



Wednesday, October 27
9:00am-10:30am

904 - The Practical Approach to Developing Successful Business in China

Roger Fulton

Executive Vice President – Human Resources, General Counsel & Corporate Secretary
Linamar Corporation

Audrey Chen

Partner
Jun He Law Offices, Lex Mundi member firm for China

Andrew Pollock

Associate
Blake, Cassels & Graydon LLP, Lex Mundi member firm in Ontario, Alberta, Quebec

Charles Wilkinson

Senior Corporate Counsel
Ashland, Inc

Faculty Biographies

Audrey Chen

Audrey Chen is a partner of Jun He Law Offices. Ms. Chen practices in Jun He's Beijing office. Ms. Chen specializes in foreign investment, banking and financing, M&A and general corporate work.

Ms. Chen has previously worked in the New York office of Jones Day Reavis & Pogue where she advised clients on investment projects in China as well as on international business transactions.

Ms. Chen has extensive experience in energy, mining, automobile, retail, real estate, technology and IP projects. She has advised on various aspects of, and negotiated complicated legal documents in connection with, such projects. She has also assisted many domestic and international clients from different industries in IPOs, venture capital financing and acquisitions. Ms. Chen's clients include many major domestic corporations and Fortune 500 companies.

Ms. Chen Received a BA from Beijing Shifan University, the LLM from Renmin University of China, and the LLM University of California at Berkeley, School of Law (Boalt Hall).

Roger Fulton

Roger B. Fulton is the executive vice president-human resources, general counsel & corporate secretary of Linamar Corporation in Guelph, Ontario, Canada. His responsibilities include all legal, secretarial and certain human resource functions for Linamar's global operations.

Prior to joining Linamar, Mr. Fulton served as in-house counsel at Stelco Inc., Canada's largest steel producer, finishing his career there as general manager of human resources and legal affairs.

He currently sits on the board of directors of the St. Joseph's Health System and several of its committees and has been a past presenter at the Canadian Corporate Counsel Association National Conference.

Mr. Fulton received an honors BA from McMaster University and is a graduate of the University of Western Ontario School of Law.

Andrew Pollock

Andrew Pollock practices in the business group at Blake, Cassels & Graydon LLP and advises on business law matters for Canadian and international clients in the areas of mergers and acquisitions, financings, securities offerings and joint ventures.

Mr. Pollock returned to the Toronto office after a term in the Blakes Beijing office where he assisted Canadian, Australian, US and European companies doing business in China and assisted Chinese companies doing business in Canada. In Toronto, Mr. Pollock continues to maintain his China practice, working with foreign companies with existing or anticipated activities in China and Chinese clients with international investment interests.

Charles Wilkinson

Charles F. Wilkinson is a senior corporate counsel for Ashland Inc, a Fortune 500 company providing products and services through Ashland Distribution, Ashland Performance Materials, Ashland Consumer Markets ("Valvoline"), Ashland Water Technologies, and Ashland Aqualon Functional Ingredients. He has global responsibility for Ashland's international trade activities and transactions (including EAR, ITAR, FCPA, and OFAC compliance), government relations (political action committees and lobbying), commercial and government contracts, acquisitions and divestitures, and corporate real estate.

Prior to joining Ashland, Mr. Wilkinson held several law department positions with Lockheed Martin in Baltimore, Maryland and Marietta, Georgia, and with Hercules Incorporated, Wilmington, Delaware. In those positions his responsibilities included commercial and government contracts, international transactions, economic development, real estate, and litigation. Before entering corporate practice, he was a US Air Force Judge Advocate with assignments in the US and overseas.

Mr. Wilkinson is a member of the State Bar of Illinois and the State Bar of Georgia. He belongs to ACC's Corporate and Securities Law Committee, Information, Technology Law & e-Commerce Committee, International Legal Affairs Committee, Law Department Management Committee, and Real Estate Law Committee.

Mr. Wilkinson received a BS from Loyola University of Chicago and a JD from Northern Illinois University.

