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# CHINA<sup>1</sup>

## I. Overview of China<sup>2</sup>

China is a republic, with a socialist system of law based primarily on the Civil Law model. The constitutionality of laws is determined by the National People's Congress and its Standing Committee, which also exercise the highest level of legislative power of the country. Most of the laws governing the activities of for-profit and not-for profit organizations were adopted from 1978, when China began to open up and undertake economic reform. The registration procedures, auditing and reporting requirements in China are often criticized as burdensome and unclear. The discretion of government authorities in executing the laws is also frequently criticized. However, as a result of the pro-business stance that China has adopted to incentivize its economy, in recent years the government has made improvements towards simplifying the regulatory burden on for-profit organizations.

## II. Registration Procedures

### A. For-Profit Organizations

#### a. Laws

China recognizes two types of companies: 1) companies limited by shares and 2) limited liability companies. Both are subject to the Company Law<sup>3</sup>. The Company Law sets out the primary legal structures of both types of companies. The detailed registration procedure requirements are stated in the Regulation on the Administration of Company Registration (*The Company Registration Regulation*)<sup>4</sup>. As per this regulation, an organization not registered as a company is forbidden from holding itself out as a company when undertaking activities.

Other than these two laws, other significant legislation includes: (i) the Joint Venture Law<sup>5</sup> and the Enforcement Regulations of Joint Ventures Law<sup>6</sup>, which set

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<sup>1</sup> The following memorandum was prepared by pro bono counsel for the ABA Center for Human Rights. It is intended as background information only and should not be relied upon as legal advice on a particular case. The views expressed herein have not been approved by the House of Delegates or the Board of Governors of the American Bar Association, and, accordingly, should not be construed as representing the policy of the American Bar Association.

<sup>2</sup> Disclaimer: The associate who wrote this section is not qualified to practice China law, and relied on publicly available information such as China statutes, government websites, and other websites.

<sup>3</sup> The Company Law, amended in 2013, available at [http://www.fdi.gov.cn/1800000121\\_23\\_71637\\_0\\_7.html](http://www.fdi.gov.cn/1800000121_23_71637_0_7.html) (in Chinese); [http://www.fdi.gov.cn/1800000121\\_39\\_4814\\_0\\_7.html](http://www.fdi.gov.cn/1800000121_39_4814_0_7.html) (in English)

<sup>4</sup> Regulation on the Administration of Company Registration, amended in 2014, available at [http://www.saic.gov.cn/zcfg/xzfgfxwj/xxb/201402/t20140227\\_142236.html](http://www.saic.gov.cn/zcfg/xzfgfxwj/xxb/201402/t20140227_142236.html) (in Chinese); <http://tradeinservices.mofcom.gov.cn/en/b/2005-12-18/17120.shtml> (in English)

<sup>5</sup> The Joint Venture Law, amended in 2001, available at [http://www.gov.cn/banshi/2005-08/31/content\\_69775.htm](http://www.gov.cn/banshi/2005-08/31/content_69775.htm) (in Chinese)

<sup>6</sup> Enforcement Regulations of Joint Ventures Law, amended in 2011, available at [http://www.gov.cn/gongbao/content/2011/content\\_1860719.htm](http://www.gov.cn/gongbao/content/2011/content_1860719.htm) (in Chinese)

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out specific requirements for China-foreign joint ventures; and (ii) the Foreign Investment Company Law<sup>7</sup> and the Detailed Enforcement Regulations of Foreign Investment Company Law<sup>8</sup>, which set out specific requirements for foreign investment companies. All of these laws and regulations are discussed further below.

i. Limited Liability Companies

a) Registration/deregistration authority: the Authority of Industry and Commerce (*AIC*)

b) Registration Process:

1) Company name pre-approval: before making an application for registration of a new company, the proposed company name is subject to AIC pre-approval. AIC will check if the company name complies with the Regulation on the Supervision of Company Name Registration<sup>9</sup>. Most of the published internal practices of the AIC indicate that the decision must be made immediately or within one or two business days.

2) Application for registration: an application letter together with all the required documents for setting-up the new company needs to be submitted to the AIC within 6 months after the pre-approval of the company name. The Company Registration Regulation lists the following required documents:

- Application letter for company registration signed by the legal representative of the new company;
- Letter proving that the shareholders of the new company have authorized a specific person to apply for company registration on their behalf. That same person should file the application letter and attachments with the AIC;
- Articles of association of the new company;
- Qualification certificates of the shareholders: for legal persons, their registration certificates, and for natural persons, their ID cards or passports;
- Documents indicating the names and residences of the company's directors, supervisors and managers, and the certificates relating to their appointments, elections or engagements;

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<sup>7</sup> The Foreign Investment Company Law, adopted in 2000, available at [http://www.gov.cn/banshi/2005-08/31/content\\_69774.htm](http://www.gov.cn/banshi/2005-08/31/content_69774.htm) (in Chinese)

