



CHINA BRIEFING

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Downsizing or Liquidating a China Business

An Executive Business Summary By Dezan Shira & Associates



Downsizing Staff and the Chinese Labor Law
The Company Law and the Liquidation Process
Financial and Tax Considerations
Accurately Assessing Liabilities
Formation of the Liquidation Committee
Applying for Bankruptcy



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Welcome to this issue of China Briefing magazine

Welcome to this special executive report concerning downsizing or liquidating a business in China. While the current global economic problems continue to wreak havoc, and particularly amongst businesses in China who are solely export focused, it is prudent for executives facing difficult decisions in China to be aware of their responsibilities when faced with tough decisions. The Chinese government has already stated that it intends to seek prosecution for foreign executives and legally responsible persons for not properly meeting statutory obligations when closing a business in China. Just walking away is an option that now carries the risk of being permanently barred from entry to China, possible apprehension at immigration in the future, heavy fines, and jail sentences. The government has also raised the possibility of seeking prosecutions overseas in the executives own domicile. Although difficult, executives who wish to live to fight another day in China, when faced with the possible closure of a business in the country must still do so in accordance with the law.

In this special issue then, updated from our previous commentary on the subject (China Briefing Archives, March 2007), we outline the responsibilities foreign executives have when it comes to winding up a business in China, and the procedures that need to be followed. It is a difficult subject, however in accordance with most business matters, still requires attention to detail and regulatory compliance.

During such times it can be useful to turn to the classics for inspiration. Sun Tzu's "The Art of War" provides a few clues:

What is essential in war is victory, not prolonged operations. (*Closing a business now and cutting losses still means you can live to fight another day and re-invest later when times are better*)

Treat your men as you would your own beloved sons, and they will follow you into the deepest valley. (*Treat your staff well and have faith in their ability to follow you even when it's tough*)

Strategy without tactics is the slowest route to victory. Tactics without strategy is the noise before defeat. (*If you have to withdraw, do it strategically and not just run away*)

Speed is the essence of war. (*If its obvious your business is unsustainable at the present – get out as soon as you can*).

We trust our clients and readers will not have to close their operations or downsize in China. However, if it proves a strategically wise move to do so, we hope you find the following pages useful. Professional assistance during these difficult times can also always be provided by our practice Dezan Shira & Associates. Our partners are also on hand to provide strategic and restructuring advice if required.

Yours faithfully;

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Salary Reduction Under China's Labor Law

[By Chris Devonshire-Ellis, Senior Partner, Dezan Shira & Associates]



With many businesses facing economic problems, the legal focus of business in China is shifting to an understanding of the implications of the new labor law, and specifically, its provisions for the reduction of staff salaries.

The Labor Contract Law is not specific on the reductions of salaries due to economic conditions. However, Article 41 of the law recognizes the reality of “serious difficulties in production and/or business operations” in the context of terminating staff. When it comes to being faced with the choice of either terminating employment contracts, or reducing salaries, local governments in China are keen to see the staff retained. The Chinese government’s overriding concern is maintaining social stability ahead of economic concerns. Salary reduction is an alternative that both government and

employer can agree upon rather than face stiff compensation penalties for terminating staff contracts.

The procedure, however, is not just a matter of agreement between the employer and employee and an amendment to the contract. While not specifically mentioned in China’s labor law, businesses are encouraged to “consider the opinion” of the labor union and the relevant local labor administration bureau. In practice this means that a report, outlining the economic situation of the business, together with the required contingency plan over salary reductions, needs to be filed with, and agreed by both bodies. In fact, when faced with an economically bleak picture, the labor union may be able to help the company manage the transition. The approval of the Labor Union and the local labor authority will allow amendments to employment

contracts to be made, then agreed upon.

China does see certain criteria as being important when it comes to the health of businesses. Key among these are maintaining profitability, employee retention and business sustainability. Businesses in China with a track record of success yet facing difficulties in maintaining salary levels would be well advised to enter into discussions with the labor union or the local labor authority and work with them to reach an effective compromise in staff retention.