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Overview

- I. Tips, Trends and Common Mistakes – Andrew Pollock
- II. Foreign Investment: The Nuts and Bolts – Audrey Chen
- III. A View from the Trenches Part I – Charles Wilkinson
- IV. A View from the Trenches Part II – Roger Fulton
- V. Questions and Answers

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I. Tips, Trends and Common Mistakes

- A. Not All Investment Is Welcome Investment
- B. Decentralization of Approval Authority Functions
- C. Joint Venture Issues
- D. Adequate Funding of Chinese Subsidiaries
- E. Exit Strategies
- F. Employment Issues

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A. Not All Investment is Welcome Investment

- Move away from manufacturing focus to knowledge-based and value added sectors
- Shift in tax incentives
- Focus on development of local brands in international markets

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B. Decentralization of Approval Authority Functions

- De-centralization has increased, with approval for larger investments being delegated to local authorities
- Differences in approach to regulatory function and application of the law between various local authorities

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C. Joint Venture Issues

- Chinese legal definition of joint venture
- Negotiating the contract; alignment of interests
- Flexibility of a CJV
- Requirement in certain industry sectors
- Corporate governance issues
- Role of legal representative
- Company seal

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D. Adequate Funding of Chinese Subsidiaries

- Ensure initial funding of entity is sufficient and that planning for funding by way of equity/debt is planned well in advance
- Regulatory process for increasing registered capital
- Shareholder loans

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E. Exit Strategies

- Offshore holding company
- On-shore sale of assets or equity
- Milestones/events of termination to be included in constating documents and/or joint venture contract
- Liquidation
- Put/call rights
- Government approvals

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F. Employment Issues

- Thresholds for termination
- Re-instatement of terminated employees
- Confidentiality/non-disclosure
- Requirement for written employment contracts
- Enforcement of company policies
- Social benefit contributions
- JV employment issues – “shared” employees

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II. Foreign Investment: The Nuts and Bolts

- A. Restrictions on Foreign Investment
- B. Business Structures – Entities commonly used by Foreign Investors
- C. Business Structures– The process of setting up a CJV
- D. M&A Issues
- E. Taxation of Representative Offices
- F. Foreign Invested Partnerships
- G. Developments in Merger Control

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A. Restrictions on Foreign Investment

- “Foreign Investment Catalogue”-categories of foreign investment
 - Encouraged
 - Permitted
 - Restricted
 - Prohibited

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B. Business Structures – Entities commonly used by Foreign Investors

- Joint ventures – equity joint venture (EJV), co-operative joint venture (CJV)
- Wholly foreign owned enterprise (WFOE)
- Holding company
- Representative office of foreign company

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C. Business Structures – The process of setting up a CJV

- Letter of intent → Name pre-registration → preparation of joint venture contract and articles of association → Project application approval from National Development and Reform Commission → JV establishment approval from Ministry of Commerce → Related permits → Business license issued by State Administration of Industry and Commerce → Post-establishment formalities → Related permits and approvals

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D. M&A Issues

- State-owned Asset Administration and evaluation
- Assumption of debts
- Determination of purchase price, various methods of payment and timing of payment
- PRC residents' equity ownership/return investment
 - Establishment of SPV
 - Private Placement
 - M&A of Domestic Companies by SPV
 - IPO of SPV in US

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E. Taxation of Representative Offices

- Tax filing on actual basis
- Two "deemed profit" methods
- Increase of deemed profit rate
- Value-added tax and business tax payable
- Conditions for enjoying treaty benefits

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F. Foreign Invested Partnerships

- Existing models of foreign investment in RMB
 - FIVCE Model
 - Indirect Model
 - Parallel Funds Model
- New model and its main features
- Issues to be clarified or pending

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G. Developments in Merger Control

- Legislative Development
 - M&A Rules
 - Anti-Monopoly Law
 - Regulations of the State Council on the “Thresholds of Filing of Concentration of Business Operators”
 - Guidelines on submission of filing documents and the application form

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G. Developments in Merger Control (cont'd)

- Legislative Development
 - Guidelines for anti-monopoly review
- MOFCOM’s recent merger control practice

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III. A View from The Trenches – Part I

- A. Educate and protect your business team
- B. Manage the relationship with local partners and governmental authorities
- C. Provide your company with guidelines
- D. Stay up-to-date with changes happening in China

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A. Educate and protect your business team

- US laws applicable to your US company's activities
 - Foreign Corrupt Practices Act ("FCPA")
 - Trade Regulations (ITAR, EAR, and OFAC)
- SEC Accounting Provisions
 - Another way the Government enforces the FCPA
 - Accurate accounting for your investment dollars

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A. Educate and protect your business team

- Chinese enterprises may have personnel who are "government officials"
 - In these instances, otherwise common courtesies may violate the FCPA
 - Failure to abide by the FCPA can subject the company and individuals to civil and criminal penalties

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A. Educate and protect your business team

- Establishing the new entity is just the beginning
 - Many, if not all aspects of operating the business, could bring the FCPA into play
 - Chinese employees should be trained just like US employees in both US and China legal compliance

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A. Educate and protect your business team

- Resist “that’s how it’s done in China” justification for questionable acts
- Assure your US employees understand the US and China rules they have to play by

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B. Manage the relationship with local partners and governmental authorities

