Doing Business in China

2017
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1. Introduction

This guide provides an introduction to selected aspects relating to investment and business operations in the People’s Republic of China ("China") under current Chinese law and policy. China is a vast country, where national laws, local regulations and implementing procedures provide a complex framework for doing business.

We provide a brief outline of the various forms of doing business in China: equity and cooperative joint ventures, wholly foreign-owned enterprises, and representative offices. The guide also includes a summary of important areas of concern to all investors in China: mergers and acquisitions, competition issues, taxation, employment, intellectual property protection, trade and import and export rules, as well as compliance and dispute resolution issues.
2. Equity Joint Ventures

2.1 Legal status

An equity joint venture ("EJV") is a Chinese legal person with limited liability. It is established on the basis of a joint venture contract and articles of association between Chinese and foreign parties.

EJVs are regulated primarily by the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures (the "Joint Venture Law") and the Implementing Regulations for the Joint Venture Law (the "Joint Venture Regulations"). In addition, supplementary legislation covers such issues as contributions of registered capital, debt-equity ratios, registration, labor, imports and exports, foreign exchange, accounting and taxation. The Company Law of the People's Republic of China (the "Company Law") also includes certain provisions that apply to EJVs. These pieces of legislation, however, do not cover all relevant issues.

There is a lack of regulations and precedents to provide clear guidance in resolving some issues of corporate organization, management and procedures. In some cases, these issues can be resolved by including appropriate provisions in the joint venture contract or articles of association. In other cases, uncertainties may be resolved by consultation with the Ministry of Commerce of the People's Republic of China ("MOFCOM") or its local counterpart.

2.2 Establishment

The procedure for establishing EJVs (and other foreign-invested enterprises) may vary depending on the industry, the location and the ownership structure of the Chinese party.

There are general trends placing greater importance on environmental protection specifically for manufacturing EJVs and to relax the regime governing foreign-invested enterprises in non-regulated industries.

Projects with impact on the environment will require environment impact assessment ("EIA"), which is usually under the jurisdiction of the local environmental protection bureau.

In greenfield projects where a new plant needs to be built on a piece of land, the land is usually subject to a bidding process and approval of the construction plan and construction work will be necessary.

After or in parallel with the EIA and the land and construction related approvals, and depending on the specific case, additional approval may be required.

The parties will proceed to negotiate and draft the joint venture contract and articles of association and prepare a joint feasibility study, and if the Chinese party is a state owned entity, it will need preliminary approval for the project from its department in charge.

In general, the establishment of an EJV will have to be approved by the National Development and Reform Commission, and approved or recorded with MOFCOM or their local government counterparts depending on the size and business nature of the proposed joint venture and other factors.

If the EJV's business is regulated and is subject to "special market-entry measures", the Chinese party must submit documents to the appropriate examination and approval authority (generally MOFCOM or its local counterpart) for establishment approval before a formal business license will be issued to the EJV.

The EJV can register with the local bureau of the State Administration for Industry and Commerce ("SAIC") to obtain a business license and carry out a recordal with MOFCOM or local counterparts.
concerning establishment if its business is not subject to the "special market-entry measures". Approval by MOFCOM or its local counterpart is not needed. The EJV is formally established on the issuance date of the business license.

There are fewer regulatory restrictions in pilot free trade zones in selected cities in China and it is generally faster to set up an EJV within such zones.

2.3 Documentation

The Joint Venture Regulations do not set forth detailed requirements for the form or contents of documents such as the letter of intent, feasibility study, the joint venture contract and articles of association. The Chinese authorities have, however, published model forms for joint venture contracts and articles of association that are closely adhered to by the Chinese parties to joint ventures. By law, the joint feasibility study, joint venture contract and articles of association may be drafted in both Chinese and a foreign language. Under the Joint Venture Regulations, the joint venture contract must be governed by Chinese law.

In addition to the above documents, the parties will often simultaneously negotiate and execute contracts related to the joint venture's operations, such as those for technology transfer, trademark licenses, and supplies of parts or raw materials, as well as for the distribution of finished products. These related contracts may be attached to the joint venture contract as attachments.

2.4 Parties' investments

The most important concepts relating to the capitalization of an EJV are "registered capital" and "total investment." In the joint venture legislation, "registered capital" refers to the total amount of paid-in capital contributions by the parties to the joint venture. The "total investment" equals "registered capital" plus permitted financing for the EJV. The capital of EJVs must meet certain debt to equity ratios. As an example, if the total investment is less than US$3 million, at least 70% of the total investment must be registered capital.

Capital contributions may take several forms, including cash, buildings, equipment, technology, materials and the right to use land. If the capital contributions are in a form other than cash, the parties must agree on the appropriate value of the contributions on the basis of fairness and reasonableness or agree to have a third party make the evaluation. In addition, the valuation is subject to verification by official appraisers. The parties can agree upon the schedule for the capital contributions which need to be set forth in the articles of association, in accordance with the business plan.

An equity joint venture is allowed to increase or reduce its registered capital.

2.5 Term and scope of activities

EJVs in China are typically limited to a fixed term, which must be stipulated in the joint venture contract. In practice, the usual range is between 15 years and 50 years depending on the size and nature of the project, with most substantial manufacturing ventures having a term of 25 years or more. Indefinite terms are sometimes permitted, but EJVs in certain service industries, land development and real estate, natural resource exploration and exploitation projects, and other areas which are restricted must have a fixed term. Upon the expiration of its term, an EJV is to be dissolved, with the property remaining after clearance of debts to be distributed in accordance with the ratio of the parties' capital contributions except where the joint venture agreement, contract or articles of association have other stipulations.
Under the current corporate law regime of the People's Republic of China ("PRC"), all entities in China (whether domestic or foreign-invested) have definitive "business scopes" approved by the governmental authorities, which specify the range of business activities in which they are permitted to engage. The business scopes are generally brief and quite specific. They require careful drafting and are often the subject of negotiation between investors and the government authorities in the pre-establishment stage.

2.6  Foreign exchange

China's national currency, the Renminbi, is not freely convertible into other currencies. Nevertheless, China has introduced a form of current account convertibility, under which joint ventures may purchase foreign exchange for current account expenditures without the necessity of obtaining government approval. China also permits the conversion of Renminbi into foreign exchange for remittances of after-tax profits or dividends to foreign investors in EJVs. Foreign exchange remittances and receipts must go through authorized banks designated to handle foreign exchange transactions. Instead of government approval for foreign exchange remittances and receipts, the designated banks examine the documentation for the underlying transaction to ensure that the proposed payment or receipt qualifies as a current account item. EJVs also have access to the interbank market for the purchase and sale of foreign exchange through the designated banks.

Government approval is still required for the purchase and remittance of foreign exchange for certain capital account transactions. The Chinese government is gradually reducing government approval and some capital account transactions can be now be processed by the designated banks.

2.7  Financial administration

An EJV is required to adopt accounting procedures based on a dual-entry, accrual system. All accounting records, books and statements are required to be prepared and kept in Chinese. The accounting system adopted by the EJV must be reported, for the record, to the competent government authorities and the local financial and tax departments. Chinese legislation also requires an accountant registered in China to act as the auditor of the EJV.

An annual profit distribution plan has to be prepared and distribution of profits among the parties is usually in proportion to their respective contributions to the registered capital of the EJV.

EJVs are required to allocate a certain percentage of after-tax profits to a reserve fund, enterprise expansion fund and incentive and welfare fund for staff and workers.
3. Cooperative Joint Ventures

3.1 Legal status


Cooperative joint ventures take one of two different forms:

- a "pure" cooperative joint venture in which no legal entity separate from the contracting parties is established and the parties make their contributions to the project and bear the risk of profit and loss directly; and
- a "hybrid" cooperative joint venture in which a separate business entity is established and registered and the parties' liabilities are generally limited to their capital contributions to the entity.

Although the Cooperative Joint Venture Law does not explicitly distinguish between these two types of ventures, it provides that cooperative joint ventures that meet the relevant legal requirements may qualify as "legal persons" under Chinese law. The Cooperative Joint Venture Regulations make further distinctions concerning the treatment of cooperative joint ventures with legal person status and those without. A hybrid form cooperative joint venture would generally qualify as a legal person, while a pure form cooperative joint venture would not.

3.2 Establishment

The documentation required for the establishment of a cooperative joint venture and the procedures for obtaining approval or recordal of the project are very similar to those outlined above with respect to equity joint ventures.

The cooperative joint venture with legal person status can register with the local bureau of the SAIC to obtain a business license and carry out the recordal with MOFCOM's local counterpart concerning establishment, if its business is not subject to "special market-entry measures". Approval by MOFCOM or its local counterpart is not needed. The joint venture is formally established on the issuance date of the business license.

There are fewer regulatory restrictions in pilot free trade zones in selected cities in China and it is generally faster to set up a cooperative joint venture within such zones.

3.3 Parties' contributions

One of the reasons many investors in the past have chosen to utilize a cooperative joint venture structure instead of an equity joint venture has been that the investors are able to make their contributions to the joint venture in forms other than those allowed for in an equity joint venture.

The Chinese party to a cooperative joint venture might, for example, be made responsible for providing the required local labor, including the payment therefor. The Chinese party might also be responsible for providing the necessary factory or office facilities.
In some cases, it may not be permitted to count some of these forms of assistance as joint venture contributions, although practice in this regard varies considerably. Foreign investors should focus on how to categorize and structure the parties' contributions to a cooperative joint venture.

Unlike the case of an equity joint venture, a foreign party's investment in a cooperative joint venture may be repatriated prior to the expiration of the term of the joint venture, if the joint venture contract provides that ownership of all of the fixed assets of the joint venture shall revert to the Chinese party upon expiration of the joint venture term. However, the methods by which early repatriation may be accomplished are limited, and careful planning is required before establishment of the cooperative joint venture.

### 3.4 Operation

Pure cooperative joint ventures will usually have a shorter term than equity joint ventures, while hybrid cooperative joint ventures may have longer terms similar to those of equity joint ventures. Cooperative joint ventures are favored for hotels and commercial complexes and in infrastructure projects where the parties intend that the joint venture assets will stay with the Chinese party at the end of the joint venture term. Cooperative joint ventures are also commonly used for projects where the Chinese partner lacks material assets to contribute to the joint venture. Cooperative joint ventures in manufacturing are generally discouraged. The operational activities of cooperative joint ventures are restricted in much the same way as those of equity joint ventures.

It is common for cooperative joint venture contracts, especially those of pure cooperative ventures, to provide for the reversion of all of the assets of the joint venture to the Chinese party upon termination of the venture. In other cases, the liquidation procedures follow those applicable to equity joint ventures.

### 3.5 Foreign exchange

Cooperative joint ventures are generally subject to the same foreign exchange rules as equity joint ventures.

### 3.6 Profits

A substantial advantage of cooperative joint ventures is that the parties may agree on the distribution of profits at a ratio different from that of the parties' capital contributions.

### 3.7 Financial administration

An accountant registered in China must be engaged to audit and verify accounts. The parties may engage the accountant jointly or individually. A cooperative joint venture without legal person status must keep unified account books, and the parties must, in addition, keep their own separate account books.
4. Wholly Foreign-owned Enterprises

4.1 Legal status

Wholly foreign-owned enterprises ("WFOEs") are entities established under the Law of the People's Republic of China on Wholly Foreign-Owned Enterprises (the "WFOE Law") and the Detailed Implementing Rules for the WFOE Law (the "WFOE Regulations"). A WFOE can be a limited liability company or, upon approval, take another form. Currently, most WFOEs in China are established by one foreign investor, although the WFOE Regulations allow two or more foreign investors to apply jointly for the establishment of a WFOE.

4.2 Establishment

Under the existing system, the procedures for establishing WFOEs are similar to those for equity joint ventures. In certain cases, where the WFOE is engaged in certain business activities that require prior industry approval, e.g. travel agency or direct sales, then prior approval is required from the specific industry regulator.

Similar to joint ventures, a WFOE can only register its company name in Chinese. While China does recognize its own accredited "well-known" trademarks and selected Fortune 500 companies, it should be noted that having a prior Chinese trademark registration does not guarantee that the preferred Chinese characters can be registered as a company name in China.

The documentation required for the establishment of a WFOE is less burdensome than for a joint venture, for example the joint venture contract and the documents required in respect of the Chinese party are not applicable, but the procedures for obtaining approval or recordal of the project are very similar to those outlined for equity joint ventures.

The WFOE can register with the local bureau of SAIC to obtain a business license and carry out recordal with MOFCOM's local counterpart concerning establishment, if its business is not subject to "special market-entry measures". Approval by MOFCOM or its local counterpart is not needed. The WFOE is formally established on the issuance date of the business license.

WFOEs in pilot free trade zones in selected cities in China are subject to few regulatory restrictions and it is generally faster to set up a WFOE within such zones.

4.3 Parties' investments

As in the case of equity joint ventures, foreign investors' capital contributions to a WFOE may be in the form of foreign currency, machinery, equipment, industrial property, proprietary technology or Renminbi profits derived from their other investments in China. Capital contributions are subject to the prescribed debt to equity ratios.

4.4 Operation

A WFOE is permitted to operate for the period provided for in its articles of association registered with SAIC and recorded with the local counterpart of MOFCOM. Requests for an extension of the term of operation must be submitted to the authorities prior to expiry.

Under the WFOE Regulations and the Catalog for Guiding Foreign Investment in Industry (which is revised and amended from time to time), the establishment of WFOEs is prohibited in certain industries, such as broadcasting and public utilities.
4.5 Foreign exchange
WFOEs are generally subject to the same foreign exchange controls as joint ventures.

4.6 Management
The daily operations of a WFOE will be controlled solely by its own management, and should not be subject to interference by the government when operating in accordance with its articles of association.

4.7 Financial administration
The accounting rules applicable to WFOEs are similar to those applicable to equity joint ventures. Accounting books and statements printed by WFOEs themselves must be written in Chinese. Only Chinese registered accountants can verify annual accounting statements. Annual balance sheets and profit-and-loss statements must be submitted to the financial and tax authorities for the record. A WFOE must allocate at least 10% of after-tax profits to its statutory reserve fund for a certain number of years until the aggregated amount reaches 50% of the WFOE’s registered capital, whereas in equity joint ventures, the board of directors decides the proportion to be allocated to the reserve fund.

4.8 Corporate Maintenance
Similar to joint ventures, a WFOE has annual reporting requirements administered by different local government departments. These annual reporting or annual inspection requirements occur at different times of the year and are subject to local procedures. For example, a WFOE will need to submit periodic information to the local industry and commerce authority, Customs authority, foreign exchange bureau, and taxation authorities.
5. **Representative Offices**

5.1 **Legal status**

Representative offices established in China by non-resident enterprises are regulated by several national regulations, as well as local policies, which supplement the national regulations. In general, representative offices may not conduct direct business activities. A representative office is permitted only to make business contacts and engage in general liaison activities for its head office services and products. Personnel of a representative office of a non-resident enterprise should not sign contracts on behalf of either the non-resident enterprise or third parties.

In recent years, more restrictions and requirements have been imposed on representative offices, e.g. the limitation on the number of registered representatives (essentially to set a limit of four foreign personnel who can be seconded to a representative office), and the requirement to complete annual reporting to the local industry and commerce authority. Fewer foreign companies are setting up representative offices in China as a result of the limitations on activities.

