Wang Jing & Co.
敬海律师事务所
www.wjnco.com

Legal Newsletter
法律资讯

Issue 2 – February 2006

Executive Summary

Setting Up a Business in Guangdong – How to Choose Your Location? (p.2)

One key challenge when establishing a subsidiary in China is the place of investment. Not only is it relevant in which part of the country you are – in the north, the east or the south – but within a region, in which municipality, district or zone you want to be. What are the most important factors to take into consideration?

Author: Mr. Antoine Loubier

China Amends Individual Income Tax Law (p.4)

The amendment of China's *Individual Income Tax Law* will have considerable consequences for both employers and employees when calculating their income tax duties. Most importantly, the tax-free part of a salary has been increased from RMB 800 to RMB 1,600, decreasing the tax burden especially for medium- and low-income earners.

Author: Ms. Zheng Xin

Wang Jing & Co. News (p.6)

The Firm has been nominated for three awards at the ALB China Law Awards 2006, and also is proud to introduce two experienced professionals who have recently joined: intellectual property consultant and patent agent Mr. Peng Kai, and Mr. Zhou Zhiyong, associate focusing on logistics-related corporate legal affairs.

Editor	Mr. Wang Jing	(+8620) 87600085
Editorial manager	Mr. Maarten Roos	(+8620) 87690606

Add: 14th Floor, South Tower, World Trade Centre,
371-375 Huanshi East Road, Guangzhou 510095, P.R. China
Tel: (+8620) 87600082
Fax: (+8620) 87784482 / 87692221
Email: info@wjnco.com
Website: www.wjnco.com
Newsletters: www.wjnco.com/en/newsletter.htm
Guangzhou--Shanghai--Tianjin--Qingdao--Xiamen--Haikou (back cover)

Setting Up a Business in Guangdong – How to Choose Your Location?

[This article was contributed by Mr. Antoine Loubier, South China Representative of French law firm ADAMAS, and was originally published in Connexions No 29,*the business magazine of the French Chamber of Commerce in China.]*

Where to set up your business? A tricky question for the foreign investor wishing to set up a business in Guangdong Province. Should an "official" zone be chosen?

Since Deng Xiaoping's tour of the south of China in 1992 and his famous speech in Shenzhen, it would seem that the exceptional character of the "zones" has started to fade. The foreign investor might query the interest of the "zones" due to the proliferation of zones with different statutes, the standardization of special tax regimes and the economic development of Guangdong Province that presently offers, in all its big cities, infrastructures with standards as high as in most of the developed zones.

Some selection criteria can nevertheless be offered to help resolve the location consideration. Should the business be set up in a zone or not is a weighty decision that could have serious consequences once the business is set up.

Guangdong Has 23 Official Zones in 14 Municipalities.

(1) Six categories of "zones" have been set up by the Chinese government, these are:

Five categories set up by the central government including the **"*Economic Technological Development Zones*" (ETDZ)** aimed at attracting industrial investors, the **"*New/High Tech. Industrial Development Zones"* (HIDZ)** for the development of Chinese high technology, and the **"*Special Economic Zones*" (SEZ)** aimed at attracting foreign investors within a broad scope. There are also the **"*Export Processing Zones*" (EPZ)** and the « ***Free Trade Zones*" (FTZ)** set up to enhance Chinese exports and in general international commerce. Of the Guangdong zones approved by the State Council, five zones are situated in **Guangzhou**[1] and five in **Shenzhen**[2]; two zones - FTZ and HITDZ - are situated in **Zhuhai,** and three HITDZ zones in **Foshan, Zhongshan** and **Huizhou** respecrtively.

Furthermore, **« *Economic Development Experimental Zones* »,** with approved at provincial level have been established in Jiedong, Jieyang, Jianjiang, Maoming, Nao'ao, Qingyuan, Wuhuan and Chaozhou.

(2) A varying degree of zone development and setting up conditions undergoing standardization:

Despite the attractiveness of these zones multiplying along the Pearl River Delta, the success of all these zones remains very unequal. Quite a large number of zones have not really taken off mainly due to the fact that in practice the zone cannot offer the range of services and infrastructure necessary to give advantages in industrial operation or international commerce. This has not been helped by the language barriers. It is recommended that

[1] *The « Guangzhou Development District » which regroups the GETDD, GHITD, FTZ, EPZ and the « Nansha Developpment zone »*

[2] *"Shenzhen EPZ", "Shenzhen Futian FTZ", "Shenzhen Shatoujiao FTZ", "Shenzhen Yantian Port FTZ" and « Shenzhen high technology Park »*

potential investors visit a variety of zones, including the most well known ones, to speak to foreign companies already working there.

