

**Doing Business in China**  
*An Introduction*

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# About Deloitte China



# Experienced network

## First foreign accounting firm in Shanghai

- **13,500** professionals in Greater China region
- **22** offices in Greater China region



## Deloitte offices in Greater China region 在大中华区的德勤事务所



### Chinese Mainland 中国大陆

- 1 Beijing 北京
- 2 Chengdu 成都
- 3 Chongqing 重庆
- 4 Dalian 大连
- 5 Guangzhou 广州
- 6 Hangzhou 杭州
- 7 Harbin 哈尔滨
- 8 Jinan 济南
- 9 Nanjing 南京
- 10 Shanghai 上海
- 11 Shenzhen 深圳
- 12 Suzhou 苏州
- 13 Tianjin 天津
- 14 Wuhan 武汉
- 15 Xiamen 厦门

### 16 Hong Kong 香港

### 17 Macau 澳门

### Taiwan 台湾

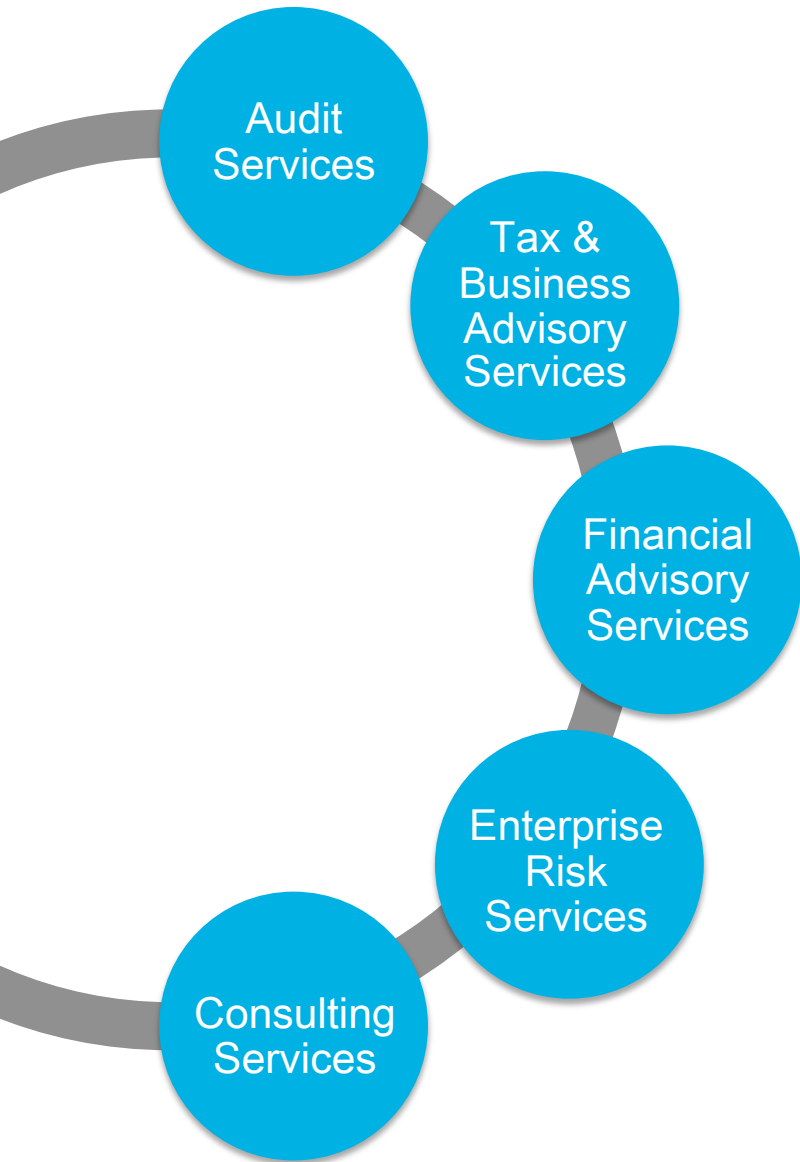
- 18 Taipei 台北
- 19 Hsinchu 新竹
- 20 Taichung 台中
- 21 Tainan 台南
- 22 Kaohsiung 高雄



# Deloitte multidisciplinary approach



# Recognized market leadership across our services



- Auditor of the largest number of companies listed in Hong Kong
- China's largest IPOs
- Largest tax & business advisory practice in the Chinese Mainland
- Largest overseas auto manufacturing acquisition by a Chinese enterprise
- Leader in risk consulting
- Largest consulting practice

# Deloitte Audit Services

**Deloitte's audit team has over 7,500 professionals across Chinese Mainland, Hong Kong SAR, Macau SAR and Taiwan**

- Auditors to the largest number of companies listed on the Hong Kong Stock Exchange
- Advisor to the PRC's Ministry of Finance

## Our services

**Annual statutory audit and special audit**

**IPO services**

## Extensive experience in domestic and overseas public offering services

- China's largest IPOs in 2009 and 2010
- Leader in Chinese US IPOs in 2011
- Listing of the first Japanese company in Hong Kong
- The first RMB IPO in Hong Kong



