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subject	Promulgation of the Regulations of Registration and Administration of Representative Offices in China of Foreign Enterprises
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Promulgation of the Regulations of Registration and Administration of Representative Offices in China of Foreign Enterprises

On November 19, 2010, the State Council of the People's Republic of China (the "PRC") (the "State Council") promulgated the Regulations of Registration and Administration of Resident Offices¹ in China of Foreign Enterprises (the "RO Regulation"), which will take effect on March 1, 2011. Followed by the issuance of two other notices² earlier this year aiming at laying more controls on the administration of resident office (the "RO") in China, the State Council ultimately issues the RO Regulation to further reinforce this purpose. As provided in the supplementary articles of this new regulation, the old Measures on Procedures for the Registration and Administration of Resident Offices in China of Foreign Enterprises (the "Old RO Measure") approved by the State Council and promulgated by the State Administration for Industry and Commerce (the "SAIC") in 1983, will be entirely substituted and abolished next year.

This issue of China Legal Report intends to provide you with a comprehensive introduction of the RO Regulation, especially those essential changes compared with this Old RO Measure and any previous rules and regulations in connection with that measure as well as a discussion of taxation issues.

I. Introduction

Resident office (the "RO"), as defined in the "RO Regulation", means any administrative office established by a foreign enterprise (the "Parent Company") within the territory of China based on this regulation (the RO Regulation) solely engaging in non-profit activities relating to the business of its Parent Company and the RO does not have legal person status. Pursuant to Article 42 of the RO Regulation, "foreign enterprise" here means for-profit organization established overseas based on foreign laws, while previously, Parent Company includes not only for-profit foreign organizations, but also non-profit foreign organizations, based on Article 1 of *Clarification on Several Questions on The Implementation of Interim Provisions of The Stated Council of The PRC on The Administration of Resident Representative Offices of Foreign Enterprises* (1981).

¹ The term "Resident Office" and "Representative Office" are synonyms for the same legal form.

² The two notices are: *Notice of the State Administration for Industry and Commerce and the Ministry of Public Security on Further Strengthening the Administration of Registration of Permanent Representative Offices of Foreign Enterprises* dated January 4, 2010 (the "Notice on Further Strengthening"), and *Notice of the State Administration of Taxation on Issuing the Interim Measures for the Administration of Tax Collection against the Permanent Representative Offices of Foreign Enterprises* dated February 20, 2010 (the "Tax Measure").

³ "Non-profit" activity is a general principle, but Article 13 also lists several exceptions. Please find relevant discussion below.

The main function of a RO, as an extension of a foreign enterprise, shall be to do survey and feasibility study on the China market as well as liaising activities for its Parent Company.

In the early 1980s, when the Old RO Measure and the *Interim Regulations of the People's Republic of China Concerning the Control of Resident Offices of Foreign Enterprises* (1980) (the "Interim RO Regulation") were promulgated, China was at its initial stage of attracting foreign investment to solve its shortage of funds. This type of vehicle exactly provides foreign investors a window to know the investment conditions in China, let its Parent Company become known to the Chinese, and set up regular contact with potential clients in this country. This idea was to win market shares before establishing any substantial presence. In addition, as it is known that the application procedure for an RO is less complicated than that for a foreign-funded enterprise. For instance, it takes generally around four months to establish a wholly foreign owned enterprise, while setting up a RO may simply need approximately two months.

However, the shortcoming of the RO for its Parent Company is also obvious as it cannot be, in principle, involved in for-profit business operation. Therefore, with the intention of enjoying the convenience of setting up and running a RO, preferential tax policies posed to RO, together with making incomes and profits from such vehicle, a wide range of RO have quietly engaged in for-profit business, which has been deemed as the trigger to the issuance of the Notice on Further Strengthening and the Tax Measure.

This new RO Regulation is comprised of forty-five articles divided into seven chapters: general principle, registered matters required, registration for establishment, registration for change, registration for cancellation, legal liabilities, and supplementary articles.

II. Main Points of the RO Regulation

In this Section II, key changes reflected in the RO Regulation will be discussed chapter by chapter.

