

CHINA UPDATE



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A Step Forward for PRC VAT Reform – Telecommunications Included into VAT Regime

Key Points

- State Administration of Tax to formally include telecoms services into the VAT system as of June 1.
- Different VAT rate will apply to telecoms services, depending on how they are categorized.
- Once included into the regime, several VAT rules will become applicable to telecoms companies.

Background

China State Administration of Tax (“SAT”) recently released the Notice on Including Telecom Industry into the Pilot Scheme on Switching from Business Tax to VAT (“Cai Shui [2014] No.43”) at end of April, which will become effective on June 1, 2014. After the telecommunications industry has been formally included in the VAT system, it is expected that the VAT reform will be expanded further to cover financial services, construction services, real estates and consumer services. We would keep monitoring the VAT reform progress.

Summary of the VAT Rule for Telecom Industry

In the newly issued Cai Shui [2014] No.43, the telecom sector is defined as the business activities of providing voice communication services by phone, transmitting, sending, receiving or applying images, text messages and other electronic data and information by using the wired/wireless electromagnetic system or photovoltaic system and other communication network resources. Telecoms services are further divided into two sub-categories and subject to different VAT rate:

Category	Scope	VAT Rate
Basic Telecoms Services	Providing voice communication services by phone by using fixed network, mobile network, satellite or Internet, as well as renting out or selling bandwidth, wavelength and other network elements.	11%
Value-added Telecoms Services	Providing text message and multimedia message services, electronic data and information transmission and application services, and Internet access services. Satellite television signal landing relay service shall be taken as value-added telecoms services.	6%

The telecoms services provided by entities and individuals in China to overseas clients are exempted from VAT.

When included into the VAT regime, several VAT rules will become applicable to telecoms companies. One typical VAT rule is when the taxpayer sends out free gifts during its business operation, that taxpayer shall recognize deemed sales revenue for the free gifts based on the market value of the gift for VAT purpose. When it is common marketing strategies for telecoms companies to present gifts and bonuses to consumers, Cai Shui [2014] No. 43 has included several clarifications on the VAT implication for common marketing models for telecoms companies:

- According to previous rules applicable to telecoms companies, neither Business Tax nor VAT should be triggered for free gifts of telephone sets, as such gifts are regarded as being sent out for free. Under the VAT regime, if the telecom company provides free gifts such as phone cards, mobile phones or telephone sets, the total money and out-of-pocket expenses charged by the telecom company shall be accounted at its applicable tax rates respectively. The new VAT rule requires that total revenue received by telecoms companies should be allocated among the sales and services, and be subject to different VAT rate (i.e. 6%, 11% or 17%).
- The telecom service provided upon claiming of bonus points by customer (where customer will be granted with certain value of free telecom service based on the bonus points they have saved up in their accounts, such as exchange of the bonus points into prepaid telephone card) is not subject to VAT.

Following Cai Shui [2014] No.43, SAT has further promulgated the Notice No. 26 on *Interim Measures for Telecom Enterprise on Levying of VAT*. Notice No. 26 has been promulgated to specifically regulate the VAT filing and payment measures applicable to China Mobile, China Unicom and China Telecom, the three state-owned telecoms companies. According to Notice No. 26, the lower tier branches of the three state-owned telecoms companies will conduct a monthly provisional filing at a levying rate determined by provincial tax authorities on the overall collected revenue for the taxable services. The provincial branches of the three telecoms companies are required to conduct a consolidated VAT filing on quarterly basis for the telecoms services carried out in that province based on the data reported by its lower tier branches. All off-set of the VAT input will be realized on provincial level, the purpose of which, as we speculate, is to allow more consistent control on the VAT filing process by provincial tax authorities and to eliminate local branches' compliance burden.

Expected Impact

The telecoms companies may consider adjusting their current marketing strategies by reevaluating the turnover tax liabilities in each current type of their marketing campaign. Furthermore, as a strategic plan, telecoms companies may possibly start to focus on their value-added services in the future and lower the proportion of their basic services, which is also consistent with government's policy in the telecom industry's restructuring.

Before the VAT reform, telecoms companies are subject to 3% Business Tax. In the short-term, the profits of telecoms companies (mainly the three gigantic China market players: China Unicom, China Mobile and China Telecom) may notice a substantial impact due to their drastic rise of turnover tax liabilities under the VAT regime. However, in the long-run, telecoms companies will see benefits from their high capital investment in base station construction and equipment procurement. Vendors to those companies shall consider possible adjustment to their current price strategies for the relevant products.