- Take time to understand applicable laws and policy before beginning the venture
- Let the other parties know that you know the rules
- Be fully prepared when working with and through the bureaucracy

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C. Provide your company with guidelines

- Business negotiations will be scrutinized by your company’s subject matter experts
 - Accounting, Treasury, EHS, Law will all have a role in looking at the proposed deal
- Business development will get special “compliance care”
 - The business development, marketing, and sales organizations need to keep meticulous notes

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C. Provide your company with guidelines

- Company should monitor activities of third parties (consultants, agents, etc.) very closely
- No cutting corners to achieve fast results.
 - Government approvals take time and the business plan has to provide for this upfront

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D. Stay up-to-date with changes happening in China

- China is not a signatory to the OECD Anti-Bribery Convention
- China has anti-bribery laws; may be difficult to know what side of them you are on

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D. Stay up-to-date with changes happening in China (cont'd)

- Central officials have an interest in ferreting our corruption
 - 12 July 2010: new rules require officials in government and state companies to report personal details from assets to the whereabouts of spouses and children, in an attempt to quash endemic corruption Beijing sees as a threat to its rule

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D. Stay up-to-date with changes happening in China (cont'd)

- Officials recognize no corruption leads to a more reliable marketplace
- Penalties can be severe in serious cases
 - 23 July 2010. Chen Shaoji, former top political advisor of south China's Guangdong Province, was sentenced to death with a two-year reprieve for accepting bribes, a court in southwestern Chongqing Municipality said Friday

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IV. A View from The Trenches – Part II

- A. Structure
- B. Amount of Investment
- C. Local Government/Process
- D. Pay close attention to the rapidly changing regulatory regime
- E. People/Turnover

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A. Structure

- WFOG
 - most closely resembles what we would consider a separate legal entity and allows you to function as such
- Think Down the Road
 - If you ever wish to sell the business; JV the business or some other transaction, there are significant tax issues in China to consider

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A. Structure (cont'd)

➤ Think Down the Road

- You should seriously consider an intermediary holding company outside of China to hold the interest in your Chinese entity (we use Barbados because of favorable tax treaties)
- If you ever enter into any of the above transactions, you can do it at the holding company level such that none of the tax issues are triggered in China

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B. Amount of Investment

➤ There is a calculation that is done that is dependent upon the amount of the investment you will make in China – this is called the “Registered Capital” and you will be required to inject this into the company within a specified time frame

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B. Amount of Investment (cont'd)

➤ If this figure is large enough, approval for your Business License to operate your new company needs to go to the Provincial capital of the province you're locating in or even Beijing to the National Government

- This results in a much longer time line to get established and more government officials to deal with
- You will need to adjust timelines and activities appropriately

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B. Amount of Investment (cont'd)

- Remember, you cannot undertake any activities in China until your company is legally established

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C. Local Government/Process

- Use the local government where you wish to locate (and in the process of deciding where to locate) – we are in the Wuxi New District Industrial Park about 50 km west of Shanghai
 - They were extremely interested in attracting our business (the areas are competing for business and jobs, so “run an auction”) and then helping us through the process of getting established and obtaining our business license

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C. Local Government/Process (cont'd)

- These are important contacts to establish and maintain – “In China, we do business with our face”
- They helped “grease the wheels” with local officials and banks, etc., and helped reduce the time to obtain the business license (and continue to be of assistance going forward)

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C. Local Government/Process (cont'd)

- Having said all that, you need someone from your company on the ground bird-dogging this entire process, or it will slow down and get mired in bureaucracy (also ensures proper procedures are being followed)

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D. Pay close attention to the rapidly changing regulatory regime

- If you read Chinese legislation on any area of the law, it looks like a model law – anyone would be happy to work and live under it
 - However, enforcement is uneven and often dependant on local and provincial governments and their “interpretation” of the particular legislation
 - Therefore, it’s very important to tap into local knowledge on how various laws are viewed and enforced

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D. Pay close attention to the rapidly changing regulatory regime (cont'd)

- Just recently, the Provincial Government where we are located (and I understand across most of China) is insisting on employers signing collective agreements with the unions at their workplace
 - Standard form collective agreements (“Mom and apple pie”)

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D. Pay close attention to the rapidly changing regulatory regime (cont'd)

- Unions are not what we are used to here – they are more consultative on issues and act more like a social club (despite some of the high profile activities we've seen recently in the newspapers)
- Everyone is in the union – for example, our Plant General Supervisor is the head of the union and our Finance Manager is also on the executive
- If managed properly, it's not an issue