I General Principle

It is expressly stipulated in this RO Regulation that the RO needs annual inspection by SAIC. Pursuant to Article 6, RO shall submit to the registration authority, SAIC, during the period from March 1st to June 30th each year, an annual report containing certificate of good standing (or similar documents that can prove the legal existence of the Parent Company) of its overseas Parent Company, business operation of the RO, and audited financial report by an accounting firm on incomes and expenses of the RO. Furthermore, in

accordance with notarization and certification of overseas legal documents system⁴, such certificate of good standing shall be notarized and certified by a notary public in the country or region where the said Parent Company is located and the embassy or consulate of the PRC stationed in that country or region.

ii Registered Matters Required

A. Registered Matters Required

In accordance with the new regulation, besides the name of the RO and the chief representative, the business scope and resident address, also required by previous rules, the RO shall also register the name and the address of its Parent Company at the registration authority, which means unlike before, any change to the Parent Company's name or address will trigger the registration for change procedure to the RO.

B. Qualifications of the Chief Representative

It is for the first time qualifications of the chief representative having been specified. Pursuant to Article 12 of the RO Regulation, a person shall not take the position as a chief representative upon the occurrence of any of the following events:

- 1) Having been sentenced to any criminal penalty due to undermining national security and public interests of PRC;
- 2) The person was the chief representative or representative of a RO whose registration establishment was canceled, certificate of registration was revoked, or this RO was ordered to close due to undermining national security and public interests of PRC, and five years has not elapsed since the date of the cancellation, revoke, or order of close; or
- 3) Any other ones required by SAIC.

C. Scope of Activities

As a general rule, RO is merely allowed to solely involve in non-profit activities, and Article 14 of the RO Regulation identifies the non-profit activities as follows:

- 1) Market survey, exhibition, and promotion in relation to the products or services supplied by the Parent Company; and
- 2) Liaising activities in relation to the product sales, service provision, and purchase and

⁴ In case of Hong Kong investors, the certificate of good standing needs to be notarized by notary public authorized by China, and checked, sealed, and delivered by China Legal Service (H.K.) Ltd.

investment within the territory of PRC by the Parent Company.

Despite the non-profit general rule, the second paragraph of Article 13 supplies an exception to it as where an international convention or treaty to which PRC is a contracting party or a signatory has provided otherwise, the provisions of the international convention or treaty shall prevail, with the exception of those clauses on which the PRC has declared reservation. Indeed, this is not entirely new, however, provided as early as in Article 35 of the Old RO Measure, nevertheless only referring to bilateral agreements instead of international convention or treaty mentioned therein. This Article 13 in the RO Regulation actually resulted from the commitment made by China owing to the accession to WTO Service Trade which requires legal services (except for PRC laws), accounting auditing and booking services, taxation services, and management and consulting services to be exceptional to the non-profit rule with regard to RO's activities.

D. Location

Presently, the RO needs special approval to its resident location⁶ or is only allowed to choose resident address from the list issued by certain authorities⁷. As amended by the new regulation, pursuant to Article 15, RO will be, generally, free to choose any venue as its registered office, with the exception that relevant authorities are entitled to require RO to change its resident location, and immediately inform registration authority, on account of national security and public interests.

E. Duration

In the Old RO Measure, the maximum duration of an RO, approved on each occasion, shall not exceed three years, but the duration is allowed to be extended in compliance with legal procedures, but each extension shall not exceed three years. While the RO Regulation lifts such limitation, simply providing that the duration of an RO shall not exceed the duration of its Parent Company, meaning that to a certain extent, the Parent Company will be able to decide the duration of its RO freely, and may not need to experience the procedure of application for duration extension regularly.

⁵ Article 3: RO shall be understood as those engaging in non-direct-profit-making operations, but for those provided for in inter-government agreements, they shall be dealt with in accordance with those agreements.

⁶ In Shanghai, according to *Several Issues on Administration of Instructed Resident Address for Resident Office Set-up by Taiwan, Hong Kong, Macao, and Foreign Enterprises*, RO's residence shall be approved by Inspection Office of National Security of Foreign-related Constructions of Shanghai.

⁷ In Xiamen, according to Article 8 of *Rules of Administration of Resident Offices in China of Foreign Enterprises of Xiamen*, resident address for RO can only be chosen from the name list circulated by foreign investment department.

F. Maximum Number of Representatives

Pursuant to Article 11 of the RO Regulation, in addition to the chief representative, the Parent Company is allowed to appoint three more representatives, which means the maximum number of representatives of a RO shall not exceed four.

