

Setting up Wholly Foreign-Owned Enterprises

What are Wholly Foreign-Owned Enterprises (WFOEs)?

WFOEs are usually organised as limited liability companies set up in China and wholly owned by one or more foreign parties. WFOEs have an independent corporate personality and are responsible for their own profits and losses (in contrast to a representative office or branch office which is not an independent economic entity). WFOEs are an alternative to a sino-foreign joint venture.

The following steps need to be followed to set up a WFOE in China:

Preparing a report and getting it approved

Preparing an application for approval to establish is the first step to set up a WFOE in China. The investing company must complete the application in the form required by the approval authority. The approval authority is usually the local Commission on Foreign Trade and Economic Relations (known by different names in certain locations) or an appropriate higher authority, depending on the amount of the proposed investment and the business of the proposed WFOE. A number of other documents will be required to support the application.

The application will state the following

- The purpose of the WFOE;
- The scope and scale of its anticipated operations;
- The technology and equipment to be used;
- Land use requirement;
- Water, electricity, coal, gas and other energy requirements; and
- Other matters which the authorities request to be included.

Other documents need to be approved

If a WFOE is to be owned by several investors, then a shareholder's agreement may be requested by the authorities. Articles of Association are always needed.

The time limit for approval of the Articles of Association varies for different types of WFOEs according to Chinese law. The stipulated maximum is 90 days after submission of all requested documents. Longer approval periods are possible if the authorities request special documents, as each such request triggers a new 90 day period.

Registration with the State Administration for Industry and Commerce (SAIC) or local AICs

It is wise to request the local AIC to review the name of the proposed WFOE and issue a decision on whether or not the name can be accepted for registration. The time limit for such a decision is 10 days. The local AIC issues a Notice of Enterprise Name Reservation, valid for six (6) months. During this period, the reserved name should not be used by any other party. The WFOE itself may carry on business operations only after it is formally established.

Within 30 days after approval of the establishment of a WFOE, the investor should apply for the registration of the WFOE with the local AIC. Upon registration, a business license is issued and the company commences its formal existence.

What needs to be done after you have a Business License for a WFOE?

- Application for an enterprise code;
- Foreign exchange registration and bank account opening;
- Tax registration with Chinese tax authorities;
- Customs registration;
- Application with the local public security bureau for approval to make company chops (seals);
- Registration with the Labour Bureau

Tax Incentives

The basic income tax rate for WFOEs (as for other foreign invested enterprises) is 30% for national tax and 3% for local tax, altogether being 33% applicable to enterprises.

For WFOEs engaging in production (manufacturing) with a term of more than 10 years, there is a 2 year income tax exemption and a further 3 year 50% reduction on the income tax from the company's first profit-making year. WFOEs not engaged in production, for example real estate developers, travel agents, retailers or wholesalers, or other investments in the service sector, are not eligible for the tax holiday.

There are other tax incentives for specific industries, further incentives for specific geographic areas, and certain other incentives. Some of these may change following WTO accession.

For further information and guidance please contact in the first instance Molly Riley by e-mail at molly.riley@cmck.com or by telephone on +86 21 5292 5196.