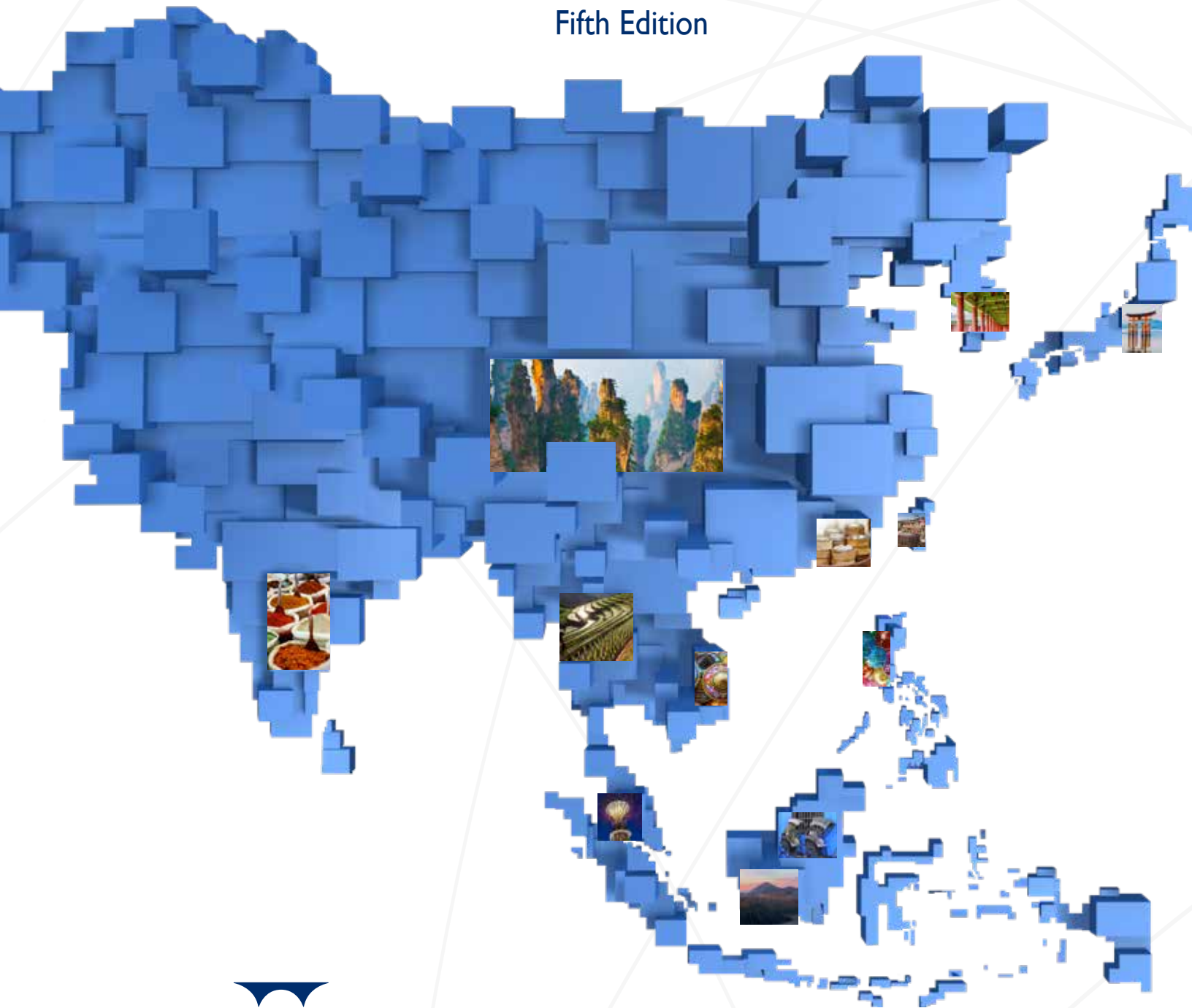


# ASIA

A Legal Guide for Business  
Investment and Expansion

Fifth Edition



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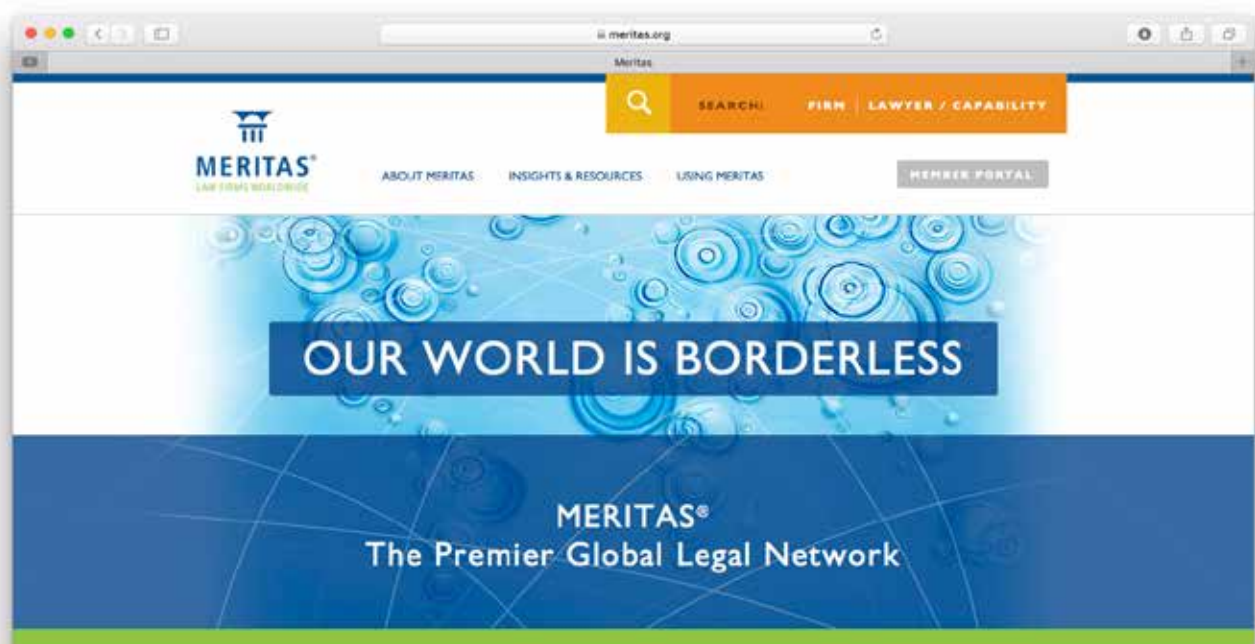
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## **1. What role will the government of China play in approving and regulating foreign direct investment?**

In the past, foreign investment in China was highly regulated. However, following China's entry into WTO in 2001, governmental approvals and regulations on foreign investments in many sectors have become more routine and less formal. A result of the development, the reform and the opening-up of China is the decision by the Chinese government to amend the laws and regulations aiming at reducing unnecessary administrative approvals and licenses. This improves the efficiency of regulation. The initial question for a foreign investor to ask is whether the proposed investment in a particular sector is permitted under Chinese laws. The Foreign Investment Industrial Guidance Catalogue (2017 version) issued by the National Development and Reform Commission (NDRC) and the Ministry of Commerce (MOC) lists the specific industries where foreign investment is encouraged or is otherwise subject to restrictive measures. The list of industries subject to restrictive measures (i.e., prohibited industries in which foreign investors are prohibited to invest and restricted industries in which restrictions on foreign ownership or management are imposed) is commonly known as the "negative list" for foreign investment (Negative List). For the investments in those restricted industries listed in the Negative List, foreign investors need to apply for the examination and approval of the MOC or its local counterparts. For the investments in the other industries, which are not in

the Negative List, an online filing with the MOC will suffice.

In case of investments in restricted industries, depending on the proposed amount of total investment in particular projects, the approval of the MOC or its local counterparts at the provincial or city level is necessary. In some cases, approvals from other PRC governmental authorities are required if the project falls into industries subject to administrative licensing requirements, such as tele-communications, insurance, and transportation. Similarly, if a proposed foreign investment project will involve investments in the infrastructure facilities, or add capacities to public facilities, or have possible harmful environmental impacts, then prior consent from NDRC and environmental protection bureau must be obtained.