# Deloitte Tax & Business Advisory Services

The only Big Four practice that works As One across Greater China Region including the Chinese Mainland, Hong Kong, Macau and Taiwan

- Significant contributor to tax legislation and education in China
- Tier 1 practice as awarded by International Tax Review
- Unique Asia Pacific International Core of Excellence for enhanced cross border capabilities

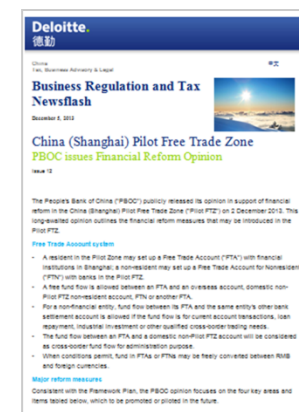
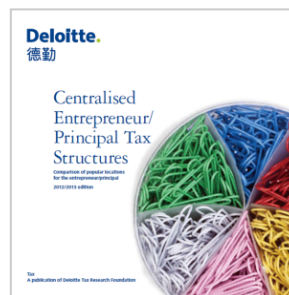
## Our services

Global Business Tax Services

Cross Border Tax

Global Employer Services

Indirect Tax





# Deloitte Tax & Business Advisory Services

## Global Business Tax Services

- Business tax
- Private company services
- R&D and government incentives
- Tax management consulting
- Tax certification services

## Cross Border Tax

- International tax
- Mergers and acquisitions
- Transfer pricing
- Business model optimization

## Global Employer Services

- International assignment services
- Compensation and benefits
- International human resources
- Risk. Talent. Rewards
- Technology

## Indirect Tax

- Indirect tax
- Customs & global trade

Plus a variety of other tax and business advisory services

# Deloitte Enterprise Risk Services

## Leader in risk consulting

- Over 1,200 dedicated professionals
- Pioneer in HK IPO Controls Review (PN21), C-SOX and Enterprise Risk Management

## Our services

- Risk intelligent services
- Regulatory readiness and facilitation compliance services
- Business continuity planning
- Information governance services
- ERP controls services
- Due diligence reviews of internal Controls under the revised Hong Kong listing rules
- Security & privacy
- Internal audit
- Computer audit
- Contract risk & compliance services
- Accounting & controls services
- IT due diligence



# Deloitte Financial Advisory Services

Over 600 professionals in Chinese Mainland, Hong Kong SAR, Macau SAR and Taiwan

- Advisors of the largest outbound auto manufacturing acquisition in 2010
- Accounting & Transaction Advisor of the Year in Asia Pacific (Atlas M&A Awards 2010)

## Our services

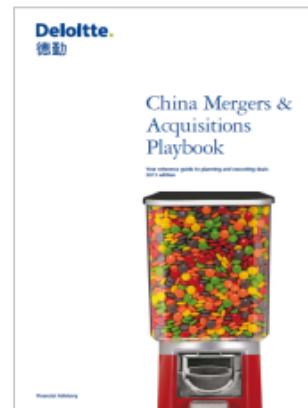
Corporate Finance Advisory

M&A Transaction Services

Valuation Services

Reorganization Services

Forensic & Dispute



# Deloitte Financial Advisory Services

## Corporate Finance Advisory

- Mergers & acquisitions advisory
- Pre-IPO advisory
- Private placement service

## M&A Transaction Services

- Financial / tax due diligence
- Vendor due diligence
- Commercial due diligence
- Merger and integration services
- Financial modeling
- Crafting business plans
- Crafting acquisition and financing agreements

## Valuation Services

- Business Valuation and Valuation Advisory Services  
Performing valuations business interests, intellectual property, intangible assets, common and preferred stock and other securities, partnership interests, employee stock option plans, private debt instruments, options, warrants, and other derivative products.

## Reorganization Services

- Debt and corporate restructuring
- Financial review & monitoring
- Debtors' advisory
- Lender support
- Closure management
- Liquidation & bankruptcy
- Receivership (HK)
- Estate management / administration

## Forensic & Dispute

- Corporate investigations
- Fraud risk management
- Foreign corrupt practices act services
- Integrity due diligence
- Litigation support
- Expert witness
- Anti-money laundering and terrorist financing risk services
- Computer forensics and data analytics

# Deloitte Consulting Services

## Largest consulting practice

- Top-tier consulting organization for both multinational and large local Chinese companies

## Our services

Strategy & Operation

Human Capital Service

Technology Service

## Recognized in China:

- CFO's Most Trusted Advisory Organization (2008-2010)
- Leader in ERP Services for China - "Gartner's Magic Quadrant for ERP Service Providers, China 2010"
- As the best advisory company among Chinese pioneer human resources service providers, 2011 – by the magazine "Top HR"
- Best Practice Award for ASBE General Classification Standard implementation, by National Accounting Informationization Committee (2011)
- Excellent IT Consulting Service Award, by the magazine "Financial Computerizing" (2011)



# Deloitte Consulting Services

## Strategy & Operation

- Strategy and Operation
- Financial Management
- Financial Service Industry – S&O