5.2 **Registration**

Only a few types of representative offices (e.g., banking, securities, insurance) are required to obtain approval for establishment, and for any subsequent changes, the majority of representative offices do not need to obtain special approval. Instead, direct registration with the industry and commerce authorities is permitted. Some local industry and commerce authorities require an applicant company to submit application materials through designated agencies, and different registration authorities may require different documents.

Documents to be submitted generally include:

- a registration form for the representative office;
- a registration form for each of the representative office's foreign personnel (including the chief representative);
- a letter of creditworthiness from the foreign company's bank; and
- copies of the foreign company's incorporation certificate, business registration certificate and constitutional document.

The foreign company's incorporation documents, letter of creditworthiness, and appointment letter for the chief representative will need to be notarized and "consularized" by the Chinese embassy in the home jurisdiction of the foreign company before submission.

In addition to attending to the above registration, the non-resident enterprise must register the representative office and its foreign personnel with the local tax bureau, and a number of other government departments including the public security bureau (for residence permits) and with the local customs authority (for importation of personal belongings).
6. Distribution

6.1 Wholesaling and retailing

Foreign investment in wholesale and retail activities was traditionally governed by standalone regulations promulgated by MOFCOM, amongst which the most important one was the Measures for the Administration of Foreign Investment in the Commercial Sector (the "Commercial Sector Measures"), which came into force on June 1, 2004.

Starting from November 3, 2016, the Commercial Sector Measures, along with other relevant regulations promulgated by MOFCOM, were repealed. As a result, the only market access requirements for wholesale and retail activities in China are based on the Catalog for Guiding Foreign Investment in Industry. The most recent Catalogue (revised in March 2015) generally allows foreign investors to establish 100% wholly foreign-owned wholesale or retail enterprises in all industries in China, except for certain specified industries, including most notably, shipping agency (which must be majority-owned by a Chinese investor), gas station (which must be majority-owned by a Chinese investor when more than 30 stores are opened under a franchising arrangement and the stores sell various types gasoline), and tobacco (for which foreign investment is prohibited in wholesale and retail activities - tobacco is still subject to a State monopoly in China).

6.2 Franchise operations

China permits foreign investors to engage in franchising activities through wholly foreign-owned or joint venture commercial enterprises. Cross-border franchising is also permitted.

In order for a foreign investor or foreign-invested commercial enterprise to become a franchisor, the franchisor must have at least two directly-operated stores that have been operating for over one year.

Applications to establish a foreign-invested commercial enterprise to engage in franchising activities must be submitted to the commerce authorities, and a specimen franchise contract must be submitted together with other application materials.

6.3 Direct selling

Pursuant to its WTO commitments, China liberalized foreign investment in wholesale and retail distribution away from a fixed location with the promulgation of the Regulations for the Administration of Direct Selling by the State Council and effective from December 1, 2005 (the "Direct Sales Regulations"). Following the promulgation of the Direct Sales Regulations, China issued implementing regulations to supplement various aspects of the Direct Sales Regulations.

At the same time as the promulgation of the Direct Sales Regulations, China issued the Regulations on the Prohibition of Pyramid Marketing, promulgated by the State Council and effective November 1, 2005 (the "Pyramid Marketing Prohibition Regulations"). The stated aims of the Pyramid Marketing Prohibition Regulations are to ban certain activities which are considered to be harmful to the society and business environment.

"Direct sales" is broadly defined as "a sales method whereby a direct selling enterprise recruits direct sellers, who market products directly to the ultimate consumers other than through a fixed place of business". The Direct Sales Regulations restrict the products that can be sold using direct sales methods in two different ways. A direct sales enterprise may only sell products that were produced by itself or by its parent or holding company. Additionally, China has limited the overall scope of products that can be sold through direct sales.
The Direct Sales Regulations impose a certain number of requirements on enterprises in China that intend to engage in direct sales in China. The Direct Sales Regulations allow investors (both foreign and local) to expand the business scopes of existing Chinese enterprises to include direct sales. MOFCOM is the issuing authority of the Direct Selling Permits. In order to apply for a Direct Sales Permit from MOFCOM, an applicant would have to submit a set of application documents. The application for the Direct Selling Permit must be submitted to MOFCOM through their provincial level counterpart where the applicant enterprise is registered. During the application process, MOFCOM will solicit the opinion of SAIC regarding the application before it decides whether to grant its approval.

6.4 E-Commerce

China introduced a cross-border e-commerce pilot program in early 2014 in order to regulate the sale of goods by overseas retailers directly to Chinese customers through approved e-commerce platforms.

Two models of retail activities are currently permitted under the cross-border e-commerce pilot program. The "bonded sale" model allows a foreign seller to route the goods through a free trade zone before dispatching them to the individual Chinese buyers. The "direct sale" model in contrast allows shipment of goods directly from a foreign seller to the individual Chinese buyers through designated courier service providers. Sales under both models are entitled to certain customs duty and import tax saving benefits, as compared to the imports through the ordinary channel of commercial trade.

Neither model requires the foreign seller to establish a legal presence in China. Nevertheless, the foreign seller is required to engage qualified third party logistics service providers and a cross-border e-commerce platform approved by China Customs in order to sell goods under the pilot program.

Starting from April 8, 2016, China also has in place a "positive list" regime for the pilot program, whereby only products listed as "permitted" on the two tariff code-based catalogues can be imported under the pilot program, subject to the product regulatory requirements specified in the relevant portions of the catalogues, such as pre-importation registration and approval of specified categories of products (e.g., cosmetics, infant milk formula, health food and medical device, etc.), as well as compliance with China's national standards and labelling requirements. Nevertheless, most of the product regulatory requirements are currently suspended until December 31, 2017.
7. Imports and Exports in China

There are several issues affecting imports and exports in China. These issues are described in the following sections below and should be considered when importing / exporting goods to / from China.

7.1 Import and export rights

China's implementation of its WTO commitment to grant import / export rights to foreign-invested enterprises was controversial. However, a significant step forward was taken when China amended the Law of the People's Republic of China on Foreign Trade (the "Foreign Trade Law"). The amendments replace the system of special, licensed import/export companies with a registration system under which enterprises, other organizations or individuals may engage in import / export business after registering with the foreign trade authorities. To implement the changes, MOFCOM issued the Measures for the Registration of Foreign Trade Operators (the "Registration Measures") on June 24, 2004. Prior to introduction of the registration system, joint ventures and WFOEs were generally only authorized to import goods, materials and equipment for their own use and to export self-manufactured products. Now, they are able to obtain import / export rights for all types of products other than goods subject to state trading. However, it is important to note that import rights do not equal distribution rights (e.g., retail or wholesale distribution rights). Even if a foreign-invested enterprise obtains import rights, it will not be able to sell the imports unless it also has distribution rights.

7.2 Taxes affecting imports and exports

Imports and exports are subject to Customs duties and value-added tax. They may also be subject to consumption tax. Please refer to the chapter on "Taxation" for further details.

7.3 Customs valuation

As part of China's accession to the WTO, China committed to adopt the Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994 (the "GATT Valuation Code"), which is reflected in the Measures of the PRC Customs for the Assessment and Determination of Dutiable Value of Import and Export Goods issued by the General Administration of Customs, amended and effective from 1 February 2014. The value of imported goods must be measured accurately in order to determine the amount of customs duty payable.

In general, all imported goods are appraised in accordance with the transaction value of the goods. However, where the transaction valuation is not an appropriate method of valuation (e.g., the goods are transferred to China free of charge or the relationship between related parties affected the price), one of the following valuation methodologies may be used:

a. Transaction value of identical merchandize
b. Transaction value of similar merchandize
c. Deductive value
d. Computed value, and
e. Derivative value

The valuation methodologies above are applied in sequence. Nevertheless, the order of deductive value and computed value may be switched upon the importer's application.
7.4 Tariff classification

China adopts a commodity classification system based on the Harmonized Commodity Description and Coding System ("HS"). Commodity classification determines the applicable customs duty rate, import / export licensing requirements, export refund rates, etc.

There are 98 different categories with detailed import and export duty rates for all goods and commodities. Both "general rates" and "most favored nation rates" are shown for each category. Failure to provide an accurate HS Code will attract penalties and can impact the customs duty rate applied to imports. If this results in underpayment of customs duty, China Customs can penalize the importer for duty evasion.

China Customs has adopted the six General Rules of Interpretation ("GRI") for classifying imports and exports in accordance with the HS system.

7.5 Customs declaration

A declaration to Customs must be made at the place of importation within 14 days of entry into the country. Taxpayers for exports must submit a declaration to Customs at the place of exportation upon arrival of the goods at the Customs supervision and control zone at least 24 hours prior to loading.

The duty payable will be calculated based on the product's customs tariff classification and the dutiable value, and is payable to a designated bank within 15 days from the date of the Customs Duty Certificate(s). If payment is not made on time, taxpayers may be liable to pay daily late payment interest of 0.05% of the total amount of duties payable commencing from the due date, or additional penalties if payment is more than three months late. A taxpayer who is unable to pay customs duties on time due to the occurrence of a force majeure event or State adjustment of tax policies may defer payment for up to six months.

7.6 Origin

Place of origin rules exist in order to implement two customs duty rates on import commodities, i.e. MFN rate and preferential rate. If the imported product has been produced in two or more countries, the last country in which there has been substantial transformation to the product shall be deemed as its country of origin, as a general rule applicable to standard custom duty rates.

Preferential custom duty rates, which are reduced rates, are applicable to imported goods that fall within the ambit of a free trade agreement. It is therefore important to ascertain the origin of the goods so as to know whether they are entitled to preferential treatment. Specific preferential rules are provided under the various free trade agreements. In some instances, the rules are product-specific.

7.7 Special customs supervision zones

China has a number of different special custom supervision zones that offer preferential customs and VAT treatment. These zones are specific geographical areas that are marked out and administered by Customs. They may be considered to be outside the Customs territory of China, but may be considered to be part of China proper by other agencies. The preferential treatment that an enterprise established

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1 Under a pilot program initiated by the General Administration of Customs ("GAC") in 2006 and subsequently expanded in 2013, qualified companies (based upon their track record of compliance and credit rating) may file import or export declarations to Customs where they are registered. Depending on the qualifications of the companies, they may further apply for release of the goods to Customs where they are registered, or Customs at the gateway port.
within the various zones may be different, and the type of activities permitted may also be different. Below is a table that lists the major types of special custom zones in China:

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<tr>
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<th>Processing</th>
<th>Logistics</th>
<th>Trading</th>
<th>Exhibitions</th>
<th>Export VAT Refunds</th>
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</table>

### 7.8 Free trade agreements / preferential trade agreements

China has signed numerous Free Trade Agreements ("FTAs") with various countries, all providing customs duty concessions for imports into China, as well as according China originating exports to these countries at preferential import duty rates. Importers / exporters should consider whether such agreements could be used to reduce the amount of customs duty paid. As of December 2016, the following FTAs are in force:

- China - Association of Southeast Nations ("ASEAN") FTA;
- China - South Korea FTA;
- China - Australia FTA;
- China - Chile FTA;
- China - Pakistan FTA;
- China - New Zealand FTA;
- China - Singapore FTA;
- China - Peru FTA;
- China - Costa Rica FTA;
- China - Iceland FTA;
- China - Switzerland FTA;
- Mainland and Taiwan Economic Cooperation Framework Agreement ("ECFA");
- Mainland and Hong Kong Close Economic Partnership Arrangement ("CEPA");
- Mainland and Macau CEPA; and
- Asia Pacific Trade Agreement.
8. **Mergers and Acquisitions**

China has a sophisticated regulatory framework for mergers and acquisitions involving foreign investors. The primary governing legislation is the Regulations on the Merger and Acquisition of Domestic Enterprises by Foreign Investors ("Foreign M&A Regulations"), which was last revised in June 2009 and is supplemented by a myriad of departmental rules governing specific industries or target groups.

### 8.1 General framework

Similar to the undertaking of greenfield projects, foreign investors acquiring Chinese companies are subject to foreign investment restrictions, which are based on the classifications of industries into "encouraged", "permitted", "restricted" and "prohibited" categories. Such classifications, which are set forth in the Catalog for Guiding Foreign Investment (last revised in April 2015) ("Catalog") affect the maximum percentage of foreign ownership allowed, as well as the level of Chinese government authorities from which approvals would be required. Although recent versions of the Catalog have opened up a number of previously restricted and prohibited sectors to foreign investors, a substantial number of industries remain restricted or prohibited with respect to foreign investment. It is expected that a "negative list", to be issued pursuant to recent changes in laws governing foreign-invested enterprises, will supersede the Catalog. MOFCOM and the National Development and Reform Commission ("NDRC") are the major Chinese agencies in-charge for foreign investment matters.

The Foreign M&A Regulations also introduced the concepts of "industries affecting national economic security" and "companies owning well-known trademarks and old Chinese trade names", a change of control in which will require approval from central MOFCOM regardless of the transaction value. In other cases, the level of the approval authorities is determined by the transaction value or the total investment amount set for the target entity.

### 8.2 National security review

The State Council and MOFCOM issued regulations in 2011 fleshing out a national security review procedure already referred to in general terms in the Foreign M&A Regulations.

A joint committee led by NDRC and MOFCOM is responsible for carrying out a review to determine whether a transaction will have a major impact on national security. If that impact cannot be mitigated, the transaction will not be permitted to go forward.

The onus is on the investor to file for a national security review before seeking approval if the transaction could raise national security concerns. The approval authority may also at its own discretion decide that a national security filing is required, and suspend approval pending the results of that filing.

A filing is required if the acquisition would give a foreign investor actual control of a domestic defense enterprise or a non-defense enterprise which (1) has a bearing on national security and (2) involves industries such as major agricultural products, major energy sources and resources, major infrastructure facilities, major transportation services, key technologies and the manufacture of major equipment.

### 8.3 Equity acquisitions vs. asset acquisitions

A foreign investor can acquire equity in a wholly Chinese-owned enterprise and convert it into a foreign-invested enterprise. When assets, rather than equity, are acquired, it is necessary to establish a commercial presence in China in order to use the assets for operational purposes. In these
circumstances, a foreign-invested enterprise may be established prior to the acquisition or, in some circumstances, may be established as part of the acquisition process.

There are certain requirements applicable to both equity and asset acquisitions. For instance, the parties are required to have the value of the equity appraised before transfer. Prices considerably lower than the appraisal result are not permitted. The transaction price and the appraisal amount may not usually differ by more than 10%.

In comparison, asset acquisitions have some advantages over equity acquisitions. The foreign investor can pick and choose which parts of the PRC target company it wishes to buy. Generally, existing obligations, liabilities or restrictions of the PRC target company will remain the sole responsibility of the PRC target company. Asset acquisitions tend to be more complex than equity acquisitions since the transaction may involve the transfer of different categories of assets and liabilities, each carrying separate statutory requirements. In addition, if a new foreign-invested enterprise is to be established for the purpose of carrying out the asset acquisition, separate approval from the Chinese authorities will be required for its establishment. Finally, there may be tax considerations for the parties in relation to the transfer of assets, as asset acquisitions are taxable in China.