To duly set up an enterprise in China, the investors are further required to file for formal registration with the appropriate Administration for Industry and Commerce (AIC) to obtain a business license.

## **2. Is it possible for foreign investors to conduct business in China without a local partner? What corporate structure is most commonly used and best for foreign investors?**

Except in those sectors where foreign ownership is subject to a cap, foreign investors may conduct business in China without a local partner. Certainly, if a foreign investor prefers, it may also set up a joint venture with a Chinese partner in a sector where no restriction on foreign ownership is imposed.

In most cases, foreign investors decide to establish in China a business structure known as a wholly foreign owned enterprise (WFOE). A WFOE is a legal entity that is 100% owned by the foreign investor. It is usually in the form of a limited liability company and can engage in a full range of business activities, from R&D, manufacturing, marketing and sales to distribution and services. The range of activities a WFOE can conduct is listed in its business license. Each WFOE must operate within its registered business scope.

To establish a WFOE in China, a number of registrations and filings with various government offices are required. Following is a summary of the application steps.

**Step One: Site selection.** The first step is to select an office location for the WFOE. It can be purchased or leased.

**Step Two: WFOE name preregistration.** Chinese law only requires that the Chinese name be registered, which is the official name of the WFOE. The company can have an English name if it so desires. In most cases, we recommend to also have a non-Chinese (English) name.

**Step Three: 1)** For investments in those restricted industries listed in the Negative List, apply for government approval with the MOC or its local counterparts at the provincial or city level. Once an approval is obtained, a certificate of approval will be issued. **2)** For investments in industries which are not in the Negative List, file the requested information through an online system regulated by the MOC. Once the filing is completed, a filing receipt will be

issued. Note that the MOC filing may be done prior to, parallel with or after Step Four below, depending on the practice of MOC and AIC in different localities.