## Human Capital Service

- Human Capital Advisory Service
- Actuarial and Insurance Solutions

## Technology Service

- Enterprise Application
- Technology Integration
- Global Delivery Center

Uniquely integrated capabilities backed up by the right business structure, style, culture, and size

Anticipate and address complex business challenges to improve business performance and drive shareholder value

# China's business and regulatory environment



# An overview

- China, or People's Republic of China, is the world's most populous country, with a population of over 1.35 billion.
- China is a single-party country governed by the Communist Party, with its seat of government in the capital city of Beijing.
- China has jurisdiction over 22 provinces, 5 autonomous regions, 4 directly-controlled municipalities (Beijing, Tianjin, Shanghai and Chongqing), and 2 mostly self-governing special administrative regions (Hong Kong and Macau).
- The Chinese government also claims Taiwan – which is controlled by the Republic of China, a separate political entity – as its 23<sup>rd</sup> province, a claim which is controversial due to the complex political status of Taiwan.
- China is the world's second-largest country by land area.
- China is a member of WTO (World Trade Organization) and APEC (Asia-Pacific Economic Cooperation).



# Business environment

- Since the introduction of economic reforms in 1978, China has become one of the world's fastest-growing major economies.
- As of 2013, it is the world's second-largest economy by both nominal total GDP and purchasing power parity (PPP), and is also the world's largest exporter and importer of goods.
- Although the economy previously was dominated by state-owned enterprises (SOEs), domestic private enterprises and foreign investments have become the main driving force of economic development.
- China has set up a number of special economic zones (SEZ), economic and technological development zones (ETDZ), export processing zones and bonded warehouse zones to attract domestic and foreign investment and export activities. Various preferential policies, covering tax, foreign exchange, custom, investment, employment, and etc., are provided to qualified enterprises or industries in these areas.
- The top three foreign direct investment concentrated industries are manufacturing, real estate and leasing, and commercial services.

# Regulatory framework

- Company Law : It was introduced on 29 December 1993 and was amended in 2005 and 2013. The latest amendment is effective from 1 March 2014. The Company Law applies to both domestic and foreign companies.
- Partnership Law : Partnerships are regulated by the Partnership Law, which entered into force on 17 April 2007.
- Other important special laws and regulations governing foreign investment are:
  - Wholly Foreign-owned Enterprises (WFOE) Law (promulgated on 12 April 1986, last amended on 31 October 2000);
  - Chinese-foreign Equity Joint Ventures (EJV) Law (promulgated on 1 July 1979, last amended on 15 March 2001); and
  - Chinese-foreign Cooperative Joint Ventures (CJV) Law (promulgated on 13 April 1988, last amended on 31 October 2000).

# Regulatory framework for foreign investment #1

- The main policies on foreign investment can be found in the “Regulations on Guiding the Direction of Foreign Investment” and the “Industrial Catalogue for Foreign Investment”.
- The Ministry of Commerce (MOC) is responsible for the administration and examination of foreign investment.
- Foreign investors may carry on business in China in the following forms, which are known as foreign investment enterprises (FIEs):
  - WFOE (limited liability company);
  - EJV (limited liability company);
  - CJV (partnership);
  - Foreign invested partnership;
  - Branch (only used by banking business); and
  - Representative office.

# Regulatory framework for foreign investment #2

- WFOE is the most popular form of foreign investment. The advantages of a WFOE include greater independence in operation, greater flexibility with respect to management structure, the ability to terminate the venture without the consent of a local partner, enhanced security in the protection of trade secrets and technology and more freedom from interference in management.
- A joint venture consists of two or more parties, at least one being foreign and one Chinese. While the foreign party may be an individual, the Chinese party must be a company, enterprise or other economic organization. Where a foreign enterprise is contemplating establishing a joint venture in China, the first step will normally be to select the appropriate Chinese partner(s). The choice of a right partner is essential to the success of the cooperation due to the complexities of the business environment. In most cases a thorough due diligence study of the partner is necessary.

# Regulatory framework for foreign investment #3

- A foreign invested partnership may be formed among more than two foreign enterprises or individuals, or foreign enterprises/individuals on the one hand and Chinese legal entities/individuals on the other hand. It is also possible for a foreign enterprise or individual to join an existing Chinese partnership. The requirements for capital contribution and other issues are referred to in the provisions of the Partnership Law.
- Except in the banking business and oil industry, branches are generally not used in China. To establish a branch in China, a foreign company must file an application with the competent government department and submit relevant documents such as articles of association and the company registration certificate issued by its home country. Upon approval, it must carry out registration procedures with the SAIC and obtain a business licence.
- A representative office is often used to establish a presence in China as it is easy to set up and cost-efficient. Generally, a representative office functions as a liaison between the foreign head office and customers in China. However, its activities are restricted to non-profit making activities.

# Exchange control

- China imposes exchange controls and the Chinese yuan is not entirely freely convertible. The State Administration of Foreign Exchange (SAFE) administers the exchange controls.
- Transactions are broadly categorized into 2 types, current account and capital account transactions.
- Current account transactions : The export/import of goods, export/import of services, income and current transfers are on current account. The Chinese yuan is freely convertible on current account with a few exceptions. Payments are permitted, provided they are genuine current account transactions.
- Capital account transactions : Capital transfers and acquisitions or disposals of non-produced/financial assets are on capital account. Foreign investors are generally not allowed to withdraw their registered capital.