8.4 Other specific target groups or acquisition means

MOFCOM has, through its guidelines issued in December 2008, clarified that neither equity acquisitions of, nor assets acquisitions from, foreign-invested enterprises are subject to the Foreign M&A Regulations. While it remains unclear as to what extent acquisitions using foreign-invested enterprises have to comply with the Foreign M&A Regulations, in practice they are generally not subject to the additional requirements set forth therein.

If a purchaser wishes to acquire a foreign-invested enterprise, it may simply acquire the foreign parent of the target rather than the target itself. This form of acquisition is particularly suitable when the parent is a special purpose vehicle established for the sole purpose of holding the foreign-invested enterprise. Offshore acquisitions are in many ways simpler and more convenient than direct acquisitions because Chinese approval requirements are normally avoided. However, the PRC tax authorities have tightened their scrutiny over offshore transactions that are deemed as trying to avoid PRC capital gains tax. As a result, an indirect transfer generally will be ‘re-characterized’ for tax purposes as a direct transfer under China's indirect transfer rules if it lacks reasonable commercial purpose and does not fall within any safe harbors, in which case the seller of the shares may be subject to enterprise income tax in China on any capital gains.

8.5 State-owned equity acquisitions

The PRC Enterprise State-owned Assets Law came into effect in May 2009 to regulate, among other things, the transfer of state-owned equity interests. Under this new law, equity transfers in state-owned enterprises generally are subject to approvals by the State-owned Assets Supervision and Administration Commission (or its local counterparts). If a transfer will result in the State losing majority control, approval from the PRC government at corresponding level would also be required.

The transfers of state-owned equity interests (other than shares in listed companies) have to be conducted at government-affiliated equity exchanges by means of an open bidding process. The minimum transfer price has to be determined by reference to the appraised value. A commitment to maintain employees stability is often one of the qualifying requirements for interested bidders. On the other hand, any proposal relating to redeployment of employees requires approval from the workers congress of the target.
It is worth noting that many departmental rules issued by the State-owned Assets Supervision and Administration Commission or its predecessor prior to the promulgation of the new law continue to apply.

### 8.6 Acquiring PRC listed companies

Since 2006, foreign investors may directly acquire tradable shares of PRC listed companies by way of transfer, private placement or other legal means for medium- to long-term investments. Where the target shares are state-owned, sellers must publish key details of potential dispositions and invite interested buyers to submit acquisition proposals for selection.

### 8.7 Mergers

PRC laws recognize two forms of merger: "merger by absorption" and "merger by new establishment." A "merger by absorption" involves the absorption by one company of another pursuant to which the absorbed company is dissolved and its registered capital and assets merged into the surviving entity. In a "merger by new establishment," each of the pre-merger companies is dissolved and a new company established holding an aggregate of the pre-merger companies' assets and registered capital.

Cross-border mergers are currently unavailable under PRC law, i.e. it is not possible to directly merge a foreign entity with a domestic company (including foreign-invested enterprises). As far as foreign investors are concerned, the only permissible forms of merger in China are between foreign-invested enterprises and foreign-invested enterprises, or between foreign-invested enterprises and domestic companies. In practice, however, mergers are rarely seen and acquisitions are more common.

### 8.8 Recent developments

There are a number of interesting regulatory developments in recent years concerning mergers and acquisitions in China.

For example, on January 19, 2015, MOFCOM released a draft of a new foreign investment law for public comment. The draft law is meant to replace the existing laws governing foreign-invested enterprises ("FIE Laws"). When passed, this law would stand as a historic event in China's reform and liberalization. The draft law aims to establish a framework for the regulation and monitoring of foreign investment in the areas of market entry and ongoing compliance, while leaving the corporate form and governance issues to other legislation such as the Company Law.

Compared to the FIE Laws, the draft law adopts a much broader definition of ‘foreign investment' based on a 'substance over form' principle. The draft law proposes a complete overhaul of the current pre-establishment approval regime governing foreign investment by replacing it with a market entry review and an information-reporting regime. A Negative List replicating the current practice in China (Shanghai) Pilot Free Trade Zone would replace the decades-old case-by-case examination and approval system. An investor would only be required to obtain market-entry approval if the investment is in a sector on the Negative List. Otherwise, the investor could simply report the establishment of or investment in the foreign-invested enterprise. Another notable development is the codification of national security review as formal law. Many hurdles need to be cleared and a consensus built before the draft law can be presented to the Chinese legislature for its first formal legislative review. The whole process may take up to two years or more.

Consistent with such legislative trend, in September 2016, the FIE Laws were amended to provide for a recordal system for the establishment and administration of corporate changes of foreign-invested enterprises in "industries that are not subject to special administration measures for entry" on a
nationwide basis, in contrast to the previous case-by-case pre-approval regime. Under administrative regulations issued in October 2016 to implement this change, "industries that are not subject to special administration measures for entry" are basically those which are not restricted or prohibited under the Catalog, which will likely be replaced in time by a "negative list" for foreign investment. These amendments and new measures represent China's attempts to further relax the regime for the administration of foreign-invested enterprises on a nationwide basis. While these changes currently only apply to newly established, greenfield foreign-invested enterprises, and do not affect the approval regime for acquisitions of domestic enterprises or foreign-invested enterprises, we anticipate that these new laws and regulations may eventually impact or eliminate approval requirements for acquisitions by foreign investors in many sectors in the future.

In addition, recent regulations of the State Administration of Foreign Exchange significantly reduced and simplified the procedures for granting and taking cross-border security, and registering a round-trip investment. Foreign-invested enterprises in pilot areas are permitted to use their registered capital for making equity investments in China, a development believed to have opened a door for foreign PE funds.
9. Antitrust and Competition Laws

9.1 Legal framework

The basic law governing antitrust and competition issues in China is the Anti-Monopoly Law ("AML"), which entered force on August 1, 2008. The AML is China's first comprehensive competition law, applying to almost all sectors of the economy. The main features of the AML are:

- a merger filing system, requiring mergers and acquisitions, meeting specific financial thresholds, to be notified to MOFCOM's Anti-Monopoly Bureau and approved prior to closing;
- a prohibition on monopoly agreements; and
- a prohibition on the abuse of a dominant market position.

In recent years, antitrust regulators in China are working on six antitrust guidelines, which will provide more clarity on the application of AML. The draft antitrust guidelines are as follows:

- Antitrust Guideline on Leniency Application in Cases involving Horizontal Monopoly Agreements;
- Antitrust Guideline for Undertakings' Commitment in Anti-Monopoly Cases;
- Antitrust Guideline for Auto Industry;
- Antitrust Guideline on Determination of Illicit Gains and Fines;
- Antitrust Guideline on the General Conditions and Procedures of Exemption for Monopoly Agreements;

The above draft guidelines are expected to be finalized and come into force in 2017.

As the AML remains relatively new, its enforcement is rapidly evolving and the information contained in this section is therefore especially vulnerable to change.

9.2 Extraterritorial application

The AML applies to both (a) agreements and conduct within China; and (b) agreements and conduct outside China, where these have the effect of restricting competition in the Chinese market.

9.3 Enforcement agencies

The Anti-Monopoly Enforcement Agency ("AEA") is responsible for coordinating enforcement, delegated in turn to three agencies:

- MOFCOM is responsible for merger control filings and investigations;
- the Department of Price Supervision of the National Development and Reform Commission ("NDRC") is responsible for pricing-related infringements; and
- the Law Enforcement Bureau for Anti-Monopoly and Unfair Competition of the SAIC is in charge of enforcing non-price-related infringements.
Among the three authorities within the AEA, both SAIC and NDRC have provincial level counterparts who are permitted to investigate infringements and enforce the AML.

In recent years, Chinese enforcement authorities have been actively enforcing the AML:

- The number of merger filings has significantly increased since 2008. For instance, MOFCOM received 286 merger notification between January and September in 2016 and closed 254 during the same period, which was a 20% increase compared to the same period in 2015.
- NDRC and its local counterparts have investigated a number of high profile cases involving various industries, such as automotive, shipping, pharmaceutical, and medical devices. In some of these investigations, the amount of fines imposed has reached nearly USD1 billion.
- Since the AML took effect in 2008, SAIC has investigated a total of 72 antitrust cases, among which 35 cases had been concluded. SAIC has started 14 new investigations in 2016.2

9.4 Merger filings – when are they required?

9.4.1 Filing thresholds

The AML requires transactions qualifying as "concentrations" to be notified to MOFCOM where, in their last completed accounting year:

- each of at least two "relevant business operators" generated at least RMB400 million (approx. USD60.47 million) in revenues from sales in or into China (excluding Hong Kong and Macau); and
- all the "relevant business operators" have aggregate revenues exceeding either RMB10 billion (approx. USD1.51 billion) globally or RMB2 billion (approx. USD302.35 million) generated from sales in or into China (excluding Hong Kong and Macau).3

Higher specific thresholds exist for banks, insurance companies and other financial institutions.

Transactions between related parties, such as reorganizations taking place entirely within a corporate group, are expressly exempted from the AML filing obligation.

It is worth noting that:

- the thresholds can be met through imports into China alone – no Chinese assets or presence are needed;
- an AML filing will be required regardless of whether a transaction takes place in China or offshore;
- transactions that are closed without filing in China, despite meeting the thresholds above, expose both the acquirer and the seller to substantial penalties (see "Penalties" below); and
- even if the thresholds set out above are not met, MOFCOM has the ability to require a filing to be made, either before or after closing. MOFCOM has stated that this will only occur where a substantial negative impact on competition.

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2 The number of SAIC investigations is sourced from the speech of a top SAIC official in 2016 China Competition Policy Forum, Beijing, October 27-28, 2016.

3 The exchange rate is 1 USD=6.6148, which is the average exchange rate between January and November 2016.
9.4.2 "Relevant business operators"

The "relevant business operators" will typically be (1) the acquiring entity and its entire corporate group; and (2) the businesses or companies being acquired, including any affiliates or subsidiaries they control. The seller will not, in most cases, be regarded as relevant. Where there are two or more acquirers, the revenues of each acquirer will usually be relevant.

9.4.3 "Concentration"

"Concentration" is a wide term, covering not just acquisitions of complete or majority control, but also acquisitions of substantial minority stakes, as well as assets-based acquisitions, where the acquirer gains rights amounting to "decisive influence" over a business for the purposes of the AML.

"Decisive influence" is also a wide concept, usually including the right to appoint one or more directors or core management personnel, and obtaining veto rights over matters such as the budget, sales and operations decisions.

9.4.4 Joint ventures

Formations of joint ventures and substantial changes to their ownership will usually give rise to a "concentration", with the "relevant business operators" being the parents to the joint venture and their corporate groups, as well as the joint venture itself. The position in relation to entirely new, "greenfield" joint ventures is less clear, and guidance should be sought before proceeding.

9.5 Merger filings – procedure

Filings are detailed, and transactions may not be closed until MOFCOM has completed its review and issued a clearance decision. The merger review process in China usually takes a significantly longer period compared to other jurisdictions. It is therefore important to address this issue early.

Once a filing is received, MOFCOM will review the filing and either declare it complete or request further information or clarification (known as the pre-acceptance phase). The formal review timetable does not commence until the filing has been declared complete.

MOFCOM has a two-track review procedure, namely:

- standard procedure; and
- simplified procedure.

9.5.1 Standard Procedure

The standard procedure typically involves the following phases:

- Pre-acceptance phase – typically 6 to 12 weeks (but can be longer);
- Phase 1 review – 30 days;
- Phase 2 review – 90 days; and
- Phase 3 review – 60 days.

The majority of cases reviewed under standard procedure are approved after Day 45 of Phase 2. However, if the parties offer commitments and / or the transaction raises significant competition law
concerns then the review process may be extended to Phase 3. In exceptional cases the parties may be required to re-file the transaction at the end of Phase 3. However, this is extremely rare.

During the review process, MOFCOM will consult with competitors, suppliers, customers and relevant industry associations. Where objections are raised, parties may need to make additional submissions to MOFCOM, either in writing or in person.

9.5.2 Simplified Procedure

In 2014, MOFCOM introduced the simplified procedure, which intends to expedite the review process for the cases raising no major competition issues. Two rules, namely the Tentative Provisions on the Applicable Standards for Cases of Concentration of Operators Subject to Summary Procedure and the Guiding Opinions on the Declaration for Concentration of Operators Subject to Summary Procedure, were issued by MOFCOM in February and April 2014 respectively. The standards for cases qualified for summary procedure are as follows:

- horizontal mergers when the parties' combined market share in the overlap market is less than 15%;
- vertical mergers when the parties' market share in the relevant upstream and downstream market is less than 25%;
- conglomerate mergers when the parties' market share in their respective markets is less than 25%;
- offshore joint ventures which do not engage in any economic activities in China;
- the acquisition of equity or assets of an offshore target which does not engage in any economic activities in China; or
- the reduction of the number of controlling shareholders in a joint venture which results in the joint venture being controlled by one or more of the remaining shareholders.

Please note that even if a transaction satisfies one of the above-mentioned conditions, MOFCOM reserves the right not to apply the summary procedures for exceptional cases (e.g., it is difficult to define the relevant market, or the concentration may have adverse impact on consumers or relevant business operators).

The new procedure has substantially accelerated the currently lengthy merger review process in China for transactions that do not have a significant impact on competition. The pre-acceptance phase in simplified procedure usually takes 4-8 weeks. It is expected that a majority of the notified transactions subject to the simplified procedure will be cleared within Phase 1. In addition, the content requirements of the simplified form are substantially less, thereby reducing preparation time.

From 2013 to the end of Quarter 3 2016, around 1% of filings have resulted in a conditional clearance or a prohibition of concentration. The conditions imposed can be wide-ranging, requiring the disposal of businesses both within and outside China. Behavioral conditions can also be imposed, for example requiring parties to refrain from further acquisitions in a particular sector, or to maintain separation between the acquirer and the businesses being acquired. More details relating to the conditions can be found in an interim rule published by MOFCOM on restrictive conditions for concentrations of undertakings, which took effect from 5 January, 2015. The rule lays out types of merger review conditions, as well as the process of forming, implementing and monitoring restrictive conditions.
9.5.3 Sanctions

MOFCOM is increasingly taking action against parties to notifiable transactions that fail to notify. As of April 21, 2016, MOFCOM has published eight penalty decisions on parties who failed to comply with PRC merger filing requirements.

9.6 Prohibition on monopoly agreements

The AML prohibits "monopoly agreements". These are defined as agreements, decisions or other concerted practices between business operators that have the purpose or effect of eliminating or restricting competition.

The following monopoly agreements between competing business operators are prohibited:

- agreements to fix or change the price of goods;
- agreements to restrict the quantity of goods produced or sold;
- agreements to divide a sales market or a raw materials procurement market;
- agreements to restrict the purchase of new technology or new equipment, or to restrict the development of new technology or new products; and
- concerted refusals to deal.

The AML also expressly prohibits direct or indirect attempts by a supplier to impose fixed or minimum resale prices on customers. In fact, the resale price maintenance issue has become a top priority in NDRC’s recent enforcement actions starting from early 2013.

