

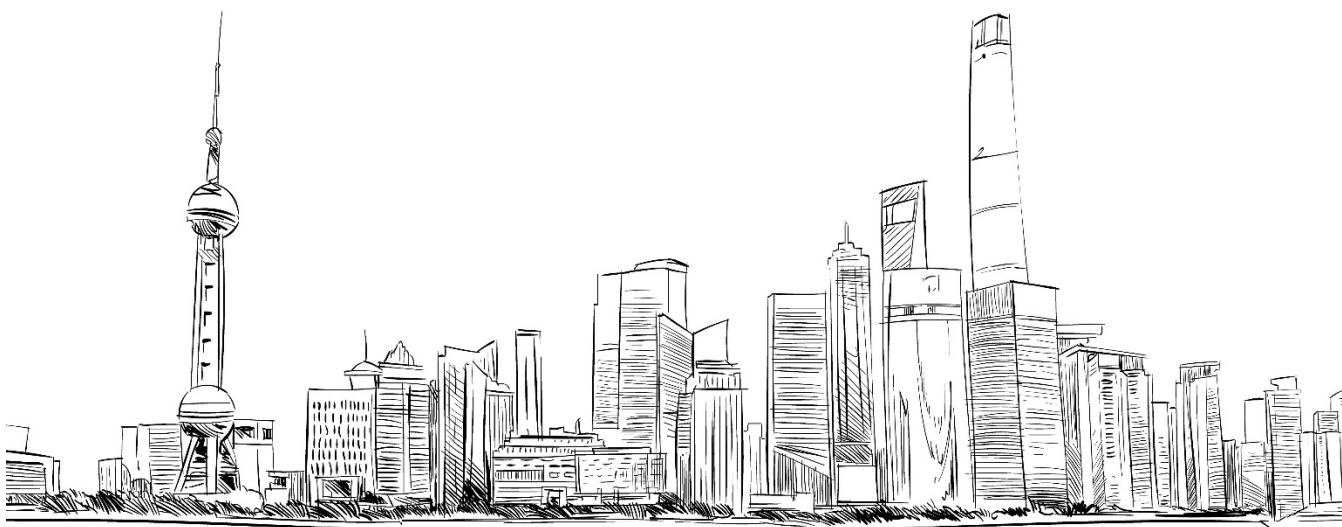


WOODBURN
ACCOUNTANTS & ADVISORS

January 28, 2019

Choosing the right registered office address in China

Prepared by:
Woodburn Accountants & Advisors



All information in this article is verified to the best of our ability and is assumed to be correct at time of release; however, Woodburn Accountants & Advisors does not accept responsibility for any losses arising from reliance on the information provided within. The information provided is for general guidance and does not replace specialized advice. © 2018 Woodburn Accountants & Advisors. All Rights Reserved.



As part of your market research and business plan, finding the right location is a key component. Understanding where you want to establish your first company is key to your success in China. There are several components one needs to look at when investigating cities and districts within cities - looking at the legal and tax issues, infrastructure, property levels, hiring capabilities, industrial clusters, your own network of suppliers and customers and relocation policies, to name a few.

Again, research for most of this information can be conducted via internet searches, social media outlets, local trade shows, local networking events or even on the ground investigations and due diligence. Working with professional real estate agents is advisable particularly as they can offer the service of location searches and providing a comparative study allowing you to analyze each city independently. The real estate agents can also provide you with information needed to help your long-term strategy in terms of rental prices and expansion capabilities both locally in the city and within China.

Is Hong Kong a better option than China?

Firstly, is China even the right location for you now? Is Hong Kong a better alternative? In general Hong Kong is a “better” location to register a company versus in Mainland China, however it will depend on your business model whether having a company registered in Hong Kong (versus in Mainland China) is to your benefit. The first step would be analyzing your overall business model: your competition, your resources, your suppliers, your customers, your financial status, the legal, tax and compliance requirements and comparing it against having a company registered in Hong Kong and a company registered in China.

The consensus will show that doing business in Hong Kong is far easier and has certain advantages from a legal, tax and compliance perspective. However, Hong Kong is a distinct commercial jurisdiction with different legislation, legal system and currency from Mainland China. You will not be able to hire local Mainland Chinese to work for you legally on the Mainland, issue official sales invoices (fapiaos) that are recognized by the Mainland tax authorities to your Mainland Chinese clients or spend a substantial amount of time on the Mainland developing and conducting business. As your business grows, you will have to consider a presence on the Mainland. Hong Kong may, however, be a good location to setup an offshore holding company for a Mainland China company.