<sup>8</sup> Enforcement Regulations of Foreign Investment Company Law, amended in 2011, available at: <http://www.mofcom.gov.cn/article/swfg/swfgbl/201101/20110107352242.shtml> (in Chinese)

<sup>9</sup> Regulation on the Supervision of Company Name Registration, amended in 2012, available at [http://www.szaic.gov.cn/zcwj/qydj/qydjfl/200809/t20080905\\_32929\\_14077.htm](http://www.szaic.gov.cn/zcwj/qydj/qydjfl/200809/t20080905_32929_14077.htm) (in Chinese)

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- Documents of tenure of office and identity certificate of the new company's legal representative;
  - Notification of the Company Name Pre-Approval;
  - Domicile certificate of the new company; and
  - Any other documents required in the regulations issued by the State AIC.

If any other laws, administrative regulations or decisions of the State Council of China require any pre-approval before registration of the company, such approval should also be submitted.

- 3) Special Pre-approval: if all or part of the business scope of a company is subject to approval before registration as stipulated by any laws, administrative regulations or decisions of the State Council, then such approval from the relevant department of the State must be obtained before applying for registration. The approval shall be submitted to the AIC when applying for registration. Many different laws and regulations set forth numerous business activities which are subject to such pre-approval, including: coal production, salt production, hotel business, internet and information services.

c) Deregistration

1) Causes for dissolving a company<sup>10</sup>

A company shall be dissolved due to the following reasons:

- when the term of operation as specified in the company's articles of association expires or another cause of dissolution as specified in the company's articles of association arises;
- if the board of shareholders or a general meeting of the shareholders resolves to dissolve the company;
- if dissolution is necessary as a result of the merger or division of the company;
- if its business license has been revoked, or it is ordered to close down or to be revoked according to the law; or
- if it is ordered to be dissolved by the people's court according to Article 182 of the Company Law.<sup>11</sup>

2) Liquidation Group<sup>12</sup>

Except where dissolution of a company is the result of a merger or division, a liquidation group shall be formed to commence the liquidation within 15 days after a cause of dissolution occurs. The liquidation group shall be composed of shareholders, in the case of a limited liability

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<sup>10</sup> The Company Law, Article 180

<sup>11</sup> The Company Law, Article 182: "Where any severe difficulty occurs to the operation management of a company, in which case the interests of the shareholders may suffer heavy losses if the company continues to exist and there is no other way to solve the problem, the shareholders representing more than ten percent of the voting rights of all the shareholders of the company may file a request with the people's court to dissolve the company."

<sup>12</sup> The Companies Law, Article 183.

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company; or shall be composed of directors or the candidates determined by the general meeting of shareholders, in the case of a company limited by shares. Where a liquidation group has not been formed to carry out the liquidation within the specified time limit, the creditors may apply to the people's court for its designation of relevant personnel to form a liquidation group and carry out the liquidation. The people's court shall accept the application, and shall, in a timely manner, organize a liquidation group to carry out liquidation.

A liquidation group shall, within 10 days from the date of its formation, submit a list of the members and person in charge of the liquidation to the AIC for its record.

3) Applying for Deregistration:

In the following circumstances, the liquidation group of a company must apply for deregistration to the original AIC within 30 days from the date of conclusion of liquidation of the company<sup>13</sup>:

- the company is declared bankrupt according to law;
- the duration of business operation prescribed in the articles of association of the company expires or any other situation for dissolution prescribed in the articles of association of the company occurs, unless the company continues to exist by virtue of an amendment to the articles of association of the company;
- the company is dissolved by a resolution of a shareholders' meeting or shareholders' assembly or is dissolved by the shareholder of a one-person limited liability company or a resolution of the board of directors of a foreign investment company;
- the business license of the company is revoked or the company is ordered to be closed down or dissolved according to law;
- the company is dissolved by the people's court according to law;
- or
- any other circumstance of dissolution set out by a law or administrative regulation.

4) Documents Required for Deregistration<sup>14</sup>

- written application for registration signed by the person in charge of the liquidation group;
- A bankruptcy ruling or dissolution judgment of the people's court, a resolution or decision made by the company according to the Company Law or a document rendered by the administration authority ordering the closing down or dissolution of the company;

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<sup>13</sup> The Company Registration Regulation, Article 42.

<sup>14</sup> The Company Registration Regulation, Article 44.

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- A liquidation report archived and affirmed by a shareholders' meeting or shareholders' assembly, the shareholder of a one-person limited liability company, the board of directors of a foreign investment company, the people's court or the administrative authority approving the company, as applicable;
  - The business license of the company; and
  - Any other documents as required by a law or administrative regulation.

## 5) Redress Mechanisms

Under the Law of Administrative Reconsideration, companies may challenge certain specific decisions from administrative authorities, such as an order to close down a company<sup>15</sup>. In these cases, companies may apply for reconsideration of such order to a higher level of administrative authority within 60 days after receiving the order.