The author is the Senior Partner of Dezan Shira & Associates. Companies requiring legal opinion on salary reductions in China may contact Marie Bi, Legal Counsel, Dezan Shira & Associates at legal@dezshira.com.

Liquidating a China Business

[By Dezan Shira & Associates]



With the global economic crisis hitting some businesses in China very hard as export sales dry up, now is a timely occasion to remind executives of affected businesses of their responsibilities when having to liquidate a business. China-based subsidiaries may also be impacted by external circumstances beyond their control that may adversely be affecting their parent companies.

In these circumstances, the interests of a number of “stakeholders” need to be properly protected and balanced – shareholders, of course; employees; customers, creditors and debtors; and the local authorities as regulators and tax collectors. The closure of a company may often provoke strong emotions and feelings of uncertainty for many of those involved, too.

There are of course regulations under Chinese law for how these processes should properly be carried out, to ensure that the company’s final bills are settled, tax is paid, staff are properly handled, and all the company’s remaining liabilities and statutory responsibilities are correctly discharged. In this special report we explain the procedures you would need to go through to close a foreign invested enterprise in China, and highlight the many related issues that you will need to address. We hope that you never have to go through the process, at least for negative reasons, but if you do, it must be done professionally and correctly.

COMPANY LAW AND THE LIQUIDATION PROCESS

The procedures for closing a WFOE – its dissolution and liquidation – are no easier or shorter than the process of setting up such a company, and normally take between six to nine months to complete.

According to PRC law, a WFOE must be dissolved if any of the following circumstances apply:

- Its term of operation expires
- the board of shareholders has adopted a resolution for dissolution to dissolve the company
- It is merged or divided
- Its business license is revoked by law, or the company is ordered to terminate or cancelled
- Where there are serious difficulties on its operation and its continuance will definitely cause significant losses to shareholders’ interests, however, such scenario cannot be solved through other channels, then, shareholders representing 10 percent of all the votes may request the people’s court to dissolve it
- Other reasons for dissolution stipulated in the original Articles of Association have occurred

Upon the declaration of dissolution, the company is required to start the liquidation procedures.

Creation of liquidation team

A liquidation team is composed of its shareholders to handle the liquidation within 15 days from the dissolution date of the company. The liquidation team shall liquidate and value the company’s assets in accordance with PRC law and the Articles of Association.

During the course of liquidation, the company shall not conduct any business activities irrelevant to the liquidation. The liquidation team shall have the right to handle the company’s ongoing businesses which are related to liquidation, i.e. to terminate employment contracts, to sell, export, transfer, assign or otherwise dispose of any and all assets belonging to the company whether they be inside or outside the PRC, as well as to conclude all business matters of the company, in accordance with PRC law and the principles set out in the Articles of Association.

The liquidation team shall exercise the following functions and powers during liquidation:

- Liquidate the assets of the company, prepare a balance sheet and list of assets, and formulate the liquidation plan
- Make an announcement for the benefit of unknown creditors and notify known creditors in writing
- Complete any unfinished business of the company
- Pay all outstanding taxes
- Settle all of the company’s claims and debts
- Dispose of the remaining assets after the company’s debts have been settled
- Represent the company in any civil litigation
- Produce the Liquidation Report and submit to the board of shareholders and the authorities for approval

Liquidation audits

Liquidation audits are generally required twice in the process:

- When the termination application is submitted to the authorities and the application is approved by those authorities

- When all termination procedures have been completed

As well as normal audit procedures, liquidation audits focus on these additional issues:

- The financial performance of the company for the six months before the date of declaring liquidation
- The completeness and truth of information on assets, such as:
 - whether the calculation of accounts receivable is correct
 - whether the bad debts write-off was properly authorized
 - whether the bank account records are complete
 - whether physical assets properly belong to the company
 - whether disposal/loss of fixed assets is approved by related authorities
 - whether investing assets are recorded and distributed correctly
- The liabilities of the company, such as:
 - whether salaries payable are calculated correctly
 - whether tax payable has been cleared properly
 - whether other liabilities have been cleared properly
- The liquidation expenses, including a check on whether these expenses were spent in compliance with the law