Step Four: Register for the business license with the local AIC.

Step Five: Filings for business registration with the following government offices or institutions:

- Public Security Bureau (in some cities)
- Account Opening Bank
- MOC (for foreign trade registration) & Customs, if the WFOE intends to carry out import and export activities

Note that the Chinese Government has in recent years carried out “Five-in-One License” registration system reform, which has streamlined the registration process by integrating applications for five separate licenses (i.e. business license issued by AIC, tax registration certificate issued by Tax Bureau, social insurance registration certificate issued by Human Resources and Social Security Bureau, organization code registration certificate issued by Quality Supervision Bureau and statistics registration certificate issued by Statistics Bureau). In other words, a WFOE will have one business license issued by AIC with a uniform social credit code in lieu of the five separate licenses in the past. However, depending on the reform progress in different localities, a separate registration with those authorities may still be needed and in most cities the input of initial information with Tax Bureau is required upon the establishment of the WFOE.

As of the date this chapter is being written, the normal time required for completing the above registration/filing steps (it varies from city to city) upon the submission of qualified documents is one to three months, but it will take longer if MOC approval is required for investments in restricted industries.

### 3. How does the Chinese government regulate commercial joint ventures composed of foreign investors and local companies or individuals?

There are two types of Sino-foreign joint ventures in China: equity joint ventures (EJV) and contractual joint ventures (CJV). They are governed by a specific set of laws and regulations.

An EJV and a CJV are both considered as “foreign investment enterprises” (FIEs). The application procedure for both is the same. The major difference between the two types of joint ventures is how profits and losses are shared by the investors. In the case of an EJV, the profits and losses are shared strictly according to the registered capital subscribed and contributed by the investors; whereas in the case of a CJV, the profit and loss distribution ratio can be set up by the parties and does not have to match exactly with each party’s capital subscription. Further, in the case of a CJV, a foreign party can recover its investment ahead of its Chinese partners, subject to certain conditions and the approval by the competent government authorities. The form of EJV is more commonly seen and widely adopted if the invested industries are not open

to 100% foreign participation, or where the Chinese domestic partners can offer certain resources, which are essential to the business of EJVs. CJVs are often used if the invested industries (such as higher education, high school education and preschool education) are only open to foreign investments in the form of CJV. For both EJVs and CJVs, it is important for foreign investors to have well-drafted joint venture contracts and articles of association with proper and enforceable provisions on the powers and procedure of the management.

There has been movement toward acquisitions of local Chinese companies by foreign investors as a way to establish a joint venture with the local Chinese firms. The acquisition can be done either through a share acquisition or asset acquisition. In either case, foreign investors would need to file the acquisition with the competent MOC or obtain approval from the competent MOC, if the industry concerned falls into the Negative List. Other registration/filing procedures are quite similar to those for setting up a joint venture from scratch. In essence, the Chinese target company will be transformed from a wholly Chinese-owned entity to an FIE. However, pursuant to the Antimonopoly Law of China, before merger and acquisition of undertakings, antitrust review will be required when the proposed business concentration reaches the statutory thresholds.

Notably, if a joint venture is to be set up by way of “greenfield” establishment, the Chinese partner of the joint venture must be a legal entity.

#### 4. What specific laws will influence the commercial relationship between local agents/distributors and foreign companies?

Under Chinese law, the relationship between local agents/distributors and foreign companies is regulated by the Law of Contracts, General Provisions of the Civil Law and relevant interpretations. All the basic Chinese contract law principles, civil rights, and liabilities apply to an agency/distribution relationship.

In addition, if the agency involves distribution of regulated products (such as medicine and medical equipment or automobiles), special industry regulations will apply, which may require special permits or impose licensing restrictions.

Since foreign trade is government-controlled in China, when engaging a local agency, a foreign investor should first investigate if the agent has a trading license, namely whether the agent has the license to conduct international trade. If the agent or distributor does not have the trading license, it will not be permitted to sign international trade contracts directly with a foreign party and will not be able to handle import/export customs declarations, in which case a second agent who has such license will have to be engaged as an intermediary for the sales transactions.

A foreign company and its local agent/distributor are free to agree upon the termination events in their contracts. The Law of Contracts also gives the contracting parties a statutory right to rescind the contract under certain circumstances, e.g., in the event of major misunderstanding or obvious lacking of fairness. If a contract is terminated due to a party's breach, the counterparty, in most cases, will be entitled to claim economic compensation (normally limited to actual losses) or liquidated damages either by operation of law or based on the contract terms. The amount of or formula for calculating the liquidated damages should be agreed in the contracts in advance. It is notable that a court or arbitration tribunal may, upon request of either party and in its discretion, adjust the liquidated damages if the amount agreed is held to be significantly higher or lower than the amount of actual losses. Further, note that indirect losses, i.e., loss of anticipated profits which are reasonably foreseeable at the time of signing the contract, are supported under the Law of Contracts and foreign companies are advised to specifically exclude indirect losses in the contracts if they desire to limit their liabilities in this regard.