In addition, there is also news about the central government considering setting up another state-owned entity to hold and operate all the base stations and relevant assets. As such, the VAT reform for the telecom industry seems to occupy only a very small part of the whole industry reform, and we would expect to see what regulatory changes and reforms the telecom industry would embark upon in the future.

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SAFE Further Improves and Adjusts Foreign Exchange Control on Capital Account

Key Points

- SAFE has streamlined its foreign exchange control on capital account
- Foreign exchange control for transferring of domestic non-performing assets to foreign investors streamlined
- Control for upfront fees of foreign direct investment by domestic institutions relaxed
- Extension of overseas loans of domestic enterprises sees relaxed foreign exchange control

The State Administration of Foreign Exchange ("SAFE") has further adjusted and streamlined its foreign exchange control on capital account by issuing the Notice of State Administration of Foreign Exchange on Further Improving and Adjusting Foreign Exchange Control Policies for Capital Account (the "Notice") on January 10, 2014, which took effect on February 10, 2014.

Highlights of the Notice

Streamlining Foreign Exchange Control for Remittance of Profits out of China

SAFE simplified the requirement of documents verification for remittance of profits out of China last year through issuance of the Guide on Foreign Exchange Administration for Service Trade (the "Guide") and the Detailed rules for Implementing the Guide on Foreign Exchange Administration for Service Trade (the "Rules"). In accordance with the Guide and the Rules, if the amount of profits remitted out of China by a foreign invested enterprise ("FIE") to its foreign investor is not more than US\$50,000 inclusive, the bank will not require any documentary verification. If the amount is more than US\$50,000, the bank shall verify the board resolution of the FIE approving the allocation and remittance of the profits, the FIE's capital verification report, the FIE's latest auditor's report and the tax payment receipt evidencing payment of the withholding tax.

The Notice further streamlines the foreign exchange control for remittance of profits out of China by FIEs by providing that for remittance of profits of more than US\$50,000, the bank will verify the board resolution of the FIE and the tax payment recipient only and will not ask for the FIE's capital verification report and auditor's report for verification.

In addition, the Notice also eliminates the limitation that the amount of profit to be remitted to a FIE's foreign investor in one year shall not exceed the total amount of the "dividends payable to" plus the "declared but unallocated profits" of the foreign investor for the relevant year as indicated in the FIE's latest auditor's report. In other words, an FIE may remit any amount of profits out of China to its foreign investor at any time as long as the board of directors of the FIE has approved such allocation and remittance and the withholding tax has been paid.

Streamlining Foreign Exchange Control for Transferring of Domestic Non-Performing Assets to Foreign Investors

The Notice abolishes the requirement that financial asset management companies shall obtain pre-approval from SAFE for foreign exchange receipts and payments with respect to foreign disposal of domestic non-performing assets. For the foreign exchange income obtained from the foreign disposal of the domestic non-performing assets, the financial asset management company can apply directly with the bank to open a special foreign exchange account to reserve the foreign exchange income, or they can choose to settle the foreign exchange income, without pre-approval from SAFE.

If a foreign investor purchases domestic non-performing assets and then disposes the non-performing assets in China, for the income the foreign investor obtains from disposal of the domestic non-performing assets, the foreign investor may apply with the bank directly for purchasing and remittance of foreign exchange, without the need to apply for pre-approval from SAFE. If the foreign investor becomes the beneficiary of the guarantee of the non-performing assets due to the foreign investor's purchasing of the non-performing assets, such guarantee will not be regarded and regulated as external security under Chinese applicable laws and regulations.

Relaxing Foreign Exchange Control for Upfront Fees of Foreign Direct Investment by Domestic Institutions Overseas

Pursuant to the Notice, if the total amount of the upfront fees for foreign direct investment by domestic institutions in overseas does not exceed US\$3 million and is not more than 15% of the total investment amount proposed by the domestic institution, the domestic institution may apply for upfront fee registration with local counterpart of SAFE by submitting its business license and organization code certificate only. If the total amount of the upfront fees exceeds US\$3 million or 15% of the domestic institution's total investment amount, other than its business license and organization code certificate, the domestic institution shall also submit to SAFE other documents evidencing the domestic institution's genuine involvement in the foreign direct investment, such as the written application the domestic institution submitted to the foreign authority in charge of foreign direct investment.