This is also provided in the Notice on Further Strengthening issued earlier this year, however, was hardly noticed by many existing ROs. In case the number of representatives of an existing RO exceeds four, such RO is only allowed to cancel existing representatives, but not entitled to add new ones until it has reduced the number of representatives to four.

iii Registration for Establishment

The required documents for the establishment registration are as follows:

- 1) Application letter for establishment;
- 2) Certificate of the Parent Company's residence and certificate for its legal existence and operation for over two years;
- 3) Articles of association or constitutional agreements of the Parent Company;
- 4) Appointment letter from the Parent Company with respect to the chief representative and representatives of the RO;
- 5) Identity certificates and resume of the chief representative and representatives;
- 6) A certificate of capital credibility issued by the bank which has business ties with the Parent Company; and
- 7) Certificate of legal use of the resident location for RO.

iv Registration for Change

In accordance with the new regulation, RO is required to do filing within sixty days after the occurrence of any change on the required registered matters. Additionally, if the RO intends to extend its duration after expiration, then it shall apply at least sixty days in advance before the expiry date.

⁸ According to Article 9 of the RO Regulation, required registered matters are name of the RO and the chief representative, its business scope and resident address, the name and the resident address of its Parent Company.

v Registration for Cancellation

Pursuant to the RO Regulation, the Parent Company shall apply for registration of cancellation for its RO within sixty days since the occurrence of any of the following events:

- 1) The Parent Company intends to end its RO's activities;
- 2) RO terminates its activities due to the expiration of its duration;
- 3) The Parent Company closes; or
- 4) Approval of the RO is revoked or this RO is ordered to close pursuant to relevant laws and regulations.

In addition, the required documents for cancellation registration are as below:

- 1) Application letter for cancellation registration;
- 2) Certificate of cancellation of the tax certificate of the RO;
- 3) Certificate issued by State Administration of Foreign Exchange of PRC and General Administration of Customs of PRC prove either all the related matters has cleared up or the RO has never applied for such certificates; and
- 4) Any other documents required by SAIC.

vi Legal Liability

Two changes are worthy of mentioning in this chapter. First of all, directly liable person-in-charge together with other directly liable persons may be fined not less than RMB 1,000 but no more than RMB 10,000 under following circumstances:

- 1) Where anyone obtains the registration or archive records of RO by submitting false materials or by any other fraudulent means to conceal any facts; and
- 2) Fabricating, altering, leasing, lending or transferring certificate of registration or certificate of representative.

The other is the five-year blocking period⁹, where a RO whose registration establishment was cancelled, certificate of registration was revoked, or this RO was ordered to close by relevant PRC governmental authorities due to violation of the RO Regulation, such RO's Parent Company will not be allowed to establish a RO within the territory of PRC within five years since the date of the cancellation, revoke, or order of close.

⁹ Pursuant to 1st and 3rd paragraphs of Article 36 of the RO Regulation.

¹⁰ Pursuant to Article 39 of the RO Regulation.

vii Taxation Issue

In addition, pursuant to relevant bilateral taxation treaties, permanent establishment (the “PE”) is normally the object of taxation. Then the question leads to whether a RO will be counted as a PE and is excluded from the beneficiary of such preferential taxation policies. On the ground of certain bilateral treaties¹¹ and *Notice of State Administration of Taxation on Explanation of Whether an RO is a Permanent Establishment under Taxation Treaty* (1999) (the “Explanation of PE”), a RO shall not be defined as a PE if it solely engages in any of the following activities:

- 1) the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;
- 2) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery;
- 3) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;
- 4) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise;
- 5) the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character;
- 6) the maintenance of a fixed place of business solely for any combination of activities mentioned in sub-paragraphs 1) to 5), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.

If a RO satisfies any of above six conditions, it will not be treated as a PE, thus the profits of its Parent Company will not be taxed in China. However, the content of the “any other activity of a preparatory or auxiliary character” as listed in point 5) above shall be defined by relevant tax bureau instructed by taxation treaties and arrangements, and therefore, unless explicitly clarified by the State Administration for Taxation, any local tax bureau shall not decide the content on its sole discretion.

III. Conclusion

Notwithstanding the facts that the RO Regulation sets more documents inspection on RO registration, like requiring RO to submit certificate of good standing which needs to be properly notarized and certified annually, and more severe legal liabilities to those in violation of the RO Regulation, as requiring person in charge to take personal liabilities

¹¹ For example, the *Agreement Between The Government Of The People's Republic Of China And The Swiss Federal Council For The Avoidance Of Double Taxation With Respect To Taxes On Income And Capital*.

under certain circumstances, the circulation of this new regulation does not purpose to restrict establishment or operation of RO. It aims at enhancing the administration of its registration, and even to show China's flexibility to foreign investors through lifting the limitation on duration and resident location. Additionally, it also aims to make it consistent to the commitment of the PRC in accession to WTO, like allowing RO to be for-profit organizations in certain limited areas.

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