Do I need to consider an Offshore Holding Company for my investment into China and if so, which jurisdiction?

Hong Kong or Singapore are the most common jurisdictions used by foreign investors to establish an offshore holding company for investment into the Chinese market. They are the two best jurisdictions



from which a solid base can be created to access China, as well as the rest of Asia.

The purpose of a holding company is to act as a buffer between the ultimate beneficiary and the China company, which could be beneficial for taxation and profit repatriation purposes. However, there is a risk that the business could be deemed to be liable for taxes in China as follows:

1. **Reduced tax rate based on the Double Taxation Agreements** : Offshore holding companies with no commercial or economic substance may be excluded from reduced withholding tax rates under tax treaties in Mainland China.
2. **Indirect transfer of assets**: An investor that has structured an equity interest in a Mainland Chinese company through an offshore holding company could, if the investor sells interests in the offshore company, be subject to an additional tax burden within China.
3. **Place of Effective Management of the Chinese Company**: If the State Administration of Taxation (SAT) deems an offshore company's day-to-day management to be in Mainland China, the offshore company may be subject to profit's tax in Mainland China. Offshore company residence can only be achieved if the offshore directors, wherever they are located, are permitted to exercise effective management of the company.

Additionally, there is a risk from the offshore holding jurisdiction in that many banks today are unwilling to approve corporate bank account applications if the offshore company is purely utilized for holding purposes. The banks want to see that these entities have commercial and economic substance within them. It is therefore recommended when deciding to establish an "offshore holding company" for the China investment to make it operational.

The "NEW" Free Trade Zones

In 2013 the State Council mapped out plans to implement a series of "Negative Lists" for market access, as part of the government's efforts to establish an open, competitive and well-regulated China market. This was first tried and tested in the "new" Free Trade Zones – initially Shanghai, but then expanded to Tianjin, Fujian and Guangdong. The pilot was a major step towards the government's aim to explore a system that could be replicated nationwide for application in early 2018 as part of efforts to streamline government administration and give more freedom to the market.

The "Negative List" lists out industries, fields and businesses from which investments are barred or limited. Market access for foreign investors, therefore, can have equal access to industries, fields and businesses that are **NOT** on the list. Governments at all levels will be responsible for enforcement. In terms of the degree of enforcement, the lists can fall into two categories of prohibited entry and limited



entry, both applying to initial and expanded investments, mergers, and other market entry behaviors by any voluntary market participants.

For the prohibited entry list, market players will not be approved to get access to such industries by the administrative authority, whereas, for limited entry, market players will have to apply for access, which will then be assessed by the authority, and then meet the requirements laid out by the government.

It is important to bear in mind that many of the policies initiated in the zones have already been rolled out to the rest of the country and this trend is likely to continue; meaning that the advantages of being in the Free Trade Zones are limited and need to be explored in-depth for each company looking to enter the market.

Manufacturing cities within China

China is still one of the most rapidly growing countries in the world and when it comes to manufacturing China reigns supreme as the largest supplier in the world. Much of China's manufacturing is in **five major metropolises**.

Shanghai is one of the most important economic, financial, trade and shipping locales in China today. This is due to its incredible rapid development of industry over the last 30 years. Shanghai is responsible for the manufacturing of communication equipment, automobiles, electronics, steel products, petrochemicals and biomedicine. Nearby in Ningbo and Hangzhou, linked to Shanghai by the Hangzhou Bay Bridge and overland high-speed rail, heavy manufacturing of consumer and commercial goods take place daily.

Following Shanghai is Beijing – another leading city in China that is largely focused on manufacturing pharmaceuticals and electronics. It is one of the leaders in bio-engineering and information technology. Beijing holds its industrial power due to its neighboring sister city, Tianjin which itself is another manufacturing giant. The city is the leader in the aerospace and aviation, mobile phones, automobiles and alternative energy products.

Guangzhou in Southern China is one of China's most prominent urban cities. There are thousands of factories located throughout each of the city's manufacturing zones and those factories manufacture everything from toothpicks to automobile parts. Finally, there is Shenzhen (Guangzhou's neighboring sister city in the South) which is known worldwide to be the electronics manufacturing hub of China and the world.

The **"Go West" campaign** is also an incentive focused program pushing foreign investors to setup and



manufacture in the underdeveloped western regions of China – this includes Chongqing, Chengdu as well as Gansu, Guangxi, Guizhou, Inner Mongolia, Ningxia, Qinghai, Shaanxi, Sichuan, Tibet, Xinjiang and Yunnan provinces.