The company could also file a lawsuit with the competent courts in accordance with the Law of Administrative Litigation<sup>16</sup> requesting withdrawal or reconsideration of the closing down order within 6 months after receiving it. In most circumstances, the company may choose either to apply for reconsideration first or to sue the court directly.

It is worth noting that applying for reconsideration before the administrative authority or filing a lawsuit against an administrative authority on a certain decision made by such authority will not suspend the execution of the decision.

### ii. Companies Limited by Shares

The Company Law and the Company Registration Regulation also govern the registration and deregistration process for companies limited by shares. The governing administrative authority, registration and deregistration process and redress process of companies limited by shares are very similar to the limited liability companies. The main difference is applies to companies incorporated by share offer, which must submit their registration applications within 30 days after the inaugural assembly. Such companies also must submit the written minutes of the inaugural assembly. If such companies intend to offer their shares to the public, the written approval issued by the securities regulatory authority of the State Council must also be submitted<sup>17</sup>.

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<sup>15</sup> The Law of Administrative Reconsideration, issued in 1999, available at: [http://www.gov.cn/banshi/2005-08/21/content\\_25100.htm](http://www.gov.cn/banshi/2005-08/21/content_25100.htm) (in Chinese)

<sup>16</sup> The Law of Administrative Litigation, amended in 2014, in force since 1<sup>st</sup> May 2015, available at: [http://www.npc.gov.cn/npc/xinwen/2014-11/02/content\\_1884662.htm](http://www.npc.gov.cn/npc/xinwen/2014-11/02/content_1884662.htm) (in Chinese)

<sup>17</sup> The Company Registration Regulation, Article 21

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### iii. China-foreign Joint Ventures

As mentioned above, the registration and deregistration of Joint Ventures between Chinese and foreign investors is governed by the Joint Venture Law and its Enforcement Regulation. According to Article 16 of the Enforcement Regulation, joint ventures in China may only be registered as limited liability companies. The registration and deregistration process and requirements for joint ventures are also quite similar to those of limited liability companies as discussed above, except for some specific requirements:

- a) Pre-approval by the ministry or bureau of commerce for registration and deregistration
- b) The documents that need to be provided by the Chinese and foreign participants of the new company to obtain a registration pre-approval<sup>18</sup>: 1) application for the establishment of a joint venture; 2) a feasibility study report of the joint venture<sup>19</sup>; jointly prepared by the participants; 3) joint venture agreement, contract and articles of association signed by the representatives authorized by the participants; 4) list of candidates for chairman, vice-chairman and directors appointed by the participants; and 5) other documents stipulated by the examination and approval authority.
- c) Conditions for Deregistration  
A joint venture may be dissolved in the following cases:<sup>20</sup> 1) Expiration of the business term; 2) Inability to continue operations due to heavy losses; 3) Inability to continue operations due to the failure of one of the contracting parties to fulfill the obligations prescribed by the agreement, contract and articles of association; 4) Inability to continue operations due to heavy losses caused by force majeure such as natural disasters and wars, etc.; 5) Inability to obtain the desired objectives of the operation and at the same time to see a future for development; and 6) Occurrence of other reasons for dissolution prescribed by the contract and articles of association.
- d) Time limit  
The Enforcement Regulation gives a 3-month time limit for the ministry or bureau of commerce to decide whether to grant the pre-approval<sup>21</sup>.

### iv. Foreign Investment Companies

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<sup>18</sup> Enforcement Regulation of Joint Venture Law, Article 7

<sup>19</sup> The law did not stipulate what specific information should be included in the feasibility study report. Normally the participants will evaluate and analyze the potential of the new joint venture and include in the report the business operational, economical, financial, technical, organizational and legal feasibility of its business.

<sup>20</sup> Enforcement Regulation of Joint Venture Law, Article 90

<sup>21</sup> Enforcement Regulation of Joint Venture Law, Article 8

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In China, foreign investment companies shall be registered as limited liability companies<sup>22</sup> unless otherwise approved by the Ministry of Commerce. The legal requirements for registration and deregistration are similar to those for limited liability companies that were discussed above, but there are some specific requirements:

- a) Pre-approval by the ministry/bureau of commerce for registration and deregistration
- b) The law specifies that approval to establish a wholly foreign-owned enterprise shall not be granted in any of the following circumstances: 1) if it is detrimental to China's sovereignty or the social public interest; 2) if it endangers China's national security; 3) if it violates Chinese laws or regulation; 4) if it fails to conform with the requirements for developing China's national economy; or 5) if it is likely to cause environmental pollution.<sup>23</sup>
- c) As in joint ventures, the foreign investor or investors shall also prepare and submit a feasibility study report of the foreign investment company similar to the report mentioned above for joint ventures together with the application for pre-approval and other documents. If there are more than one foreign investors, copy of the agreement between the investors for setting up the company shall also be submitted.<sup>24</sup>
- d) Conditions for deregistration:  
A joint venture may be dissolved in the following cases: 1) Expiration of the business term; 2) the foreign investor deciding to dissolve the enterprise due to operations not running well and heavy losses being suffered; 3) inability to continue operations due to heavy losses caused by force majeure, such as natural disasters and wars; 4) bankruptcy; 5) the enterprise's right to operate being revoked pursuant to the law due to the enterprise violating Chinese laws or regulations or harming the social public interest; and 6) occurrence of other reasons for the dissolution as prescribed in the enterprise's articles of association.<sup>25</sup>
- e) Time limit  
Same as joint ventures

## B. Not-For Profit Organizations

### a. Laws

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<sup>22</sup> Enforcement Regulation of Foreign Investment Company Law, Article 18

<sup>23</sup> Enforcement Regulation of Foreign Investment Company Law, Article 5

<sup>24</sup> Enforcement Regulation of Foreign Investment Company Law, Article 10

<sup>25</sup> Enforcement Regulation of Foreign Investment Company Law, Article 72

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China also recognizes different forms of not-for profit organizations, including: social organizations<sup>26</sup>, private non-enterprise units<sup>27</sup>, foundations and representative offices of foreign foundations. Registration of social organizations is governed by the Regulation on the Registration and Management of Social Organizations<sup>28</sup>; registration of private non-enterprise units is governed by the Interim Regulations on the Registration and Administration of Private Non-enterprise Units<sup>29</sup>; and registration of foundations and representative office of foreign foundations is governed by the Regulation for the Management of Foundations<sup>30</sup>.

According to Article 3 of the Regulation on the Registration and Management of Social Organizations, a not-for profit organization must be registered unless it falls into any of the following conditions: a) it is a “People’s Union” participating in the Chinese People’s Consultative Conference; b) it gets the approval of the Central Government of China for non-registration; or c) it is an organization carrying out activities within a government entity, a registered social/institutional organization or a corporation.

Informal not-for profit organizations appear in China in many different forms, like small community-based organizations; rural cooperatives; religious organizations; and social networks organized to achieve common goals. However, unregistered non-governmental organizations (NGOs) are regarded as illegal unless they fall into the exceptions stipulated in the laws. In 2000, the Ministry of Civil Affairs issued Provisional Measures on Banning Illegal NGOs, according to these Provisional Measures, the bureau of civil affairs could ban an unregistered NGO from undertaking activities and confiscate its illegal assets.

i. Registration/deregistration authorities

The registration and deregistration authorities for not-for profit organizations in China are the ministry and local bureau of civil affairs. The laws also require pre-written approval from the “competent authority” for registration and deregistration (in most of the cases, competent authority refers to the governmental agency in charge of the specific field of practice for a not-for profit organization).

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<sup>26</sup> According to Article 2 of the Regulation on the Registration and Management of Social Organizations, a social organization refers to a not-for profit organization founded by Chinese nationals and/or legal persons that carries out activities in accordance with its by-laws in order to achieve the common goals of its members.

<sup>27</sup> According to Article 2 of the Interim Regulations on the Registration and Administration of Private Non-enterprise Units, a private non-enterprise unit refers to a not-for profit social service organization founded by companies, public-sector organizations, social organizations or natural persons. Private non-enterprise units in China include private schools, museums, hospitals and other types of social service organizations.

<sup>28</sup> Regulation on the Registration and Management of Social Organizations, adopted in 1998, available at <http://www.icnl.org/research/library/files/China/RegsSocOrgs.pdf> (in English)

<sup>29</sup> Interim Regulations on the Registration and Administration of Private Non-enterprise Units, adopted in 1998, available at <http://www.icnl.org/research/library/files/China/InterRegsNon-Ent.pdf> (in English)

<sup>30</sup> Regulation for the Management of Foundations, adopted in 2004, available at <http://www.icnl.org/research/library/files/China/foundation.pdf> (in English)



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The registration authority and the competent authority also supervise the daily operations of not-for profit organizations.

- ii. The Regulation on the Registration and Management of Social Organizations of China requires that the social organizations shall: 1) abide by the Constitution, laws, regulations and policies of the country; 2) not oppose the basic principles enshrined in the Constitution; 3) not endanger the reunification and security of the country, its social interest or the lawful rights and interest of other organizations or citizens; 4) not breach social ethics and morality; and 5) not conduct business activities for profit.

Similar requirements also apply to social organizations, civil non-enterprise institutions and foundations.

These requirements regulate the conduct of all activities, both internal and external, of not-for profit organizations in China.

- iii. Registration and deregistration of social organizations

- a) Pre-approval of organization name: before making an application for registration of a new social organization, the proposed name is also subject to pre-approval from the bureau of civil affairs. The bureau of civil affairs will grant the pre-approval if the company name is in compliance with the law. Similar requirements also apply to private non-enterprise units and foundations.

