

DOING
BUSINESS
IN

CHINA



Foreword

This booklet has been prepared for the use of clients, partners and staff of HLB International member firms. It is designed to give some general information to those contemplating doing business in China and is not intended to be a comprehensive document. You should consult us, therefore, before taking further action. HLB China and HLB International cannot be held liable for any action or business decision taken on the basis of information in this booklet.

HLB China

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Up to date information and general assistance on international matters can be obtained from any of the member firm partners of HLB China listed in this booklet or from the Executive Office in London.

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General Information

LOCATION AND CLIMATE

Situated on the western seaboard of the Pacific Ocean north of the equator, the Asian land mass of the People's Republic of China is as large as the whole continent of Europe, with 1.37 billion people living in 3,745,190 square miles,(9,600,000 square kilometers).

China covers a wide range of climates. The southern cities, such as Shenzhen, are humid and warm throughout the year, while northern cities like Beijing have bitterly cold winters with sub-zero temperatures.

POLITICAL SYSTEM

The People's Republic of China was established on October 1, 1949. China is governed by the State Council, which is the executive organization of the National People's Congress. It is responsible and accountable to the National People's Congress. Under the State Council are various ministries, commissions and other government bureau responsible for work in specialized fields.

LEGAL SYSTEM

The National People's Congress and its Standing Committee are empowered to exercise legislative power. The State Council is also authorized to adopt administrative regulations and measures in accordance with the Constitution and statutes. At the local level, the People's Congresses of the provinces and municipalities directly under the central government may also adopt local regulations, provided they do not contravene the Constitution or state laws.

The People's Courts are the judicial organizations of the state, and the judiciary is able to exercise independent power in

accordance with the law. The Supreme Court is the highest in the land and is responsible to the National People's Congress and its Standing Committee. It supervises the administration of justice by the local people's courts which are established at different levels and are responsible to the organizations of state power that created them. There are also special courts, such as those dealing with military and maritime issues.

FACTS AND FIGURES

Area:	960,000 km ²
Population:	1.37 billion
Capital:	Beijing
Currency (unit):	RMB (yuan)
Language:	Mandarin
Time:	GMT+8

BUSINESS HOURS AND PUBLIC HOLIDAYS

Official working hours are 40 hours per week. Government departments now work a five-day week. The official public holidays in China are as follows:

New Year's day: January 1

Spring Festival Varies: Late January or February, 3 days

Qing Ming Festival: Falling on April 4-6 each year

Labor Day: May 1

Dragon Boat Festival: 5th day of the 5th lunar month

Middle Autumn Festival: 15th day of the 8th lunar month

National Day: October 1,2 & 3

Investment Factors

For foreign investors, China has offered a favourable investment environment for investors from all over the world to invest, manufacture and manage. In recent years, China's infrastructure has been greatly improved, and infrastructure constructions like transport, telecommunication, water, electricity & gas supply and etc. have been basically upgraded and the capacity and quality of energy, raw material and component supply were also obviously improved, providing favourable external production management conditions for foreign investment.

FOREIGN ECONOMIC POLICES

China began the "reform and opening up" policy in December 1978. The aim of China's macro-economic policy is to maintain a steady economic growth, to avoid big economic fluctuations and to enhance the people's living standards. The related foreign investment policies have also been adapted to the requirements of a market economy and international rules. Industrial policy has become an important way for China to control foreign investment. In accordance with the development strategy for the national economy and industrial development, China established comprehensive industrial policies for foreign investment to lead investors to invest in target industries. The Chinese government, in June 2017, issued the newly amended "Catalogue for the Guidance of Foreign Investment Industries," encouraged more foreign investment to flow into target industries, for example, agriculture, resource development, infrastructure construction, export, high-tech and research & technology industry, however, the government has specifically prescribed industries where exclusive foreign-funded enterprises are not allowed and the strategic industries and investment fields where the Chinese must hold a controlling share. In accordance with the commitments to WTO entry,

the extent of the opening of industries will be increased by a large margin. For example, the telecom service industry is to be shifted from the prohibited category into the limitation category, and the geographical area and business scope of finance, insurance, commerce and foreign trade and so on will be further enlarged. The strategy of Western Development has already been carried out in order to develop regional economies harmoniously, and the government has enacted the "Advantageous Industries Catalogue for Foreign Investment in Middle and Eastern Regions" to give preferential policies for foreign investment in these "advantageous" industries.

As for management of international trading, China has greatly reduced customs duties, gradually called off quota and warrant management, and continuously improved the transparency of establishment and implementation of related policies. In addition, foreign exchange controls will also be loosened step by step.

ATTRACTING FOREIGN INVESTMENT

During the past forty years, the Chinese government has made great progress in attracting foreign investments and developing an export-oriented economy. The Chinese government has promulgated various favourable policies for foreign investment and assigned several special regions.

