should be filed for taxpayers who are subject to IIT in China and meet at least one of the following five conditions:

- 1) Have an annual income of more than RMB120,000
- 2) Derive income from two or more places inside the People's Republic of China
- 3) Derive income from sources outside the People's Republic of China
- 4) Received taxable income for which there is no withholding agent
- 5) Other conditions regulated by the State Council

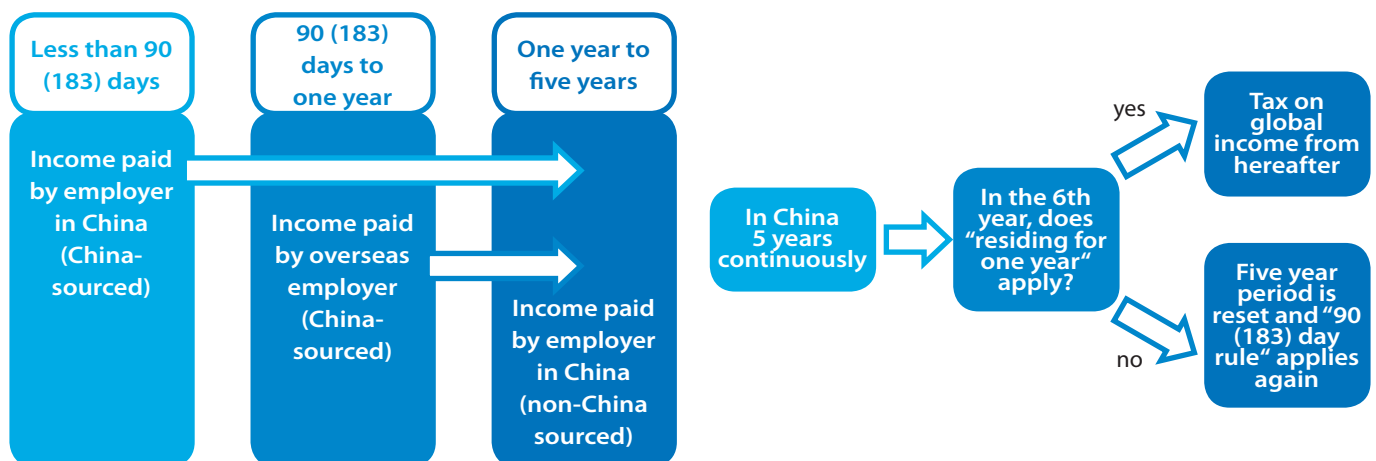
Annual income includes:

- Wages and salaries
- Income from individually-owned industrial and commercial households
- Income from subcontracting or subleasing
- Remuneration for labor services

- Author's remuneration
- Incomes from royalties
- Incomes from interests, stocks dividends and bonuses
- Incomes from lease, transfer of property
- Incidental incomes

If an individual is paid by a China-based entity, any income derived from working in China will be taxable. For non-China sourced income or income paid by overseas employers, tax liabilities for foreigners generally depend on the period of time an individual spends in China.

### China Residence and IIT Income Source Applicability Timeline



- Individuals who spend less than 90 days (or 183 days for residents of countries that have signed a double taxation treaty with China) in one calendar year in China are exempt from IIT if the employment income is paid by an overseas entity.
- Individuals who stay in China for more than 90 (183) days, but less than a year, are subject to personal income tax on their employment income derived from work performed in China – regardless of which entity is paying. (Residing in China for one calendar year means that, in a calendar year, temporary absences from China are less than 30 continuous days or 90 days altogether.)
- Individuals who reside in China for more than one year, but less than five years, are subject to personal income tax on both China-sourced and foreign-sourced income borne by a China-based entity. Foreign individuals who reside in China

for more than five years are taxed on their worldwide income.

- After an individual resides in China for five years, in the sixth year, if the individual resides in China for less than a year, the five year period is reset and the “90 (183) day rule” applies again.

## ***b. Contributing to Social Insurance Funds***

Social insurance (also called “social welfare” or “mandatory benefit”) payments are mandatory contributions to government-run funds made by both the employer and the employee (whose contribution the employer is responsible for withholding each month).