Liquidation deadlines

The liquidation team shall observe the following deadlines:

- Within seven days of beginning the liquidation, the relevant authorities must be notified
- Within 15 days of beginning the liquidation, the liquidation team must be established
- Within 10 days of establishing the liquidation team, it must notify known creditors and ask them to declare their claims
- Within 60 days of establishing the liquidation team, it shall make at least one public announcement in a national or provincial newspaper.
- Within 30 days of submitting the liquidation report, liquidation team should perform the deregistration procedures with original registration authority.

Distribution of liquidated proceeds

In accordance with PRC law, revenues from the sale or disposal of the liquidated assets shall be paid out in the following order:

- liquidation expenses, including expenses for management, sales and distribution; expenses for public announcements, lawsuit and arbitration; remuneration to members of and advisors to the liquidation team; and other expenses occurred during the liquidation
- wages and mandatory welfare payments for employees
- outstanding taxes
- outstanding secured debts
- other outstanding debts

After payments have been made in accordance with provisions above and upon completion of the liquidation procedures, the remaining revenue shall be converted into US\$, or any other foreign currency acceptable to the investor through a designated foreign exchange bank or any other method permitted by PRC law, and can be freely remitted or transported abroad.

Cancellation of registration

Once the liquidation procedures are completed, the liquidation team needs to submit a Liquidation Report, approved by the board of shareholders, to the original approval authority. The team should return its business license and cancel its registration with the relevant government authorities including the Ministry of Commerce, State Administration of Industry and Commerce (SAIC), the customs administration, the tax authorities and State Administration of Foreign Exchange (SAFE). All the company's bank accounts shall be closed.

The investor shall have the right to preserve the originals of all accounting records and business documents of the company.

Within 30 days from submission of the Liquidation Report, the company should perform deregistration with the authorities, and after deregistration, the company can repatriate the remaining funds back to the investor. These deregistration procedures

and other processes include:

- Deregistration from Ministry of Commerce, and cancellation of the Approval Certificate
- Tax audit and deregistration from local tax bureau
- Tax audit and deregistration from state tax bureau
- Customs deregistration
- Deregistration with SAFE
- Deregistration from SAIC
- Deregistration of Business Code Certificate
- Public announcement in a newspaper to terminate the business remit funds back to investors close bank accounts

In addition, some companies in particular sectors may have other specialized registrations and those should be closed off as well. Although not strictly a financial issue, foreign investors should also ensure that, for example, unused raw materials and unsold products are disposed of properly in an environmentally sensitive way, and that buildings and other major assets are dealt with properly. Do not walk away from your responsibilities.

FINANCIAL AND TAX CONSIDERATIONS WHEN LIQUIDATING

Foreign invested enterprises in China that undergo liquidation will need to deal with two main tax issues. These are:

- clearance of outstanding tax liabilities – the liquidation committee must meet any potential and actual tax liabilities. After confirmation, the liquidation committee will pay the outstanding tax liabilities to relevant departments.
- new tax liabilities during liquidation – the liquidation itself may raise new tax liabilities - for example, fixed asset disposal may raise some turnover taxes, and employee compensation will be subject to individual income tax.

We explore these in more detail in this section.

Clearance of outstanding corporate tax liabilities

Clearance of outstanding tax liabilities

As regular readers will know, many foreign enterprises currently receive various incentives, which may include

“tax holidays” such as a two year exemption and three year 50 percent reduction of Corporate Income Tax. Such “tax holidays” normally only apply to companies on the assumption that they are expected to operate for at least ten years.