Both NDRC and SAIC have issued implementing rules to define further types of monopoly agreement, which can be between competitors or non-competitors. In late December 2010, NDRC issued the Regulations on Price Monopoly and SAIC issued the Regulations on Prohibition of Monopoly Agreement. The NDRC rule clarifies that among others, agreement to fix or change commissions or discounts that affect prices, or use an agreed price as base for negotiation with the third party will be viewed as monopoly agreement. The SAIC rule clarifies agreements allocating product sales by territory, by customer or by category or volume, restricting the purchase, lease or use of new equipment or jointly refusing to supply or sell products to a business operator among competitors, will be viewed as monopoly agreements.

9.6.1 Exemption from the prohibition

The prohibitions on horizontal and vertical monopoly agreements are not applicable if the parties are able to prove that:

- the agreements would not seriously restrict competition in the relevant market; and
- consumers can share the benefits resulting from these agreements; and
- one of a list of specified goals are met. These include technological advancement and / or product development, improvements in overall product quality, increases in efficiency, and reduction in costs.

There is currently no mechanism under the AML which would allow parties to apply in advance for a formal ruling that a given case falls within an exemption. Parties to agreements are therefore expected to self-assess whether an agreement, if later investigated by SAIC or NDRC, would qualify for an
exemption. However, NDRC is currently working on a draft guideline, which aims to provide general conditions and procedures for application of exemptions (See Sub-Section Legal Framework).

9.7 Prohibition on abuse of dominant market position

The AML defines a "dominant market position" as the ability of one or more business operators to control the price or quantity of goods in a relevant market or to otherwise affect conditions of a transaction, so as to hinder or influence the ability of other business operators to enter into the market.

9.7.1 When is a business operator dominant?

This is often a complex analysis based on a number of criteria, including market share, control over the market, financial and technical resources and barriers to market entry.

Under the AML, a dominant market position is presumed to exist where one, two, or three business operators achieve combined market shares of 50%, 66%, or 75% respectively. However, if any of the operators has a market share of less than 10%, or can produce evidence to rebut the presumptions, then that operator will not be assumed to have a dominant market position.

9.7.2 Types of conduct prohibited

A dominant market position is not, in itself, unlawful. It is only the abuse of such a dominant market position that raises issues. The AML prohibits the following types of conduct by business operators occupying a dominant market position:

• selling goods at prices that are unfairly high or purchasing goods at prices that are unfairly low;
• without a legitimate reason, selling goods at below cost price;
• without a legitimate reason, refusing to deal with a business operator;
• without a legitimate reason, restricting a trading partner by requiring it to deal only with the dominant operator(s) or with other designated operators;
• without a legitimate reason, tying goods or attaching other unreasonable conditions to a transaction; and
• without a legitimate reason, treating equivalent trading partners in a discriminatory manner with respect to price or other trading conditions.

This list is not exhaustive, and the AEA is empowered to define further abuses. As with monopoly agreements, both NDRC and SAIC have issued detailed rules to further define the abuse of dominant market position.

9.8 Penalties

For anti-competitive agreements and conduct, fines of up to 10% of the total turnover in the preceding year can be levied, plus confiscation of illegal gains resulting from the agreement or conduct. In addition, agreements that violate the AML are automatically invalid. Cease and desist orders can also be issued in respect of anti-competitive behaviour. It is expected that Antitrust Guidelines on Determination of Illicit Gains and Fines will provide more detailed mechanism in penalty determination once finalized.
For failure to make a merger filing, or closing a transaction before clearance is granted, fines of up to RMB500,000 (approx. USD75,588) are available, plus the ability for MOFCOM to order the annulment or unwinding of the transaction.

9.9 Procedure

Rules have been published setting out how investigations are conducted. These include basic details of a "leniency" program, which rewards those confessing illegal conduct or agreements with either full or partial immunity from fines. NDRC is working on a draft guideline regarding leniency application in cases involving horizontal monopoly agreements. We expect that this draft guideline will give the parties more certainty in leniency application.

9.10 Litigation

In addition to administrative enforcement, the AML allows customers, competitors and third parties to bring civil damages claims against any business that has caused them to suffer loss by engaging in a monopoly agreement or abusing its dominant market position.
10. Intellectual Property Protection

China is a member of the WTO and consequently a party to all major intellectual property conventions of the organization, as well as others, including the Paris Convention, Patent Cooperation Treaty, Berne Convention, Universal Copyright Convention, Geneva Convention and Madrid Agreement on International Registration of Marks.

10.1 Patents

The Patent Law of the People's Republic of China (the "Patent Law") was amended on December 27, 2008. The revision came into effect on October 1, 2009 and was supplemented in 2010 with revised Implementing Regulations (the "Implementing Regulations"). The Implementing Regulations were published on December 30, 2009 and came into effect on February 1, 2010.

In 2015, China's Supreme People's Court amended the Several Rules on the Application of Law in the Adjudication of Patent Disputes No. 1 (2001), which became effective on February 1, 2015 ("2015 Opinion"). The 2015 Opinion aimed to streamline judicial opinions with the current Patent Law. For example, certain compensation calculation methods have been revised in the 2015 Opinion, and the RMB500,000 ceiling has been removed when determining infringement damages.

The Supreme People's Court published a draft judicial opinion on patent disputes entitled the Interpretation on Several Issues Related to Adjudicating Patent Infringement Disputes No. 2. This draft opinion came into effect on April 1, 2016 ("2016 Opinion"). This opinion also takes a practical approach and provides further guidance on how patent disputes should be determined. It also introduces the fair, reasonable and non-discriminatory ("FRAND") requirements for standard essential patents.

The Patent Law and its Implementing Regulations adopt a "first-to-file" rather than "first-to-invent" system. There are three types of patents: patents for inventions of 20 years duration from the application filing date; patents for utility models of 10 years duration; and design patents of 10 years duration. The system is compliant with the WTO Agreement on Trade-related Aspects of Intellectual Property Rights ("TRIPS Agreement"), with Paris Convention priority. This means that if a patent application for an invention or utility model patent is first filed in another Convention-member country within 12 months before the filing date in China, the prior filing date will be regarded as the priority date in China. In the case of design patent applications, the relevant period is six months.

The Patent Law grants protection to inventions, utility models and designs. An invention comprises any new technical solution regarding a product or a process or an improvement thereof. This includes pharmaceutical products and substances obtained by means of a chemical process. Utility model comprises any new technical solution proposed for the shape or structure of a product or a combination thereof that is capable of practical use. Design relates to any new shape or pattern of a product or the combination of color, shape and pattern thereof that creates an aesthetic feeling and is suitable for industrial application.

The revised Patent Law tightens the criteria for patenting designs to combat "junk" design patents. To enjoy protection, designs must now possess "obvious distinctions" from either the prior art or combinations of prior art features. The patenting of two-dimensional designs (e.g., labels) will be prohibited where the graphics or colors or their combination are mainly used as indications of source.

The patentability of business method software patents remains unclear and obtaining protection is difficult.

Foreign applicants are required to submit patent applications in China through an officially designated patent agent, and should not apply directly to the Patent Office. International applicants may be granted a Chinese patent only after the applicant has carried out the relevant procedures in the PRC Patent Office. A patent applicant whose application is rejected by the Patent Office may request a re-examination by the Patent Review Board ("PRB"). The decision of the PRB may be appealed to a People's Court.

Under the revised Patent Law, inventions that are completed in China need to first be filed in China or undergo a security review in China, before being filed overseas. Parties that fail to do so risk losing their patent rights.

In addition, the revised Patent Law expands the definition of "prior art" to include any technologies or designs that are known to the public inside or outside China before the application date.

The right to apply for patents in relation to inventions, utility models and designs lies in the first instance with the inventor, subject to contractual provisions to the contrary. Where inventions, utility models or designs are created as a result of carrying out employment duties or primarily by using the materials and resources of an employer, the right to apply for patents belongs to the employer. The right to apply for patents in relation to inventions or designs unrelated to employment belongs to the inventor or designer. As in other jurisdictions, defining the scope of employment is crucial in determining patent rights. The Patent Law further states that in cases where inventions or designs are created as a result of using the materials and resources of the employer, if the employer and the employee have entered into a contract stipulating ownership of the patent application rights and patent rights, the contract will prevail.

The revised Patent Law creates a new basis for rejecting patent applications that warrants close attention by patent owners accustomed to relying on continuation or continuation-in-part filing strategies. Prior applications for similar technologies or designs filed by any party, including the same applicant, will in future be deemed conflicting.

From the date a patent is granted, any party may apply to the PRB to invalidate the patent on the ground that its grant does not comply with the Patent Law. The PRB's decision in an invalidation application may be judicially reviewed.

Patent infringement occurs when aspects of a product fall within the scope of the protected claims of a patented item. The time limit for patentees to file infringement actions is two years from the date the patentee becomes aware of or should have become aware of the infringing activity. Infringement suits may be brought either through the People's Courts or through local Patent Management Bureaus. Administrative decisions may, however, be appealed to the People's Courts. As an interim measure, the patent owner may request the Court to issue orders for preservation of property and / or evidence. Security must be provided with the application.

The Patent Law stipulates that compensation for patent infringement should be calculated by reference to the loss suffered by the patent owner or the gain reaped by the infringer as a result of the infringement. If the patent owner's loss and the infringer's gain are both difficult to calculate, one to three times the reasonable patent license fee may be considered. The 2015 Opinion amended this position by providing that courts are not to be bound by the one to three times multiplier but will instead have the discretion to decide a figure outside this range. The revised Patent Law additionally provides that the patent owner is entitled to claim back reasonable expenditures incurred as a result of any actions taken to stop infringement. It also raises the maximum amount of statutory damages the court can award in situations where the license fee is difficult to determine from RMB500,000 to RMB1,000,000. Furthermore, the 2016 Opinion proposes to introduce a pro-patentee damage calculation and a reversed
burden of proof. If it is difficult to determine the actual loss suffered by a rights holder, a court shall require the rights holder to furnish evidence to prove the gains obtained by the infringer. However, where a rights holder has provided prima facie evidence, but the account books and materials are mainly controlled by the infringer, the court may then order the infringer to submit the account books and materials. If the infringer refuses, then the court may determine the amount in accordance with the right holder's claim.

The revised Patent Law permits two categories of acts, which previously would have been regarded as patent infringement. Parallel importing has essentially been legalized. A new "Bolar Exemption", which allows the manufacture, use and import of patented pharmaceutical products or medical devices to obtain regulatory approval, has also been introduced.

In addition, the revised law adds provisions on compulsory licensing, mainly to codify existing regulations and ensure compliance with China's obligations under the TRIPS Agreement. On March 15, 2012, the State Intellectual Property Office ("SIPO") issued the revised Measures for Compulsory Licensing of Patent Implementation (the "Measures"). The Measures incorporate relevant provisions from the Patent Law and set out the procedural requirements for compulsory license applications. Overall, these Measures formalize the procedures for the application and issuance of compulsory licenses, including for the purpose of dealing with public health crises, and arguably provide patentees with greater legal certainty.

As in Europe, various forms of compulsory licenses may be applied for in different cases, such as non-exploitation of a patent or national emergency, but all are subject to payment of license fees to the patentee as mutually agreed by the parties or as stipulated by the Patent Office.

The current Patent Law is subject to another round of revisions, and the most recent draft of the fourth amendment to the Patent Law was released for public comments on April 1, 2015. For dispute resolution, the Notice on Improving the Handling of Patent Ownership Disputes issued on May 17, 2016 sets out five requirements local intellectual property bureaus should follow. These include stricter thresholds for case filing, fast mediation, prompt communication, information disclosure and supervision and guidance. Along with the Key Working Points on Administrative Affairs for 2016 issued on May 19, 2016, SIPO has announced that the Patent Administration Department will publish information on patent administrative enforcement cases on a monthly basis as part of its effort to be more transparent. These changes reflect China's continued efforts to improve its patent law system. This is evidenced in SIPO's Patent-Intensive Industries Catalogue (2016) released on October 27, 2016, which found that patent-intensive industries can strongly enhance the national economy and are highly competitive in the market.

10.2 Trademarks

The Trademark Law of the People's Republic of China (the "Trademark Law") was amended for the third time with effect on May 1, 2014. The revisions to the Implementing Regulations of the Trademark Law (the "Implementing Regulations") were published on April 29, 2014 and also came into effect on May 1, 2014.

On July 14, 2016, SIPO published an opinion on reforming trademark registration, which proposed improvement measures including the introduction of additional ways of registration and delegation of

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6 http://www.sipo.gov.cn/tz/jg/201504/t20150401_1095939.html
7 http://www.sipo.gov.cn/tz/jg/201605/t20160526_1271586.html
8 http://epaper.legaldaily.com.cn/fzrb/content/20160520/Articel060009GN.htm
registration and examination functions. One of the main objectives of the reform is a further reduction in the existing nine-month trademark examination time period.\footnote{http://www.saic.gov.cn/zwgk/zyfb/zyjd/201607/t20160725_170018.html (see Article 10).}

The Trademark Law imposes a strict first-to-file rule for obtaining trademark rights, whereby the first party to file for registration of a mark pre-empts later applicants. Prior use of an unregistered mark is generally irrelevant for trademark registration purposes, unless the prior mark in question is a well-known mark, or the later filing is a bad-faith pre-emption of the prior mark that has achieved a certain degree of fame through use.

An application for trademark registration must be filed with the Trademark Office of the SAIC. Under the revised Trademark Law, the Trademark Office is required to complete preliminary examination of an application within a shortened timeframe of nine months from the filing date. After a trademark application has been granted preliminary approval by the Trademark Office, it will be published in the PRC Trademark Gazette. If no opposition is filed within the statutory three-month opposition period, the PRC Trademark Office will publish an announcement in the Trademark Gazette and issue a registration certificate.

The Trademark Law provides that any "visually perceptible" sign capable of distinguishing the goods of one natural person, legal person or other organization from those of another may qualify for registration as a trademark. The sign may take the form of words, figures, letters, numbers, three-dimensional signs, color combinations, sounds, or a combination of any of these elements. The revised Trademark Law allowed the registration of sound marks for the first time. However, single-color marks, smell and taste marks are still not available for registration. Collective marks and certification marks may be registered as trademarks in China. Geographical indications may be registered as collective or certification marks.

The revised Trademark Law permits multi-class trademark applications. Applicants are generally required to follow standard specifications of goods and services when filing their trademark applications, and the Trademark Office will issue amendment notices if changes to non-standard specifications are necessary.

Under the revised Trademark Law, oppositions based on absolute grounds may be filed by anyone, but oppositions based on relative grounds (i.e., conflicts with prior trademarks or other rights) may only be filed by a prior rights holder or a "materially-interested party". Under the revised Trademark Law, if the Trademark Office rejects an opposition, the opposed mark will proceed straight to registration. If dissatisfied, the opposing party has no opportunity to appeal the Trademark Office's decision but will instead have to apply to the Trademark Review and Adjudication Board to invalidate the disputed trademark. Alternatively, a party interested in removing a mark may consider filing a cancellation action against that mark based on three years of non-use, if applicable.

A trademark registration is valid for 10 years from the final date of approval (i.e., upon expiration of the three-month opposition period or, for international trademark registrations extended to China under the Madrid Agreement or the Madrid Protocol, the date of filing), with further 10-year renewal terms available. Under the revised Trademark Law, renewal applications can be filed with the Trademark Office during the last 12 months of the current term or, subject to payment of an additional fee, within six months after expiration of the term.

