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Solutions for China Entry & Growth*

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## Market Insights

### Opportunities for Luxury Boutique Hotels Boom in Lower-Tier Cities



China's Hotel industry has been enjoying annual double-digit growth over the past five years. Having saturated first-tier cities such as Shanghai, Beijing and Guangzhou, some investors/owners are now eyeing lower-tier cities for future development.

Chinese travelers are familiar with brand name hotel chains, which guarantee a standardized experience. However, the Chinese travelers are also beginning to explore boutique luxury hotels that offer the same quality standards, personalized service, and a unique travel experience.

As hotel rates in China's second-tier cities have been catching up to the first-tier markets, opportunities exist for relatively high return on investment. For example, average revenue per available room (RevPAR) in Chengdu rose by 18% to CNY406 this year, surpassing Beijing's CNY404. Similarly, second-tier cities like Hangzhou, Nanjing, and Shenzhen are also catching up.

Nonetheless, there are several factors potential entrants should consider prior to making significant commitments, two of which are:

1. **Location** - Where a hotel is located and its surroundings not only determines the amount, but also the quality of foot traffic; understanding the customer demographics of the surrounding area is vital to success.
2. **Concept** - The overall style and feel of a boutique hotel is critical to the guest experience; regional tastes (or offering guests a local experience) should be taken into consideration when designing the layout and décor.

China's expanding middle class and increased spending on domestic travel will continue to drive growth in the hotel/travel industry, creating opportunities in the boutique luxury hotel sector. However, navigating China's business landscape is not always straightforward; companies should conduct proper research on the market, regulatory environment and ownership structure.

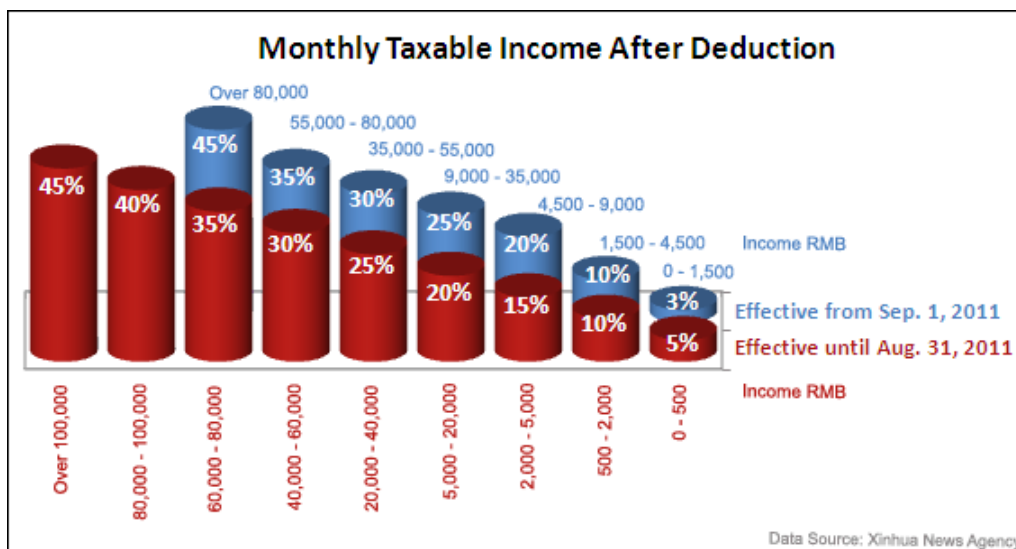
For more information about hotel industry market research in China, please email Mark Ray at [mark.ray@jljgroup.com](mailto:mark.ray@jljgroup.com).

## Tax Updates

### Amended Individual Income Tax Law to Start Soon

Last month, China's 11th National People's Congress announced a number of significant changes in the Individual Income Tax (IIT) Law, which will come into effect on September 1st, 2011. The adjustments will have direct implications on employees or on employers who set net salaries in employment contracts; this includes foreign direct invested companies. Below are three of the major amendments:

1. Chinese employees' IIT minimum threshold will be raised from RMB 2,000 to RMB 3,500 a month. Foreign employees' IIT payment minimum threshold will remain RMB 4,800. This minimum threshold is for income after deductions for public housing fund and basic social benefits premiums, including pension, medical and unemployment.
2. IIT return filing schedule will be extended from the current requirement of within the first 7 days of the following month to within the first 15 days of the following month. This adjustment is aligned with other taxes to be paid on the same period of time, such as Enterprise Income Tax, Value Added Tax, etc.
3. The IIT rate brackets will also be amended. The lowest bracket of 5% will be changed to 3% and the 15% and 40% brackets will be removed. Effective Sep. 1st, 2011, the payable IIT will be calculated according to the following table after the minimum threshold deduction - RMB 3,500 for local Chinese and RMB 4,800 for foreigners.