Note, this "tax holiday" incentive has been done away with in the new Corporate Income Tax Law, implemented since Jan. 1, 2008. There is a grandfathering rule within transition period however, for those enterprises that have not yet embarked on their tax holiday. Their tax holiday will be deemed to have commenced from the effective date of the new law

Corporate income tax refund for reinvestment of profits

Article 10 of the old Enterprise Income Tax Law for on enterprises with foreign investment and foreign enterprises stated that a foreign investor that directly reinvests its share of the profits distributable from a foreign investment enterprise, by either increasing the registered capital of that foreign investment enterprise before the profits were distributed or establishing another foreign investment if the profits were distributed, could obtain a refund of 40 percent of the tax paid on the reinvested amount, subject to approval of the tax authorities. In addition, if profits were to be reinvested for at least five years, and if the investor withdrew the reinvested profits within five years, the tax refunded would need to be returned to the tax authorities.

Therefore, if a foreign investor reinvested its share of the profits distributable from a foreign investment to non-taxable project, and its operation period was less than five years, then 40 percent refundable tax amount or whole tax amount would need to be remitted back. The formula was:

Tax refund = A/[1 - (B + C)] x B x D
where

A = reinvested amount

B = original foreign enterprise income tax rate applicable to the enterprise

C = local income tax rate applicable to the enterprise

D = refund rate

Although this regulation has been abolished in new Corporate Income Tax Law, if the operation period for the foreign



enterprise enjoying this preferential treatment is less than five years, then the tax refund shall be remitted back to the local government when liquidating.

Treatment for accrued expenses in liquidation

According to new PRC GAAP, manufacturing enterprises should accrue 2 percent into the trade union fund. It should be noted that the 2 percent accrued into the trade union belongs to the trade union on liquidation, not to the liquidation committee.

For enterprises with normal operations, several transaction taxes e.g. stamp duty, deed tax should be declared within a certain period after the relevant activity occurs. But majority of taxes are declared periodically, for example monthly.

Thus, after liquidation begins, there is a possibility that the enterprise's remaining tax amount is not declared and paid. And business transactions before liquidation could still be completed within the liquidation period and would bring new tax liabilities. Both these issues will need to be taken into account by the liquidation committee.

New tax liabilities during liquidation

During the liquidation period, asset disposal and termination of employees, amongst other issues, may possibly create new tax liabilities.

Asset disposal

There is no difference between assets transferring during liquidation and assets disposal in daily operations. But as the purpose of assets transfer during liquidation is for assets distribution, the tax liability would be considered differently. Part of the tax liability would be considered as a liquidation expenses and paid preferentially in advance of other expense.

Import VAT and custom duty

Customs prescribe different monitoring years for imported products of different kinds. During the monitoring period, goods should be depreciated at true value if Customs authorizes their sale, transfer or move for other uses, for example during liquidation. In this situation, both import VAT and custom duties should be levied.

The relevant formula is:

Price after tax = CIF price x [1 - actual number of months used/(management years x 12)]

Secondly, if a foreign invested enterprise wishes to transfer goods originally imported with an import VAT exemption, if goods are left with a Chinese partner or transferred or sold to a domestic enterprise, Customs would calculate the tax amount based on the depreciation year. If they are transferred to other foreign enterprises enjoying preferential tax treatment, then the goods could still enjoy such preferential treatment.

Turnover taxes

Turnover taxes involved in assets transfer during liquidation will usually be value added tax, business tax, consumption tax and land appreciation tax. There is no specific regulation related to turnover taxes for assets transfer in liquidation.

Assets taxes

Relevant taxes could include urban real estate tax and vehicle and vessel usage tax for foreign invested companies. During liquidation, before transfer of such vehicles and vessels, foreign enterprises would still have tax liabilities.

Individual income tax

Employees from liquidated enterprises would usually receive a certain amount of compensation, and foreign enterprises must withhold individual income tax for such payments in the normal way. If they do not do so, then tax bureau would pursue these tax amounts, which may increase the cost of liquidation.

Corporate income tax

Based on the new Corporate Income Tax Law, if an enterprise terminates its business activities after the beginning of a tax year with the result that the actual

period of operations during such tax year is less than 12 months, its actual period of operations shall be treated as a tax year. When an enterprise is liquidated according to the law, the liquidation period shall be treated as a tax year.