Trademark owners pursuing oppositions and cancellations may seek formal recognition of their marks as "well-known" (\textit{	ext{chi ming}} in Chinese), thereby aiding attempts to block others from registering similar marks covering technically dissimilar goods or services. Determinations on well-known status are made on a case-by-case basis. An interpretation issued by the Supreme People's Court allows courts to formally recognize the well-known status of a mark during a civil dispute. The revised Trademark Law also provides clarification as to the proceedings in which well-known mark protection can be sought.
Where a PRC-registered trademark is assigned, the assignor and assignee must execute an application, which must be filed for approval with the Trademark Office. Upon approval, the assignment will be gazetted. Legal title to the trademark is not deemed to pass from the assignor to the assignee until the assignment has been approved by the Trademark Office.

The Trademark Law requires a trademark registrant to enter into a written license contract when licensing a PRC-registered trademark to third parties. The revised Trademark Law no longer requires submission of a copy of the trademark license agreement for recordal purpose. However, a trademark license that has not been recorded may not be used against a bona fide third party.

The revised Trademark Law provides a modified list of acts of registered trademark infringement. Moreover, it expands on the fair use defense. This includes an exception for the legitimate use of generic and directly descriptive wordings. More importantly, the revised Trademark Law now provides a prior use exception. Although not stipulated, prior use will most likely need to have occurred in China for the exception to apply.

Interim measures are available in trademark infringement cases brought before civil courts, including the issuance of injunctions and seizure of evidence by judicial authorities. The revised Trademark Law has significantly increased the amount of statutory damages of up to RMB3,000,000, which is six times the previous amount, in cases where the plaintiff's loses, the defendant's profits, or trademark royalties cannot be easily proved. Further, the civil courts can compensate trademark owners for enforcement-related expenses, including legal and investigation costs (although such awards are normally modest). The revised Trademark Law also introduces punitive damages in cases involving bad faith infringement of a trademark.

Administrative enforcement authorities, known as Administrations for Industry and Commerce ("AICs"), and civil courts are authorized to confiscate and destroy infringing products and trademark representations and the equipment used to make them.

Under the revised Trademark Law, AICs are now entitled to impose much higher fines. If there is no illegal turnover or the illegal turnover is less than RMB50,000, the AICs can impose a fine up to RMB250,000. Where the illegal turnover is over RMB50,000, the AICs can impose fines of up to five times the illegal turnover. The revised Trademark Law also provides for heavier penalties in cases involving repeat offenders or other serious circumstances.

There may be criminal liability if the value of the counterfeited goods exceeds certain thresholds. Currently, the matter will be regarded as serious and criminal liability could attach where the value of the goods exceeds RMB50,000.

The 11th edition of the Nice Classification will enter into force on January 1, 2017. The Trademark Office has made corresponding changes to the Classification Index of Similar Goods and Services, which will also take effect on January 1, 2017. In general, the Trademark Office adheres quite strictly to the Classification Index, and applications to register trademarks in China should be for "standard" items as the Trademark Office may issue amendment notices for applicants to fix "non-standard" items.

10.3 Copyright

The Copyright Law of the People's Republic of China (the "Copyright Law") was amended with effect from October 27, 2001, and its Implementing Regulations (the "Implementing Regulations") were amended with effect from September 15, 2002. The Copyright Law was again amended in 2010 with effect from April 1, 2010 (the "2010 Amendment") and the Implementing Regulations were revised with effect from March 1, 2013. The 2010 Amendment was in response to a 2009 WTO dispute, and attempts to confirm that "illega" works can obtain copyright protection. In recent years, the PRC National Copyright Administration ("NCA") and the State Council have been working on draft
amendments to revise the Copyright Law. Between 2012-2014, the proposed draft amendments have gone through four rounds of public consultation. The latest draft amendments were released for public comments on June 6, 2014. While various stakeholders have been consulted, the draft law has still not been submitted to the Standing Committee of the National People's Congress.

The current Copyright Law introduces protection for (1) written works, (2) oral works, (3) musical, dramatic, Chinese folk art, choreographic and acrobatic works, (4) works of fine art and architectural works, (5) photographic works, (6) cinematographic works, (7) graphic works, (8) model works, and (9) computer software. The Copyright Law does not protect databases, i.e., collections of original information that do not qualify for copyright protection. However, if the means of compilation satisfies the requirement of originality, then such compilation can be protected.

The Implementing Regulations provide protection for performances and sound recordings produced or distributed by foreigners and stateless persons, provided that (1) the performances or sound recordings are performed or created in China, or (2) the foreign country where the foreigner performed or created the performances or sound recordings has signed treaties with China. Likewise, protection is explicitly recognized for rights in radio and television programs broadcasted by foreign radio and television stations, provided the country where the radio / television station is located has signed treaties with China.

In compliance with Article 3 of the Berne Convention, the Implementing Regulations clarify that works created by foreigners or stateless persons that are published in China within 30 days after first publication outside China will be deemed to have been simultaneously published in China.

Under the Copyright Law, an author's moral rights of attribution, revision and integrity are perpetual. A citizen's right of publication and the various economic rights are protected for the duration of the life of the author plus 50 years. For works of a legal person or other organization, or works for hire vested in a legal person or other organization, as well as for photographic works and cinematographic works, the right of publication and other economic rights are protected for a period of 50 years from the date of first publication.

Registration is not a precondition to copyright enforcement but can provide prima facie evidence of ownership in enforcement actions.

The Implementing Regulations require exclusive license agreements to be in writing, and also provide for the voluntary recordal of licenses and assignments. Both full and partial assignment of economic rights in copyrighted subject matter are permissible.

The Copyright Law and relevant judicial interpretations introduce provisions on the enforcement of copyright through civil and administrative measures. Preliminary injunctions may now be sought against copyright infringers, but this is rare in practice. In cases where the plaintiff's damages or the infringer's profits cannot be determined, statutory damages of up to RMB500,000 may be awarded. In the latest draft amendments to the Copyright Law, this ceiling has been raised to RMB1,000,000.

The NCA and local copyright bureaus, the primary government bodies designated to handle administrative enforcement against infringers, are authorized to exercise a wide range of powers. These include the power to issue administrative injunctions, confiscate the illegal income of infringers, confisicate and destroy infringing copies, impose fines, and confiscate materials, tools and facilities primarily used for the production of infringing copies. The 2013 amendment to the Implementing Regulations empowers the local enforcement authorities to fine infringers up to five times the revenue generated from the illegal transactions, or up to RMB250,000 in cases where the revenue cannot be calculated. However, in practice, the copyright bureaus' enforcement capability is poor, as they do not have sufficient resources. In several provinces such as Guangdong and Zhejiang, a local administrative body called the Bureau of Culture, Radio, Television, News and Publication has been established to
handle administrative enforcement for copyright, and appears to have greater resources for anti-piracy actions.

The Criminal Code sets out the criminal penalties for copyright infringement. For individuals and sole proprietors engaged in the illegal reproduction or distribution of copyrighted works, crimes may be deemed to have been committed when the value of the counterfeited works manufactured or stored exceeds RMB50,000, the illegal income generated exceeds RMB30,000, or the unauthorized units reproduced exceed 500 units. For enterprise offenders, the thresholds are three times the above amounts.

10.4 Internet

Article 10(12) of the Copyright Law provides a "right of communication through information networks" for copyright holders. The Measures for the Administrative Protection of Internet Copyright (the "Internet Copyright Measures"), which came into effect on May 30, 2005, facilitate more efficient administrative enforcement against copyright infringement on the Internet by imposing administrative liability on Internet service providers ("ISPs") and by providing for administrative penalties. Under the Internet Copyright Measures, upon receipt of a notice from a copyright owner of alleged infringement, the ISP is required to remove the offending content from its service and retain records of the provided information. Similar take-down provisions are found in the Regulations for the Protection of Right of Communication through Information Networks ("RPRCIN"), which entered into force on July 1, 2006 and was revised on March 1, 2013. The RPRCIN introduced civil liability for circumventing technical protection measures, as well as ISP liability and safe harbors for third party copyright infringement. According to the newly amended RPRCIN, an infringer may be fined up to five times the revenue generated from the illegal transaction, or up to RMB250,000 in cases where the revenue cannot be determined. The Supreme People's Court also introduced judicial interpretations which explicitly criminalize online infringements, subject to the requirement in the Criminal Code that such infringements be for profit. The civil enforcement against online infringements is governed by a separate judicial interpretation concerning online copyright disputes, which was last amended on January 1, 2013.

The China Academy of Telecommunication Research's annual report for Internet copyright protection in 2015 revealed that China copyright enforcement authorities investigated and penalized a total of 383 copyright infringement cases in 2015. Of these 383 cases, 59 cases were transferred to the judiciary for criminal treatment. In total, around RMB4.5 million in administrative penalties were issued and 113 websites were shut down.

10.5 Computer software


To implement the TRIPS Agreement, the Software Regulations provide for rental rights and the right of communication through information networks for software. Consequently, online distribution of software without authorization (whether for profit or otherwise) is considered a prohibited form of reproduction. Further, the Software Regulations provide explicit protection against activities that attempt to circumvent or sabotage technological measures used by software copyright owners. Likewise, the Software Regulations outlaw the removal or alteration of electronic rights management information incorporated into works to facilitate copyright protection.
In the case of software owned by legal persons and other organizations, the period of protection is 50 years, ending on December 31 of the fiftieth year after the work was published. If the software is not published within 50 years after its creation, no protection is provided.

The Software Regulations permit registration for the purpose of providing prima facie evidence of ownership and validity of software. The Measures for the Registration of Copyright in Computer Software apply to the registration of software copyright, exclusive software copyright license contracts, and assignment contracts.

Under the Software Regulations, administrative and civil liability for infringement by reproducers of software appears to be provided on a strict liability basis, and reproducers will only be able to avoid liability if they can prove they were lawfully authorized. Parties accused of distributing or renting software can be pursued if they are unable to provide evidence that the software is from a lawful source. The Software Regulations impose a significant limitation on the ability of copyright owners to pursue infringing end-users, i.e. parties that use software, but do not copy it in the routine sense. A party that possesses infringing software will not be liable to pay compensation if he or she did not know or did not have any reasonable grounds to know that the software was infringing. However, they may be ordered to immediately stop using such software and destroy infringing copies.

Rights holders can file complaints with either civil courts or administrative enforcement authorities. The Software Regulations also give administrative authorities powers to deal with infringements, including the power to issue injunctions, confiscate illegal income of infringers, confiscate or destroy infringing products, and impose fines. In serious cases, administrative authorities may also confiscate materials, tools, and facilities primarily used for the production of infringing copies.

The Software Regulations specify a maximum fine of RMB100 for each pirate reproduction. Alternatively, a fine of one to five times of the value of the goods may be imposed in cases involving unauthorized reproduction of all or a portion of the software, as well as unauthorized distribution, rental or transmission via information networks (e.g., the Internet). Furthermore, fines of up to RMB200,000 may be imposed for wilful evasion or destruction of anti-circumvention measures.

The Software Regulations refer to the possibility of obtaining preliminary injunctions in software disputes brought before the Chinese courts. In addition, the Software Regulations explicitly state the possibility of pursuing copyright violations under China's Criminal Code.

10.6 Domain names

China has issued various regulations to regulate the use of domain names. These include the Measures for the Administration of Internet Domain Names in China, which took effect in 2004, and the Detailed Implementing Rules of the China Internet Network Information Center for the Registration of Domain Names (the "Registration Rules"), effective from 2002. The Registration Rules were amended in 2009, and again in 2012. The current Registration Rules are effective from May 29, 2012.

In March 2016, the Ministry of Industry and Information Technology ("MIIT") circulated a new Draft Regulation for the Administration of Internet Domain Names in China. Although further amendments may be expected following public consultation, it is worthwhile to highlight some of the key changes that the Draft Regulation brings. The proposed changes include the removal of having a requisite capital for registry approval and the addition of the requirement of good credit records for the main registered personnel. Depending on further clarifications, Article 37 of the Draft Regulation is quite vague and may significantly impact foreign websites in China. This provides that network access for domain names within China should be provided by domestic domain name registration service agencies.
and could mean that domain names that are not part of these agencies will not gain network access. The result of this provision will be that overseas registered domain names will need to register a local domain name. Otherwise an Internet access provider cannot provide that domain with the necessary network access services. If this provision remains unchanged and comes into force, businesses with foreign domain names will have to apply for registration of a Chinese domestic domain name.

The Registration Rules cover applications to register domain names with ".cn" as the top-level domain and Chinese-language domain names administered by the China Internet Network Information Center ("CNNIC"). Any natural person or organization that can independently assume civil liability may apply for domain name registration. Applications should be submitted in writing. The "first-to-file" principle continues to apply, i.e., priority is given to the first applicant who files a valid application. Applications for approval can be made to the domain name registrar for the assignment of domain names.

The Registration Rules have strengthened the privacy of domain name registration information through explicit provisions on the transmission, storage, disposal, and destruction of such information.

Domain name dispute resolution is governed by several measures, which focus on the procedural rules for registration and dispute resolution. These measures apply to disputes that arise due to the registration or use of ".cn" domain names or Chinese-language domain names under the administration of the CNNIC. Such disputes can be accepted and resolved by special dispute resolution bodies recognized by the CNNIC, which include the Domain Name Dispute Settlement Center of the China International Economic and Trade Arbitration Commission ("CIETAC") and the Hong Kong International Arbitration Center ("HKIAC"). Any organization or person that believes there is a conflict between a domain name registered by another party and its lawful rights and interests may submit a complaint to one of these dispute resolution bodies. If the complaint meets the specified conditions, the domain name holder will be required to participate in the dispute resolution proceedings. The measures are only applicable to disputes relating to domain names that have been registered for less than two years. Rulings of the dispute resolution bodies, however, are not final. Either party is entitled to commence civil litigation before, during or after such proceedings.

The Supreme People's Court Explanation issued in October 2002 makes it clear that the following conduct constitutes trademark infringement: registering, as a domain name, words that are identical or similar to the registered trademark of a third party, and using that domain name to carry out e-commerce trade in related products, thereby easily causing confusion among the relevant public.

10.7 Trade secrets

A trade secret is defined in both the Law of the PRC Against Unfair Competition ("Unfair Competition Law") and the PRC Criminal Code as technical and business information which is private, able to bring economic benefits to the rightful party, is practical, and for which that party has adopted measures to maintain its confidentiality. The Draft Anti-Unfair Competition Law released in early 2016 proposed language that changes the requirement for the information to bring economic benefits to the rightful party to the information needing to have "commercial value". A non-exhaustive list of measures to maintain confidentiality is set forth in the Several Provisions on the Prohibition of Acts of Infringement of Trade Secrets (the "Trade Secrets Provisions"), effective from November 23, 1995 and amended on December 3, 1998. Such measures include disclosing secrets on a need-to-know basis only, adopting physical preventive measures such as locking, marking information "confidential", requiring access codes and passwords, and requiring confidentiality agreements.

Trade secrets are protected under the Anti-Unfair Competition Law. Under the legislation, business operators are prohibited from infringing upon commercial secrets by obtaining the commercial secrets of others by theft, inducement, coercion or other illicit means; revealing, using or allowing others to use commercial secrets obtained by such means; and revealing, using or allowing others to use
commercial secrets of others which are in their possession by violation of agreements or other requests for confidentiality by the owners concerned. If a third party knows or should have known of such acts violating the law, but obtains, uses or reveals commercial secrets of others, this will also constitute infringement.