Legal and Tax Considerations when choosing a Registered Office Address in China

As part of your research and business plan it is important to understand the following considerations when registering your address in China. Take advice from a corporate service provider or lawyer about these perspectives.

LEGAL PERSPECTIVE

- Registered Office Address is needed for any type of company registration. A lease agreement for a commercial, retail or industrial property must be signed and documents from your landlord must be provided to the Ministry of Commerce (MOFCOM) as well as the Administration of Industry and Commerce (AIC). A residential lease agreement will not be permitted by the authorities.
- Virtual office addresses are illegal and should be avoided. If you decide to use this option problems may occur later when site visits are conducted by certain government bodies, for example during initial registration inspections, approval processes from the State Administration of Taxation (SAT) or just general spot-checks. Currently most government bodies are relaxed about this, but there is no guarantee that your company will not be targeted or just simply will not be picked out of a lottery for inspection.
- A one-year lease agreement must be signed – any agreement shorter than this will be denied during the registration process. As soon as you sign the lease agreement use it for the registration process. Delaying the company registration process, may cause the government bodies, such as the MOFCOM or AIC to reject the lease agreement. An example, if you delay the process by 6 months and there is only 6 months remaining on the lease agreement, then the MOFCOM or AIC may ask you to re-sign the agreement accordingly, so it is one-year old from the date of submission.
- Commercial property (i.e. an office building) is utilized for a Representative Office, Consulting Company or even Trading Company. A retail property is utilized to establish a retail trading company. Industrial properties would fall under warehousing facilities or manufacturing plants and these properties would need to reflect the business scope of your future company.



- The key is remembering that, unlike other jurisdictions, only ONE company can be registered in ONE registered office space. For small startup's we recommend contacting business centers in the city where you plan on establishing your company to see whether they can offer any small office spaces. Some business centers or workspaces even offer a "for registration purposes only" address which is a 1-person workstation (approximately 3-4sqm in size).
- You are suddenly realizing that the location (i.e. city) you have chosen is not a success for your business and now you wish to change cities. You wish to move your company located in City A to City B. Unfortunately, this is impossible in China. Each city has its own governmental authority and as such moving from one city to another is bypassing the authority level of that government office. There are two solutions available: The first is registering a new company in City B, transferring all assets and staff, followed by liquidating the company in City A OR the second is keeping the original company in City A and registering a Branch Company in City B. Advise: Choose your city wisely and do your research.

TAX PERSPECTIVE

- Each city is made up of districts. When you choose an office space, remember that you are registering your company in that city, within that district. Each district has its own local government office – some of which are more liberal than others. The key note here, though, is that each district has its own tax bureau. When you register your company in a certain district, you are automatically registering with that district tax bureau.
- Tax incentives may be offered by the State or local government. The government is looking to attract specific industries; in high-tech, environmental, R&D, etc. It is our recommendation to understand what these tax incentives are and what the specific criteria are before using this as a determining factor to in choosing one's registered office address location.
- Should you wish to change office space and move to a new district in the future (i.e. you need a larger office space due to expansion) you will need to perform a closure audit with the old tax bureau and re-apply with the new tax bureau. Depending on your business – particularly if you are doing any form of domestic sales for goods and/or services – this can result in a "halt" of your business as you would not be able to purchase official invoices called "fapiaos" from either the old or new tax bureau until the audit and re-application are completed. This process can last a minimum of three months.

Conclusion



WOODBURN
ACCOUNTANTS & ADVISORS

It is every real estate agents' mantra: Location, location, location. You've certainly heard the phrase enough and may wonder what inspires agents to say the word three times. Choosing a location for a new business, especially in such a large country as China, is one of the most important decisions entrepreneurs make during the planning phase of launching their China ventures. The location of a business can affect many aspects of how it operates, such as total sales, talent acquisition and retainment, how costly it is to run and the legal and tax consequences. Do not rush the decision to choose your Chinese city. The best recommendation an advisor can give you is to meet with real estate agents locally to discuss your lease objectives, your company's goals together with your financial budget to filter and determine the right location for your business.

For more information:

Contact us: info@woodburnglobal.com

Find us on: woodburnglobal.com

Subscribe **FREE** to our latest legal, tax and trade news on China and Hong Kong delivered directly to your inbox from our website at woodburnglobal.com

Woodburn Management Consulting (Shanghai) Company Limited

47/F Hong Kong New World Tower, 300 Huaihai Zhong Road, Shanghai 200021, China

T: +86 21 5116 2893

E: info@woodburnglobal.com

W: woodburnglobal.com