

Break Through the Chinese Wall

**- Legal and practical guidelines
for establishing a company in China**

May 2010

© Capital Associates, Beijing – China

© NCO China, Beijing – China

Cover design: lisbethfink.dk

About the book

“Break Through the Chinese Wall” is an accessible handbook which provides an introduction to the fundamental rules, regulations and common practices related to establishing and running a business in China. The handbook provides answers to the most frequently asked questions from our clients.

The handbook has been jointly written by Capital Associates and NCO China. Capital Associates is a Chinese law firm specialised in providing commercial legal services and assistance to foreign companies investing in and trading with China. NCO China is a consulting firm that offers corporate services with regard to the establishment of an enterprise in China, Hong Kong etc., and provides accounting, tax and HR services to foreign investors in China. Both Capital Associates and NCO China serve a variety of clients; from large multinational companies to small and medium sized enterprises.

China’s rapid development means that regulations and practices are constantly changing. The handbook is meant to be an introduction to the current laws and practices in China. Updates and further information regarding the subjects covered by the handbook can be obtained from our offices or websites. Please refer to the contact information in the back of the book.

Birgitta Bundgaard, Lawyer

Jette Renneberg, Economist

Disclaimer notice:

Please note that the content of this book is for general information only, and not legal advice. Capital Associates and NCO China take no responsibility for errors or inaccuracies in the information provided, either existing or due to changes in laws, regulations and administrative practices. Any liability that might arise from your or a third person’s use or reliance on the information in the book is expressly disclaimed by Capital Associates and NCO China.

The Chinese Anti-Monopoly Law

One of the most important laws passed by China since its entry into the WTO is the Anti-Monopoly Law, which came into effect on 1 August, 2008.

The Anti-Monopoly Law, which was 14 years on the drawing board, is the first comprehensive competition law in China's history, and represents a major step forward in China's transformation into a market economy. Generally, it applies equally to foreign and domestic enterprises, but it also includes some protectionist provisions.

The law is influenced by European anti-monopoly law and covers the traditional range of antitrust topics, including restrictive agreements, abuse of dominance, merger clearance and trade cartels. In addition, it covers a fourth area; the prohibition of "administrative monopoly", which is known as abuse of administrative powers by public agencies and organizations.

The Anti-Monopoly Law is broad in scope and its provisions are somewhat vaguely defined. Companies that intend to complete a business transaction that falls within its scope should become familiar with these provisions as they can significantly increase the time, costs, and risks connected with such transactions.

Anticompetitive agreements and abuse of dominance

The Anti-Monopoly Law bans monopolistic arrangements, such as cartels and other forms of collusion, and provides for the investigation and prosecution of monopolistic practices.

However, the law also lists some situations where an agreement will be immune from the law; for example, an agreement will not be prohibited if the business operator can prove that:

- the purpose of the agreement is to improve technology or the research and development of a new product,
- the market competition in the relevant market will not be seriously prejudiced, and
- consumers will enjoy the benefits brought about by such agreement.

It is, however, important to be aware that there is little experience in China with such provisions for exemption, and it may take some time before a stable body of judicial and administrative experience develops.

Besides prohibiting anticompetitive agreements, the Anti-Monopoly Law prohibits monopolies from using their dominant status in the market to curb competition, fix prices, enforce package sales, and refuse or enforce trade.

It is important that foreign investors and foreign invested enterprises are fully aware of the monopoly activities proscribed by the law, and ensure that their activities in China comply with them.

Merger control

One consequence of the Anti-Monopoly Law is that big mergers must now be approved in 3 places in the world: the EU, the US and China.

In China, all companies seeking mergers or acquisitions must notify the relevant anti-monopoly law enforcement department, if the transaction meets either of the following two alternative turnover thresholds:

- The total worldwide turnover of all parties to the transaction in the previous fiscal year exceeded RMB 10 billion, and the China turnover of each of at least two parties to the transaction exceeded RMB 400 million.
- The total turnover in China of all parties to the transaction in the previous fiscal year exceeded RMB 2 billion, and the China turnover of each of at least two parties to the transaction exceeded RMB 400 million.

However, it must be emphasized that even if the turnover of the companies involved do not meet either of the two standards listed above, law enforcement bodies can still carry out investigations if evidence show that a company could potentially limit competition. For instance, although the turnover of companies in some industries is low, their market share could be large enough to restrict competition.

