

TYPES OF INVESTMENT VEHICLES IN SHANGHAI

The principal forms of business entities available to foreign investors in Shanghai are:-

- (1) Foreign Investment Enterprises
 - (a) Equity Joint Venture (EJV)
 - (b) Cooperative Joint Venture (CJV)
 - (c) Wholly Owned Foreign Enterprise (WOFE)
- (2) Foreign Enterprises
 - (a) Representative office (RO)
 - (b) Branches of Foreign Enterprise
 - (c) Enterprises other than those listed above that have establishments or places of business in China and engage in production or business operations, e.g. factory, places for exploitation of natural resources, contracted project sites.

LAWS AND REGULATIONS RELATING TO FORMATION OF BUSINESS ENTITIES IN SHANGHAI

When choosing among different forms of business entities, it should be noted that not all types of entities are available for all kinds of industries. The formation, organisation, management of most of these entities are governed by their respective laws and regulations, which are special laws relating to the particular form of business entities in question. In 1994, the first company law of China, which is a “general law”, was enacted. Briefly speaking, special law should be used and general law should only be relied upon in circumstances when there is no provision in special law.

The laws governing the establishment and management of business entities in Shanghai are:

General Law

Company Law of PRC

Special Law

Law of the PRC on Chinese Foreign Equity Joint Ventures

Law of the PRC on Chinese Foreign Cooperative Joint Ventures

Law of the PRC on Enterprises Operating Exclusively with Foreign Capital

Different Forms of Business Entities Available to Foreign Investors

| | EJV | CJV | WFOE | RO | Branch |
|-----------------------------------|--|---|---|--|---|
| Special Law | Law of the PRC on Joint Ventures Using Chinese and Foreign Investment | Law of the PRC on Chinese Foreign Cooperative Joint Ventures | Law of the PRC on Enterprises Operating Exclusively with Foreign Capital | Law of the PRC on Enterprises Operating Exclusively with Foreign Capital | No special law applicable, Governed only by Company Law |
| Legal Person (corporation) | Yes, Limited Liability Company | Yes, Limited Liability Company Except specified on the constitution | Yes, Limited Liability Company, but can be in other forms on application and approval | No | No |
| No of Owner | Min. 2, one must be Chinese Party | Min. 2, one must be Chinese Party | Min. 1 | N/A | N/A |
| Board of Directors | Yes, not less than three persons | Yes | Depends. If no BOD is established, the General Manager is the CEO | N/A | N/A |
| Capital Required | At least 25% contributed by foreign parties. Minimum according to industry | Minimum according to industry | Minimum according to industry | No capital requirement | [See below] |
| Audit | Required | Required | Required | Not required | [See below] |
| Profit and Loss Sharing | In accordance with the proportion of capital contribution | In accordance with the contract of the CJV | Solely borne by the foreign investor | N/A – a representative office should not conduct business in China | Solely borne by the foreign parent |

Branch

In theory, branches of foreign companies can be registered under the Company Law but practically, since there is no implementation regulation relating to the registration and administration of branches in China, only certain industries are allowed to set up branches in China and only in certain locations. Currently, the only industries allowed to set up branches in China are

- (1) Branches of foreign banks, which are governed by a special set of regulations implemented by the People's Bank of China (the Central Bank) and
- (2) Branches of foreign companies operating in one of the designated districts in Beijing, which are engaged in high-technology industry. Separate regulations promulgated by local government apply.

COMPANY LAWS OF PRC

The Company Law of the People's Republic of China was promulgated in 1993 and became effective on 1 July 1994. Two types of corporate entities are allowed to be formed under the Company Law:

- (1) Limited Liability Companies (LLC)
- (2) Companies Limited by Shares (Joint Stock Company, JSC)

| | LLC | JSC |
|-----------------------------------|---|---|
| No of Shareholders | 2 to 50 | At least 5 promoters, majority of the promoters must be domiciled within China. Established by promotion – promoters must subscribe to all the shares Established by share offer – promoters must subscribe to at least 35% of the shares. Remaining shares shall be offered to the public. |
| Minimum Registered Capital | RMB 100,000 TO RMB 500,000, depending on industry. Higher capital requirement may be needed for particular kinds of business, which will be provided for separately in laws or administrative regulations | RMB10 million. Higher capital requirement may be needed for particular kinds of business, which will be provided for separately in laws or administrative regulations |
| Capital Contributions | Cash, tangible assets, industrial property, non-patented technology, land-use rights. Industrial property and non-patented technology should not exceed 20% of the registered capital, except as otherwise provided in other laws | Promoters can contribute in form of cash, tangible assets, industrial property, non-patented technology, and land-use rights. Industrial property and non-patented technology should not exceed 20% of the registered capital, except as otherwise provided in other laws |
| Share Transfers | Requires consent of majority of the shareholders if transfer to non-shareholders | Must be made through a securities exchange. Promoter shares may not be transferred within 3 years of the establishment of the company. Directors, supervisors and management should not transfer their shares during their term of office |
| Board of Directors | 3 to 13 directors (some exceptions) | 5 to 19 directors |
| Supervisory Committee | Required – For small company: 1-2 For large company, not less than 3 | Not less than 3 persons. |

EJV, certain CJV and WOFE are limited liability companies. Foreign investors cannot set up solely owned Joint Stock Company but may set up Joint Stock Company with Chinese partners. Joint Stock Company can be established through promotion or share offering. Currently, PRC government encourages the setting up of JSC only in high-technology production industries. The minimum capital requirement is RMB 30 million and the foreign investor should not own less than 25% of the registered capital.

General Procedures for Setting up a Business Entity in Shanghai

Application procedures for different types of Business Entities are different. Please refer to our respective Fact Sheets. In general, it is a two-step procedure Step one: applicant should obtain approval from respective authorities. Step two: registration made with the Administration for Industry and Commerce. The foreign enterprise may engage an agent authorized by Shanghai

Municipal Foreign Economic Relations and Trade Committee to handle its application on its behalf.

Approval Authorities

Authorities for approval are distributed among various State Council Departments and are delegated to their local offices.

Criteria for Granting Approval

Please note that the Shanghai Government works on an “approval system” instead of a “registration system”, that is, the application may be rejected without any reason given.

Nevertheless, Shanghai has been reckoned as having the most liberal policies in approving establishment of business in the country. However, the following criteria have been considered beneficial to the City and therefore approval is more likely to be secured:

- (1) The enterprise will use advanced technology and equipment
- (2) The enterprise will use advanced management technique and has proven management experience, as reflected by the status of its parent company.
- (3) The enterprise will export all or most of its produced products.

Moreover, it is important that the necessary requirements be fulfilled and documents required by the government be fully and accurately submitted. Some of the requirements are:

- (1) The parent company/investor should have at least one to three years of operating results.
- (2) A business address (for commercial operations) located in a building, which is approved by the government to house foreign enterprises, is required. For manufacturing concerns, the factory should be located at a site approved by the government.
- (3) For non-Chinese documents, certified translation by approved translator are required.
- (4) Notarization of statutory documents of the parent company may be required.

Capital Requirement

China adopts a registered capital system. All registered capital has to be paid up in cash, physical assets or intangible assets. If capital is not in the form of cash, valuation by a local “valuation professional” is needed according to regulations relating to the particular industry.

Strict capital injection requirement should be fulfilled. “Capital” includes not only registered capital but also promissory loans from the parent company or financial institutions. Different regulations for different industries govern the minimum capital requirements and schedule of injection. Local auditors should be engaged to issue audit report on capital injection. If capital is not injected according to the schedule, business license and certificate granted may be withdrawn.

Name

The foreign enterprises operating in Shanghai has to submit its proposed name to respective government department for approval.

Business Address

A separate business address, located in commercial buildings or sites approved by the government, is required as the office / factory address.

Post establishment Registration Procedures

Upon the issuance of the registration certificate, the applicant is required to complete post-establishment registration procedures, including

- (1) Opening of bank accounts
- (2) Registration with the National Tax Bureau and Local Tax Bureau
- (3) Application of “Enterprise Code”
- (4) Preparation of statutory stationery, including company chops
- (5) Registration with the State Statistics Bureau
- (6) Registration with the Customs Office.
- (7) Application for Employment Visa (For expatriate staff)

Time Required

The process registration process normally takes less than 60 days.