In spite of being aware of this lack of services, the investor may nevertheless base his choice on a zone's tax exemption offer, an incentive often promoted by the zone's economic development department (or even development company) as the "be all and end all". However, it must be noted, <u>that whatever the location, the setting-up conditions and the tax incentive policies are very similar</u> as they should, in principle, be limited to the application of the central government's tax incentive policies.

<u>Essential Criteria for Setting Up a Business:</u>

The choice of location must take into account several criteria from the outset, including long-term goals. A hasty decision can lead to serious financial or operational difficulties. If these are insurmountable, the only solution is moving the business, which would entail costly and heavy administrative procedures.

(1) First criterion: operational requirements.

A study of the operational requirements of the project (infrastructure, equipment, services, energy supply and potential for increase, etc.) constitutes the principal selection criterion of the location consideration. These aspects of the project are necessarily studied (at least partially) in the *feasibility study report* submitted to the approval authorities. However, it is recommended that a thorough study of these requirements be carried out for commercial as well approval reasons.

In the case of companies whose operations cross several sectors (such as industrial and local or international commerce), the setting up of branches, storage locations, sales or administrative offices, in other locations in order to be respond to new requirements, still remains possible, without necessarily having to reconsider the initial production site choice.

(2) Second criterion: the setting up conditions practiced by the local authorities.

The numerous legal texts concerning foreign investment, promulgated on a national level since the beginning of the 1980s, leave very little legal room for maneuver by local authorities. The latter have little power to loosen or tighten any legal regulations passed down from Beijing. The same goes for the principal setting up conditions: type of setup, capital constitution, particular license requirements, etc.

However, in this country of age-long traditions, administrative practices have over the last few years had difficulty in following the rapid changes in the national legal framework. The foreign investor is often confronted by requirements that can be very constraining, and that can affect the legal or operational balance of the investment as it was initially conceived. In contrast, as mentioned in the Chinese press in 2004, some local authorities, preoccupied by economic development, were tempted to approve certain projects, such as real estate operations, that went against the regulations on a national level.

Generally speaking, and in particular for investment projects in small municipalities, the foreign investor would be wise to check that the setting up conditions and the advantages (often tax related) that he is offered are completely within the legal framework set out. With this in mind, setting up a business in an official zone that clearly states the setting up conditions and that has an approval commission for projects would seem safer and would facilitate the setting up procedures.

Whatever the reason and wherever the location, any tax advantages or approval for projects outside of the legal framework will always remain susceptible to reconsideration at any moment, putting the investor in a difficult situation.

It is therefore essential to get in contact at an initial stage with the main authorities of the locations in question to find out how they interpret the national laws and their eventual procedures in these cases. It is advisable to check the legal aspects of the project.

Conclusions

The zones approved by the Chinese government can certainly be of interest to foreign investors on condition that they fulfill all of the project's operational requirements for the business set up. The legal conditions are in principal clearly stated and the procedure for approving projects facilitated by each zone's own approval commission. However, the fiscal policies must be in line with the laws in application.

In the context of Guangdong's rapid economic development, there have been local government or private project initiatives aimed at offering foreign investors an alternative to setting up their business in the "zones"

The European Park set up in the Xiaolan Municipality, inaugurated in 2003, is a good example. In 2003-2004, more than 10 French SME's were set up in this developing 12 hectare "high-tech zone", situated between Guangzhou and Zhuhai.

This formula was developed in response to experience gained on the ground: the necessity to be able to offer foreign investors the complete range of services enabling the delivery, after several months of incubation, of an operational business. The accompaniment starts with project validation, complete assistance of the financial and legal part of the project, personnel recruitment, up to the operational launch of the business.