Under a Supreme People's Court Interpretation on intellectual property crimes issued in 2004, the infringement of a trade secret causing loss in excess of RMB500,000 will be regarded as serious and will trigger criminal prosecution under the PRC Criminal Code. Loss caused in excess of RMB2.5 million are considered exceptionally serious.

China's legal framework for the protection of intellectual property is comprehensive, but the challenge is for China to enforce the legislation effectively and transparently. In November 2016, SIPO issued the Guiding Opinions on Accelerating the Building of Strong IPR Cities, which proposed that by 2020, China will build around 20 cities characterized by leading intellectual property and innovation-driven development in national priority development areas.\(^\text{12}\) By 2030, the goal is for China's main cities to be characterized by smooth mechanisms, integration, full vitality, and openness of intellectual property development.\(^\text{13}\)


\(^{13}\) Ibid.
11. Employment Issues

11.1 Employment contracts

Under China's Labor Law and Employment Contract Law, employers, including foreign-invested enterprises ("FIEs"), must conclude an individual written contract with each full-time employee. Employment contracts may be for a fixed or open term (or, more rarely, the term may be determined based on the completion of a project), though in light of potential difficulties that employers may encounter in trying to terminate employees, it is generally advisable for employers to fix the term of an employment contract to keep the term relatively short. However, under the Employment Contract Law (and subject to local interpretations of the law), employers will only be able to sign or renew an employment contract with an employee for two fixed terms after January 1, 2008, before having to sign an open-term contract with that employee. As of the date of publication, with the exception of Shanghai, this requirement under the Employment Contract Law effectively shortens the time for an employee to become entitled to request an open-term contract from 10 years to the expiration of the second fixed term contract (which may take place in as short as two years if both contracts are for a one-year term).

Probationary periods are generally included in the first employment contract signed with an employer. Under the Employment Contract Law, the allowable length of the probationary period depends on the length of the contract term, with a maximum possible period of six months.

Restrictions apply to agency or contingency workers who can be hired only for "temporary" (lasting for no more than six months), "auxiliary" (supporting core business of a company, as determined through the mandatory "employee consultation" procedures), or "substitutable" (where the employee who originally took the position is on leave for a certain period of time for full-time study or leave) positions, and cannot exceed 10% of a company's total workforce.

11.2 Labor unions and collective contracts

There is strong political pressure to establish labor unions in FIEs, although national law assigns the primary responsibility for initiating union establishment with the employees rather than enterprise management. The labor union may be controlled by an enterprise branch of the Communist Party. Other bodies potentially participating in "democratic management" of FIEs are employee representative councils and employee representatives on Supervisory Boards.

Collective contracts may be concluded between an enterprise and its labor union or an elected employee representative. If an enterprise receives a written request for collective bargaining from its labor union or an elected employee representative, enterprise management cannot refuse the request unless it has a justifiable reason for doing so. Collective contracts are binding for all employees of the company. Accordingly, individual employment contracts cannot include standards that are lower than those set forth in the collective contracts. However, it is possible to agree in an individual employment contract on terms that are more favorable to the employee.

There are also special consultation procedures for the adoption of employee handbooks and other company rules and matters that directly affect the immediate interests of the employees.

11.3 Representative offices

Representative offices are a special case. Representative offices are not permitted to directly employ their staff. Instead, representative offices enter into labor service contracts with qualified labor service
companies, pursuant to which Chinese nationals are employed by the labor service companies and are then seconded to work as the staff of the representative offices.

In exchange for providing this employment service, the labor service companies receive a service fee. Depending on the practice of the particular labor service company and the labor service contract agreed to by the relevant representative office, salary and social insurance and housing fund payments in respect of the Chinese staff may be paid to the labor service company, which then distributes payments to the staff and social insurance and housing fund authorities respectively, or salary and social insurance and housing fund payments may be paid by the representative offices directly to the staff.

While there is no employment contract between representative offices and their Chinese staff, representative offices may enter into agreements with their Chinese staff that supplement the provisions of the relevant labor service contracts. Such supplementary agreements typically cover subjects such as remuneration, duties, certain company policies and confidentiality and non-competition obligations.

Though technically, representative offices are not the employer, labor service companies will generally bring in the representative offices as co-defendants if the employee raises any claims against the labor service company in relation to a dispute with the representative office.

Expatriate (non-Chinese, including Hong Kong, Macau and Taiwan residents) staff of representative offices generally are employed by the foreign parent company pursuant to employment contracts governed by foreign law. Such expatriates should be registered as representatives in accordance with registration formalities prescribed by the Chinese authorities. One representative office is only allowed to have up to four registered representatives.

### 11.4 Termination and resignation

In China, there is no concept of "at will" employment or simple termination with notice as in some other countries. While employees generally may resign upon 30 days' prior notice to the employer or 3 days' notice during the probationary period, employers in China are permitted to unilaterally terminate employees only in accordance with circumstances stipulated in relevant laws and regulations.

In some permitted circumstances of termination (such as where an employee is incompetent and remains incompetent after training or assignment to another post), 30 days' prior notice (or pay in lieu) and severance payments are required. The severance payment will generally equal one month's total wages for each year of service. For any period of service after January 1, 2008, if the employee's monthly wage exceeds 300% of the average local wage, then his "monthly wage" amount is capped at that ceiling, and the employee would only be entitled to up to 12 months' wages for severance. The specific statutory calculation methods are subject to local regulations.

There are also grounds for summary dismissal with no severance payable (e.g. serious violation of company rules and regulations).

### 11.5 Social insurance and housing

Under Chinese law, both Chinese citizens and expatriate employees are required to participate in China's social insurance scheme. In practice, most cities now mandate expatriates working under a work permit in China to participate in the social insurance system, though some cities (e.g., Shanghai) currently have not yet implemented a system to mandate social insurance contributions for expatriate employees. China's social insurance scheme consists of five funds: Old Age Pension Insurance, Basic Medical Insurance, Occupational Injury Insurance, Unemployment Insurance and Maternity Insurance. Employers and employees are required to make contributions to the funds, and in some cases to individual employee government-held accounts, in accordance with rates determined by
local authorities. In addition, employers and employees are required to contribute to a Housing Provident Fund for the purpose of buying, building and renovating employee housing. Housing fund contributions are currently not required for expatriates.

11.6 Visas and residence

Under various laws and regulations, all foreigners, except those with permanent resident status in China, may only work in China with prior permission of the relevant authorities. The term "work" in these rules is defined as engaging in behavior of a remunerative nature, and "work in China" means discharging one's employment duties in China pursuant to either (a) an employment contract signed directly with a legal person in China, regardless of the length of employment in China or (b) an employment contract signed with a legal person outside China, the source of employment compensation is located outside China, and the work performed within China territory is for more than 3 months (90 days) in any year. According to a notice regarding the trial procedures for foreigners to enter China and accomplish short-term work assignments, there will be a short-term work certificate that came into effect as from January 2015. Foreigners who will stay in China not more than 90 days under the following circumstances must go through a certain process to obtain short-term work authorization in China: 1) to carry out assignments regarding technology, scientific research, management, guidance with domestic partners; 2) to be on trials with domestic sports institutions (including coaches, athletes); 3) to shoot films (including commercials, documentary); 4) to perform in fashion shows (including car models, models for print advertisement); 5) to participate in a commercial art performance; and 6) other circumstances as recognized by human resources and social security departments.

Generally, the immigration and labor registration procedures for a foreigner working in China can be summarized as completing the following six steps and obtaining the required permits as stated below: (1) medical examination; (2) Work Permit Notice; (3) Single Entry "Z" Visa; (4) Temporary Residence Registration; (5) Work Permit; and (6) Residence Permit. A Residence Permit functions as a multi-entry Chinese visa, which will enable the foreigner to stay in China for a certain period of time (normally one year) and to exit and re-enter China for international travel within this period.

For foreign representative offices in China who wish to employ a foreigner as a chief representative or ordinary representative, the Work Permit Notice is not required. Instead, the representative office should first register the foreigner with the local Administration Bureau for Industry and Commerce as its chief representative or ordinary representative. Thereafter, the foreigner can go through the above steps (other than step 2) to secure his / her Work and Residence Permits. There is a cap (which is currently 4) on the number of representatives that a representative office may register.

Change of status, where the foreigner first arrives on either a business or a tourist visa, and then seeks to obtain a Work Permit directly in China, may be possible in some localities but usually limited to very exceptional cases.

Different rules and application procedures apply to Chinese nationals with permanent residence abroad and permanent residents of Hong Kong, Taiwan and Macau.
12. Taxation

This section introduces the major taxes applicable to foreign investors doing business in China and outlines recent legislative developments.

12.1 Income taxes

12.1.1 Enterprise income tax

Historically, one income tax system applied to domestic enterprises ("DEs") and another applied to foreign enterprises ("FEs") and FIEs. FIEs include Sino-foreign equity joint ventures, cooperative joint ventures, and wholly foreign-owned enterprises. The statutory income tax rate was 33% (comprising a 30% national rate and a 3% local rate) and applied to DEs and some FIEs. Many FIEs enjoyed 15% or 24% preferential tax rates, as well as tax holidays.

Introduced with the goal of creating a level playing field, the Enterprise Income Tax Law ("EIT Law") was promulgated on May 16, 2007 and took effect on January 1, 2008. The EIT Law provides unified income tax treatment for both DEs and FIEs. On December 11, 2007, the State Council released the Enterprise Income Tax Implementing Rules ("Implementing Rules"), which also took effect on January 1, 2008. Pursuant to the EIT Law and the Implementing Rules, a resident enterprise (including an FIE) is subject to tax on its worldwide income. Foreign tax credits are allowed for income taxes paid to other countries by the resident enterprise, limited to the Chinese income tax payable on the same income.

Non-resident enterprises and other economic organizations which have establishments in China, or which derive certain income from China, are subject to tax only on their income from China sources. Group consolidation is not allowed in China.

For many foreign investors, the EIT Law results in a higher tax burden with the elimination of most preferential tax rates and holidays and a harmonized tax rate of 25%. However, the EIT Law provides for a transition period of five years for FIEs that enjoyed certain preferential rates or tax holidays under the old system. The tax rate for these existing FIEs increased gradually from the pre-2008 concessionary rate to the new rate of 25% by 2012. Although the EIT Law repealed most tax incentives for FIEs, it provides tax incentives for both FIEs and DEs that invest in high technology, venture capital, and certain other encouraged industries.

Withholding tax is imposed on dividends, interest, royalties, rental income, gain from the transfer of property and other China-sourced income, which is derived either:

• by a non-resident enterprise without an establishment in China; or

• by a non-resident enterprise with an establishment in China, when the income is not effectively connected with that establishment.

Dividends were exempted from withholding tax under the old system but are now subject to withholding tax under the EIT Law. The statutory withholding tax rate on all forms of passive income paid to non-resident enterprises is 20% but the Implementing Rules reduce the rate to 10%. The statutory withholding tax rate is also subject to reduction by a tax treaty when applicable. However, with the exception of a handful of tax treaties that address certain types of royalties and capital gains, the vast majority of China's tax treaties generally do not improve the withholding tax treatment that is already available under the domestic law.
12.1.2 Individual income tax

In accordance with the Individual Income Tax ("IIT") Law, IIT is imposed on all individuals, including both Chinese and foreign nationals, residing in or deriving income from China. Chinese residents are generally subject to tax on their worldwide income while non-residents are taxed on their China-sourced income only. IIT is imposed on income from wages and salaries at progressive rates from 3% to 45%; on capital gains at a flat 20% rate; and on interest, dividends and royalties at a flat 20% rate. China instituted annual income tax returns from 2006 for individuals earning over RMB120,000 per year (roughly USD17,000).

12.2 Turnover taxes

12.2.1 Value-added tax

The sale of goods, repair and replacement services and the provision of labor services in relation to the processing of goods within China are subject to value-added tax ("VAT"). VAT is also levied on the import of goods into China unless the imports are specifically exempted under special rules. Provision of other services and transfer of immovable or intangible properties within China used to be subject to business tax, but are now brought within the scope of VAT under the VAT pilot program. According to Cai Shui [2016] No. 36, the phrase "provision of services within the territory of China" is interpreted to mean that either the service provider or the service recipient is located in China, but should exclude services provided by a foreign individual or unit to a Chinese individual or unit if such services take place completely outside of China.

The standard VAT rates for general VAT taxpayers are 17% for the sale or importation of goods, 11% for the transfer of immovable properties and land use rights, 6% for the transfer of intangibles other than land use rights, and 17%, 11% or 6% for the provision of services, depending on the nature of services. General VAT taxpayers may utilize input VAT credits, including the VAT paid for the purchase of fixed assets, to offset against output VAT. The standard VAT rate for small-scale VAT taxpayers is 3%, with an exception that small-scale VAT taxpayers will be taxed at 5% on revenues from the leasing or sale of immovable property. No input credits are available to small-scale VAT taxpayers. In general, exports are exempted from VAT, and the related input VAT may be wholly or partially refunded. The non-refundable portion is absorbed as a cost of export.

12.2.2 Stamp duty

Stamp duty is levied on the execution or receipt in China of certain documents, including contracts for the sale of goods, the undertaking of processing work, the contracting of construction and engineering projects, leases, loans, and agency and other non-trade contracts. Stamp duty is also levied on documentation effecting the transfer of property / shares, on business account books and on certificates evidencing rights and licenses. The rates of stamp duty vary. For the transfer of shares in a Chinese enterprise, the applicable stamp duty rate is 0.05% of the contract value for each party.

12.2.3 Consumption tax

Consumption tax is levied on the importation, production and processing of 14 categories of consumable goods, including tobacco; liquor and alcohol; luxury cosmetics; expensive ornaments, pearls, jewels and jade; firecrackers and fireworks; oil products; motor vehicle tyres; motor cycles; motor cars; golf balls and golf equipment; luxury watches; yachts; disposable wooden chopsticks; and solid wood flooring.
12.3 Other taxes

Customs duties are imposed on exports and imports of goods. Most export items are duty free, and the duty to be paid on exports that are not exempt is based on the FOB value. Imports are generally assessed on their CIF (cost, insurance and freight) value, with all included charges verified by the customs administration. When applicable, the rate of duty ranges from 0% to 270%, depending on the nature and the country of origin of the goods concerned. Customs duties paid are deductible expenses for enterprise income tax purposes.

Land appreciation tax ("LAT") is levied on gains realized from real property transactions at progressive rates from 30% to 60%, based on the land value appreciation amount, which is the excess of the consideration received from the transfer or disposition of real property over the total deductible amount.

Deed tax is levied on the purchase or sale, gift or exchange of ownership of real property. The transferee / assignee is the taxpayer. Generally, the rates range from 3% to 5%.

Other taxes include real estate taxes, vehicle and vessel taxes and resource tax.

12.4 Transfer pricing rules

The EIT Law includes rules on transfer pricing. Under these rules, all business transactions between related parties must be settled according to an "arm's length" standard. If the parties fail to meet this requirement, the tax bureau may make special adjustments.