- b) Registration

“Pre-approval for preparation activities”: social organizations need to obtain an additional approval for “preparation activities” (i.e. holding members meetings, adopting the organization’s by-laws, and electing the people in charge of the operation of the organization and the legal representatives. Before undertaking these activities, the founder of a social organization must first obtain approval from the competent authority and then make an application to the bureau of civil affairs for their approval to do so. .

- 1) When applying for “preparation activities” approval founders of social organizations need to submit the following documents: application letter; a written approval for undertaking preparation activities from the competent authority; a record of assets and proof of the right to use such assets; ID and résumé of founder; a draft of the by-laws.
- 2) Time limit: within 60 days of receiving the documents, the registration authority must decide whether or not to approve the preparation activities. In case of refusal it must provide reasons. Once approval is granted, the social organization can begin to take preparation activities. After the preparation activities are completed, the social organization

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can file the registration application with the registration authority within 6 months of the preparation activities pre-approval. The registration authority shall then review the registration application within 30 days and issue the registration certificate in case of approval.

c) Deregistration

- 1) A social organization could be deregistered if: its objective has been achieved; its members decide to terminate it; separation into different organizations, or combination with other organizations and other reasons for closure<sup>31</sup>.
- 2) A social organization must establish a liquidation group under the supervision of a competent authority before deregistration. Within 15 days after the completion of the liquidation process, the social organization must apply to the registration authority for deregistration and submit the application letter signed by a legal representative, the written approval from the competent authority and the liquidation report.
- 3) The regulation does not set out a time limit for the registration authority to approve the deregistration. However, according to the Law of Administrative Approval<sup>32</sup>, a 20-business day time limit would apply.
- 4) Redress Mechanisms for administrative reconsideration and litigation are also available against the decisions made by the authorities on these matters.

iv. Registration and deregistration of private non-enterprise units

a) Registration:

There is no preparation activities approval required for private non-enterprise units - the founder may directly apply for registration with the required documents, which are the same as those required for registration of social organizations. The time limits for approval are also the same.

b) Deregistration:

The deregistration process of private non-enterprise units is the same as the one for social organizations.

v. Registration and deregistration of foundations and representative office of foreign foundations

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<sup>31</sup> See Regulation on the Registration and Management of Social Organizations, Article 21. The Regulation does not clarify the specific reasons for deregistration of a social organization. But a social organization could be deregistered or dissolved, in accordance with the law, by an order of an administrative authority or by a decision of the People's court.

<sup>32</sup> Law of Administrative Approval, adopted in 2004, available at [http://www.gov.cn/flfg/2005-06/27/content\\_9899.htm](http://www.gov.cn/flfg/2005-06/27/content_9899.htm) (in Chinese)

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a) Registration:

There is also no preparation activities approval required for foundations and representative offices of foreign foundations.

For applications for registration of foundations, the following documents are required: an application letter, draft by-laws, records of assets and proof of use of premises, a list of board members and proof of their identities, the resume of the chairman, vice chairman and the secretary of the board; and the written approval of the competent authority.

For applications for registration of representative offices of foreign foundations, the following documents are required: an application letter, proof of registration of the foundation in a foreign county and its by-laws, the ID and resume of the responsible person, proof of use of premises; and the written approval of the competent authority. The registration approval time limits are the same as for social organizations.

b) Deregistration:

Foundations and representative offices of foreign foundations may be deregistered upon: closure on their own initiative according to their by-laws; incapability of carrying out public benefit activities in line with the missions stipulated in their by-laws; or closure on their own initiative for other reasons. The deregistration approval time limits are the same as for social organizations.

### III. Tax Laws

#### A. For-Profit Organizations

##### a. Laws

To attract foreign investments, China used to apply preferential tax treatment to foreign investment companies and joint ventures, but things changed in 2008. Now all companies are governed by the Enterprise Income Tax Law<sup>33</sup>. Pursuant to this law, the income tax rate for ordinary companies is 25%. However, the law also provides favorable tax treatment for small meager-profit enterprises at a reduced income tax rate of 20% and important high-tech enterprises at a reduced income tax rate of 15%. Enterprise income tax may also be exempted or reduced on the following types of income:

- i. incomes generated from engagement in agriculture, forestry, husbandry and fishery;
- ii. incomes generated from investment in the business operations of important public infrastructure projects supported by the state;
- iii. income generated from environmental protection, energy and water saving projects and other projects satisfying related requirements;

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<sup>33</sup> Enterprise Income Tax Law, adopted in 2008, available at [http://www.fdi.gov.cn/1800000121\\_39\\_3339\\_0\\_7.html](http://www.fdi.gov.cn/1800000121_39_3339_0_7.html) (in English)

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- iv. incomes generated from technology transfer and other projects satisfying related requirements; and
  - v. If a non-resident enterprise has no organ or establishment within the territory of China, or its incomes have no actual connection to its organ or establishment inside the territory of China, its incomes sourced inside the territory of China.