If the domestic institution fails to receive the approval from the foreign authority for the foreign direct investment within six months after remittance of the upfront fees, the domestic institution shall report to the local counterpart of SAFE concerning how the upfront fees have been used in overseas and wire the remaining fees back to China. The domestic institution may apply with the local counterpart of SAFE to extend the six-month period up to 12 months based on solid reasons.

Further Relaxing Foreign Exchange Control on Extension of Overseas Loans of Domestic Enterprises

The Notice has expanded the scope of domestic enterprises that are allowed to extend overseas loans to foreign companies. Domestic enterprises were only allowed to provide their wholly owned overseas subsidiaries or their overseas shareholding companies with loans before taking effect of the Notice. Under the Notice, domestic enterprises are now permitted to extend overseas loans to any foreign companies that have an equity relationship with the domestic enterprise. In other words, a domestic company will be able to provide overseas loans to another overseas company which is under the same control as this domestic company, previously forbidden prior to the Notice.

Domestic enterprises are currently subject to a 30% limitation for the overseas loans they can provide. The overseas loans provided by domestic enterprises shall not exceed 30% of the domestic enterprise's equity interests. If the domestic enterprise does have need to increase such percentage, they can apply for increasing the percentage with the local counterpart of SAFE under the Notice, and no need to seek final approval from SAFE anymore.

SAFE also has canceled the requirement that the overseas loans quota registered with SAFE's local counterpart has a validity of two years. According to the Notice, domestic enterprises may apply for the term of the overseas loans quota based on their business needs. In addition, if the domestic enterprise is unable to recover the principal and interests of its overseas loans it has extended, the domestic enterprise may apply for deregistration of such overseas loans with the local counterpart of SAFE based on solid reasons.

Streamlining Foreign Exchange Control for Financing Leasing Companies Engaging in Foreign Financing Leasing Activities

Pursuant to the Notice, financing leasing companies engaging in foreign financing leasing activities shall register the incurrence of external credit with the local counterpart of SAFE within 15 working days. They can open a foreign exchange account with the bank directly for reserving the foreign exchange rent income or they may choose to settle the foreign exchange income, without the need to obtain approval from SAFE. In addition, financing leasing companies incurring external credit are not subject to the limitation of overseas loans quota of domestic enterprises.

Financing leasing companies referred hereby include foreign invested financing leasing companies approved by the Ministry of Commerce of China, financing leasing companies approved by China Banking Regulatory Commission (subject to regulatory rules applicable to financial institutions) and domestic financing leasing companies jointly approved by the Ministry of Commerce of China and the State Tax Bureau.

Conclusion

We have seen SAFE's continuous efforts to improve and adjust its foreign exchange control in both capital account and current account, which will encourage foreign direct investment in China to some extent. For example, SAFE's effort on streamlining the foreign exchange control on remittance of profits by FIEs to their foreign investors may provide foreign investors willing to invest in China with some comfort, as one of the major concerns foreign investor usually have is that they will not be able to wire profits out of China at the end of the day.

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Shanghai Strengthens Supervision on Leaders in State Owned Enterprises

Key Points

- Shanghai government issued new provisions on supervision of concurrent position of the leaders in state owned enterprises.
- The implementation of the provisions is the deepening of the SOE reforms initiated from the end of last year with regard to improvement of company governance and utilization of human resource.

Background

It was reported on April 27, 2014, that the Shanghai government recently issued the Provisions on Strengthening the Supervision of Vertical Concurrent Position of the Leaders in State Owned Enterprises Directly Managed by Shanghai People's Government (the "Provisions"), which restrict the leaders of state owned enterprises directly managed by Shanghai People's Government (the "SOEs") from taking leadership positions in affiliated enterprises. These Provisions are parts of Shanghai's state-owned enterprises reforms since the issuance of the Opinions on Further Deepening Shanghai State Owned Asset Reforms to Promote Enterprise Development on December 17, 2013, also known as the "20 Article Scheme", intending to improve the SOE management mechanisms and state owned asset administration and supervision in Shanghai, where the improvement of company governance is emphasized.