- The favourable policies mainly cover Hi-tech industry, agriculture, forestry, telecommunications, energy, export-oriented sectors.
- The special regions include five Special Economic Zones (SEZ), i.e. Shenzhen, Zhuhai, Xiamen, Shantou and Hainan (Shanghai's Pudong Area is not an SEZ, but is treated in the same way), 14 coastal cities (Beijing city is treated as a coastal city) and 52 state-level hi-tech development zones or hi-tech bases.

- These special regions can provide overseas investors with a more advantageous environment in advanced infrastructures, land and qualified human resources.

PROMOTING FOREIGN TRADE

After China's entry into the WTO, the "reform and opening up" policy has entered a new development stage and China will open to the outside world in an all-round, multi-layered and wide-ranging way. In November 2002, the 16th National Congress of the Communist Party of China (CPC) was held and the new central collective leadership was chosen, which maintained the stability of the national political situation and the continuity of various guidelines and policies; it also safeguarded China's "reform and opening up" for a smooth advance. China has already put forward the grand development goal of building a well-off society in an all-round way. To realize the goal, absorbing foreign investment will exert an important, irreplaceable role. The Chinese government has already completely straightened out and amended related laws and rules and policy-based documents according to the requirements of a market economy and the commitments to WTO agreement, and also has enabled laws and rules and policies to be established openly, impartially, and transparently.

FINANCIAL INSTITUTIONS

The financial institutions in China can be divided into several groups according to their natures as follows:

1. Central bank, the central bank of China is the People's Bank of China (PBOC).
2. Policy Banks, such as State Development Bank, China Agriculture Development Bank and etc.;
3. Commercial Banks

- State-owned Commercial Banks (also called Specialized Banks), such as Industrial and Commercial Bank of China, Agricultural Bank of China, Bank of China, China Construction Bank;
 - Regional Banks and Joint Stock Banks, such as Communication Bank, Ever Bright Bank of China, CITIC Industrial Bank;
 - Co-operative Commercial Banks, such as Urban Cooperate banks, Rural Cooperate banks and etc.;
4. Trust and Investment Companies
 5. Securities Companies
 6. Finance Companies
 7. Leasing Companies
 8. Insurance Companies
 9. Mutual Funds
 10. Sino-foreign Financial Institution and Foreign Financial Institutions

Foreign financial institutions may establish representative offices, branches, subsidiaries and joint ventures in approved areas upon the approval of the PBOC. The activities of foreign banks are supervised by the PBOC and restricted in foreign currency deposit-taking and lending. Foreign banks should obtain special approval to engage in RMB business.

FOREIGN EXCHANGE CONTROL

The RMB is not a freely convertible currency now, and the foreign exchange rate system is a controlled floating one on the basis of market demand by the State Administration of Foreign Exchange (SAFE). On December 1, 1996, China announced its acceptance of Article 8 of the International Monetary Fund, that is, RMB could be freely converted under current account.

The major policies and regulations of foreign exchange control on Foreign Invested Enterprises (FIEs) are as follows:

1. APPLYING FOR FIE'S EXCHANGE CONTROL REGISTER

Within 30 days from the issuance of business license, FIE's should apply for an Exchange Control Register from the local administration on foreign exchange control.

2. OPENING A FOREIGN CURRENCY ACCOUNT

FIEs should choose a bank that has the right to undertake foreign currency operations to open their foreign currency account. The government will mainly control the inflow and outflow of FIEs' foreign currency under current account, the use and settlement of foreign currencies under capital account, its deposit and loans denominated in foreign currencies.

SECURITY MARKETS

China has 2 formal security exchanges, one is the Shanghai Security Exchange, and the other is the Shenzhen Security Exchange. All listing and trading of securities are operated in these 2 security exchanges.

An Initial Public Offering (IPO) in the domestic market has 2 forms, one is in A shares, which is denominated in RMB and bought by domestic investors, the other is in B shares, which is denominated in foreign currencies for foreign investors. For IPOs in foreign markets, there are H shares in the Hong Kong Security Exchange, N shares in the New York Security Exchange and S shares in the Singapore Security Exchange and etc.

The most important institutions related to securities are as follows:

- Securities Committee of State Council of securities regulation to formulate such policies as the number of enterprises allowed to list and their IPO volumes allowed.
- Chinese Securities Regulatory Commission (CSRC), the executive body of SCSC in charge of drawing up regulations and guidelines.
- Security Transaction Executing Commission, the consulting agency for CSRC.

INSURANCE MARKET

The Chinese insurance market is now opened not only to domestic companies but also to foreign companies. There are several national-wide insurance companies as well as regional ones. Types of insurance companies include state-owned, joint stock and sino-overseas joint ventures.