# China's tax environment



# Corporation taxation #1

**Residence** : An enterprise is resident om China if it is either established in China, or if its place of “effective management” is in China. “Effective management” is defined as substantial and overall management and control over manufacturing and business operations, human resources, financial and property aspects of the enterprise.

**Basis** : Residents are taxed on worldwide income, while non-residents are taxed on China-source income, and income effectively connected with their “establishments” in China. “Establishment” has a broad definition under China domestic tax law.

**Taxable income** : Taxable income is the amount remaining from gross income in a tax year after deducting allowable expenses and losses, non-taxable and tax-exempt items, and any prior year loss carry forward.

**Taxation of dividend** : Dividends paid by a resident enterprise to another resident enterprise is not taxable. Foreign dividends are taxable.

**Capital gains** : Capital gains are taxable.

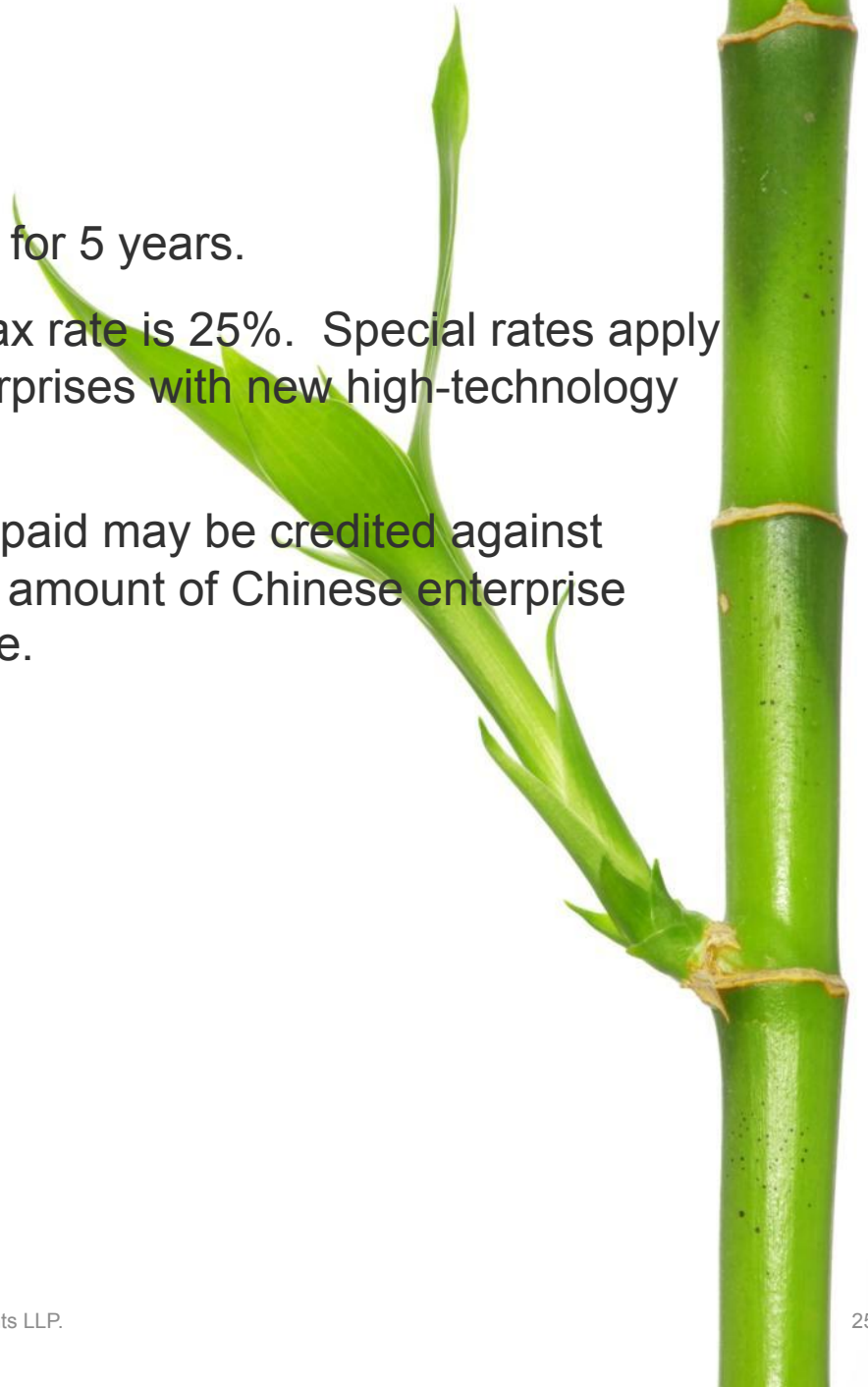


# Corporation taxation #2

**Losses** : Losses may be carried forward for 5 years.

**Rate** : The standard enterprise income tax rate is 25%. Special rates apply to small-scale enterprise (20%) and enterprises with new high-technology status (15%).