Highlights

These Provisions were issued as a result of a survey taken last year that found that more than two thirds of leaders in SOEs act as leaders or officers in affiliates. Though the whole text of the Provisions remains to be published, the main points according to reports from major media in China regarding these Provisions as follows:

- In principal, leaders in SOEs will not be permitted to take a concurrent position in affiliated enterprises in general.
- Only under certain circumstances where concurrent position is of necessity may such leaders concurrently hold positions in affiliated enterprises. In such cases, they cannot hold more than two positions, subject to the filing with the Organization Department of Shanghai Municipal Committee of the Communist Party of China ("Organization Department").
- Under extremely special circumstances where the leaders in SOEs are necessary to take more than two concurrent positions, such concurrent positions should obtain prior approval by the Organization Department or State-owned Assets Supervision and Administration of Shanghai.
- The leaders shall never act as leaders in vertically affiliated enterprises with interest conflicts, and will not be permitted to pay compensation for the held concurrent position(s) in any case.
- The SOEs shall correct any non-compliance concurrent positions within a specified period, otherwise the responsible SOEs and leaders may receive administrative or even criminal liabilities.

Conclusion

The Provisions aim to achieve the goal of making the SOEs to be governed more in accordance with the laws and market-oriented economy to reduce opportunities for corruption and to enhance efficacy for operation in SOEs. The reforms, although positive, will be challenged by the deeply rooted bureaucratic culture, which means the current progression will be a long term revolution that needs to be pushed.

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MOFCOM Issues Interim Rules and Guidelines on Simple Cases of Concentration

Key Points

- MOFCOM clarifies in the Interim Rules the standards to distinguish simple cases of concentration from other cases.
- The Guidelines establish a procedural structure for the filing of simple cases of concentration with MOFCOM by business operators.

Background

On February 11, 2014, the Chinese Ministry of Commerce ("MOFCOM") issued the *Interim Rules on Applicable Standards for Simple Cases regarding Concentration of Business Operators* (the "Interim Rules"), which took effect on February 12, 2014. The *Interim Rules* identified six categories under which the business operators may file a simple case of concentration for the review of MOFCOM.

Subsequently, on April 18, 2014, MOFCOM further issued the *Guidelines on the Filing of Simple Cases regarding Concentration of Business Operators (for trial implementation)* (the "Guidelines"). The Guidelines took effect from the date of publication and specify the documents required for filing of a simple case with MOFCOM, the publication of the simple case notice form, and MOFCOM's recognition on the simple case.

Highlights

Interim Rules

1. Criteria for Recognition of “Simple Cases”

According to Article 2 of the Interim Rules, the following concentrations will be regarded by MOFCOM as simple cases:

- In the same relevant market (i.e. horizontal relationship), the total market share of all business operators participating in the concentration is less than 15%.
- Where the business operators to the concentration are in an upstream-downstream relationship (i.e. vertical relationship), the market share of the parties in each of the upstream and downstream market is less than 25%.
- For concentrations involving business operators that are neither in horizontal relationship nor in vertical relationship, the market share of each of the parties to the concentration is less than 25% in its market.
- A business operator to the concentration establishes a joint venture outside China which does not engage in any economic activities in China.
- A business operator to the concentration acquires equities or assets of an overseas enterprise which does not engage in any economic activities in China.
- A joint venture that is jointly controlled by two or more business operators will be controlled by one or more of such business operators after the concentration.

2. Exceptions to Simple Cases

Though the Interim Rules clearly outline the criteria for determining simple cases, MOFCOM still retains considerable discretion in assessing simple cases. According to Article 3, a concentration in any of the following circumstances will not be treated as a simple case (even if it satisfies the above criteria):

- A joint venture controlled by two or more business operators becomes controlled by one of such operators through concentration and the joint venture competes with the controlling operator in the same relevant market.
- The relevant market related to the concentration is difficult to define.
- The concentration may have an adverse effect on market entry or technology development.
- The concentration may have an adverse effect on consumers or other relevant operators.
- The concentration may have an adverse effect on the development of national economy.
- Any other circumstances that will have an adverse effect on market competition.

The Interim Rules, however, neither provide any procedural rules for filing of a simple case nor specify any timeframe on the review of a simple case by MOFCOM.

Guidelines

While the Interim Rules are silent on the procedural benefits that a simple case might merit, the Guidelines clarify certain practical issues on the filing and determination of a simple case.