Employment Regulations

LEGISLATION OF EMPLOYMENT

The Labor Contract Law of the People's Republic of China was adopted at the 28th Session of the Standing Committee of the 10th National People's Congress of the People's Republic of China on June 29, 2007 and is hereby promulgated and effective as of January 1, 2008. This Law is formulated to improve the labor contract system, specify the rights and obligations of both parties to labor contracts, protect the lawful rights and interests of employees and establish and develop a stable and harmonious labor relationship.

SOCIAL WELFARE AND SECURITY

Pursuant to The Tentative Ordinance on Collection and Payment of Social Insurance Premium promulgated on January 22, 1999, The employers and individual payers which/who are referred to in this Ordinance are obliged to pay the basic endowment insurance, basic medical insurance and unemployment insurance (hereinafter collectively referred to as the "Social Insurance") in accordance with the relevant laws, administrative regulations and rules set by the State Council.

The payments made and the number of funds to which payments must be made by a foreign investment enterprise vary according to location, as the Governments of provinces, autonomous regions and municipalities may, based on the actual situation of the locality, include urban self-employed entrepreneurs as payers of basic endowment insurance and basic medical insurance, and may include social organizations and their full-time staff, private non-enterprise units and their employees as well as urban self-employed entrepreneurs and their employees into payers of unemployment insurance.

Employers shall make a social insurance registration with the local Social Insurance Agency. The items to be registered shall include: name, residence, place of business, type of the unit, name of the legal representative or principal, bank account number as well as other items required by the labor and social security departments under the State Council.

Different provinces have different local social welfare contribution scheme, Suggest to consult HLB member firms to understand local policies of social welfare scheme and assess the impact to the business.

EMPLOYMENT CONTRACTS

An employer has established labor relationships with employees from the date of use of labor services. The employer shall establish a register of employees for inspection.

An employer shall lawfully establish and improve rules and systems, protect the labor rights enjoyed by employees and perform labor obligations. Where an employer formulates, amends or decides on rules and systems that are directly related to the personal benefits of employees or important matters such as labor rules and systems, working hours, rest days, labor safety and health, insurance benefits, employee training, labor discipline and labor quota administration, it shall hold a discussion with an employees' assembly or all employees, submit proposals and give suggestions and determine the issue following fair consultation with labor unions or employees' representatives.

In the process of decision-making and implementation of rules and systems and important matters, where a labor unions or employee deems it improper, they shall have the right to raise the issue with employers and amendments and improvements shall be made through consultation. The employer shall

publicly announce the rules and systems that are directly related to the personal benefits of employees or the decisions on important matters, or inform the employees of such rules, systems and decisions.

ALTERNATIVE EMPLOYMENT CONTRACT

Labor contracts are divided into labor contracts with fixed terms, labor contracts with unfixed terms and labor contracts where the term of service equals to the period of completion of a certain task.

Labor contracts with fixed terms shall refer to labor contracts the termination date of which is agreed between employer and employees.

Labor contracts with unfixed terms shall refer to labor contracts the termination date of which is not agreed between employers and employees.

In any of the following circumstances where the employee requests or agrees to renew or conclude labor contracts, the labor contract with unfixed terms shall be concluded unless employees request the conclusion of a labor contract with fixed terms:

1. The employee has been working with the employer for 10 consecutive years;
2. Where the employer implements the labor contract system for the first time or labor contracts are re-concluded due to restructuring of state-owned enterprises, the employee has been working with the employing unit for 10 consecutive years and there is less than 10 years before the statutory retirement age; or
3. Where a labor contract with fixed terms has been concluded for two consecutive times and no labor contract is renewed for employees that do not fall within the circumstances specified.

Where the employer fails to conclude a written labor contract with an employee from one year of the use of labor services, a labor contract with unfixed terms shall be deemed to have been established between the employing unit and the employee.

WORK PERMITS

Work permits are certificates proving the identity of enterprise workers.

Since China adopted its opening up policy joint ventures, sino-foreign cooperatives and foreign-funded enterprises (collectively, foreign-invested enterprises) have been set up. In general, these enterprises have some employees from foreign countries (or Hong Kong, Macau or Taiwan) as official staff.

Foreign employees of foreign-invested enterprises shall be provided with the same work permits as those required by Chinese employees. Work permits for foreign workers are only valid for their participation in the activities of their own enterprises or connected production and business activities, and may not be used as substitutes for passports or for residence or travel documents.

Types of Business Organizations

The principal forms of business enterprise open to foreign investors in China are classified under the following headings.