Antoine Loubier
ADAMAS

China Amends Individual Income Tax Law

The *Individual Income Tax Law of P.eople's Republic of China* was revised for the third time and adopted at the 18th session of the Standing Committee of the 10th National People's Congress of the People's Republic of China on 27 October 2005 and came into force as of 1 January 2006. On 19 December 2005 the State Council promulgated the *Regulations for the Implementation of the Individual Income Tax Law*, which took effect on the same day. Previous revisions took place respectively on 31 October 1993 and on 30 August 1999.

There are three highlights to the latest revision:

(1) The minimum taxable income for Chinese citizens was increased from RMB 800 to RMB 1,600.

(2) Provisions were added that relevant high income individuals should handle tax payment declaration

procedures.

(3) Provisions were added that a withholding agent shall make the withholding declaration for all the taxpayers and in full amount.

Background of the Third Revision

China promulgated the first individual income tax law in September 1980 and confirmed RMB 800 as the starting point of levying taxes. The establishment of the socialist market economy, steady growth of economic purchasing power and rapid development of the economy, have lead to a substantial increase of individual income, and its taxes have become an important source of national revenue. The salary and income of the labors in China and the resident consumptive level have greatly increased. But the starting point of levying taxes on individual income was reconfirmed in 1999, resulting in a fairly heavy tax burden for the middle- and low-income brackets.

In 1980, China collected only RMB 160,000 in personal income tax (ITT), but this figure jumped to RMB 99.6 billion in 2001, making income tax the fourth highest of China's different sources for tax revenues. However, within personal income tax, the proportion of high-income items, such as remuneration from personal services, and from production and operation, increased at a lesser rate. Statistics indicate that of China's RMB 7,000 billion personal bank savings, 80 percent belongs to less than 20 percent of the depositors, while the income tax they pay amounts to less than 10 percent of total IIT. Also, the GDP proportion of personal income tax lags far behind that of other low-income countries. Generally speaking, China's taxation system is ineffective in collecting IIT, and most of those on high income do not pay the appropriate amount of tax.

Deficiencies in the IIT system have drawn the Chinese government's attention. Revision of the IIT Law was put on the legislative work agenda last year, and governments at various levels are intensifying their efforts to penalize tax evasion. They have two aims. First, to increase government revenue; and second, to narrow the income gap. Adjusting the threshold should help to lead high-income brackets to pay more taxes and meanwhile protect the interests of low-income groups, as any additional income means a lot to them. So the Chinese government decided to raise the starting point of levying taxes on individual income up to a proper amount of RMB 1,600.

In summary, the IIT rates currently applicable for Chinese citizens are as below:

IIT Rate and Deducted Amount for Quick Calculation
(Applicable to Income of Wages and Salaries)

Grade	Monthly Taxable Income Exceeding RMB	Monthly Taxable Income Not Exceeding RMB	Tax Rate %	Deducted Amount for Quick Calculation RMB
	0	500	5	0
2	500	2,000	10	25
3	2,000	5,000	15	125
4	5,000	20,000	20	375
5	20,000	40,000	25	1,375
6	40,000	60,000	30	3,375
7	60,000	80,000	35	6,375
8	80,000	100,000	40	10,375
9	100,000		45	15,375

(Note: "monthly taxable income" mentioned in this schedule refers to the amount remaining after deduction of 1,600 yuan and after deduction of social security including the basic endowment insurance fund, the basic medical insurance fund, the unemployment insurance fund and the housing accumulation fund.

The following example illustrates the calculation of monthly individual income tax payable by a Chinese mainland individual receiving monthly salary of RMB 10,000.

The quick calculation method is RMB 10,000 – RMB 1,600 = RMB 8,400 which falls in the category (4) and the tax rate of 20% shall be applicable. And the corresponding deducting amount for quick calculation is RMB 375. So a national individual receiving monthly salary of RMB 10,000 shall pay IIT RMB 8,400 x 20% - 375 = RMB1,305.

For foreigners, overseas Chinese, Hong Kong, Macao or Taiwan residents, in comparison of the old Individual Income Law and the latest Individual Income Law, the IIT rate applicable is unchanged (same to the IIT Rate applicable to Chinese mainland residents) but the IIT threshold for foreigners is changed from the previous RMB 4,000 (RMB 800 + RMB 3,200) to the present RMB 4,800 (RMB 1,600 + RMB 3,200).

Ms. Zheng Xin
Wang Jing & Co.