1. A Simplified and Shortened Notification Form

In conjunction with the Guidelines, MOFCOM has issued a new shortened notification form for simple case filing as Annex I to the Guidelines (“Simplified Form”), which requires less extensive information compared with MOFCOM’s existing form for non-simple cases. In particular, the filing parties would no longer be required to provide the following information to MOFCOM:

- Detailed information on all affiliates of the filing parties – the Simplified Form requires only the introduction of the filing parties’ affiliates that engage in business related to the concentration.
- Detailed information on the structure of supply and demand in the relevant markets including the list of main suppliers and customers.
- Analysis on the market entry.
- The horizontal or vertical cooperative agreement between the filing parties, such as license agreement, R&D agreement, distribution agreement, etc.
- Opinions of the other parties (such as the government authorities, trade union, competitors, customers, etc.) on the concentration.

2. Procedures for Filing of a Simple Case

Prior to the formal filing, the parties may request a pre-filing consultation with the Anti-Monopoly Bureau (“AMB”) of MOFCOM in order to clarify whether the contemplated concentration meets the criteria for simple cases as set forth in the Interim Rules. Such consultation, however, is not a mandatory procedure.

After receipt of the filing materials, MOFCOM will accept the filing as a “simple case” if it determines that the relevant criteria are met. If MOFCOM does not accept the filing as a simple case, the parties must re-file their transaction under the normal procedure and submit more extensive materials required for an ordinary case.

A new public notice form, as Annex II to the Guidelines, is required to be submitted by the filing parties. MOFCOM will post the completed public notice form on its official website for comment. Third parties have ten days to comment and provide evidence to MOFCOM on whether the transaction merits simple case treatment. If MOFCOM considers that a concentration does not qualify as a simple case by review of the evidence submitted by third parties, it will withdraw the simple case status and the filing parties must re-file the transaction under the normal procedure.

Moreover, MOFCOM has the discretion to withdraw the simple case status at any time during the review process. The filing parties will have the right to express their opinions when MOFCOM decides to withdraw the simple case status.

Conclusion

The issuance of the *Interim Rules* and the *Guidelines* signifies that MOFCOM is aiming to streamline its merger and acquisition review process by adoption of a fast-track mechanism. However, both regulations remain silent on the precise timing required for a simplified review by MOFCOM. In addition, due to MOFCOM's considerable discretion on withdrawal of the simple case status, the parties to the concentration shall be cautious in using the simple case mechanism and be aware of the risk of longer process resulting from withdrawal of the simple case status by MOFCOM.

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Updates Concerning the Amendments to the PRC Company Law

Key Points

- Amendments to the PRC Company Law applicable to the foreign investment sector
- Detailed implementing rules released to implement the Amendments to the PRC Company Law
- Confusion and breakthrough in terms of implementation of the Amendments to the PRC Company Law

Background

On December 28, 2013, the Standing Committee of the National People's Congress of the People's Republic of China released its "*Decision on Amending the Marine Environmental Protection Law of the People's Republic of China and Other Six Laws*", deciding to amend the PRC Company Law for an adoption of a new company registration system, among others. This decision has taken effect since March 1, 2014. This new company registration system relaxed the governmental supervision required to a large extent, especially in registered capital aspect. In the last issue of our Chinese Update we have introduced and analyzed the amendments ("**Amendments**") to the Company Law of the People's Republic of China ("**PRC Company Law**").

To implement the Amendments, the State Council of the People's Republic of China ("**State Council**") and its executive agencies as well as the Supreme People's Court of the People's Republic of China ("**Supreme People's Court**") have issued a series of new implementing rules and amended the existing rules which had conflicts with the Amendments. The newly issued implementing rules and the amended rules have implemented the Amendments extensively and comprehensively.

Application of the Amendments in Foreign Investment Sector

As expected in the last issue of our China Update, a similar company registration system has also been adopted and implemented in foreign investment sector starting from March 1, 2014.

- Articles 217, 26 and 80 of the PRC Company Law

Pursuant to Article 217 of the amended PRC Company Law, the amended PRC Company Law applies to foreign-invested limited liability companies and companies limited by shares, unless otherwise provided in laws on foreign investment. Further, in accordance with Articles 26 and 80 of the amended PRC Company Law, the minimum amount of registered capital and the capital contribution period for limited liability companies and companies limited by shares¹ are not required; unless otherwise provided by laws, administrative regulations or decisions of the State Council.