Part of the reason for adjusting the tax rates and thresholds is to balance the large increase in income tax revenue in recent years, and the changes in social insurance. By the second quarter of 2011, the Chinese government collected approximately RMB 355.5 billion of Individual Income Tax revenue, an increase of 35.4% year-on-year according to the Ministry of Finance. As a result of these changes the number of IIT payers in China is expected to drop from the current of 84 million to 24 million.

For more details about the amended Individual Income Tax Law, please contact [vicky.xu@jljgroup.com](mailto:vicky.xu@jljgroup.com)

## Human Resources

### Changes in Shanghai Social Insurance Schemes



With the implementation of the new China Social Insurance Law on July 1, 2011, employees who work in Shanghai but do not hold Shanghai hukou will have their comprehensive insurance and town-based social insurances schemes changed.

According to the new regulation, the previous comprehensive insurance and town-based social insurance schemes for employees in Shanghai were ended. From July 1, 2011 onward, all Chinese employees who work for companies located in Shanghai are now entitled to city-based social insurance.

Employees who hold urban hukou and were taking part in comprehensive insurance must switch to city-based social insurance and are entitled to the same social insurance and contribution rate as those with Shanghai hukou. Their social insurance benefits include pension, medical insurance, work-related injury insurance, maternity insurance and unemployment insurance. The switch to city-based social insurance is immediate and the contribution base is the gross salary of the employee. The minimum and maximum contribution bases are RMB 2,338 and RMB 11,688.

Those employees who took part in comprehensive insurance and hold rural hukou must also switch to city-based social insurance and are entitled to receive three of the social insurance benefits, including pension, medical insurance and work-related insurance. These employees will transition over a 5 year period using a gradually increasing percentage of the Shanghai average salary as their contribution base.

Employees who took part in town based social insurance are now entitled to all city-based social insurance benefits and have two options to make the switch. They can either switch to city-based social insurance immediately with their current salary as the contribution base or over a three year transitional period where the contribution base is 60% of the Shanghai average salary and the contribution rate for each benefit is increased gradually each year.

For more information on the changes to social insurance in Shanghai, email [joyce.xia@jljgroup.com](mailto:joyce.xia@jljgroup.com)

## China FDI

### SME Classification Standards New Addition - Micro-Enterprises

On June 18, new Small and Medium Enterprises (SMEs) classification standards (the "new standards") were jointly issued by the National Development and Reform Commission, the National Bureau of Statistics, the Ministry of Finance, and the Ministry of Industry and Information (MIIT).

According to the new standards, the classification of SMEs will be subdivided into three enterprise categories: small, medium and the new addition – micro enterprise.

Different industry parameters were taken into account, such as the number of employees; sales volume; total assets value; and more. Furthermore, the MIIT said that the new standards will ease the government's data collection procedure and will allow the government to more easily identify needs of and create preferential policies for SMEs.

According to the new standards, general micro-sized enterprises are those with 20 employees or less, or have annual revenue of RMB 3 million or less. In the past general SME classification required less than 2,000 employees or RMB 300 million in annual revenue, under the new standards companies should have less than 1,000 employees or RMB 400 million in annual revenue. Depending on the industry, there are deviations from these general requirements.

A government official spokesman stated that micro-enterprises are an important channel for the Chinese employment system. Employment capacity, labor flexibility and low start-up cost are the main advantages of micro-enterprises over larger enterprises. The second national economic census data (2008) shows that 38.7% of all employees in China were working in micro-enterprises at the time the census was conducted.

Premier Wen Jiabao has said that the government is working this year to develop labor-intensive industries, service companies, and innovative technology companies. These efforts are aimed to match the employment needs of different levels and the structural characteristics of China's labor force. Support and development of micro-enterprises will play an important role in those efforts.

For more information about SMEs new classification standards and micro-enterprises, contact Tim Lamb [tim.lamb@jljgroup.com](mailto:tim.lamb@jljgroup.com)