1. Foreign invested enterprises ("FIEs"):

"Foreign invested enterprises" refers to equity joint ventures, cooperative joint ventures with limited liability, wholly foreign-owned enterprises, and foreign invested companies limited by shares.

a) Wholly foreign-owned enterprises ("WFOE"):

Wholly foreign-owned enterprises are established exclusively with the foreign investor's capital. They are limited liability companies, the profits and losses of which are borne solely by the foreign investor;

b) Equity joint ventures:

An equity joint venture is a separate legal entity and takes the form of a limited liability company registered in China. The partners have joint management of the company, and the profits and losses are distributed according to the ratio of each partner's capital contribution;

c) Cooperative joint ventures:

A cooperative joint venture may operate under a structure similar to that of a Western-style partnership, or the parties to the venture may apply for approval to have the company structured as a separate legal entity with limited liability. The profit and loss distribution ratio is defined in the contract and can vary over the contract term;

d) Joint stock companies:

Joint stock companies, also known as companies limited by shares, are established primarily in order to be able to list on Chinese or foreign stock markets. The capital stock of a joint stock company is made up of equal-value shares. Contributions are made by both domestic and foreign shareholders.

2. Foreign enterprises:

In general, foreign enterprises are enterprises other than foreign investment enterprises in China that have establishments or places of business in China and engage in production or business operations. Foreign enterprises that do not have establishments or places of business in China but derive certain China-source income are also included in this category. Foreign enterprises include representative offices, places for the exploitation of natural resources, contracted project sites, and companies providing labor services or employing business agents.

3. Branches of foreign enterprises:

Under the Company Law, a foreign company may establish branches in China. A branch does not have the status of a Chinese legal person, and the foreign company assumes the civil liabilities of its branches in China. However, only foreign banks have been granted licenses to open branches. Conditions for setting up a branch of a foreign company and any applicable limitations will be set out when the implementation regulations of the Company Law are issued.

Foreigners are able to become legal representatives or directors of Chinese companies.

LEGAL, ACCOUNTING AND AUDITING REQUIREMENTS Accounting and Reporting

A FIE is required to maintain a complete accounting system and prepare financial statements. Three kinds of primary accounting books should be set up, namely, journals, general ledger and subsidiary ledgers and their

supporting documents. Computerized accounting records are also allowed. All supporting documents, accounting books and financial statements should be prepared in Chinese. However, a foreign language can also be adopted along with Chinese. Generally, RMB is adopted as the base bookkeeping currency. If a foreign currency is used, the financial statements must be converted into RMB at the year-end. In China, the accounting year is the calendar year, i.e., January 1 to December 31. However, if a FIE experiences difficulties in computing its taxable income according to the calendar year, another fiscal year is also allowed upon the approval of tax authorities. Enterprises that commence business in the middle of a year or have operated for less than 12 months in a tax year may treat the actual operating period as a tax year. The accounting system is based on the accrual basis instead of the cash basis.

Auditing

A FIE is required to appoint a Chinese CPA firm to audit its annual financial statements, accounting records and to issue an auditor's report. All vouchers, accounting records and financial statements should be provided to the auditors. The statutory annual audit of a FIE's financial statements is mainly for the purpose of the tax authorities. The annual financial statements and auditor's report should be filed within 5 months after the end of the year.

OTHER BUSINESS ARRANGEMENTS OPEN TO FOREIGN INVESTORS

To acquire foreign technology, equipment and know-how, China utilizes different methods of attracting foreign investment. In addition to the forms of business enterprise mentioned above, these include barter trade, compensation trade and processing arrangements.

Barter Trade

Under barter trade arrangements, China will import machinery, equipment or foodstuffs in exchange for other products. Successful dealings have occurred principally with Japan under this type of trade agreement, since China has a surplus of coal, which is in great demand in Japan.

Compensation Trading

Under a compensation trade arrangement the foreign trade partner will supply China with equipment, technical services and raw materials where needed, receiving the manufactured product as payment. Factory premises are provided by the Chinese, built to foreign specifications, and a stable workforce is guaranteed to produce goods at reasonable prices under the supervision of the foreign firm's representatives. China is paid for the processing costs (mostly labor charges expressed as a processing fee), the fee being substantially discounted and then applied against the initial cost of the equipment. China later becomes the owner of the equipment, and thereafter the full processing fee is charged.

Large-scale compensation trade involves the supply by foreign firms of technology, equipment and the materials necessary for key construction projects undertaken by the state. The foreign firms' contributions will be repaid in the form of products produced by the enterprises, once they have been constructed. Negotiations for large-scale compensation trade are handled by related Chinese ministries and state commissions.

Medium and small-scale compensation trade also involves the supply of technology, equipment and necessary materials to Chinese enterprises other than those key projects undertaken by the state. The foreign firms' contributions are paid for in products turned out by the enterprises, including textiles and other products of light industries, such as mechanical and electrical products, ores

produced by locally run medium-size and small mines, and agricultural and rural sideline produce. Foreign applicants for medium- and small-scale compensation trade in China can negotiate with the import and export administrations, foreign trade bureaus or industrial bureaus of the provinces, municipalities, and autonomous regions.