Other than these general tax regulations, preferential tax treatments are also granted to enterprises registered or practicing in special economic zones and free trade zones. So far there are 7 economic zones and 4 free trade zones in China, and each may adopt different tax treatments. For instance, some very important high-tech companies in Xiamen Special Economic Zone may be exempted from income tax altogether for two years from the first year they generate taxable income.

## B. Not-For Profit Organizations

### a. Laws

The tax treatment for not-for profit organizations in China is also set out in the Enterprise Income Tax Law and Implementing Regulations of Enterprise Income Tax Law<sup>34</sup>. However, social organizations, private non-enterprise units and foundations are actually not allowed to undertake for-profit activities by the regulations governing their registration as mentioned in Section II.

Under Chinese tax law, a not-for profit organization may be exempted from income tax if it satisfies following requirements<sup>35</sup>:

- i. It is legally registered as a non-profit-making organization;
- ii. It is engaged in charitable and non-profit-making activities;
- iii. Apart from the reasonable and relevant expenditures of the organization, all income obtained is used for the charitable or non-profit-making activities approved in its registration documents or prescribed in its articles of association;
- iv. Any assets and interest obtained from its assets are not used for distributions (Paying reasonable salaries to staff are not regarded as distributions);
- v. After the organization is deregistered, any remaining assets are used for charitable or non-profit-making purposes or donated through the registration and administration authorities to other organizations that have the same nature and purposes as those of the deregistered organization, and the same is announced to the public;
- vi. The donors do not retain or enjoy any right over assets donated to the organization;

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<sup>34</sup> Implementing Regulations of Enterprise Income Tax Law, adopted in 2008, available at [http://www.fdi.gov.cn/1800000121\\_39\\_1563\\_0\\_7.html](http://www.fdi.gov.cn/1800000121_39_1563_0_7.html) (in English)

<sup>35</sup> Implementing Regulations of Enterprise Income Tax Law, Article 84

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- vii. Expenditures on salaries and welfare for staff are controlled within the prescribed percentage; and
  - viii. the organization does not distribute its assets in any disguised form.

Not-for profit organizations satisfying the requirements above must apply for recognition of tax exempt status with their local tax bureau. In practice, tax bureaus may accept applications twice a year, each with a specific deadline. The law does not clarify how long the bureau may take for such recognition, so a 20 business day time limit would also apply under the Law of Administrative Approval. Redress mechanisms of administrative reconsideration and administrative litigation are available where an organization reasonably believes the tax bureau has wrongly decided not to grant it tax exempt status.

After recognition of its tax exempt status, not-for profit organizations receive an income tax exemption for incomes like donations, membership fees and government subsidies.

#### C. Analytical comparison

China generally regards all profit-making activities are taxable regardless of whether such activities are taken by for-profit organizations or not for profit organizations. Tax exemptions and preferential tax treatments for for-profit activities are granted mainly as incentives for high-tech enterprises and local business development.

### IV. Financial Transaction Laws

#### A. For-Profit Organizations

##### a. Laws

##### i. Foreign Investment/Foreign Funding Laws

a) The registration of foreign investment companies and China-foreign joint ventures are discussed in section II above.

b) Limited/forbidden industries for foreign investors: the National Development and Reform Commission and the Ministry of Commerce issue the Industry Catalog for Guiding Foreign Investment from time to time. The catalog lists all the encouraged, restricted and forbidden industries for foreign investors. Examples of forbidden industries include: transgenic organism research, mining of radioactive minerals and movie making. Examples for restricted industries include: gold mining, legal consultancy and cinema management.

##### c) Foreign exchange registration

The Interim Regulation on the Foreign Exchange Registration and Management of Foreign Investment Companies<sup>36</sup> requires foreign investment companies and China-foreign joint ventures to apply for foreign exchange registration with the

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<sup>36</sup> Interim Regulation on the Foreign Exchange Registration and Management of Foreign Investment Companies, adopted in 1996, available at <http://www.treasurer.org.cn/webinfosmains/index/show/46804.html> (in Chinese)

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foreign exchange bureau within 30 days after receiving their registration certificates. Such companies may only open their foreign exchange bank accounts after obtaining the registration certificates. This regulation also requires annual inspection with the foreign exchange bureau.

ii. Political Contribution Laws

There is no practice of political campaigning in China, so political contributions likewise do not exist.