When terminating the business with its local agent/distributor, how to protect the business reputation of the foreign company in China, e.g. how to prevent the ex-agent/distributor from improperly acting under the brand name of the foreign company, would also be a matter of concern. A well-drafted contract with specific post-termination obligations is important.

#### 5. In what manner does the Chinese government regulate merger and acquisition activities by foreign investors? Are there any specific areas or industries that are heavily restricted or completely prohibited to foreign investors?

There are extensive regulations governing mergers and acquisitions by foreign investors in the key sectors of the Chinese economy. Foreign investment is restricted or prohibited in certain sectors, as specified in the Negative List and other market entry related regulations, including the national Market Access Negative List, which equally applies to both domestic and foreign investments. Below are some of the restricted and prohibited industries for foreign investors:

##### Prohibited Industries

- 1) Research, development, culturing and cultivation of valuable fine varieties rare in and unique to China and production of related propagation materials (including high-quality genes from the cultivation industry, the animal husbandry industry and the aquatic products industry).
- 2) Prospecting and mining of tungsten, molybdenum, tin, antimony and fluorspar.
- 3) Prospecting, mining and dressing of rare earths.
- 4) Prospecting, mining and dressing of radioactive minerals.

- 5) Application of techniques for the processing of soft lozenges of Chinese traditional medicines, such as steaming, parching, frying and calcining and the production of secret formulations of proprietary Chinese traditional medicines.
  - 6) Smelting and processing of radio-active minerals, and production of nuclear fuel.
  - 7) Manufacture of weapons and ammunition.
  - 8) Air traffic control.
  - 9) Postal service companies, and domestic express mail delivery.
  - 10) Wholesale and retail of tobacco, cigarettes, flue-cured tobacco leaves and other tobacco products.
  - 11) Social surveys.
  - 12) China legal affairs consulting (excluding the provision of information on the effect of the China legal environment).
  - 13) Development and application of human stem cell, gene diagnostic and treatment technologies.
  - 14) Mandatory education institutions.
  - 15) News agencies.
  - 16) Edition and Publication of books, newspapers and periodicals.
  - 17) Edition, Publication and production of audio and video products and electronic publications.
  - 18) Companies engaged in the production or operation of radio or television programs (inclusive of the introduction business).
  - 19) Film production companies, distribution companies and cinema chain companies.
  - 20) Internet news information services, online publishing services, network audio and video program services, venues providing internet access services, internet culture (except for music) business and internet public information release services.
  - 21) Gambling industry.
  - 22) Sex industry.
- Restricted Industries**
- 1) Selecting breeding of new varieties of agricultural crops and the production of seeds.
  - 2) Manufacture of vehicles, vessels and satellite television and radio ground receiving facilities.
  - 3) Construction and operation of power grid.
  - 4) Railway passenger transportation companies.
  - 5) Domestic water transportation companies.
  - 6) International maritime transportation companies.
  - 7) Specific value-added telecommunications services.
  - 8) Vessel agency.
  - 9) Construction and operation of petrol stations.
  - 10) Banks.
  - 11) Insurance companies.
  - 12) Securities companies.
  - 13) Futures companies.
  - 14) Market surveys.
  - 15) Education for higher education, high school and pre-school education.
  - 16) Medical institutions.
  - 17) Production of television and radio programs.
  - 18) Construction and operation of cinemas.
- If a target area of investment is restricted, approval on foreign investment from MOC must be obtained first before applying for the business license. If it is not restricted or prohibited, an online filing with the MOC (instead of the application for approval from the MOC) for the foreign investment needs to be completed. Further, if the foreign investor's market share reaches a certain threshold, antitrust review and approval by MOC will be required. With the growing number of multinational companies expanding business operations into China, antitrust has become an increasing concern for the Chinese government. The Antimonopoly Law of China and other relevant regulations are intended to maintain the free market economy and fair competition among all businesses in China. Such laws and regulations include the Antimonopoly Law, Foreign Trade Law, Price Law, Methods for Reviewing a Concentration of Undertakings, Methods for Filing a Concentration of Undertakings, and Thresholds for Prior Notification of Concentrations of Undertakings, among others.



With respect to proposed acquisitions of Chinese entities by foreign investors, antitrust reviews and approvals from MOC are required when certain thresholds are reached:

- The total worldwide turnover of all undertakings of the concentration exceeds rmb10 billion and the turnover in China of each of at least two undertakings exceeds rmb400 million; or
- The total turnover in China of all undertakings is above rmb2 billion and the turnover in China of each of at least two undertakings is above rmb400 million.
- Even if the above thresholds are not met, when the facts and evidence collected indicate that the market concentration may have an impact of excluding or limiting competition, an antitrust filing may then be required.
- When a foreign investor contributes to the concentration of a sector by merging and acquiring a domestic enterprise or by other means (which involves Chinese national security), the matter is subject to review with respect to national security exposure as required by state regulations which are in addition to the normal review on business concentration.
- If a proposed merger or acquisition is in a key economic sector, or involves the transfer or control of well-known Chinese trademarks, it may also be subject to government scrutiny.