Processing and Assembling Trade

The processing and assembling trade constitutes a form of cooperation in which foreign firms place orders with Chinese factories to carry out certain manufacturing activities for export. These activities generally consist of processing or assembling commodities according to the foreign firm's specifications, with the parts or semi-processed items supplied by the foreign firm. The advantages of foreign processing and assembling businesses are that they do not require Chinese enterprises to make sizable investments, use scarce foreign exchange or buy costly equipment. Increased pressure from domestic sales and exports has created shortages in raw and semi-finished material, components and spare parts.

The main activities of the processing and assembling trade are concentrated in the coastal cities in the Pearl River delta region, Fujian province and Yangtze River delta region. In order to encourage and facilitate the development of the processing and assembling trade, materials and components imported for processing and assembling products for export are exempt from customs duties.

Taxation

GENERAL

The main taxes applicable to foreigners, foreign investment enterprises and foreign corporations doing business in China are as follows.

1. Taxes on Income:
 - Corporate Income Tax
 - Individual Income Tax ("IIT")
2. Taxes on transactions
 - Value-Added Tax
 - Consumption Tax
3. Other Taxes
 - Customs duties
 - Stamp tax
 - Vehicle and vessel tax
 - Motor vehicle acquisition tax
 - Deed tax
 - Land appreciation tax
 - Resources tax
 - Cultural business construction fee
4. Taxes on Property
5. Local Levies

Tax Legislation Structure

For the time being, State Organizations having authority to formulate tax laws or tax policy mainly include the National People's Congress and its Standing Committee, the State Council, the Ministry of Finance, the State Administration of Taxation, the Tariff and Classification Committee of the State Council, and the General Administration of Customs.

- a) Tax laws are enacted by the National People's Congress, e.g., the Individual Income Tax Law of the People's Republic of China; or enacted by the Standing Committee of the National People's Congress, e.g., the Tax Collection and Administration Law of the People's Republic of China.
- b) The administrative regulations and rules concerning taxation are formulated by the State Council, e.g., the Detailed-Regulations for the

- Implementation of the Tax Collection and Administration Law of the People's Republic of China, the Detailed Regulations for the Implementation of the Individual Income Tax Law of the People's Republic of China, the Provisional Regulations of the People's Republic of China on Value Added Tax.
- c) The departmental rules concerning taxation are formulated by the Ministry of Finance, the State Administration of Taxation, the Tariff and Classification Committee of the State Council, and the General Administration of Customs, e.g., the Detailed Regulations for the Implementation of the Provisional Regulations of the People's Republic of China on Value Added Tax, the Provisional Measures for Voluntary Reporting of the Individual Income Tax.

The laws of China stipulates that within the framework of the national tax laws and regulations, some local tax regulations and rules may be formulated by the People's Congresses at provincial level and their Standing Committee, the People's Congresses of minority nationality autonomous prefectures and the People's Governments at provincial level.

CORPORATE INCOME TAX

The 10th National People's Congress passed the new Corporate Income Tax Law ("New Law") on 16 March 2007. The New Law provides a single income tax regime for both domestic and foreign investment enterprises ("FIEs"). The New Law took effect on 1 January 2008.

New CIT Rate

The new standard corporate income tax ("CIT") rate is 25%. The reduced CIT rate of 20% would apply to small-scale and thin-profit enterprises and the preferential CIT rate of 15% is only available to high / new technology enterprises which require support from the State.

Taxpayers

The New Law introduces the concepts of "tax resident enterprise" and "non-tax resident enterprise" to differentiate taxpayers:

Taxpayers	Definition	Taxable Income
Resident Enterprise	Established in China under PRC laws Established under foreign laws but has its place of effective management in China	Worldwide income
Non-resident Enterprise	Established under foreign laws, and has its place of effective management outside China	China-sourced income

Foreign enterprises established outside China without a "substantive presence" in China will need to determine whether their place of effective management is based in China.

CIT Preferential Policies

The New Law grants tax preferential treatment on an industry basis rather than on a location basis. The main tax preferential policies in the New Law include:

- "Encouraged" high-tech enterprises are eligible for a reduced 15% CIT regardless of location in China;
- CIT exemption / reduction remains for specific technology transfer and investments in infrastructure, agriculture, forestry, animal husbandry and fishery industries;
- "Super deduction" is allowed for R&D expenses and salary expenses for employment of handicapped workers;
- CIT credit is granted to specific venture capital enterprises and investments in environmental protection, energy, water conservation and specific safety equipment.

Tax Base

Enterprises with foreign investment with their head office in China pay income tax on their world-wide income. Foreign enterprises pay income tax only on their income derived from sources within China.

The income tax base for enterprises with foreign investment and foreign enterprises is the taxable income which is the amount remaining from its gross income in a tax year after allowable deductions for costs, expenses and losses.