**Foreign tax credit** : Foreign income tax paid may be credited against Chinese enterprise income tax, up to the amount of Chinese enterprise income tax payable on the foreign income.



# Non-residents taxation

**Dividends** : 10% withholding tax is imposed on dividends paid to a non-resident shareholder, unless the rate is reduced under a tax treaty.

**Interest** : A 10% withholding tax applies to interest paid to a non-resident lender, unless reduced tax treaty rate is available. A 5% business tax is also applicable.

**Royalties** : A 10% withholding tax is imposed on royalties paid to a non-resident licensor, unless the rate is reduced under a tax treaty. A 6% VAT may also be applicable.

**Technical service fees** : Technical service fees paid to a non-resident service provider are subject to 25% enterprise income tax to the extent that the services are rendered in China. A 6% VAT is generally applicable regardless of the location of service.

# Other taxes on corporations

**Real estate tax** : It is levied on land and buildings, payable by the owner of the real estate at 1.2% per annum (on the original cost), or at 12% per annum (on rental income).

**Urban land use tax** : This tax is imposed on land area occupied at ranges ranging from RMB0.6 to RMB30 per square meter.

**Stamp duty** : Stamp duty at varying rates applies to contracts, agreements and certain legal documents.

**Deed tax** : Deed tax is imposed at 3%-5% on the total value of real estate upon transfer of the ownership rights.

**Land appreciation tax** : This tax is imposed on gains realised on the transfer of real estate. The gain is calculated based on sales proceeds less certain deductions, and the rate ranging from 30% to 60%.

# Anti-avoidance rules

**Transfer pricing** : China's definition of related party / associated enterprise is a broad one, with a strong emphasis on control. Contemporaneous documentation is required to be prepared unless exemptions apply.

**Thin capitalization** : Excessive interest expense from related party financing is non-deductible for tax purpose.

**Controlled foreign companies (CFC)** : Resident enterprises must include their relevant share of the undistributed profits of a CFC in their taxable income.

**General anti-avoidance rule** : It requires a bona fide business purpose for any business arrangement that has the effect of reducing, deferring or avoiding taxable income.

**Disclosure requirements** : Disclosure of related party transaction in annual tax return is required. There are also disclosure requirements on direct and indirect share transfers, contracting or services provided by non-residents, etc.

# Administration and compliance

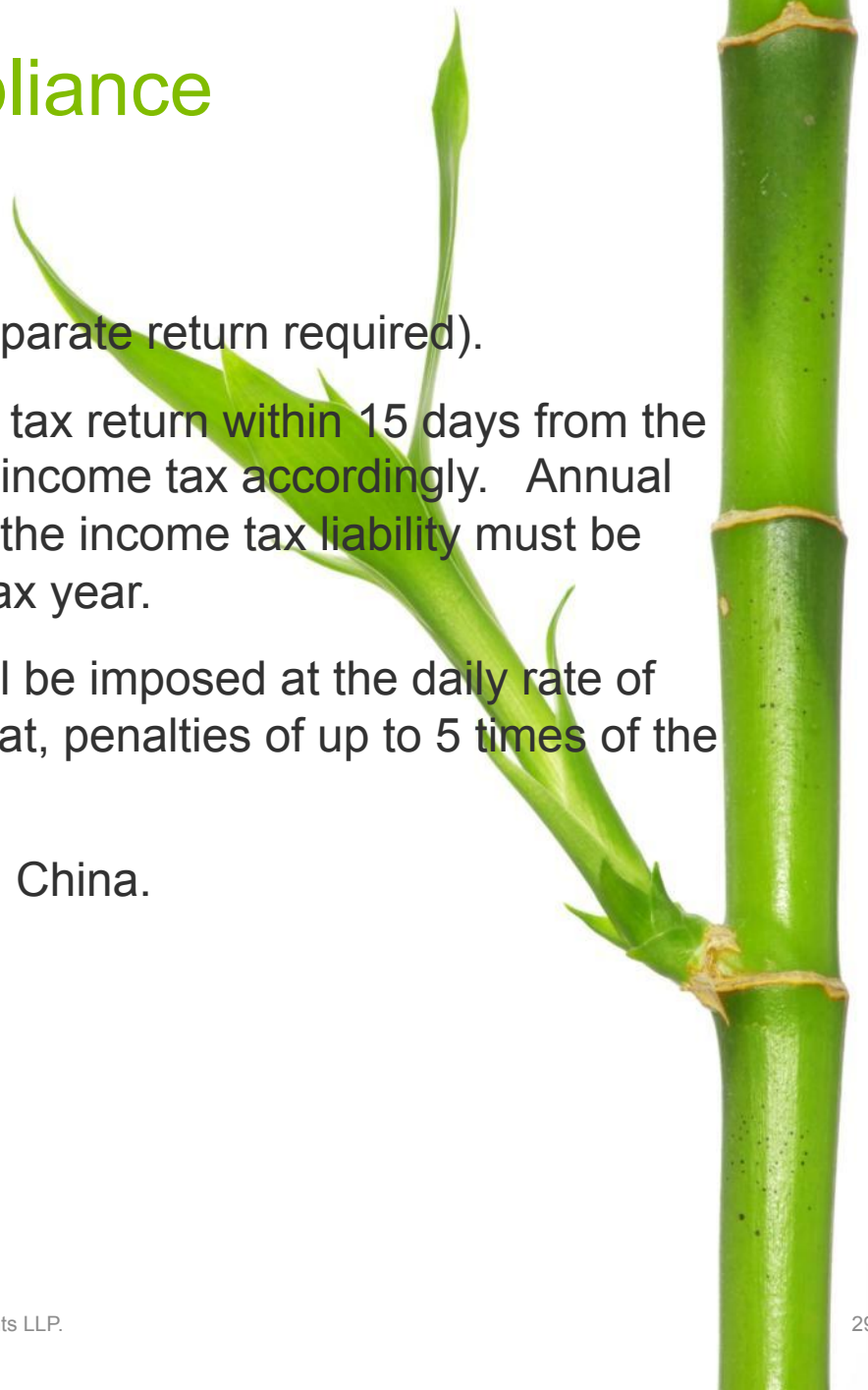
**Tax year** : Calendar year.