The filing obligation applies to:

- Mergers and acquisitions
- Share or asset sales that give one company control over another
- Deals in which one company can gain control of or be able to impose decisive influence over another firm through the signing of contracts or other means

The Anti-Monopoly Law provides two exemptions that would allow companies to avoid submitting a transaction for review. Under the first exemption, no notification is required when a company possesses more than 50 percent of the voting shares or assets of each of the other companies involved in the transaction. To qualify for the second exemption from notification, a company not involved in the concentration must possess more than 50 percent of the voting shares or assets of each company that is involved in the concentration.

Regardless of the thresholds and exemptions stated above, foreign investors should always apply for approval from the Ministry of Commerce in the following situations:

- The purchase of a domestic company affects national economic security
- The purchase takes place in a key sector
- The purchase causes a transfer of the operating rights of a famous domestic brand

The list of strategic sectors, in which the state wishes to retain control, includes military-related manufacturing, power production and grids, petroleum, gas and petrochemicals, telecom manufacturing, coal, civil aviation, and shipping.

Natural monopolized industries, which are mainly owned by the state, are exempted from the Anti-Monopoly Law for reasons of economic development and public interest.

Enforcement

The Anti-Monopoly Law is expected to have a significant impact on the development of business activities in China. However, the actual effect will depend on the proper, impartial, and effective implementation of the law by various enforcement authorities.

The Anti-Monopoly Law Enforcement Agency (AMEA) has primary responsibility for enforcing the Anti-Monopoly Law. The AMEA is comprised of three government authorities: the Ministry of Commerce, the National Development and Reform Commission (NDRC) and the State Administration for Industry and Commerce (SAIC).

AMEA is empowered to perform on-the-spot inspections, question interested parties, examine and copy relevant data, retain evidence

and make inquiries into a company's bank accounts. Further, AMEA is authorized to delegate its powers to other government agencies, thereby making it possible to increase the overall enforcement of the Anti-Monopoly Law.

The Ministry of Commerce is responsible for anti-monopoly investigation of issues such as mergers and acquisitions, while the NDRC will decide on price issues, and SAIC will decide on issues related to the abuse of dominant positions.

The Supreme People's Court has designated specialized intellectual property courts as the courts responsible for hearing cases brought forward under the Anti-Monopoly Law. This includes damage action cases and cases involving judicial review of the decisions of AMEA.

As regards decisions concerning merger control, the parties will need to apply to the Ministry of Commerce for administrative reconsideration, before they can bring an administrative lawsuit to challenge such decisions. In contrast, as to decisions arising from the investigation of monopoly agreements or abuse of dominance, parties may directly challenge such decisions before the courts.

Companies that violate the Anti-Monopoly Law can be subject to severe penalties. Among other things, fines of between 1% and 10% of the violator's turnover can be imposed, and mergers or acquisitions that trigger merger review in China and other parts of the world may not be closed, until merger clearance is obtained from the Chinese authorities.

Useful links

Help and advice when establishing a FIE in China

- www.capitallaw.cc
Capital Associates' website.
- www.ncochina.com
NCO China's website.

Government and organizations

- <http://english.gov.cn/index.htm>
The official website of the Chinese central government.
- www.ebeijing.gov.cn
Official website of the Beijing Municipal Government.
- www.shanghai.gov.cn
Official website of the Shanghai Municipal People's Government.
- www.china.org.cn
Government portal site to China that offers broad access to news about China.
- www.fdi.gov.cn
Website of the Chinese Ministry of Commerce directed to foreign investors. The site comprises government news and information about investment directions, economy, statistics and law.
- <http://english.mofcom.gov.cn/>
Official website of the Chinese Ministry of Commerce.

- www.chinainvest.com.cn
China International Electronic Commerce Centre's website. Contains investment news and information about investment projects in China.
- www.tdctrade.com
Hong Kong Trade Development Council's website. Provides information about CEPA.
- www.tid.gov.hk/english/cepa/
Website of Hong Kong Trade and Industry Department. Provides full text documents on all CEPA agreements and annexes.
- www.adb.org
Website of the Asian Development Bank.

Other sources of information about China

- www.transparency.org
Website of Transparency International, a coalition against corruption.
- www.hoover.org/publications/clm
Website of the Hoover Institution of Stanford University. Provides information about China's leadership politics and its foreign and domestic policies.
- www.chinaeconomicreview.com
China Economic Review is a monthly magazine published in Hong Kong covering business, finance and economics in China.
- www.worldbank.org/transitionnewsletter
World Bank newsletters on developing economies.