Any foreign enterprise which has no establishment or place in China but derives income of profits interest, rental, royalties and other income from sources within China or which, though it has an establishment or place in China, its said income is not effectively connected with such establishment or place, is taxed on the basis of the gross amount of such income.

Withholding Tax Rate

The New Law provides a flat 20% tax rate for dividends, interest, royalties, rentals, capital gains or other income derived by non-resident enterprises from sources in China.

- If there is a tax treaty concluded between China and the country of which the investor is a tax resident, withholding tax rate on divided remittance would be reduced to 10% in most cases (Hong Kong and Singapore company is taxed at 5%) and
- Withholding tax on other income, e.g. interest, royalties and capital gains, would continue to be reduced to 10%.

INDIVIDUALS

Individual Income Tax

Foreign individuals residing in the PRC for less than one year are subject to IIT on their PRC sourced income only. Remuneration from foreign employers to individuals working in the PRC is exempt from tax if the individual resides in the PRC for less than 90 days in a calendar year, provided that the remuneration is not borne or paid by an establishment in the PRC. This 90-day period may normally be extended to 183 days if the individual is entitled to protection under a relevant tax treaty/tax arrangement.

Employees of foreign employers can reduce their IIT liability and be taxed based on the actual number of days residing in the PRC if certain criteria are met.

Individuals who do not domicile in the PRC but reside in the PRC between one to five years may, with approval, pay tax only on their PRC sourced income and non-PRC sourced income, the payment of which is borne by PRC establishments. They will be taxed on their worldwide income for each full year residing in the PRC from the sixth year onward.

Individual Income Tax Rates for Employment

Income from wages and salaries is taxed according to the following progressive rates, ranging from 3% to 45%:

Grade	Monthly Taxable Income *	Tax Rate (%)	Quick Deduction
1	Income of 1,500 yuan or less	3	0
2	That part of income in excess of 1,500 to 4,500 yuan	10	105
3	That part of income in excess of 4,500 to 9,000 yuan	20	555
4	That part of income in excess of 9,000 to 35,000 yuan	25	1,005
5	That part of income in excess of 35,000 to 55,000 yuan	30	2,755
6	That part of income in excess of 55,000 to 80,000 yuan	35	5,505
7	That part of income in excess of 80,000 yuan	45	13,505

* Monthly taxable income is calculated after a monthly standard deduction of RMB3,500. For foreign individuals working in China (including residents of Hong Kong, Taiwan and Macau), the standard monthly deduction is RMB4,800.

Where and individual's income tax liability is borne by the employer, the tax liability is calculated on a grossed-up basis and an adifferent tax rate table will be used to reflect the tax-on-tax effect.

Employment Income

For IIT purposes, taxable income refers to "wages, salaries, bonuses, year-end bonus, profit share, allowances, subsidies or other income related to job or employment".

Certain employment benefits for foreign individuals could be specifically treated as not being taxable under the IIT law if certain criteria can be met. These include:

- employee housing cost (with supporting invoices) borne by an employer;
- reasonable home leave fares of 2 trips per annum for the employee (with supporting invoices);
- reasonable employee relocation and moving costs (with supporting invoices); and
- reasonable reimbursement of certain meals, laundry, language training costs and children's education expenses in the PRC (with supporting invoices).

any cash allowance paid to cover expected work-related expenditures (such as an entertaining or travel allowance) will be fully taxable to an employee. iit may be reduced by reimbursing specific work-related expenses incurred by an employee (which may include entertainment, health or social club fees, local travel, newspapers and journals, telephone costs, etc.) instead of paying an allowance. the expense reimbursement may not be subject to iit if prescribed administrative procedures are followed.

Income Other than Employment Income

Privately owned business; sole proprietorship enterprises; business on a contract or lease basis

Income earned by individuals from privately-owned businesses, sole proprietorship enterprises or from the operation of a business on a contract or lease basis is generally subject to IIT at progressive rates from 5% to 35%.

The 35% marginal rate applies to annual taxable income (gross revenue less allowable costs, expenses and losses) over RMB 100,000.

Author's remuneration

Such income is taxed at a flat rate of 20%, applied to 70% of the taxable income.

Income from labour services

Such income is taxable at 20% if the taxable income (after allowable deductions) from a single payment does not exceed RMB20,000; 30% for the portion over RMB20,000 but not exceeding RMB50,000; and 40% for the portion exceeding RMB50,000.

Income from interest, dividend, transfer of property, royalty income, rental income and other income

Such income is normally taxed at a flat rate of 20%. However, IIT may be reduced or exempted for certain income meeting certain prescribed conditions.

Allowable deductions

There are specific and complex tax rules to address the deductions available for income derived from the operation of privately-owned business, sole proprietorship enterprises and from the operation of a business on a contract or lease basis. Certain deduction caps are similar to those applicable to companies that are subject to corporate income tax. In addition, a monthly deduction of RMB3,500 is allowed to be deducted from the net income derived from these businesses.