**Consolidated return** : Not permitted (separate return required).

**Filing requirement** : Provisional income tax return within 15 days from the end of each quarter, and pay provisional income tax accordingly. Annual income tax return and final settlement of the income tax liability must be made within 5 months of the end of the tax year.

**Penalties** : A late payment surcharge will be imposed at the daily rate of 0.05% of the underpaid tax. On top of that, penalties of up to 5 times of the underpaid tax may be imposed.

**Rulings** : There is no ruling procedure in China.



# Personal taxation

**Basis** : Individual who is Chinese tax resident and non-Chinese tax resident staying in China for more than 5 years are subject to individual income tax on his / her worldwide income. Non-Chinese tax resident individual staying in China for less than 5 years is subject to individual income tax only on China-source income.

**Residence** : No specific definition.

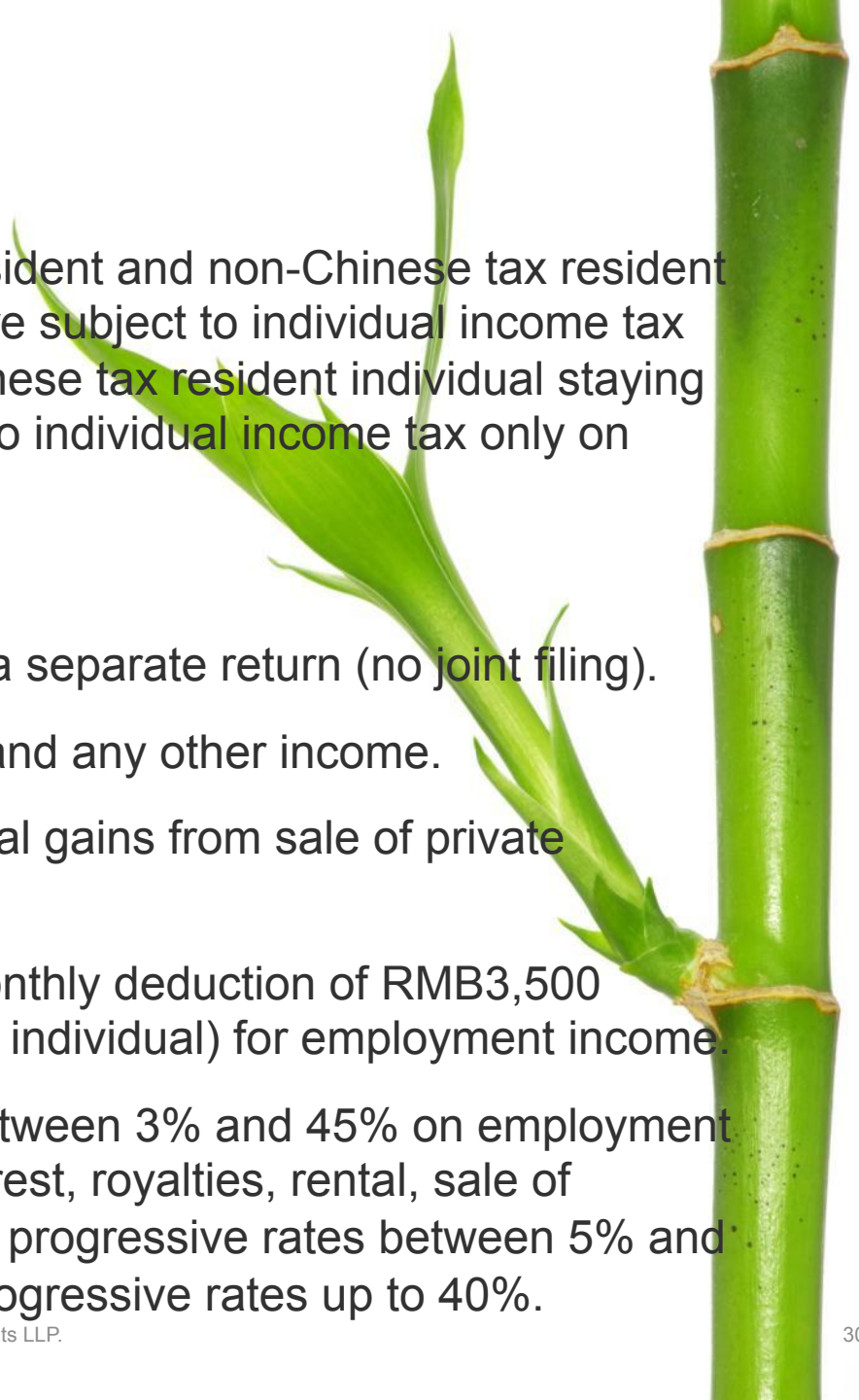
**Filing status** : Each individual must file a separate return (no joint filing).