B. Not-For Profit Organizations

a. Laws

i. Foreign Investment/Foreign Funding Laws

a) Currently China only recognizes foreign chambers of commerce<sup>37</sup>(in the form of social organization) and branches of foreign foundations. The registration process and requirements are discussed in Section II above.

b) The Chinese State Administration of Foreign Exchange issued in 2009 the Notice of the Foreign Exchange Management for Donations of Institutions within China. Pursuant to this notice, Chinese not-for profit organizations must open a foreign exchange bank account specially in order to receive foreign donations, and submit the following documents to the bank in order to receive such donations:

- An application letter with a commitment that the donation will not violate any requirement of law, that the approval and recording process required by relevant state regulations are obtained (the research indicates that the approval and recording requirement may apply only when Chinese organizations are donating overseas, as the relevant clause applies on both giving and receiving donations) and the organization will assume any related liabilities;
- A copy of the registration certificate of the organization; and
- A donation agreement listing the purpose of the donation.

The bank will review such documents and report to the local foreign exchange bureau any suspected or abnormal donation giving or receiving information.

ii. Political Contribution Laws

Same as above.

C. Analytical Comparison

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<sup>37</sup> Interim Regulation on Management of Foreign Chambers of Commerce, adopted in 1989, available at <http://swshzz.chinanpo.gov.cn/6036/62165.html> (in Chinese)

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It seems China has adopted strengthened rules towards the practices of foreign not-for profit organizations in China and towards overseas funding to Chinese not-for profit organizations.

## V. Auditing/Reporting Requirements

### A. For-Profit Organizations

#### a. Laws

- i. Annual audit: the Company Law requires all companies to prepare financial and accounting reports at the end of each fiscal year (normally by 31<sup>st</sup> December). Such reports must be audited by an accounting firm according to law.
- ii. Annual report publication: from 2014, the State Council of China stopped the annual inspection it used to undertake through AIC of all corporations, including joint ventures and foreign investment companies. Instead the State Council adopted a mechanism of company annual report publication<sup>38</sup>. The new mechanism requires companies to submit an annual report to the local AIC between 1<sup>st</sup> January and 30<sup>th</sup> June each year via the AIC online submission system and such annual report must then be published online. The Reform Plan for Registered Capital Registration System only requires the report to include the capital contribution status of the shareholders and assets status of the company, although local AICs may have detailed requirements as to other information to be covered in the report like contact details, shareholding status and so on. The AIC will randomly inspect reports submitted, and if it finds in such inspection any company whose report contains false information, it will publish the company in a list of companies with abnormal operation on its official website.

### B. Not-For Profit Organizations

#### a. Laws

- i. Annual inspections: annual inspections are still applicable for not-for profit organizations. And the requirements are also stipulated in the Regulation on the Registration and Management of Social Organizations, the Interim Regulations on the Registration and Administration of Private Non-enterprise Units, and the Regulation for the Management of Foundations.

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<sup>38</sup> Reform Plan for Registered Capital Registration System, issued in 2014, available at [http://www.gov.cn/zwggk/2014-02/18/content\\_2611545.htm](http://www.gov.cn/zwggk/2014-02/18/content_2611545.htm) (in Chinese)

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In general, every year before 31<sup>st</sup> March, all types of not-for profit organizations need to submit an annual work report to the ministry or bureau of civil affairs, and such report needs to get the pre-approval by the competent authority (as explained in Section II. B). The content of such report must cover: whether the organization has practiced in compliance with laws, regulations and state policies; whether the organization has completed the required registration process; the activities taken according to the by-laws; and any change in personnel, organization structure and financial management.

Other than the requirements above, foundations also need to submit their finance accounting report; auditor's report; and any records of their fundraising, donation receiving, and financial support-providing activities. Foundations also need to publish their annual work reports on the media appointed by the ministry or bureau of civil affairs after the authority has completed its annual inspection on such report.

- ii. Financial auditing is required under the conditions of term of office change or legal representative change of a not-for profit organization.

#### C. Analytical Comparison

China has applied less strict annual report requirements on for-profit organizations. The requirements for not-for profit requirements remains the same. Not-for profit organizations are subject to dual inspections on their annual work reports (ministry or bureau of civil affairs and the competent authority) – by contrast, for-profit organizations are only subject to random inspection by the AIC.

### **VI. Penalties for Non-Compliance**

In China, penalties incurred due to non-compliance with the regulatory scheme include administrative and criminal penalties. As the regulatory scheme mainly governs the relationships between government authorities and the various organizations, in China they are regarded not as civil but as administrative relationships. Below we discuss the main administrative penalties and criminal penalties in China.

Normally the administrative authority in charge will have a certain level of discretion over whether a specific activity of an organization is in violation of the law and what penalty would apply within the scope stipulated in the law. The redress mechanisms of administrative reconsideration and litigation mentioned in section II are available for the penalties executed by administrative authorities according to the laws.

#### A. For-Profit Organizations

##### a. Laws

##### i. Administrative

##### a) Registration



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The Company Registration Regulation sets out the penalties for non-compliance with registration requirements. It lists a series of company and personal non-compliance actions, for instance: registration of a company through a false certificate or other deceptive means; not taking any activities within 6 months after registration; failure to notify or announce creditors when undergoing liquidation; concealing assets, making false records in balance sheets or property checklists or distributing assets before paying off debts when undergoing liquidation; or engaging in any business operations irrelevant to the liquidation when undergoing liquidation.