If an enterprise terminates business operations during a tax year, it shall carry out full and final settlement of corporate income tax for the current period with the competent tax authorities within 60 days from the date on which it actually terminates business. Before an enterprise deregisters, it shall file a return with and pay tax to the authorities in accordance with law in respect of its income from liquidation.

The relevant formulas are:

Liquidation gains/losses = (gains/losses from inventory disposal) + (gains/losses from non-inventory disposal) + (gains/losses from asset disposal)

Net assets/retained assets = (liquidation gains/losses) – (salary/mandatory welfare benefits payable) – (liquidation expenses) – tax due – other liabilities – losses on bad debts + income from repaid debts

Liquidation income = net assets/retained assets – (undistributed profits + various funds + paid-in capital)

In most cases, the liquidation period will probably be the final tax payment period. According to current law, profits from the current year could only be set off against the previous year's loss. Therefore, classification of income and expenses for the liquidation period and the previous year is quite important. Choosing the correct liquidation date could mean significant tax efficiencies.

Special treatments for liquidation on bankruptcy

Normally liquidation is performed when assets are greater than liabilities, and there should be no problem in paying any taxes that become due.

But if foreign enterprises make losses due to poor operation and management and cannot pay their tax liabilities, or assets are less than liabilities during liquidation, then the enterprises would be considered as insolvent or bankrupt. Because assets from such insolvent enterprises cannot meet all their liabilities,



it is very important to determine the order in which taxes are tax cleared.

Currently when a foreign enterprise performs insolvency liquidation, it is not the Bankruptcy Law but other civil laws that apply. But in these civil laws there is no specific definition of insolvency expenses, and foreign enterprises may therefore have some flexibility when dealing with this issue.

According to the regulations, the tax should be paid before assets disposal, otherwise it would affect assets transfer. These tax liabilities would be paid preferentially. But for other tax liabilities, if they are considered as liquidation expenses, it may affect the repayment rights for other debts, while if they are combined with other due taxes, then it would affect repayment rights for other debts before tax due. Overall, the tax authorities might lose some income.

All this complexity means a foreign enterprise must, in such circumstances, think very carefully about how it proceeds, and take proper professional advice.

Tax deregistration

After the foreign enterprise completes all its liquidation procedures and pays its taxes, the relevant tax bureau would proceed to cancel its tax registration. After that, the foreign enterprise can complete the other deregistration procedures mentioned previously.

The following materials should be submitted to the tax bureau:

1. Application letter, with relevant authorization certificate and other documents
2. Liquidation audit report
3. Liquidation report
4. Tax clearance certificate for all taxes
5. Approval letter for liquidation from authority that approved original establishment

6. Application and Examination Form for Tax Registration Termination, and other documents required by tax bureau.

ACCURATELY ASSESSING LIABILITIES - EMPLOYEES

As we have already explained, when liquidating a company, salaries, mandatory welfare benefits and severance payable to employees are paid second only to liquidation expenses themselves. For companies with a large workforce, this can be a large cost and needs to be quantified accurately.

Only once the “workforce” has been clearly defined can the liability be assessed. Therefore the first step should be to cross-reference the full list of employees with the corresponding labor contracts and information concerning salary payments. Employees should have been paid their salaries in full up to the end of the month preceding the announcement of the liquidation. The labor contracts will also tell you how long each employee has officially worked at the company – compensation for termination of employment will be calculated based on the salary and length of employment. Finally, evidence of payment of the various mandatory welfare benefits should be checked to ensure there is no money owed.

Checking the contractual obligations should be a relatively straightforward task. The date of contract commencement and its term should be stated on the document. Most employment contracts will have a length of one year and there will be a section where the employee signs to extend the contract every year. For employees that have worked for the company less than ten years, there is effectively no severance pay because the liability for the company is limited to the period left on their employment contract.

Some employment contracts may have a clause stipulating the amount of compensation to be paid in the event of one of the parties violating the contract terms. In this situation if the amount specified for contract violation is lower than the remaining amount unpaid in

salary, the company's liability is limited to this amount. Irrespective of whether the remaining period of the contract is paid up or whether the contract violation penalty is paid, the company should have no responsibility for payment of social welfare for the employee after official termination of employment.