**Taxable income** : Employment income and any other income.

**Capital gains** : Taxable (except for capital gains from sale of private residence occupied for 5 years or more).

**Deductions and allowances** : Fixed monthly deduction of RMB3,500 (Chinese individual) / RMB4,800 (foreign individual) for employment income.

**Rates** : Progressive tax rates ranging between 3% and 45% on employment income. 20% tax rate for dividends, interest, royalties, rental, sale of properties. Business income is taxed at progressive rates between 5% and 35%. Personal service fee is taxed at progressive rates up to 40%.



# Administration and compliance

**Tax year** : Calendar year.

**Filing and payment** : For employment income, typically the return is filed and tax payment made monthly on a withholding basis. For other income, mostly by withholding basis as well. Annual filing is required for individuals with annual income exceeding RMB120,000.

**Penalties** : A late payment surcharge will be imposed at the daily rate of 0.05% of the underpaid tax. On top of that, penalties of up to 5 times of the underpaid tax may be imposed.

# Indirect taxes

**Value added tax :** It applies on supply and import of goods, and services (pilot VAT reform program launched in Shanghai in 2012 and expanded nationwide on 1 August 2013). Standard rate is 17% (lower rate of 13% for certain goods), services under pilot VAT reform program are subject to 6% (modern services), 11% (transportation) and 17% (leasing). 3% rate applies for small-scale VAT payer.

**Business tax :** It is imposed on services (will be replaced by VAT), assignment of IP and sale of immovable properties. Tax rates are 3% or 5% for most services, and 5% to 20% for entertainment related services.

**Consumption tax :** It applies to alcohol, cosmetics, jewelry, luxury watches, tobacco, etc, at rates ranging from 1% to 45%.



# Summary



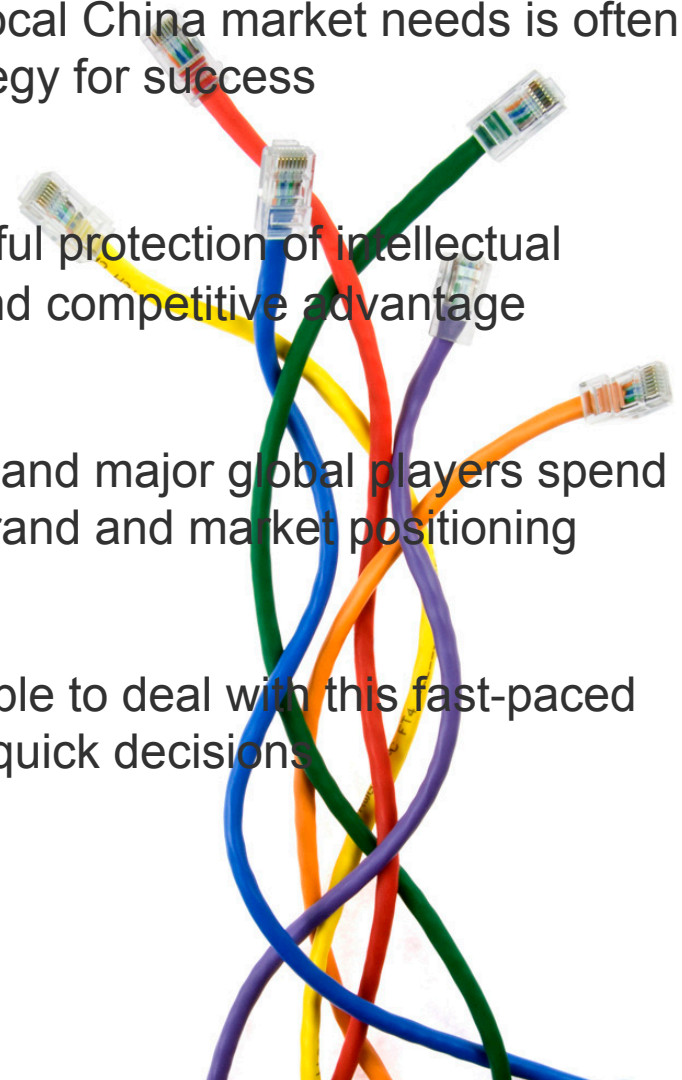
# Key Success Factors for Doing Business in China