- No. 648 Decree of the State Council

As to foreign invested enterprises ("FIEs"), besides the PRC Company Law, the registered capital and the capital contribution of FIEs were historically regulated by (i) the Detailed Rules for the Implementation of the Law of the People's Republic of China on Wholly Foreign-owned Enterprises promulgated by the State Council ("**Implementation Rules on WFOEs**") and (ii) the provisions on capital contribution in Sino-foreign equity joint ventures ("**Provisions**") promulgated in 1988 and 1997 jointly by the Ministry of Foreign Trade & Economic Cooperation (the predecessor of the Ministry of Commerce of the People's Republic of China ("**MOFCOM**") and the State Administration for Industry & Commerce of the People's Republic of China ("**SAIC**") with the approval of the State Council.

On February 19, 2014, the State Council released its decree No. 648, namely the State Council's Decision on Repealing and Amending Certain Administrative Regulations ("**Decree No. 648**"), deciding to repeal the Provisions and amend the Implementation Rules on WFOEs, among others. This decision has taken effect since March 1, 2014. In accordance with the Decree No. 648, starting from March 1, 2014 the shareholders of FIEs are no longer required to pay (i) either all registered capital within six months in case of payment in a lump sum, (ii) or at least 20% of the registered capital within three months and the remainder within two years after the establishment of FIEs in case of payment by installments. The shareholders may make capital contribution at any time before expiration of FIEs' operation period. Furthermore, the Decree No. 648 has also amended other articles of the Implementation Rules on WFOEs which had conflicts with the Amendments.

¹ A company limited by shares established by way of a share offer is excluded, to which the registered capital is the total paid-in share capital as registered with the registration authority.

Implementation of the Amendments

Recently, the State Council and its executive agencies as well as the Supreme People's Court have issued a series of new implementing rules and amended the existing rules which had conflicts with the Amendments, mainly including:

- i) the State Council's (1) Guofa (2014) No.7, namely the Notice of the State Council on Promulgation of the Scheme for Reforming Capital Registration System, which was promulgated and took effect on February 7, 2014; and (2) Decree No. 648, which was promulgated on February 19, 2014 and took effect on March 1, 2014; and
 - ii) the SAIC's (1) decree No. 63, namely the Decision on Amending the Detailed Rules for the Implementation of the Regulations of the People's Republic of China on the Administration of Registration of Enterprises as Legal Persons, the Administrative Provisions on the Registration of Foreign-funded Partnerships, the Administrative Measures for the Registration of Sole Proprietorships and the Administrative Measures for the Registration of Individually-owned Businesses, which was promulgated on February 20, 2014 and took effect on March 1, 2014; (2) decree No. 64, namely the Administrative Provisions on Registration of Registered Capital of Companies, which was promulgated on February 20, 2014 and took effect on March 1, 2014; and (3) Gong Shang Qi Zi (2014) No. 28, namely the Notice on Ceasing Annual Inspection of Enterprises, which was promulgated and took effect on February 14, 2014; and
 - iii) the Notice on Performing Joint Report of the Business Operation of Foreign Invested Enterprises for the Year of 2014 ("**Shang zi han (2014) No.175**"), which was jointly promulgated by MOFCOM, the Ministry of Finance, the State Administration of Taxation, the National Bureau of Statistics and the State Administration of Foreign Exchange and took effect on April 18, 2014; and
 - iv) the Supreme People's Court's Fashi (2014) No. 2, namely the Decision on Amending Provisions on Issues Relating to Application of Company Law of the People's Republic of China, which was promulgated on February 20, 2014 and took effect on March 1, 2014.
- Registered Capital System

Implementing the system for registration of capital subscription

– From March 1, 2014, the old system for registration of paid-in capital has been ceased. Meanwhile, a new system for registration of capital subscription has been adopted. Under the new system, the shareholders of a company are only required to register the registered capital of the company that they subscribed with the registration authority. The shareholders may at their will agree on the respectively subscribed capital amount, the method and time limit of contribution and etc., which only need to be recorded in the articles of association of the company. Nevertheless, the shareholders shall be responsible for truthfulness and legitimacy of their capital contribution.

Relaxing the requirements for registration of registered capital

– From March 1, 2014, the regulatory authorities have no longer limited (i) the minimum amount of registered capital and registered capital contribution (unless otherwise provided in laws, administrative regulations and State Council's decisions); (ii) the ratio of initial contribution of capital; (iii) the ratio of monetary capital contribution; and (iv) the time limit for full contribution. Furthermore, the paid-up capital has no longer been an item to be registered with the registration authority and no capital verification report has been required upon company registration.