However employees that have worked with a specific company for more than ten years have a right to enjoy "open-ended contracts". These employees can receive a month of pay (based on the average salary they earned during the most recent year of employment) for every year they have worked with the company. For employees that have worked their entire life at the same company and are approaching retirement this can be a considerable amount, potentially up to three years of salary. In some cases it would be cheaper to pay their salary until retirement, however there is no allowance for this under current labor laws.

Of course most foreign invested enterprises have only been operating here in China for a decade or less, so in theory the liability for employee compensation should not be huge. Unfortunately it is not uncommon to find instances where foreign investors have taken over the operations of state-owned enterprises (SOEs), and perhaps unwittingly, absorbed the liability for payment of workers' severance pay during their period of work for the company prior to its incorporation as a foreign-invested enterprise. Although labor laws state that labor contracts should be terminated, severance paid by the old employer and new contracts signed with each worker, in practice these payments have not always been made. Certain areas in China have issued regulations requiring the new owner of the business to be responsible for all such legacy liabilities. Investors involved in projects of this nature where workers used to be affiliated to SOEs would be advised to check the exact status of the potential liabilities they have incurred or may incur.

Once the basic salary liability has been calculated, the social welfare and housing fund situation should be verified. Some companies going into liquidation face cash flow problems, and one of the first expenses to be neglected is often employees' benefits. Checking the

receipts from the social security bureau and the housing fund center will tell you when the latest payments were made for each employee. Note that the social security bureau has the right to add on a late payment penalty for outstanding contributions at a rate of 0.3% per day, but the housing fund center cannot do this. This can also mount up to a large sum if such payments remain outstanding for a number of months.



RISKS IN JUST "WALKING AWAY" FOR FOREIGN INVESTORS

Although most foreign investments in China are successful and generate considerable profits for their investors, some investors do wish to close down their businesses either because of poor profitability, global restructuring, or for some other reasons. However, can a foreign investor choose to just "walk away" if there are no substantial assets left in their business? Will the investor who does so incur any liability that can be enforced against him or his other assets in China or elsewhere?

Can a foreign investor make a strategic retreat from their Chinese investment without being chased by the creditors? The short answer, not surprisingly and quite properly, is "no." This is a critical issue that must be considered not only during the closing down of a business, but also in the process of running of the enterprise.

Limited liability of FIEs and potential liabilities for foreign investors

Foreign invested enterprises such as WFOEs and JVs are independent legal persons and own their own assets and properties. The foreign investors, in principle, only bear the limited liability

for their investment to the extent of their registered capital originally brought into China. However, under certain circumstances, foreign investors may be held personally liable for their investment activities beyond the capital contribution obligation. The potential liabilities applying to those foreign investors who "walk away" differ from those who face bankruptcy or voluntary liquidation.

Penalties for "walking away"

According to business registration regulations in China, it is the investor's obligation to register properly when the business is created and update the registration authority in the event of any significant changes of circumstances. If a foreign invested company is being wound up, the foreign investor is required to de-register the company before they may take back any remaining assets of the company. In other words, you must tell the authorities.

Deregistration can only take place after the company has gone through liquidation procedure, as described above, including a liquidation audit, and the payment of any liabilities to the tax authorities, Customs, employees, and creditors.

If a foreign investor fails to meet this obligation, and instead "walks away" without going through a proper liquidation, the registration authorities are entitled to impose a fine of between RMB10,000 and RMB100,000 on the company and to revoke its business license. In addition, the legal representative of the FIE whose business license is revoked, and who is personally liable for such revocation, shall be banned from being appointed to director, supervisor, or other senior management positions for three years in any other business entity in China as from the date of revocation of the business license. The names of the "walk away" investors are blacklisted in the official archives of the registration authorities, such people and they may be barred from the China market in the future.

In many cases of this kind there are remaining assets or property in a failed FIE. In this situation, as well as the legal representative being sanctioned as discussed above, under Chinese law it is held that a foreign investor who did not go through a liquidation proceeding but took

back the assets of the FIE should be held liable for all of the company's remaining debts and liabilities.