- www.cia.gov/library/publications/the-world-factbook/
U.S. CIA World fact book.
- www.expatsinchina.com
A guide for foreigners living in China.

Logistics

- www.maps-of-china.com
Maps of Chinese cities, provinces and regions in the principal areas of China.
- www.primecargo.com
Website of the international transportation and freight forwarding company Primecargo.
- www.dsv.com
A transportation company that offers end-to-end transport and logistics solutions.

News in English

- www.chinadaily.cn
Website of China Daily, the Chinese government's official mouthpiece.
- www.scmp.com
Website of South China Morning Post, which is a little less censored than China Daily.
- www.shanghaidaily.com
Website of the local Shanghai newspaper
- <http://english.peopledaily.com.cn>.

Chambers of commerce

- www.amcham-china.org.cn
The American Chamber of Commerce in China.
- www.europeanchamber.com.cn
The European Chamber of Commerce in China.
- www.pek.britcham.org
The British Chamber of Commerce in China.
- www.ccifc.org/
The French Chamber of Commerce in China.
- www.dccc.com.cn
The Danish Chamber of Commerce in China.
- www.swedishchamber.com.cn
The Swedish Chamber of Commerce in China.

Abbreviations

AIC	Administration of Industry and Commerce
AMEA	Anti-Monopoly Law Enforcement Agency
ASBE	Accounting Standards for Business Enterprises
BLTB	Beijing Local Tax Bureau
CAS	Chinese Accounting Standards
CBRC	China Banking Regulatory Commission
CCPIT	China Council for the Promotion of International Trade
CEPA	Closer Economic Partnership Arrangement
CIETAC	China International Economic and Trade Arbitration Commission
CJV	Contractual or Cooperative Joint Venture
CO (CEPA)	Certificate of Hong Kong Origin (CEPA)
COFCOM	Commission of Commerce
CPA	Certified Public Accountant
CSRC	China Securities Regulatory Commission
DTT	Double Taxation Treaty
EJV	Equity Joint Venture
EPZ	Export Processing Zones
FESCO	Foreign Enterprise Service Corporation
FIE	Foreign Investment Entity
FIP	Foreign Invested Partnership
FR	Factory Registration with TID (CEPA)
HKTDC	Hong Kong Trade Development Council
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
LoI	Letter of Intent
MII	Ministry of Information Industries
MOFCOM	Ministry of Commerce
MOLSS	Ministry of Labour and Social Security
NDRC	National Development and Reform Commission
NPC	National People's Congress

PBOC	People's Bank of China
PRC	People's Republic of China
RMB	Renminbi
RO	Representative Office
ROOs	Rules of Origin (CEPA)
SAFE	State Administration of Foreign Exchange
SAIC	State Administration for Industry and Commerce
SAR	Special Administrative Region (Hong Kong and Macau)
SAT	State Administration for Taxation
SIPO	State Intellectual Property Office of the PRC
TID	Hong Kong Trade and Industry Department
TRIPs	Trade-Related Aspects of Intellectual Property Rights (agreement under WTO)
WFOE	Wholly Foreign Owned Enterprise
WIPO	World Intellectual Property Organization
WTO	World Trade Organization

References

We have found inspiration for the handbook on the websites listed under “Useful links”. In addition, various materials from events and presentations together with “Danmarks Nationalbank, Quarterly Review 1, 2009” have been used.

Last, but not least, we have drawn on the long experience of Capital Associates and NCO China in advising clients.

Contact information

Beijing

Capital Associates

Tel: + 86 8447 9588

Email: lukalu@capitallaw.cc

www.capitallaw.cc

NCO China, Beijing

Tel: + 86 10 8447 8118

Email: enquiry@ncochina.com

www.ncochina.com

Shanghai

NCO China, Shanghai

Tel: + 86 21 51699589

Guangzhou

NCO China, Guangzhou

Tel: + 86 20 8751 4381

Tianjin

NCO China, Tianjin

Tel: + 86 22 8210 1281

Denmark

NCO (China Consult APS)

Tel: + 45 3917 9895

NCO China is an affiliate of AFP Group, with offices in
Hong Kong - Taipei - Singapore - New Delhi – Zurich