The following deductions are provided for income labour services, author's remuneration, rental income, and royalty income;

■ If the amount received in a single payment is not more than RMB4,000, a standard deduction of RMB800 is allowed;

■ If the amount received from a single payment exceeds RMB4,000, a deduction equal to 20% of the payment is allowed.

For transfer of property, the original cost plus reasonable expenses are deductible.

No deduction is allowed against income from interest, dividend or other income.

Tax Filing and Payment

IIT is normally withheld from wages or salaries by employers and paid to the tax authorities on a monthly basis. Individual income tax returns must be filed within 15 days following the end of each month.

Annual IIT Self Reporting Requirement

Starting from 1 January 2007, individuals under four circumstances are required to perform annual self-IIT reporting with the PRC tax authorities. Foreign individuals may be exempted from this obligation in certain situations.

VALUE-ADDED TAX (VAT)

VAT is levied on the increased value of commodities at different stages of production or circulation, or on the value-added of commodities. All enterprises and individuals engaged in the sale or import of goods or the provision of processing, repair or maintenance services in China have to pay VAT. There are four main VAT rates in China: a basic rate of 17 per cent, three lower rates of 13 per cent, 11 per cent and 6 per cent. For taxpayers that export goods, the tax rate shall be zero, except as otherwise provided by the State Council.

Taxpayers

VAT taxpayers include any enterprise, unit and other individual engaged in sales of goods, importation of goods, provision of services of processing, repairs and replacement (hereinafter referred to as 'taxable services' in short) within the territory of the People's Republic of China.

VAT payers are divided into general taxpayers and small-scale taxpayers. A general taxpayer pays the excess amount of output VAT over input VAT. A small-scale taxpayer's liability is calculated using a simplified method based on the sales value without offset or deduction for input VAT. The basic rate at which value-added tax is levied on small-scale taxpayers shall be 3%, and a transitional rate is 5%. Any adjustments to the leviable rate shall be determined by the State Council.

Taxable Items and Tax Rates

Table of VAT Taxable Items and Rates

Coverage of collection	Rates
Exportation of goods (except otherwise stipulated by the State)	0%
(1) Value added tele-communication; (2) Financial and insurance businesses; (3) Modern service industry; (4) Life service industry; (5) Sales of intangible assets (other than transfer of the right to the use of the land).	6%
(1) Communications and transportation; (2) Post; (3) Basic tele-communication; (4) Construction; (5) Leasing of immovable properties; (6) Sales of immovable properties; (7) Transfer of the right to the use of the land;	11%
(1) Food grains and edible vegetable oils; (2) Tap water, heating, air conditioning, hot water, coal gas, liquefied petroleum gas, natural gas, methane gas, and coal/charcoal products for household use; (3) Books, newspapers, and magazines; (4) Feeds, chemical fertilizers, agricultural chemicals, agricultural machinery and covering plastic film for farming purposes; and (5) Other goods specified by the State Council.	13%
Goods other than those listed above, services of providing processing, repairs and replacement services, and leasing of tangible moveable property.	17%

Computation of Tax Payable

a. General taxpayers

To compute the VAT payable, general taxpayers need to separately calculate the output tax and the input tax for the current period. Then the difference between the output tax and the input tax shall be the actual amount of VAT payable or refundable in the case of exporters.

The formula for computing the tax payable is as follows:

Tax payable = Output tax payable for the current period - Input tax for the current period deductible input VAT from previous periods, or
Tax refundable = Input tax for the current period - Output tax payable for the current period

Output tax payable = Sales amount in the current period × Applicable tax rate

b. Small-scale taxpayers

A simplified method for calculating tax payable on the basis of sales amounts and leviable rates shall apply to small-scale taxpayers engaged in the sales of goods or taxable services. The formula for calculating such tax payable is as follows:

Tax payable = Sales amount × leviable rate

The criteria for small-scale taxpayers shall be specified by the competent authorities for financial and taxation affairs under the State Council.

Tax Exemptions

The following items shall be exempt from value-added tax:

1. Self-produced agricultural products sold by agricultural producers;
2. Contraceptive medicines and devices;

3. Antique books;
4. Instruments and equipments imported to be directly used in scientific research, scientific experiments and educational activities;
5. Materials and equipment imported from foreign governments and international organizations as free assistance;
6. Articles imported directly by organizations for the disabled for special use by the disabled; and
7. Self-used goods which are sold.

Except as provided in the preceding paragraph, items to which value-added tax exemption and reduction is applicable shall be specified by the State Council. No region or authority shall specify any item to which value-added tax exemption and reduction is applicable.