Liabilities for foreign investors in bankruptcy

The Enterprise Bankruptcy Law of the People's Republic of China stipulates in Article 5, "(t)he validity of any bankruptcy proceedings commenced in accordance with this law shall extend to the properties of the debtor outside of China." For the first time, a claim can be made over the assets of foreign investors in a bankruptcy case in an extraterritorial jurisdiction outside of Chinese territory. The bankruptcy administrator is responsible for bringing actions against any debtors on behalf of the company during bankruptcy proceedings.

According to the bankruptcy law, any foreign shareholder who had not fully paid up their registered capital shall be held liable for this inadequate capitalization.

Enforcement of judgment or arbitration award against foreign investors

If a Chinese court makes a ruling to hold a foreign investor liable for their Chinese entity debts, the petition for enforcement against the investor may be made either

by the Chinese creditors or the bankruptcy administrators in one of two different ways.

Firstly, in the event that the foreign investor has assets or other investment in China, the Chinese creditors or the bankruptcy administrator may make a petition to the court to freeze these properties. The foreign investor shall either settle the debt with their Chinese creditors to release the frozen property, or their properties shall be auctioned and used to pay to the creditors. It should be noted that according to the mutual arrangements on recognition and enforcement of civil judgments between Mainland China and Hong Kong and Macau, the assets and properties of the foreign investor located in Hong Kong and Macau may also be subject to enforcement by their creditors in Mainland China.

Secondly, even if the foreign investor does not have any assets or investment in China, and there is no mutual agreement on recognition and enforcement of civil judgments between China and the investor's country of origin, he is still not safe from the claims of the Chinese creditors in China. In this case, the Chinese creditors may file a petition to a court in the foreign investor's home

jurisdiction for the recognition and enforcement of a court judgment against the foreign investors according to the applicable law in that jurisdiction.

In addition, if there is an arbitration agreement between the foreign investor and its Chinese creditors, and the Chinese creditors file for arbitration in an established arbitration commission instead of civil litigation in a Chinese court, the application made by the Chinese creditors for recognition and enforcement of the arbitration award obtained from the arbitration institution shall be upheld pursuant to the so-called New York Convention of 1958, the United Nations Convention on Recognition and Enforcement of Foreign Arbitration Awards, with 142 signatory countries.

Conclusion

It is therefore clear that, whatever the circumstances and whatever may have happened in the past, foreign investors cannot, and should not, simply "walk away" from a failed business in China. With the growing confidence of the Chinese people, and the proper protection of both local and international laws, the interests of Chinese creditors, employees and the community at large are now defensible.

In the Face of Global Uncertainty, China Steps Up Regulation of Foreign Investors

In the wake of the global financial crisis, the Chinese government has moved in recent months to institute several guidelines for investors in the country. These range from how mass layoffs are to be handled to how the government will treat investors who attempt to flee the country without properly tying up their business requirements.

Companies based in several provinces are now required to apply for approval from their local human resources and social security authorities before a layoff of 40 or more workers. These regulations amend the national Labor Contract Law implemented last January. According to the national labor contract law, companies that want to lay off more than 20 employees must first apply for approval from labor unions

and report their plan to labor authorities. These provincial regulations are in response to China's Ministry of Human Resources and Social Security which advised local governments late last year to ensure stable employment levels and monitoring labor-intensive factories that are susceptible to layoffs.

In addition to changes to the labor law on the provincial level, foreign investors should also be aware that Beijing recently began seeking help from foreign governments to pursue overseas investors who flee the country without properly liquidating their assets.

China's ministries of commerce, foreign affairs, justice and public security jointly issued a guideline late

last year for cross-border investigation and litigation of fugitive foreign investors. The government laid out in the guideline how they would follow both international rules and domestic regulations to address such cases and seek assistance from foreign countries. China will request extradition or case transfer when a "huge amount of money" is involved the guidelines stated.

Investors who "walk away" from their China operation now face will not only face problems in China, but in their home country as well.



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