The AIC is in charge of imposing the penalties and the penalties range from correction orders to fines to even revocation of registration in very serious cases.

b) Tax

The Law on the Administrative of Tax Collection<sup>39</sup> governs the payment of taxes and penalties. For company income taxes, the law mainly punishes tax evasion, delays in tax payment, refusal to pay tax and other similar activities. The tax bureau is in charge of imposing penalties, and penalties mainly include correction orders and fines.

c) Foreign exchange registration

According to the Foreign Exchange Registration and Management of Foreign Investment Companies, the Foreign Exchange Bureau could levy fines of RMB 1000-10000 for any violation of the regulation (including not undertaking foreign exchange registration), depending on the seriousness of such violation.

d) Annual report publication

According the Reform Plan for Registered Capital Registration System, companies that do not complete the publication of their annual reports in time will be put on the list of companies with abnormal operation, and will be removed from the list only after they submit the report; if no report is submitted for 3 consecutive years, the company will never be removed from the list and will be published in a “black list” of companies with serious violations of the law.

ii. Criminal

a) Liquidation

Article 162 of the Criminal Law of China<sup>40</sup> states that if, in the process of its liquidation, a company or enterprise conceals its assets, records false

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<sup>39</sup> Law on the Administrative of Tax Collection, adopted in 2001, available at [http://www.china.org.cn/business/laws\\_regulations/2007-06/22/content\\_1214782.htm](http://www.china.org.cn/business/laws_regulations/2007-06/22/content_1214782.htm) (in English)

<sup>40</sup> Criminal Law of China, amended in 1997, available at: [http://www.npc.gov.cn/englishnpc/Law/2007-12/13/content\\_1384075.htm](http://www.npc.gov.cn/englishnpc/Law/2007-12/13/content_1384075.htm) (in English)

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information in its balance sheet or inventory of assets, or distributes the company's or enterprise's assets prior to full payment of its debts, thus causing serious harm to the interests of the creditors or others, the persons who are directly in charge and the other persons who are directly responsible for the crime shall be sentenced to fixed-term imprisonment of up to five years or be fined between RMB 20,000 and RMB 200,000 or be subject to some combination of criminal detention and fine.

b) Tax

Chapter 6 of the Criminal Law lists several criminal liabilities for serious tax evasion through deceptive measures. The penalties include fines amounting to 1-5 times of the tax evaded for the company and imprisonment of the responsible person.

B. Not-For Profit Organizations

a. Laws

i. Administrative

As mentioned in Section II, the ministry or bureau of civil affairs could ban an unregistered NGO from undertaking activities and confiscate its illegal assets.

The Regulation on the Registration and Management of Social Organizations, Interim Regulations on the Registration and Administration of Private Non-enterprise Units and the Regulation for the Management of Foundations also sets out penalties for non-compliance, which include: registration through deceptive means, non-practice for one year after registration, refusal to permit annual inspections or other inspections conducted by the authorities; fabrication of false accounting books and records, publication of false information, undertaking profit-making activities and so on.

The ministry or bureau of civil affairs is taking charge of imposing the penalties and the penalties range from warnings to correction orders to temporary halting of activities to even revocation of the registration of the organization.

ii. Criminal

Article 162 of Criminal Law, as stated above, may also apply to the same acts undertaken by not-for profit organizations.

C. Analytical comparison

There are some differences in the administrative and criminal penalties for non-compliance by for-profit versus not-for profit organizations in China. The differences are mainly based on the different nature of the two types of organizations as regarded by the Chinese law, and the different rules on registration, taxation, audit and reporting of the two types of organizations.

D. Statistics on actual penalties for each group (if, available)

Not available

## OVERVIEW CHART

<b>Issue</b>	<b>For-Profit Organizations</b>	<b>Not-For Profit Organizations</b>	<b>Similarities/Differences</b>
Registration Procedures	No pre-approval requirements unless required by specific laws	Pre-approval required	More administrative supervisions over not-for profit organization
Tax Laws	Income tax	Exempt from income tax	Lesser tax burden for not for profit organizations
Financial Transaction Laws	1) Foreign investment companies are allowed to register in China  2) Foreign funding under the supervision of State Administration of Foreign Exchange	1) Only foreign chambers of commerce and branches of foreign foundations are allowed to register in China  2) Foreign funding under the supervision of State Administration of Foreign Exchange	More restrictions on foreign not-for profit organizations entering into China
Auditing/Reporting Requirements	No annual inspection required	Annual inspection required with pre-approval	More administrative supervision of not-for profit organization
Penalties	Revocation of registration if the company is seriously non-compliant	Revocation of registration if the organization is seriously non-compliant	Similar redress mechanisms