Excluding the application to 27 sectors

– However, the following 27 sectors shall keep regulated by the original and existing provisions and not be subject to the system for registration of capital subscription temporarily: companies limited by shares established by way of a share offer, commercial banks, foreign invested banks, financial asset management companies, trust companies, financial companies, financial leasing companies, auto finance companies, consumer finance companies, money brokers, village banks, loan companies, rural credit cooperatives, rural fund cooperatives, securities companies, futures companies, fund management companies, insurance companies, insurance agency and insurance brokers, foreign invested insurance companies, direct sale companies, foreign labor cooperation companies, financing guarantee companies, labor dispatching companies, pawn shops, insurance asset management companies, and small loan companies.

- Annual Report and Disclosure System

Starting from March 1, 2014, the old system of annual review for companies has been ceased. A new system of annual report and disclosure for companies has been adopted. Under the new system, companies are required to submit their annual reports to the registration authority via a credit disclosure system from January 1 to June 30 each year. Companies' annual report will be disclosed to the public and any of entities and individuals may search for such report online. Companies shall be responsible for truthfulness and legitimacy of their annual reports.

- Credit Disclosure System

The Chinese government will establish and develop a credit disclosure system. The registration authority will record and disclose the information in connection with the registration, filling and supervision of companies in such system. A name list respecting business irregularities will also be established to record the companies which fail to submit their annual reports within the required time limit or cannot be reached via their registered domiciles (business premises). Such name list will be disclosed to the public via the credit disclosure system as well.

- Registration System

Simplifying the process for registration of domiciles – the registration authority will register a domicile for an applicant as long as the applicant submits the proof of its legal use of such domicile.

Promoting the system for electronic registration and management – the Chinese government will establish a system of digital certificate for management of registration as well as promote e-business licenses and full-course electronic registration and management. E-business licenses have equal legal effect with their hardcopies.

Relaxing administrative interventions in autonomy of companies – the registration authority will relax its administrative interventions in autonomy of companies. For the application materials that applicants submit for registration, the registration authority only implements a formality examination.

Confusion and Breakthrough

We have seen significant innovations in the reform of company registration system. Nevertheless, this reform is pretty new for Chinese regulatory authorities. It is hard for them to avoid any confusion in the course of implementation. Naturally, some breakthroughs have also emerged together.

- Confusion

During a transition period from the old company registration system to the new one, companies have been encountering some confusion, especially in annual report aspect. Before the reform, companies entirely understood how to go through the yearly annual review within the required time limit. But, for the annual report for 2014, it seems unclear as to how to complete it, despite the fact that the deadline is approaching.

Over the years, SAIC and other regulatory authorities jointly issued notices instructing companies going through yearly annual review and conducted review for companies collaboratively. However, for 2014 the Shang zi han (2014) No.175, the sole notice instructing annual report of 2014, was jointly issued by MOFCOM and other regulatory authorities but excluded SAIC, the main authority in charge. In accordance with the Shang zi han (2014) No.175, FIEs shall complete their information filling via an online joint submission system to complete the annual report for 2014 during the period from April 21 to June 30, 2014.

Currently, FIEs have started filling their information online as required. It seems that the data filled by FIEs is required to be more accurate. Any inaccuracy could impact the process for annual report. For the time being, it is unclear as to how to go through the process of annual report with the local branches of SAIC.

- Breakthrough

On January 11, 2014, the Management Committee of Suzhou Industrial Park issued the *Implementing Scheme on the Reform of Industrial and Commercial Registration System*. This implementing scheme allows:

- i) a real property for residential use to be registered as the domicile of a company as long as all landlords of the building consent on such registration and the landlords' consent can be verified by the owner committee or the property management company;
- ii) a real property to be registered as the domicile of more than one companies through an agency being engaged in corporate secretary service.

In addition, this implementing scheme adopts a system of registration replacing the system of approval for establishment of FIEs. FIEs can be directly registered with the registration authority for establishment with reference to domestic companies. Furthermore, it also allows a Chinese individual to set up joint ventures with foreign investors. This actually means a relaxation of market access far more than a reform of company registration system.

Conclusion

Although there is some confusion in terms of implementation of the reform, we expect that the regulatory authorities can collaborate with each other and perform their respective duty and function well. Along with the promoting of the new system and the accumulating of the authorities' experiences, the confusion may be eliminated gradually. All aspects of the reform are expected to be implemented and performed sufficiently. Meanwhile, companies may be liberated from tedious registration affairs and devoted themselves to their business operation.

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