Social insurance contributions from the employee and employer can vary considerably depending on the city in which the contributions are being made. For a company that has employees based in a number of cities around the country, this means that the overall cost to the company for an employee earning RMB10,000 in one city may be quite different to someone on the same salary based in another city.

There are five social security funds:

1. Pension
2. Unemployment
3. Medical
4. Occupational injury
5. Maternity

In addition, there is a mandatory housing fund that is not strictly considered a type of social welfare. The housing fund is generally included within the scope of social security because the contributions are mandatory and come from both the employer and the employee, apart from some special areas where the employee does not need to make a contribution. When the employee purchases a house, the money in the housing fund can be used to pay the initial down-payment on the house, or to subsequently pay back the loan to the bank.

While employees must also contribute to several social insurance funds, the portion contributed by the employer is normally higher than the portion contributed by the employee. In fact, social security payments typically add an approximately additional cost of between 30 and 45 percent of an employee’s salary each month.

Mandatory contribution rates are stipulated by local governments and exact calculations of social security payments are quite complicated. Percentages are

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not technically based on the employee's monthly salary, but rather on a theoretical "base" salary calculated based on a given formula.

Social Security Fund Contributions		
Fund	Approximate Contribution (% of employee's monthly salary)	
	Employee	Employer
Pension	8% <sup>1</sup>	10-22% <sup>2</sup>
Unemployment	0.1-1%	0.2-2%
Medical	2% <sup>2</sup>	7-12% <sup>2</sup>
Occupational injury	N/A	0.4-3% <sup>3</sup>
Maternity	N/A	0-1%
Housing Fund	Normally matched with employer	7-13%
Total	10.1%+	24.6-53.0%

Source: Dezan Shira & Associates

<sup>1</sup> Uniform nationwide

<sup>2</sup> Much lower in some cities

<sup>3</sup> Also depends on the degree of danger during work

In late 2011, the government clarified that foreigners are included in the social insurance system at the same rates as Chinese citizens (housing fund aside), but implementation varies by region.

Given the complicated requirements for social insurance contributions, many companies choose to outsource their payroll processing and related human resources administration services. This ensures continuity (which can falter if an HR manager is absent or suddenly resigns), transparency and the confidentiality of salary information.



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## Further Resources

### *How does the hukou system impact employing Chinese workers?*

"A hukou refers to the system of residency permits which dates back to ancient China...Unlike in the earlier days, the hukou no longer formally restricts Chinese citizens from seeking employment outside their hukou region. However, the hukou determines a citizen's entitlement to social welfare and benefits, such as the housing fund and education. Therefore, somebody who works outside his hukou region will generally not be able to participate in the social benefits of the employment region."

*-Human Resources and Payroll in China Technical Guide*

### *Registered capital – how much is enough?*

"...Your registered capital is also your limited liability status. So the higher it is, the more creditworthy you are. But the real question for you is, what the Chinese authorities will consider as an adequate capitalization for a specific project? This will be analyzed case by case based on the Feasibility Study Report – and in the major FDI destinations they have done this many times, so they probably know what they are talking about (further inland, that may not always be the case).

Registered capital is also required to fund the business operations until it is in a position to fund itself...Often the happy foreign investor will naively assume he's got a great deal with a "minimum amount" being identified. However, the business can come to a shuddering halt if the registered capital amount is insufficient to support operational cash flow."

*-Establishing a Business in China Technical Guide*

### *Do non-resident enterprises have to pay corporate income tax (CIT) on their China-sourced income?*

"Non-resident enterprises with or without establishment or place in China, and those with income not effectively connected with such establishment or place, shall pay CIT on their China-sourced income.

...The income tax payable on such income derived by non-resident enterprises shall be withheld at source, and the payer shall be the withholding agent. The withholding agent shall withhold tax from the amount of each payment that is paid or that becomes due at the time of payment or at the time the payment falls due, which means that the withholding obligation arises when such income is remitted or when the payer accrues the amount as a cost or expense under the accrual method of accounting, and the China enterprise who remits the fund overseas shall be the withholding agent."

*-Tax, Accounting and Audit in China Technical Guide*



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