12.5 Tax treaties

China has signed bilateral tax treaties with approximately 105 jurisdictions. The treaties are primarily to avoid double taxation and to prevent tax evasion. The tax treaties generally follow the model treaty of the Organisation for Economic Co-operation and Development ("OECD") and the model United Nations treaty.
13. Dispute Resolution

Along with rapid economic growth, the number of commercial disputes submitted to litigation or arbitration in China has increased in recent years. Purchase contract disputes are at the top of the list, most of which relate to the quality of goods.

Disputes in the areas of construction, loans, freight, shipping and warehousing, intellectual property (including transfer of technology, trademark, copyright, IT, software), financial derivatives, funding, financing, insurance, joint ventures and mergers and acquisitions are also escalating.

Meanwhile, issues faced by disputing parties have become more complex. For example, as investment products and structures become more innovative and complicated, issues arising can now include matters such as satisfaction of conditions precedent, valuation adjustment mechanism, variable interest entities and dividend pay-out. In 2013, the Supreme People's Court rendered its judgment for the first valuation adjustment mechanism case. In the capital increase agreement under dispute, the company undertook to compensate the PE investor if the company failed to achieve the profit target while the former shareholder agreed to assume liability if the company failed to provide such compensation. In trying to balance the rights of the parties, the court confirmed the effectiveness of the compensation mechanism between the PE investor and the former shareholder. However, the court denied the effectiveness of the compensation mechanism between the company and the PE shareholder as the mechanism guaranteed one shareholder's profit regardless of the company's losses which was adverse to the interest of the company and its creditors. It was also in violation of Chinese law. On the other hand, CIETAC arbitrators have taken a different approach on this issue. In an arbitration dispute administered by CIETAC in 2014, the arbitral tribunal, out of respect for party autonomy and freedom of contract, upheld the validity of the valuation adjustment clause between the PE investor, the existing shareholder and the target company.

13.1 Common methods of dispute resolution

The most common forms of dispute resolution in China include arbitration, litigation, and alternative dispute resolution ("ADR") methods such as negotiation, mediation and conciliation. Similar to other regimes, ADR methods are less adversarial and more informal than arbitration and litigation. As dispute resolution develops, there also exist combinations of these methods. Some dispute resolution clauses provide that any dispute shall first be discussed among the parties, then submitted to a mediation center and finally submitted to litigation or arbitration. In addition, negotiation or mediation during the litigation or arbitration proceeding is also quite common in China.

Arbitration and litigation each have their own advantages and disadvantages. The choice of method depends on a variety of factors including the needs of the parties. For example, for international transactions involving a Chinese party, arbitration is generally recommended due to the ease of enforcement of awards internationally, and the flexibility allowed to the parties to choose the place of arbitration and the procedures for the arbitration. Each method is discussed below.

13.1.1 Litigation

China's legal system is based on the civil law system. Various courts for claims arising from commercial disputes are the Supreme People's Court, Higher People's Courts, intermediate level courts and the basic-level courts. In recent years, special courts have been set up to handle specific category of disputes, such as intellectual property court is set up to handle exclusively intellectual property disputes.

Mandarin Chinese is the official language of civil proceedings. All foreign language documents to be submitted to the courts must be translated into Chinese. Parties submitting these documents shall be responsible for their translation and cost.
The plaintiff institutes a suit by filing a complaint with the competent court having jurisdiction over the matter. The docketing department of a court is in charge of acceptance of law suits.

Unlike common law jurisdictions, there is no discovery process in China. Each party may decide to only submit favourable evidence, as there is no obligation to disclose all documents. Documents created outside China need to be notarized and legalized in order to be accepted as evidence.

Several types of costs may be payable by litigants. The most important of these is the case acceptance fee, which is levied on a sliding scale based on the value of the claim (the aggregate amount of damages sought by the plaintiff). The general rule on costs is that the losing party will pay the case acceptance fee. If both parties are held liable, the case acceptance fee may be shared. Generally, the case acceptance fee is cheaper than the arbitration fee collected by the arbitration institutions.

In principle, the hearing shall be open to the public except in the cases related to state secrets, privacy, commercial secrets or divorce. In recent years, the courts have endeavoured to improve the transparency of civil proceedings. There is a national platform disclosing judgments made by all the courts. An increasing number of courts have set up their own platforms permitting the public to search the status of cases handled by the courts. The Supreme People's Court also maintains a database where it is possible to conduct searches for enforcement actions being taken against individuals or entities.

In a domestic case without any foreign factor, the Chinese law has fixed a term within which the courts shall conclude the case.

The first instance proceeding of a general case should be completed within six months. The head of the court can approve one extension of six months, while further extensions shall be approved by the higher court. The appeal proceeding should be completed within three months. The head of the appealing court can only approve extensions in special cases. However, these time limits do not apply to foreign related cases. It is quite common that the courts may take one to three years to conclude a foreign related case.

Judgments made by the first instance court are appealable. Judgments made by both the appellate or first instance courts without any party's appeal within the prescribed period shall be final. The appeal mechanism gives the parties a chance to rectify any errors made by the first instance court. In case of any errors in the final judgment or material injustice in the proceeding, the parties can apply to the court at a higher level for a rehearing of the case. In addition, the court issuing the final judgment or at the higher level can also initiate the rehearing process by itself or upon the request of the people's procuratorate.

13.1.2 Arbitration

Arbitration is a popular alternative to litigation and China has a well-established structure for resolution of disputes by arbitration.

Arbitration in China is conducted by arbitration commissions located in various provincial capitals and cities. CIETAC is China's principal international arbitration body and deals with domestic and international commercial disputes.

In arbitration proceedings, the parties can choose the place of arbitration, arbitration rules, and their own arbitrators. Parties can appoint one or three arbitrators. This allows parties the opportunity to select professional arbitrators who can also be industry experts.

In an arbitration proceeding conducted in Chinese, the parties may not have to translate the English documents into Chinese as long as the arbitrators can read English. In addition, documents created outside China do not need to be notarized and legalized.
The arbitration process is usually held in private. This avoids any possible adverse influence from the media. Parties can also be assured that their business relationship and details of the dispute will not be disclosed in an open court hearing.

Unlike litigation, the award is final and binding on the parties when it is rendered by the tribunal. The award cannot be appealed to the courts. The award can only be set aside or refused enforcement in limited circumstances where: (i) the parties did not include an arbitration clause in their contract or conclude a written agreement; (ii) the party against whom enforcement is sought was not asked to appoint an arbitrator or take part in arbitration proceedings or was unable to present its case for reasons for which they were not responsible; (iii) the arbitration tribunal or procedure did not conform to the applicable rules; (iv) the matters decided in the award exceeded the scope of the agreement or arbitration institution; or the award violates public interest. For a domestic award (i.e. where the dispute in question has no foreign elements), other than the above grounds, it can also be set aside or denied enforcement if the other party has concealed evidence which has a substantial impact on the impartiality of the award.

The enforcement of foreign-related and foreign awards is subject to a reporting system. A court which intends to refuse enforcing a foreign-related or foreign arbitral award shall report it to the court at the next higher level, i.e. the Higher People's Court, for review. If the Higher People's Court also agrees to deny enforcement, it shall report its decision to the Supreme People's Court for approval. No foreign arbitral award shall be denied enforcement unless the Supreme People's Court so approves. The court may intervene as necessary to preserve evidence for the purpose of the proceedings, or to maintain the status quo of the parties, or to prevent the other party from removing assets from the jurisdiction which may be used for later enforcement.

13.1.3 Alternative Dispute Resolution

In China, conciliation is quite common in both civil and arbitration proceedings. In civil proceedings, the court can conduct conciliation if the parties agree. The court will issue an official mediation paper according to the parties' settlement agreement, which can be enforced in the same way as a judgment. In line with Chinese culture, PRC judges usually endeavour to conciliate a case. It is quite normal for judges to ask parties during the open hearing whether they agree to settle the dispute and then assist the parties to reach a settlement. Nevertheless, conciliation is not a mandatory procedure.

In arbitration, the rules of some arbitration institutions provide that where both parties have the desire for conciliation, the arbitral tribunal may conciliate the case during the course of the arbitration proceedings. If one party so desires, the arbitral tribunal may, upon request, approach the other party to see if it is agreeable to conciliation. With that agreement, the arbitral tribunal will proceed to conduct conciliation. If conciliation does not result in an agreement, the arbitral tribunal will continue with the arbitration and render an award. The parties are prohibited from using any statements made by the parties during the conciliation as grounds for any claim, defense or counterclaim in later arbitral or judicial proceedings. To mitigate the risk that arbitrators may be influenced by information obtained in the course of mediation, CIETAC amended its arbitration rules in 2012 giving the parties the right to choose CIETAC, rather than the arbitral tribunal, to conduct conciliation.

In addition, there are several commercial conciliation institutions in China. The most prominent one is China Council for the Promotion of International Trade ("CCPIT") / China Chamber of International Commerce ("CCOIC") Mediation Center. The settlement agreement reached by the parties with the help of the commercial conciliation institution is binding on the parties. However, in the event that one party breaches the settlement agreement, the parties have to submit the dispute to a competent court or arbitration institution for enforcement of the obligations under the settlement agreement.
Administrative remedies can also provide an efficient and effective means of resolving disputes in China. Depending on the type of dispute in question, there are a number of government departments and organizations that can provide assistance by mediating the dispute between private parties. Primary among these is the SAIC and its local offices, which has a statutory obligation to mediate contract or consumer related disputes at the request of the parties. SAIC is also empowered to investigate and impose sanctions in a number of areas, including cases of trademark infringement and unfair competition.

13.2 Enforcement actions available

In China, judgments and awards are enforced by the courts. The PRC Civil Procedure Law grants a creditor up to two years to apply for enforcement of the judgment or award.

13.2.1 Enforcement of domestic judgments and awards

When a party applies for an execution of the judgment, the execution officer of the court will notify the party against whom enforcement is to be made and require performance within a stipulated time limit. Failure to perform within this time limit will result in measures for compulsory execution which can include orders to transfer the cash in the debtor's bank account or to seize and place the debtor's assets on auction.

A court may grant a stay of execution where the prevailing party seeks a postponement; a non-party presents a reasonable objection to the execution; one of the parties ceases to exist or dies and the other parties must await the appointment of a successor; or in other circumstances which the court deems appropriate.

A court may also terminate the execution of the judgment. This may take place when the prevailing party withdraws the application for execution; a higher court revokes the legal document upon which the execution is based; the losing party dies and leaves no estate or persons to assume obligations; the losing party, being a citizen, is unable to make repayment due to poor financial circumstances or has lost the ability to work; or in other situations the court deems appropriate. A ruling by a court to stay or terminate execution will take effect immediately.

To improve the transparency of enforcement proceedings, the courts have set up an online platform for the public to check if an enforcement proceeding has been initiated against an individual or a company. In addition, to expedite a debtor's performance of its obligations under a judgment and award, there is an online platform by which the public can check the status of debtors who have failed to honor their obligations under a judgment or an award.

Domestic and foreign-related award is enforced through the same procedure as a domestic judgment.

13.2.2 Recognition and enforcement of foreign judgments

Chinese law provides for the enforcement of foreign court judgments in accordance with international treaties concluded or acceded to by China, or pursuant to the principle of reciprocity, provided they do not violate basic principles of Chinese law, state sovereignty and security or public interest. Reciprocity is interpreted as the practice of a foreign court to enforce a judgment issued by a Chinese People's Court in the event there is no treaty. Previously, reciprocity was very difficult to establish but this changed recently with the release of a decision by the Nanjing Intermediate People's Court. On 9 December 2016, the court decided to recognize and enforce a Singapore judgment based on the principle of reciprocity. This is the first time that a Chinese court relies on reciprocity to enforce a foreign commercial judgment. The decision suggests that if a foreign court has previously enforced a Chinese judgment, there is a greater chance that the court judgment of that foreign nation will be
enforced in China. On the other hand, parties seeking to enforce the judgment of a foreign court that has no international treaty or reciprocity relationship with China will need to re-litigate their cases.

On July 14, 2006, the Hong Kong SAR and the PRC signed an Arrangement on Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters by the Courts of the Mainland and of the Hong Kong Special Administrative Region pursuant to Choice of Court Arrangements between Parties Concerned (the "Arrangement"). The Arrangement applies only to contracts entered into after August 1, 2008 which contain an exclusive choice of jurisdiction clause selecting either Hong Kong or China. Judgments which do not fall within the Arrangement will have to be enforced at common law; this usually means re-litigating the issue in the place where enforcement is intended.

The Arrangement covers final judgments in civil and commercial matters (excluding employment, family and contracts for personal arrangements). Only money judgments will be recognized and enforceable. Recognition extends to the interest on judgments, as well as costs judgments. Non-monetary judgments, such as injunctions, do not fall within the mutual recognition regime.

A similar recognition regime has been entered into by the Mainland with Macau by way of the Arrangement between the Mainland and Macau Special Administrative Region on the Mutual Recognition and Enforcement of Civil and Commercial Judgments. This Arrangement has been effective since April 1, 2006 and applies retrospectively to any judgment issued after December 20, 1999. It differs in some ways from the Hong Kong Arrangement. For example, unlike the Hong Kong Arrangement, it applies to judgments in labor disputes as well as judgments for civil damages resulting from criminal proceedings.

Civil judgments made in Taiwan can also be recognized and enforced in Mainland by a Chinese court pursuant to the Provisions of the Supreme People's Court on the Recognition and Enforcement of Civil Judgments Made by Courts of Taiwan Region (effective as of July 1, 2015). However, recognition may be denied in limited circumstances, e.g. the dispute falls within the exclusive jurisdiction of the Chinese court or enforcement may prejudice the principle of one-China policy.

13.2.3 Enforcement of foreign awards

Generally, it is easier to enforce arbitral awards than court judgments overseas through the New York Convention 1958 (the "New York Convention") which was ratified by more than 142 member states including China.

Pursuant to the New York Convention, an arbitral award made in one member state is enforceable in another state. Since the awards are readily enforceable in many countries, parties facing adverse awards are generally inclined to comply with them voluntarily. The grounds of refusing enforcement of arbitral awards are limited. They are basically confined to procedural irregularities that occurred in the arbitration process and the ground of public policy.

As between Hong Kong and the Mainland, a Hong Kong award is enforceable in China pursuant to Arrangement Concerning Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong Special Administrative Region. The grounds of refusing enforcement of arbitral awards are similar to those laid down under the New York Convention. Macau awards are recognized and enforced in China pursuant to the Arrangement on Mutual Recognition and Enforcement of Arbitral Awards Made in the Mainland and Macau Special Administrative Region ("Macau Mutual Arrangement"). The enforcement regime provided in the Macau Mutual Arrangement is very similar to that applicable to Hong Kong awards. Taiwan awards can be recognized and enforced in China pursuant to Provisions of the Supreme People's Court on the Recognition and Enforcement of Arbitral Awards Made in Taiwan Region. The grounds for non-recognition of Taiwan awards are similar to Hong Kong and Macau awards, except it is required that enforcement of the Taiwan award shall not prejudice the "one China principle".
14. Anti-Bribery and Compliance

Transparency International's 2016 Corruption Perception Index\(^\text{14}\) ranked China at #79 out of 176 countries. Although China improved four places from the previous year, companies doing business in China need to be continually vigilant and regularly review their compliance policies and business practices. In recent years, the Chinese anti-corruption landscape has become more stringent than ever, with an increased focus on bribe-givers and multinational corporations doing business in China, and the introduction of additional compliance risks for executives in responsible positions.