Note, if the target of the proposed merger and acquisition includes state-owned assets, then the merger

and acquisition must be conducted through public procedures which require an asset or enterprise evaluation from an independent appraiser.

During the merger and acquisition, certain target sectors are subject to national security scrutiny, including military industrial enterprises and ancillary enterprises; enterprises located near key and sensitive military facilities and other enterprises related to national defense and security; and significant agriculture products, energy and resources, infrastructure, transportation, technology, equipment manufacturing enterprises related to national security, the control of which may be acquired by the foreign investors.

## 6. How do local labor statutes regulate the treatment of employees and expatriate workers?

The employment relationship is governed and protected by the Chinese Labor Law, the Labor Contract Law, as well as a series of state and local labor regulations in terms of social security, paid leave and so forth.

An employer is required to sign labor contracts with its employees. Failure by the employer to sign labor contracts may result in the employer being liable to pay double salary to the employee or to conclude an open-ended labor contract with the employee.

The labor practice of an employer must comply with all the applicable local and state regulations with respect to wages and benefits, working hours and working conditions,

confidentiality and non-compete, probation, duration and termination of employment, severance payment, etc. All such matters are to be addressed in the labor contract. If disputes arise between the employer and the local employees, labor arbitration will be sought first. If either party is unsatisfied with the result of the arbitration, a lawsuit can be initiated at the local court.

In the event of noncompliance with relevant labor laws and regulations, the employer may be demanded to rectify the noncompliance and to pay economic compensations to the employees concerned. For example, a wrongful termination may subject the employer to punitive damages amounting to twice of the standard severance pay or reinstatement of the employment, if so requested by the employee. In addition, employers may also be subject to administrative penalties (e.g., fines), imposed by the labor authority for violation of relevant labor laws and regulations. In more severe cases, employers who violate the Criminal Law, e.g., in forcing employees to work by restricting their personal freedom, will be charged with criminal offenses.

The hiring of expatriates is governed by a comprehensive set of regulations, including the Regulations on the Administration of Employment of Foreigners in China, which were first promulgated in 1996, revised in 2010 and 2017, respectively. The local employer must file for employment authorization with the local labor bureau. Once the employment authorization is obtained, a foreign

employee can apply for a work visa to come to China. After the employee lands in China, the employer will need to apply for a work permit for the employee. In addition, the employee will also need to register with the local public security bureau for a resident permit.

An expatriate who lives and works in China is subject to Chinese individual income taxation, regardless of whether his/her wages are paid by the employer in China or overseas. However, a bilateral tax treaty may exist between China and the expatriate's home country that provides for certain exemptions or exceptions. For example, an expatriate is exempt from Chinese taxation if a) his/her stay in China in a given year is less than 90 days in the aggregate, or b) his/her stay in a given tax year is less than 183 days in the aggregate and his/her salary is paid by the foreign employer and not charged to its affiliated Chinese entity.

### **7. What role do local banks and government agencies play in regulating the treatment and conversion of local currency, repatriation of funds overseas, letters of credit, and other basic financial transactions?**

Foreign exchange is a government-controlled area in China. The use or exchange of foreign currency is subject to strict foreign exchange control regulations. However, foreign exchange spending under current items is permissible upon documentary proof of certain usage, such as:

- To pay for imported goods
- To pay for services rendered by a foreign company
- To pay for wages of expatriates in China
- To pay for overseas business travel expenses
- To pay for foreign currency loans
- To pay for dividends to a foreign party

Note that payment of dividends to a foreign party is subject to fulfillment of certain conditions. For example, no dividends could be distributed before the previous years' losses of the company have been made up. Further, before the dividend distribution, FIEs shall allocate 10% of the after-tax profits as the statutory reserve fund, which will be capped at 50% of their registered capital. Also, the enterprise income tax on the dividends should be withheld on behalf of the foreign investors before the dividends may be paid. There is no difference to foreign investors from different jurisdictions in terms of foreign exchange policies, but foreign investors from certain countries/regions (e.g., Hong Kong) may enjoy a preferential withholding tax rate pursuant to the bilateral tax treaties between such countries/regions and China.

In China, once the registered capital is contributed and paid into the company, it cannot be withdrawn unless (a) the company is liquidated or (b) the company reduces its registered capital under certain circumstances and subject to certain conditions. As an exception, in the case of a CJV, the

foreign investor may recover its investment during the term of cooperation subject to fulfillment of certain conditions.

Since June 1, 2015, the State Administration of Foreign Exchange (SAFE) has delegated most of its power on foreign exchange registration and administration of foreign exchange payments in connection with inbound and outbound direct investments to the local banks. To initiate a foreign exchange banking transaction, certain documents must be submitted to the bank for approval. For instance, when applying for remittance of dividends of FIEs to foreign shareholders, the board resolutions and tax clearance certificate would be needed.