- **Thorough knowledge of local business environment**
  - Laws/regulations
  - Market size (customers)
  - Competitors
  - Business customs
- **Local partners**
  - Qualified local partners could help overcome barriers in tapping into local market, however building the relationship is often painful
- **“Guanxi” or connections, especially with government**
  - Carefully developed relationship with government (national and local) is essential in many areas, though they alone do not guarantee success
- **Localization (People)**
  - Local management team who understand both the company culture and China’s environment can be a key differentiator in reducing cost, and effectively executing China strategy



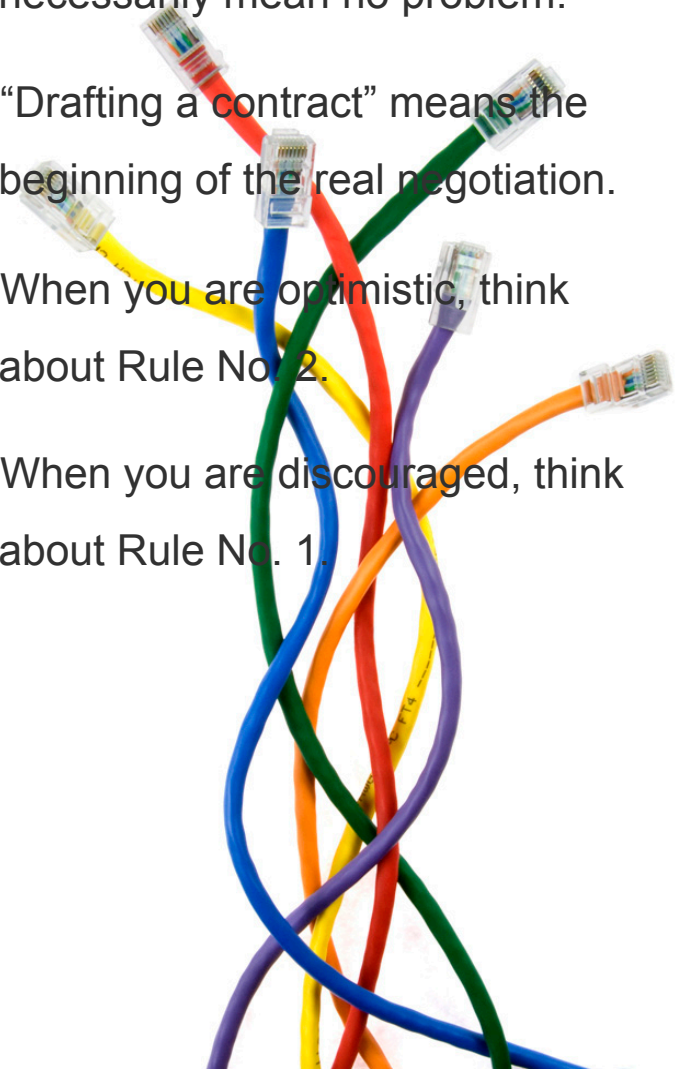
# Key Success Factors for Doing Business in China

- **Localization (products and services)**
  - Tailored products and services to the local China market needs is often overlooked but could be a crucial strategy for success
- **Protection of Intellectual Properties**
  - Rampant piracy in China prompts careful protection of intellectual property in an effort to protect brand and competitive advantage
- **Branding and Market positioning**
  - Branding is distinctly different in China and major global players spend significant resources to localize their brand and market positioning
- **Speed of decision making and action**
  - the local management team must be able to deal with this fast-paced environment and be confident making quick decisions



# Ten Rules for Doing Business in China

1. Everything is possible
2. Nothing is easy
3. Patience is the essence of success
4. The answer “Yes” is not necessarily an indication of agreement or confirmation
5. “You don’t understand our country” means they disagree
6. “Provisional regulations” means they can change the rules anytime they want, even retroactively
7. “Basically, no problem” does not necessarily mean no problem.
8. “Drafting a contract” means the beginning of the real negotiation.
9. When you are optimistic, think about Rule No. 2.
10. When you are discouraged, think about Rule No. 1.





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#### About Deloitte in Greater China

We are one of the leading professional services providers with 22 offices in Beijing, Hong Kong, Shanghai, Taipei, Chengdu, Chongqing, Dalian, Guangzhou, Hangzhou, Harbin, Hsinchu, Jinan, Kaohsiung, Macau, Nanjing, Shenzhen, Suzhou, Taichung, Tainan, Tianjin, Wuhan and Xiamen in Greater China. We have nearly 13,500 people working on a collaborative basis to serve clients, subject to local applicable laws.

#### About Deloitte China

The Deloitte brand first came to China in 1917 when a Deloitte office was opened in Shanghai. Now the Deloitte China network of firms, backed by the global Deloitte network, deliver a full range of audit, tax, consulting and financial advisory services to local, multinational and growth enterprise clients in China. We have considerable experience in China and have been a significant contributor to the development of China's accounting standards, taxation system and local professional accountants.

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