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E. People/Turnover

- Turnover in China is a real issue – numbers vary, but it runs roughly at 30%
- There are multiple factors at work
 - High demand for workers of all skills/abilities
 - The young work force is especially mobile and restless – they will move for another 10¢/hr or a different opportunity
 - The young work force is also aggressive – they will do a job for 6 months and if not promoted, move to the next level in another company because they have experience and continue this jumping around to gain title and pay

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E. People/Turnover (cont'd)

- Be Creative
 - We have more layers in China than elsewhere in the organization in order to provide levels to be promoted into
 - Provide lots of training and challenges to keep employees engaged
 - We offer full lunch/dinner cafeteria paid for by the company (this is basically a must in China) as well as bus transportation for workers (again, very important in order to be attractive as an employer)
 - As a result, our turnover is 9%

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Overview

- I. Central Government Policies and Directions
- II. Key Issues in FDI and M&A
- III. Updated Legislations for Foreign Investment and M&A
- IV. The Practical Approach for Foreign Investment and M&A in China

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I. Central Government Policies and Directions

- Being Selective to Foreign Investment
- Key Industries Control (NDRC role)
- Decentralization of the Approval Authorities

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II. Key Issues in Foreign Direct Investment and M&A

- Restrictions of Foreign Investment
- Business Structures-entities commonly used by foreign investors
- Business Structures-the process of setting up a CJV in China
- Other Issues to be Considered

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➤ **Restrictions of Foreign Investment**

- “Foreign Investment Catalogue”-categories of foreign investment
 - ◆ Encouraged
 - ◆ Permitted
 - ◆ Restricted
 - ◆ Prohibited

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➤ **Business Structures – entities commonly used by foreign investors**

- Joint ventures – equity joint venture (EJV), co-operative joint venture (CJV)
- Wholly foreign owned enterprise (WFOE)
- Holding company
- Representative office of foreign company

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➤ **Business Structures-the process of setting up a CJV in China**

- Letter of intent → Name pre-registration → JVC/AOA preparation → Project application approval from NDRC → JV establishment approval from MOC → Related Permits before-set up → Business license issued by SAIC → Various post-set up formalities → Related Permits and Approvals

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➤ **Other Issues to be Considered**

- State-owned Asset Administration and evaluation
- Assumption of debts
- Employees Transfer
- Determination of purchase price, various methods of payment and timing of payment
- PRC residents' equity ownership/return investment
 - Establishment of SPV
 - Private Equity Placement
 - M&A of Domestic Companies by SPV
 - IPO of SPV in US

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III. Updated Legislations for Foreign Investment and M&A

- Being selective to industries and areas/key industry control
 - Foreign Investment in Central-Western China
 - Favorable Policies in Certain Industries Commercial Bank M&A Loans
- Taxation of Representative Offices of International Companies
- SAIC's Rules on Foreign Invested Partnerships
- Developments on Merger Control
- New Policy issued by State Council on April 6, 2010 to further encourage foreign investment

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➤ **Taxation of Representative Offices of International Companies**

- Tax Filing on Actual Basis
- Two "Deemed Profit" Methods
- Increase of Deemed Profit Rate
- Value-added Tax and Business Tax Payable
- Conditions for Enjoying Treaty Benefits

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➤ **SAIC's Rules on Foreign Invested Partnerships**

- Existing Models of Foreign Investment in RMB Funds
 - FIVCE Model
 - Indirect Model
 - Parallel Funds Model
- New Model Recognized by Registration Rules and its Main Features
- Issues to be Clarified or Pending on Development

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➤ **Developments on Merger Control Law and MOFCOM Practice**

- Legislation Development
 - M&A Rules
 - Anti-Monopoly Law
 - Regulations of the State Council on the Thresholds of Filing of Concentration of Business Operators
 - Guidelines on Submission of Filing Documents and the Application Form
 - Guidelines for Anti-Monopoly Review/Anti-Monopoly Review Flow Chart
- MOFCOM's Recent Merger Control Practice

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IV. A Practical Approach for Foreign Investment and M&A in China

- Fully understand the background, reasoning and expectation of such change
- Possible investment structures change/alternatives
- Conduct due diligence and understand associated legal risks
- Pay close attention to the rapidly change regulatory regime
- Work out feasible strategies with the advisors in compliance with the legal regime

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Extras from ACC

We are providing you with an index of all our InfoPAKs, Leading Practices Profiles, QuickCounsels and Top Tens, by substantive areas. We have also indexed for you those resources that are applicable to Canada and Europe.

Click on the link to index above or visit <http://www.acc.com/annualmeetingextras>.

The resources listed are just the tip of the iceberg! We have many more, including ACC Docket articles, sample forms and policies, and webcasts at <http://www.acc.com/LegalResources>.