### **8. What types of taxes, duties, and levies should a foreign investor expect to encounter in negotiating an inbound investment in China?**

A foreign company doing business in China is subject to Chinese taxation, including the following:

#### **CORPORATE INCOME TAX**

Pursuant to the new Enterprise Income Tax Law, a uniform rate of 25% is applied on all companies, whether Chinese-owned or foreign-owned. However, preferential tax rates are provided to encourage sectors such as energy conservation and environmental protection, public utility infrastructure projects, agricultural and husbandry, and high-tech. Even if a foreign company does not have any permanent establishment in China, it is subject to Chinese taxation for any income derived from sources

within China. However, China has signed bilateral treaties with a number of countries/regions for avoidance of double taxation. If any inconsistency arises between the treaties and the Chinese Enterprise Income Tax Law, the treaties shall prevail.

### **VALUE-ADDED TAX (VAT)**

The standard VAT rate is 17% which is levied on the sale of most products. Also, VAT has been levied nationwide to replace business tax for certain services since August 2013 and for all services since May 2016. The standard VAT rate is 6% on the provision of most services. A rate of 11% is provided to certain special products (such as grains, books and periodicals, newspapers, and fertilizers) and certain services (such as transportation, postal, basic telecommunications and construction services, and leasing service of real property), as well as the sale of real property and land use rights.

### **CONSUMPTION TAX**

FIEs that manufacture, commission the processing of, import or sell taxable consumer goods such as cigarettes, spirits and alcohol, cosmetics, valuable jewelry, gems and jade, firecrackers and fireworks, refined petroleum products, motor vehicle tires, motorcycles, light motor vehicles, golf balls and equipment, high-end watches, yachts, disposable wooden chopsticks and wooden flooring shall pay consumption tax, which will be levied based on proportional rates ranging from 3% to 56% or a fixed amount tax or a combination of both.

### **STAMP TAX**

A stamp tax is levied on the execution of legal documents, ranging from 0.005% to 0.1% of the transaction value.

### **DEED TAX**

The transferee of any transfer of right or ownership to land and buildings shall be levied deed tax ranging from 3% to 5% of the transaction value, and a preferential rate of 1% to 2% may apply to qualified individual transferees.

In addition to the above taxes, a provincial surcharge in the range of 10% to 12% of the turnover taxes (VAT and Consumption Tax) is levied according to the applicable provincial regulations.

## **9. Do comprehensive intellectual property laws exist in China and do they provide the same levels of protection for foreign investors as local companies? Will local courts and tribunals enforce IP laws uniformly, regardless of the nationality of the parties?**

China's legal system for intellectual property protection consists of international treaties and domestic IP laws and regulations. China has promulgated a series of intellectual property protection laws and regulations, including Patent Law, Trademark Law, Copyright Law, Anti-Unfair Competition Law, Regulations on the Protection of Rights to Information Network Communication, and Regulations on Computer Software Protection. In addition, the competent authorities in China offer special protection for those well-known trademarks which

are familiar to the public in China no matter if such trademark is registered or not. Whether a trademark is a well-known trademark shall be recognized by either the Trademark Bureau or a competent court. The recognition of well-known trademarks adheres to the principles of recognition in individual cases and passive protection. It is also notable that China's Anti-unfair Competition Law provides some protection for unregistered trademarks, packaging, trade dress and trade secrets.

On the enforcement side, there are three special IP courts set up in Shanghai, Beijing and Guangzhou in 2014. Further, in January of 2017, the Supreme People's Court approved the establishment of several specialized IP tribunals as an internal department under the People's Court in certain other cities including Nanjing, Suzhou, Wuhan and Chengdu. A number of local courts have set up special IP sections that handle only IP cases. The Patent Bureau and Trademark Bureau also handle petitions concerning claims for illegal or improper registration of patents and trademarks. Further, the local AIC also conducts investigations and "raids" to confiscate counterfeit goods or to shut down illegal operations.

IP infringement has been a big concern for many foreign investors. As a precautionary step, registrations for trademarks, patents, and domain names should be filed. In addition, noncompetition and nondisclosure agreements should also be signed with the local suppliers, customers, agents, and employees, as appropriate.

## **10. If a commercial dispute arises, given the choice between local courts or an international arbitration venue, which would offer a more beneficial forum for fair dispute resolution for foreign investors?**

In the case of a dispute, the parties can initiate a lawsuit with the local Chinese court or pursue arbitration if the parties agree to arbitrate. Litigation at a local Chinese court can be time-consuming and possibly affected by local influence. The trial can take a few months to several years to complete. There will be one level of appeal after each trial. In comparison, arbitration usually takes much less time, and it is final and non-appealable. As such, arbitration has been favored by many foreign investors as a more desirable way for resolving foreign commercial disputes. The most prestigious Chinese arbitration commission that handles foreign commercial disputes is the China International Economic and Trade Arbitration Commission (CIETAC) which is headquartered in Beijing. CIETAC has a list of arbitrators for the parties to choose from, including those from foreign countries. The parties can also specify that the arbitration proceeding be conducted in a foreign language. In 2013, Shanghai International Economic and Trade

Arbitration Commission, also named as Shanghai International Arbitration Center (SHIAC), was separated from CIETAC. Hence, parties intending to choose SHIAC should make specific reference to its new name rather than using the previous CIETAC Shanghai Branch.