CONSUMPTION TAX

Taxpayers

The taxpayers of Consumption Tax include all enterprises, units, household businesses and other individuals engaged in production or importation of taxable consumer goods within the territory of the People's Republic of China and sales of taxable consumer goods as determined by State Council. Taxable consumer goods exported by the taxpayers are exempt from Consumption Tax, unless the taxable consumer goods are restricted by the State from exportation.

Taxable Items and Tax Rates

Table of Consumption Tax Taxable Items and Rates

Category Number	Taxable items	Tax rates (tax amount)
1.	1.1 Tobacco (1) Grade A Cigarettes (2) Grade B Cigarettes 1.2 Cigars 1.3 Cut tobacco	56% plus RMB0.003/each pc 36% plus RMB0.003/each pc 36% 30%
2.	Alcoholic drinks 2.1 white spirits made from cereal 2.2 yellow spirits 2.3 beer (1) Grade A beer (2) Grade B beer 2.4 other alcoholic drinks	20% plus RMB0.5 per 500g(500ml) RMB240 per tonne RMB250 per tonne RMB220 per tonne 10%
3.	Cosmetics	30%
4.	Precious jewellery, pearls, precious jade and stones 4.1 Gold and silver jewellery 4.2 Other jewellery, pearls, precious jade and stones	5% 10%
5.	Firecrackers and Fireworks	15%

6.	<p>Refined oil</p> <p>6.1 Gasoline</p> <p>(1) Leaded petrol</p> <p>(2) Unleaded petrol</p> <p>6.2 Diesel oil</p> <p>6.3 Aviation kerosene</p> <p>6.4 Naphtha</p> <p>6.5 Solvent oil</p> <p>6.6 Lubricants</p> <p>6.7 Fuel Oil</p>	<p>RMB 1.40 per litre</p> <p>RMB 1.00 per litre</p> <p>RMB 0.80 per litre</p> <p>RMB 0.80 per litre</p> <p>RMB 1.00 per litre</p> <p>RMB 1.00 per litre</p> <p>RMB 1.00 per litre</p> <p>RMB 0.80 per litre</p>
7.	<p>Motorcycles</p> <p>7.1 cylinder capacity within 250ml</p> <p>7.2 cylinder capacity above 250ml</p>	<p>3%</p> <p>10%</p>
8.	<p>Motor cars</p> <p>9.1 Passenger cars</p> <p>(1) Those with a cylinder capacity (i.e. emission capacity) of less than 1,000ml (including 1,000ml)</p> <p>(2) Those with a cylinder capacity of between 1,000-1,500 ml (including 1,500 ml)</p> <p>(3) Those with a cylinder capacity of between 1,500-2,000 ml (including 2,000 ml)</p> <p>(4) Those with a cylinder capacity of between 2,000-2,500 ml (including 2,500 ml)</p> <p>(5) Those with a cylinder capacity of between 2,500-3,000 ml (including 3,000 ml)</p> <p>(6) Those with a cylinder capacity of between 3,000-4,000 ml (including 4,000 ml)</p> <p>(7) Those with a cylinder capacity of more than 4,000ml</p> <p>9.2 Middle Business Vans</p>	<p>1%</p> <p>3%</p> <p>5%</p> <p>9%</p> <p>12%</p> <p>25%</p> <p>40%</p> <p>5%</p>
9.	Golf balls and equipment	10%
10.	Luxurious watches	20%
11.	Yachts	20%
12.	Wooden one-off chopsticks	5%
13.	Wooden floor boards	5%
14.	Battery	4%
15.	Paint	4%

Computation of Tax Payable

The computation of Consumption Tax payable shall follow the ad valorem principle, quantity-based principle or combined principle. Generally, the producers of taxable consumer goods are the taxpayers and the Consumption Tax shall be paid on sales of the goods by the producers. The computing formula is:

- a. Tax payable = sales amount of taxable consumer goods × applicable tax rate
 - b. Tax payable = sales volume of taxable consumer goods × tax amount per unit, or
 - c. Tax payable = sales amount of taxable consumer goods × applicable tax rate + sales volume of taxable consumer goods × tax amount per unit
- Imported taxable consumer goods to which the ad valorem method is applied in computing the tax payable shall be assessed according to the composite assessable price and the applicable rate.

Special note: The commentary in this booklet does not cover taxes levied in Hongkong and Macau which become Special Administrative Regions of the PRC on July 1, 1997 and December 20, 1999 respectively. Hongkong and Macau continue to retain their own tax systems and the taxes applicable in Mainland China do not apply in Hongkong and Macau.

OTHER TAXES

The business environment in China is unique. Foreign investors are also subject to various tax obligations depending on the business scope and operation activities, such as customs duties, stamp tax, vehicle and vessel usage tax, motor vehicle acquisition tax, deed tax, land appreciation tax, resources tax, taxes on property and local levies, etc. Please consult HLB China's business and tax advisers who have special experience of the business environment in China and will meet your business and tax advisory needs.

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