❑ Wang Jing & Co. News

Wang Jing & Co. Nominated for Three China Law Awards

Once again, the Firm has been recognized among China's top domestic law firms by receiving three nominations for the 2006 ALB China Law Awards to be held on 10 March at the Westin Hotel in Shanghai. The nominations, based on peer recommendations and a careful selection process, were received for the Guangdong Law Firm of the Year, Insurance Law Firm of the Year and Shipping Law Firm of the Year categories, and mark the continuing predominance of the firm in these three areas.

The evening, organized by Asian Legal Business, looks to become a great success. The Firm will be represented by managing partner Mr. Wang Jing and senior client service manager Mr. Maarten Roos from the Firm's Guangzhou office and Shanghai-based senior partner Mr. Zhong Cheng and senior consultant Mr. Wang Hongyu. In the two previous editions of these "legal oscars", the Firm brought home the awards for 2004 China Insurance Law Firm of the Year and 2005 Guangzhou Law Firm of the Year respectively.

Firm Welcomes New Team Members

Mr. Peng Kai

Over the past year, the Firm has seen a strong increase in demand for its intellectual property (IP) related legal services from both existing and new Clients. To broaden its strengths particularly in patent-related work, Mr. Peng Kai was recruited to join the Intellectual Property Team as patent attorney and IP consultant.

Mr. Peng has a bachelor's degree in engineering from the Beijing Institute of Technology, and a masters degree from Zhongnan University of Economics and Law. He worked on IP matters both in a corporate and a legal setting, but his most extensive experience was gained between 1997 and 2005, when he was in charge of patent dispute resolution at the Intellectual Property Bureau (SIPO) of Hunan Province. In 2003 he was also appointed evaluation expert at the Hunan Judicial Evaluation Centre, and in 2004 he studied US intellectual property law at the John Marshall Law School in Chicago as a visiting scholar.

As a former government official, Mr. Peng brings to the firm in-depth expertise on administrative handling of patent registrations and intellectual property disputes. He also speaks fluent English and is familiar with the American and European patent systems, and so will be a valuable asset in the further development of the Firm's IP Group.

Mr. Zhou Zhiyong

Following the continuing strong development of the Firm's work shipping-related corporate affairs, Mr. Zhi Zhiyong has joined the Firm.

Mr. Zhou graduated from Shanghai Maritime University in 1991. From 1996 to 2004 he was legal counsel to Maersk (China) Shipping Company, the China arm of the world's biggest shipping company, dealing with claims litigation and managing various corporate projects.

Mr. Zhou qualified as a lawyer in 2005, and his practice mainly focuses on litigation and logistics-related business operations, management and legal affairs.

This newsletter is published by the Corporate & Commercial Group of Wang Jing & Co, a PRC law firm assisting Chinese and multinational clients in business operations in China and abroad. The Firm's lawyers are based in the following offices:

GUANGZHOU
14/ F., South, World Trade Centre
371-375 Huanshi East Road
Guangzhou, P.R. China 510095
Tel. (+8620) 87600082
Fax. (+8620) 87784482
info@wjnco.com

SHANGHAI
1909-11, Merchant Building,
166 Lu Jia Zui East Road,
Shanghai, P.R. China 200120
Tel. (+8621) 5887 8000
Fax. (+8621) 5882 2460
shanghai@wjnco.com

TIANJIN
2007-08, TEDA Centre,
No. 16, 3rd Avenue, TEDA
Tianjin, P.R. China 300457
Tel. (+86 22) 2532 3818
Fax. (+86 22) 2532 3820
tianjin@wjnco.com

QINGDAO
Suite 3009, Flagship Tower, New World Cyber Port, 40 Hong Kong Zhong Road
Qingdao, P.R. China 266071
Tel. (+86 532) 8666 5858
Fax (+86 532) 8666 5868
qingdao@wjnco.com

HAIKOU
Suite 809, Haiyou Building,
4 Huaxin Road, Haikou,
Hainan, P.R. China 570105
Tel. (+86 898) 6672 2583
Fax. (+86 898) 6672 0770
hainan@wjnco.com

XIAMEN
Suite 1601, Bank Centre,
189 Xia He Road,
Xiamen, P.R. China 361021
Tel. (86 592) 268 1376-9
Fax. (86 592) 268 1380
xiamen@wjnco.com