In addition to arbitration in Mainland China, the parties can also choose arbitration in a foreign country or in the special regions of China, e.g. Hong Kong Special Administrative Region, Macau Special Administrative Region. China is a member of the 1958 UN Convention on Recognition and Enforcement of Foreign Arbitral Awards and as such, an arbitration award issued in a member country (e.g. U.S.A., U.K., Singapore, etc.) can be enforced in China. Pursuant to the Arrangements of the Supreme People's Court on the Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong Special Administrative Region and the Arrangement between the Mainland and the Macau Special Administrative Region on Reciprocal Recognition and Enforcement of Arbitration Awards, an arbitration award issued in Hong Kong or Macau is also enforceable in Mainland China. Hong Kong International Arbitration Centre and Singapore International Arbitration Centre are popular choices of foreign investors in their dealings with Chinese partners. To enforce a foreign arbitration award, a petition must be filed with the local Chinese court having jurisdiction.

## **11. What recommendations can you offer for how best to negotiate and conduct business in China?**

### **KNOW WHO YOU ARE DEALING WITH.**

China is a vast country with many diverse elements and aspects. Corporate China is the same. As a foreign investor, get to know your Chinese business partners or counterparts before you start serious negotiations with them. For example, whether you are dealing with a Chinese state-owned enterprise (SOE) or a western-style Chinese entrepreneur, there will be differences. The same is true if you are dealing with a Chinese company located in a rural area where you may expect huge language difficulties that you would not have with a Chinese company located in the coastal area.

### **BE BETTER INFORMED THAN YOUR RIVALS AND YOUR PARTNERS.**

Although Chinese companies have made great achievements over the last two decades, the management of Chinese companies is not always as professional as you might expect. If you rely on the recommendations and advice from your Chinese business partners too much, it can be risky.

### **GUANXI IS NOT EVERYTHING.**

Guanxi is probably the most widely publicized Chinese term in the business world. Many Chinese business people build up their business entirely

on Guanxi (connections) that they have, especially in less urban regions of China. With the development of the Chinese economy and the increasing complexity of Chinese law, Guanxi becomes less important in China nowadays. In the coastal areas of China, business and transactions are done more and more in a straightforward way, and Guanxi now seems another name for a sound public relationship and mutual respect and trust based on long-term cooperation and assistance. Therefore, do not rely on any Guanxi that is easily offered.

## **12. What practical advice can you share with investors who decide to do business in China?**

### **LAWS AND REGULATIONS CHANGE FREQUENTLY.**

The Chinese government is constantly active at all levels. Laws and regulations change frequently. For example, it is common for administrative divisions to change the implementation of a particular law or state regulations by introducing new administrative decrees or provisions such as in the areas of foreign exchange control, taxes, and foreign direct investments.

Therefore, it is advisable to structure a deal as simply as possible. In the past few years, we have seen many sophisticated deal structures for mergers and acquisitions of Chinese companies fail because of unexpected changes in laws and regulations.

### **DO NOT UNDERESTIMATE THE IMPORTANCE OF GOOD DOCUMENTATION.**

China's procedural laws place great importance on written contracts and documents and there are no depositions of evidence under Chinese law. The arbitration or litigation courts in China rely heavily on written evidence because judges and arbitrators tend to base their judgments purely on the written evidence they are asked to examine. Also, the appeal courts in China only have desk reviews on appeal documents in most cases. Therefore, if a party does not have a working and reliable filing system, it may easily lose a lawsuit or an arbitration case in China.

### **PAY HIGH ATTENTION TO COMPLIANCE RISKS.**

The Chinese government is trying to reform its legal system by more stringently implementing legal requirements, particularly in the areas of anti-corruption, anti-monopoly and environment protection. Some noncompliance activities are no longer tolerated by the authorities, even though in the past these non-compliances rarely turned into real problems. After several market-stunning investigations initiated by the central government, it is observed that the current Chinese leadership is redefining the importance of legal compliance. A foreign investor must pay high attention to identify any noncompliance in its China operations

and assess the associated legal risks, rather than choosing to "ignore" it only because in the past similar noncompliance practice broadly existed in China.