14.1 Legal framework

Bribery of public officials is regulated by the PRC Criminal Code (the "Criminal Code"). The Criminal Code (revised in 2015) prohibits the giving of money or property to an incumbent or former public official, a person related to the public official or a person close to the public official, for the purpose of securing illegitimate benefits. While this prohibition applies to both individuals and companies, the Criminal Code also imposes statutory penalties on persons in charge of a company or directly responsible for its business activities for bribery offences committed by the company.

Commercial bribery is regulated by the Criminal Code and the PRC Anti-Unfair Competition Law ("AUCL"). Under the Criminal Code, commercial bribery means the giving of money, property or anything of value to any employee of a company, enterprise or other entity for the purpose of seeking improper interests and benefits. Under the AUCL, commercial bribery means the giving of money or property, or secret and off-the-book kickbacks to a business counterparty or its employee, or using other means to bribe a business counterparty or its employee for selling or purchasing goods. The Interim Provisions on Prohibition of Commercial Bribery also describe the forms of the commercial bribery under the AUCL, which include any money or property provided to the business counterparty or its employee for promotion, publicity, sponsorship, scientific research, labor, consultancy, commission, reimbursement, or any other benefits such as trips or visits.

In April 2016, the Supreme People's Court and the Supreme People's Procuratorate released the Interpretation of Several Issues Concerning the Application of Law in Handling Criminal Cases Related to Graft and Bribery ("Interpretation") clarifying sentencing criteria in both official and commercial bribery cases. The Interpretation provides guidance on the definition of bribery and expressly states that bribes include intangible benefits such as material benefits of monetary value (e.g. exemption of debt) and other benefits for which payment is made in exchange (eg membership service or paid travel).

Enterprises committing commercial bribery can be placed on a blacklist by the SAIC under its Interim Measures for the Administration of the List of Dishonest Enterprises Committing Serious Illegal Activities ("Interim Measures"). The Interim Measures, which became effective on April 1, 2016, applies to all companies registered in China, including state-owned-enterprises, private companies and foreign-invested enterprises, and blacklists enterprises committing certain illegal activities including commercial bribery. Blacklisted companies which repeatedly violate the law may be subject to joint sanctions imposed by multiple government authorities such as restrictions or prohibitions in relation to business operations, import and export, market entry and exit, registration of new companies and safety and production licensing. They may also receive additional sanctions even if the violations did not result in significant administrative penalties under the AUCL, e.g. where the bribe amount was relatively small.

\(^{14}\) Transparency International's 2016 CPI was released on 25 January 2017.
14.2 Facilitation payments

There is no exemption for facilitation payments under the Criminal Code. Any form of payment or property would be assessed according to the elements of the offence under the Criminal Code or AUCL.

14.3 Gifts, hospitality and other payments

Gifts and entertainment continue to pose challenges for companies doing business in China. While the Criminal Code does not establish quantitative limitations on gifts or hospitality expenses, there is a threshold amount for the prosecution of official bribery of RMB30,000 (or RMB10,000 with aggravating factors) for individual bribe-givers, RMB200,000 (or RMB100,000 with aggravating factors) for corporate bribe-givers, and RMB30,000 for bribe-recipients. Likewise, the criminal threshold for prosecution of commercial bribery is RMB60,000 for individual bribe-givers, RMB200,000 (or RMB100,000 with aggravating factors) for corporate bribe-givers, and RMB60,000 for bribe-recipients. However, a 1995 internal regulation applicable to public officials of central party and government organs requires public officials to hand over the gift to the government if the value of the gift exceeds RMB200 per person per occasion. Public officials are also obliged to turn the gift in if the cumulative value of all the gifts received by the public officials exceed RMB600 per person per year.

As a result of inflation, a gift of the value of RMB200 is no longer considered a sizable gift in China. We have observed that the 1995 internal regulation mentioned above has only been loosely followed. Whether a hospitality expense can be considered as bribery will need to be determined on a case-by-case basis, taking into account all the facts and circumstances surrounding the case, and applying the criteria in the said 1995 regulation. In practice, most multinationals in China adopt a threshold amount of around RMB200 to RMB500 (about USD29 to USD73) for courtesy gifts or entertainment by meal, per occasion, per person. Many companies also provide for a frequency limit, for example, no gifts can be given to the same person over three to four times per year. Some industry associations have set up benchmarking rules on gifts, meals and entertainment, for consideration by the members to level the playing field.

In the healthcare sector, a donation could be considered as commercial bribery if it is provided in an inappropriate way for purchasing or selling goods. The Administrative Measures on Accepting Donations for Public Welfare by Healthcare Entities (for Trial Implementation) ("New Donation Rules") promulgated in 2015 provide specific guidance on donations to healthcare and family planning entities for the non-profit purpose of public wealth such as training, academic or research. The New Donation Rules prohibit donations to these entities to be used for any illegal or commercial purpose, or as commercial bribery or an incentive to purchase the goods.

14.4 Extraterritoriality and foreign public officials

The prohibition against official bribery applies to acts taking place within China or elsewhere. For commercial bribery, offers of bribery to employees of Chinese enterprises or companies (including foreign-invested companies) outside China and acceptances by Chinese companies and their employees outside China would potentially attract extraterritorial liability.

The Criminal Code was also revised in 2011 to prohibit bribery of foreign public officials or officials of international public organizations. Under Article 164 of the Criminal Code, bribery of foreign public officials

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15 These aggravating factors include (a) the giver offers bribes to more than three officials; (b) the giver uses illegal gains to give bribes; (c) the giver seeks promotion and change of position by offering bribes; (d) the giver offers bribes to officials who are responsible for supervision and management over food, medicine, safe production, environment protection, etc. and who carry out illegal activities; (e) the giver offers bribes to judicial officers which affects justice in judicial activities; and (f) the bribery act has caused loss of more than RMB500,000 and less than RMB1 million.
officials means the giving of money or property to foreign government functionaries or officials of international public organizations for the purpose of seeking improper commercial interests. For the purpose of this offence, a foreign public official means a foreign government functionary or an official of an international public organization.

14.5 Penalties

Individuals who are found guilty of paying bribes to public officials face up to life imprisonment plus confiscation of property or a criminal fine. Individuals who are found guilty of paying bribes to former public officials or persons related or close to the public officials can be sentenced to criminal detention or fixed-term imprisonment plus a criminal fine. Companies that offer bribes to public officials or the persons related or close to public officials can be subject to a criminal fine. Responsible persons directly in charge of those companies and persons directly responsible for such offenses face up to five or three years imprisonment respectively (depending on the status of the recipients), and a criminal fine and confiscation of illegal personal gains (if any). Bribe recipients can also be liable. A public official who receives a large amount of bribes can be sentenced to imprisonment including the death penalty. A non-official bribe recipient (e.g., former public official or person related or close to the public official) can be sentenced to criminal detention, fixed-term imprisonment, confiscation of property and a criminal fine.

In relation to commercial bribery, under the Criminal Code, penalties for individual bribe givers are up to ten years imprisonment and a fine. For the company or legal entity involved, the penalty is a criminal fine for the legal entity, while persons directly in charge of the company and other persons who were directly responsible for the offense face up to ten years imprisonment and a criminal fine. The AUCL establishes administrative penalties for business operators committing commercial bribery in circumstances where the violations have not constituted criminal offences. The penalties include an administrative fine ranging between RMB10,000 and RMB200,000 and confiscation of illegal gains.

In relation to the bribery of foreign public officials, penalties are up to ten years imprisonment and a fine for individuals involved. For legal entities, the penalties are a criminal fine while persons who are directly in charge and other persons who are directly responsible for the offense face up to ten years imprisonment and criminal fine.

14.6 Defences

Bribe givers of official bribery may seek to have their punishment mitigated or waived if they "voluntarily confess" their bribe-giving activities. However, recent changes to the law require the underlying crime to be relatively minor and offenders to assist with exposing corrupt activities which lead to successful investigations. Further, leniency for voluntary disclosure will not be available in certain circumstances, such as when bribes are offered to more than three persons, or when the bribery results in "harmful consequences".

For commercial bribery, reasonable business expenditures may be a defence as long as it is supported by a genuine underlying transaction with proper documentation. Similarly, low-value promotional gifts may be acceptable depending on the purpose of the gift and its value.

14.7 Enforcement authorities

The Public Security Bureau has the jurisdiction to investigate commercial bribery crimes related to non-public officials. The Procuratorate has the jurisdiction to investigate official bribery and prosecute bribery related to public officials or commercial bribery. The AIC has the power to investigate and sanction companies for commercial bribery that is not a criminal offence in nature. In addition, if a
member of the Communist Party of China ("CPC") is involved, the Central Commission for Discipline Inspection ("CCDI") of the CPC can also investigate and penalize the corruption activity in accordance with special CPC disciplinary rules.

14.8 Compliance programs

The Criminal Code and AUCL do not specifically recognize compliance programs as instruments to mitigate or eliminate liability for legal entities. However, if a legal entity can prove that it had exercised due control over its employees by means of a compliance program or otherwise, a company may seek leniency or mitigate the risk of liability arising from the corrupt behavior of its employees.

While having a compliance program does not offer a legal defense for the offense of bribery, it is recommended that legal entities adopt a robust compliance program to prevent internal corruption and bribery. It is also useful to draw a clear line between the legal entities' liability and the employees' individual liability in order to mitigate the potential legal risks of the legal entity.

14.9 Whistleblowing

Chinese laws provide Chinese citizens and entities with the right (and a general obligation) to report crimes such as corruption, commercial bribery, embezzlement and malfeasance. These rights were enhanced on March 30, 2016 when the Supreme People's Procuratorate, Ministry of Public Security and Ministry of Finance released new regulations offering greater protection and incentives. Local authorities also encourage reports in relation to commercial bribery by offering monetary rewards.

Organizations doing business in China need to be in a position to respond to and manage internal complaints swiftly and in a credible manner. Companies implicated in whistleblower complaints alleging that it is involved in a bribery scheme may attract an investigation by Chinese authorities or the attention of foreign enforcement bodies such as the US Department of Justice, the US Securities and Exchange Commission or the UK's Serious Fraud Office. In addition to compliance with Chinese laws, it is imperative that compliance programs are aligned with standards laid down by global regimes (such as the US Foreign Corrupt Practices Act and the UK Bribery Act) and best practices adopted by peer entities in the same or similar industry.
15. Baker McKenzie in China

Baker McKenzie has maintained a presence in China since the late 1970s. With over 40 years' experience in advising on doing business in the region, we bring an in-depth understanding of China's cultural, political and legal structure. We partner with clients, taking into account their commercial objectives and work through complex issues through strategic advice, innovative approaches and exceptional practical solutions. We add value by helping clients manage risks and seize opportunities in today's complex, ever changing global economy.

Our offices in Hong Kong, Beijing and Shanghai were established in 1974, 1993 and 2002 respectively. Our team encompasses over 300 lawyers, who are fully conversant with the systems, practicalities, and language of law, and are fluent in English, spoken and written Mandarin, as well as other Chinese dialects and European languages. These lawyers are backed by a team of experienced paralegals and translators.

We provide dedicated on-the-ground legal services to foreign multinational companies and domestic corporations doing business in China. With our diverse capabilities and experience, we serve clients across all major industry sectors. We are regularly involved in high-profile and first-to-market transactions with blue-chip multinational corporations and financial institutions and regularly coordinate significant cross-border assignments for market leading companies. In recent years, we have also assisted a number of leading PRC entities on their significant outbound investment projects across the globe.

In China, Baker McKenzie provides dedicated legal services across the broad spectrum of corporate law, including:

- Antitrust & Competition
- Banking & Finance
- Capital Markets & Securities
- Compliance & Investigations
- Consumer Goods & Retail
- Construction
- Corporate Services
- Dispute Resolution & Litigation
- Employment & Compensation
- Energy, Mining & Infrastructure
- Environment & Climate Change
- Financial Services
- Healthcare
- Hotels, Resorts & Tourism
- Information Technology & Communications
- Insurance
- Intellectual Property
- International Trade
- Investment Funds
- Mergers & Acquisitions
- Private Equity
- Real Estate & Property
- Restructuring & Insolvency
- Regulatory & Compliance
- Tax
- Wealth Management

Baker McKenzie's long-standing involvement in China has allowed us to become a highly respected and recognized legal advisor to central and local governmental bodies in the region. As a testament to our acknowledged expertise, we were one of the first foreign law firms to represent the Chinese government...
in foreign legal proceedings in the early 1980s. Over the course of the last few years, we have had the privilege of advising the Legislative Affairs Committee of the National People's Congress and key Chinese Ministries on a platform of legislative reforms. Our Chairman is a member of the International Business Leaders Advisory Council hosted by the Beijing Mayor's office.

We also have extensive experience in dealing with Chinese government ministries and agencies at all levels as well as with major foreign trade and investment organizations in China. We keep abreast of China's rapidly evolving legal structure through regular contact with government departments which draft and implement legislation at both national and local levels. Relationships with ministries and institutions enable us to provide clients with the most timely and detailed advice on foreign investment and trade opportunities.

Our lawyers bring the following key attributes to China-related business and trade:

• Depth and breadth of accumulated understanding and comparative experience across many industry sectors;
• A strong and diversified team of dedicated China legal specialists, all of whom are fluent in Mandarin and English; and
• The benefit of a respected and recognized reputation amongst China's central and local governments and the business communities.

As part of our proactive, business-focused and user friendly service, we also provide the following value-added benefits:

• **Doing Business in China** – a comprehensive guide on setting up and doing business in China
• **News Alerts** – regular updates outlining developments and changes in China law as they take shape and evolve
• **Seminars** – we hold regular seminars and workshops focusing on new developments and topical issues of relevance to businesses

**Latest awards**

• **Winner of "Innovation in the Business of Law (Internationally Headquartered Law Firms)"** (for establishment of Baker & McKenzie FenXun (FTZ) Joint Operation Office, the first Joint Operation between an international and a Chinese law firm in the Shanghai Free Trade Zone and also in China) – Financial Times Innovative Lawyers Awards, Asia Pacific 2016
• **International Law Firm of the Year** – China Law & Practice Awards 2016
• **Most Responsive International Firm of the Year: China and Hong Kong** – Asian-MENA Counsel Representing Corporate Asia & Middle East Survey 2016
• **In-house Community Firm of the Year: China** (for Corporate and M&A; Projects and Project Financing) – Asian-MENA Counsel Representing Corporate Asia & Middle East Survey 2016
• **In-house Community Firm of the Year: Hong Kong** (for Anti-Trust/Competition; Aviation; Compliance/Regulatory; Corporate and M&A; Employment; Insurance; Intellectual Property; Litigation and Dispute Resolution; Real Estate/Construction; Taxation; Telecommunications, Media & Technology) – *Asian-MENA Counsel Representing Corporate Asia & Middle East Survey 2016*

• **Corporate Citizenship Law Firm of the Year** – *ALB Hong Kong Law Awards 2016*
Baker McKenzie helps clients overcome the challenges of competing in the global economy.

We solve complex legal problems across borders and practice areas. Our unique culture, developed over 65 years, enables our 13,000 people to understand local markets and navigate multiple jurisdictions, working together as trusted colleagues and friends to instill confidence in our clients.