### **PAY ATTENTION TO THE ENVIRONMENTAL ISSUES.**

The Chinese government is making an increasing effort to resolve the environmental problem such as environment pollution, climate changes and fog and haze. Such efforts include revision and promulgation of the Environmental Protection Law (effective as of January 1, 2015) and relevant laws, regulations and policies; establishment of carbon-trade mechanism and market; and reforming and strengthening the enforcement of environmental appraisal regime for construction project. The new Environmental Protection Law imposes heavier legal consequences for the violation of the law and provides for the public interest litigation against the environmental pollution, ecological destruction, which harm public interest. Therefore, for foreign investors to be engaged in industries with large amounts of carbon emission or hazardous substances or in infrastructural facilities construction projects, high attention should be paid to environmental issues as the Chinese government appears to have a real commitment to environmental pollution control.

### 13. Does China currently have any data privacy laws or regulations? How do they affect business activities?

In China, laws protecting personal data privacy mainly include the Cybersecurity Law, the General Rules on the Civil Law, the Consumer Rights Protection Law and the Criminal Law.

The competent regulatory authorities have also promulgated such lower-level regulations as the Provisions on Protecting the Personal Information of Telecommunications and Internet Users. To provide practical rules for data privacy protection, the Chinese government is contemplating a series of regulations and rules, such as those relating to the security assessment of personal information and important data to be transmitted overseas.

The mentioned laws and regulations will primarily affect the following aspects:

- (1) **Collection and Use of Personal Data.** In the course of business activities and employee management, business undertakings may need to collect and use personal data, such as name, birth date, ID number, address, phone number, credit card and password. When collecting and using such personal data, the undertakings shall comply with the principles of legality, justification and necessity.

For this purpose, the undertakings need to obtain the consent of those from whom the data is collected in advance.

- (2) **Protection of Collected Personal Data.** The undertakings are required to take technical and other necessary measures to ensure the security of the collected personal data and prevent it from being divulged, damaged, lost or tampered with.
- (3) **Storage and Transfer of Personal Data.** This should be a big concern for many foreign investors. According to the Cybersecurity Law and other related laws and regulations, certain information, such as the following, is required to be stored within China:
  - (a) personal information and important data collected or generated in Critical Information Infrastructure;
  - (b) information involving state secrets;
  - (c) personal financial information like credit data collected by banking institutions; and
  - (d) map and car-hailing data.
 With respect to the personal data in the Critical Information Infrastructure, where necessary such data may be transferred outside of China; but the precondition is that a security assessment has been passed in advance. However, relevant implementation rules have not come out yet and it remains to be seen how Critical Information Infrastructure is defined and the security assessment works.

### 14. Are there any recently passed laws or regulations in China that are expected to affect the activities of foreign investors in the future?

**Foreign Investment Industrial Guidance Catalogue (2017 version), amended on June 28, 2017 and effective since July 28, 2017.**

This is the seventh edition of Foreign Investment Industrial Guidance Catalogue since 1995. In this edition, the encouraged industries for foreign investment have been increased, including the development and manufacturing of VR or AR facilities, development and manufacturing of key components of 3D printers, construction and operation of hydrogen filling stations, construction of urban parking facilities, etc. Besides, the Negative List, specifying the prohibited industries and restrictive industries for foreign investors, has been formally adopted. As a general trend, control over foreign investment in the cultural industry has been strengthened.

In addition, in November 2017, China announced major steps to open up its financial sector, including increasing or removing or committing to increase/remove the cap of foreign ownership in securities firms, fund management companies and future companies, banks and life insurance companies.

**Interim Measures on the Administration of Filings for the Formation and Modification of Foreign-invested Enterprises, issued on October 8, 2016 and amended on July 30, 2017.**

By the implementation of these Interim Measures, the regulatory formalities for foreign direct investments in certain industries in China have been simplified. If foreign investors invest, either by way of “greenfield” establishment or by an acquisition (rather than merger and acquisition between related parties), into an industry which is not in the Negative List, an online filing with the MOC will suffice. That is, it would no longer be necessary to get the approval from the MOC on the establishment or acquisition. Nevertheless, foreign investors still need to complete the registration of the establishment or acquisition with the competent AIC.

**General Provisions of the Civil Law of the People’s Republic of China, issued on March 15, 2017 and effective since October 1, 2017.**

As the first step to compile the Uniform Civil Code of China, a new law, i.e. the General Provisions of the Civil Law of the People’s Republic of China, has been formally promulgated. Similar to the General Principles of

Civil Law of the People’s Republic of China, it governs the civil relations among the civil subjects, including the relations between foreign investors and their local partners or agents. The new law emphasizes the protection of personal information, virtual properties and private rights. More importantly, it extends the limitation of actions into three years. The Uniform Civil Code of the People’s Republic of China is expected to be formulated in 2020.

In addition to the above, the Anti-unfair Competition Law was formally amended by the National People’s Congress on November 4, 2017 and became effective January 1, 2018. This is the first amendment to the Anti-unfair Competition Law since 1993. It further specifies the unfair competition behaviors and redefines the business bribery conducts which would have significant influences on the business operation of enterprises. Besides, it expressly prohibits the false trading and internet unfair competitions and reinforces the legal consequences for violations.

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