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Market Insights

China's 12th Five-Year Plan: Roadmap for the Energy Sector

Every five years, China's central government issues what is known as a "Five-Year Plan", which sets general economic and development goals for the country. This year, the 12th Five-Year Plan (2011-2015) was released, which includes important guidelines for China's largely state-owned energy sector. Some key points include:

- **Optimize the development of fossil fuels** – Focus on the upgrade of coal mine operations, control coal production, promote clean & efficient usage of coal, and develop oil & natural gas resources; implications include continued consolidation in the mining sector, systematic extraction of coal bed methane, and development of clean and energy-efficient technology
- **Develop alternative energy** – Hydro, nuclear, wind, solar energy and biomass power will continue to be developed; alternative energy is targeted to make up 11% of primary energy consumption by the end of 2015
- **"5+1" structure for overall energy planning** – China plans to develop 5 multi-source energy centers in Western China, areas/provinces include: Shanxi, Ordos Basin, Southwest China, East Inner Mongolia, & Xinjiang; focus on developing nuclear power in East and Central China
- **Optimize power transmission & configuration** – Investment earmarked for the optimization of power grid systems, including development of Ultra-High Voltage power transmission and Smart Grid (RMB 800+ billion investment estimated over the next 5 years)



The Chinese government will continue the structural reform of the energy sector, promote innovation in energy-related equipment, continue to emphasize energy saving and environmental protection, as well as encourage international cooperation and overseas investment by Chinese companies in the energy sector.

Some government initiatives may present opportunities for foreign companies in energy and related sectors to enter and grow in China, although barriers, such as fierce competition, exist. It is advised that companies keep track of more specific policies and initiatives as elaborations on the national plan are released over the next few months, and conduct proper market research before taking action.

For more information about China's energy sector outlook in the next five years, please email Mark Ray at mark.ray@iljgroup.com

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Clarification on Non-Resident Enterprise Income Tax



China State Administration of Taxation recently issued notification No.24 to further clarify issues related with non-resident Enterprise Income Taxation (EIT) on their China-derived income from financial leasing, property rentals, equity investments as well as equity transfers. Within this regulation, there are two important areas to be highlighted.

1. In a situation where a domestic resident enterprise enters into a contract with a non-resident enterprise on interest, rental, royalty payment, etc:
 - a. When the domestic company fails to make the payment prior to contract date or the payment date is extended, such payment is still recorded as a cost and a pre-tax deduction is made for the annual Corporate Income Tax (CIT) declaration, and the related non-resident EIT should be withheld and paid in the tax year of declaration.
 - b. When deferred payment is not expensed in the above situation but instead is included in an asset price and amortized when the asset is put into use, the related non-resident EIT on the total payment should be withheld and paid in the tax year when the asset is recorded on the balance sheet.
 - c. If the domestic company makes the payment before the contract date, the non-resident EIT should be withheld on the actual payment date in accordance with relevant stipulations related with withholding of EIT.
2. Tax on non-resident enterprises' equity investment income:
 - a. When a domestic company distributes investment income such as dividends and bonuses to non-resident enterprises on their equity investment, non-resident EIT should be withheld and paid on the date when the decision for distribution is made.
 - b. If the payment takes place prior to the profit distribution decision, related non-resident EIT should be withheld on the actual payment date.

The announcement is effective from April 1, 2011, and applies to all outstanding tax liabilities incurred before this date. Non-resident enterprises refer to enterprises that are set up in accordance with the law of a foreign country (region) and whose actual administrative institution is outside China. Non-resident enterprises include those with or without establishments within China, and have income sourced from China.

For more details about Non-Resident Enterprise Income Tax, please contact henry.ren@iljgroup.com.

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Human Resources

Salary Increase Guideline



Shanghai Labor and Social Security Bureau, in cooperation with the General Labor Union, Confederation of Enterprises, and Entrepreneur Association, annually publishes the Salary Increase Guideline.

The guideline is created by considering the economic development of the city, consumer prices, employment, labor costs and wage levels. It includes guidance on average, upper, and lower level wage increases and is a useful reference for enterprises to determine salary increases and compensation distribution.

The key points of the guideline are:

- Recommended average wage increase is 11%; upper limit wage increase is 16%; the minimum wage increase should be no less than 4%
- Enterprises should establish a mechanism for normal wage increases including negotiations to set reasonable levels of wage growth across different positions
- Enterprises in stable financial operation and with average economic returns are recommended to

increase the employees' wages according to the average guideline of 11%. Those with average wages lower than 60% of the city average should increase wages by 16%

- When determining wage increases, focus should be given on improving the wages of front-line workers. Increases in front-line worker wages should be no less than the average increase in the company. In cases where front-line workers wages are not increased, management should also not receive an increase in wages

For more information on Salary Increase Guideline, please contact Joyce Xia at joyce.xia@iljgroup.com.

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China FDI

Industry Catalogue for Foreign Investment

Last month, China's National Development and Reform Commission released a new draft of the "Industry Catalogue for Foreign Investment". The catalogue details several industries in relation to foreign direct investment into China. The industries are separated into 4 categories, including: encouraged, permitted, restricted and prohibited. Industries that are not listed will be considered as permitted.



Unlike the 2007 catalogue which encourages more manufacturing industries in general, the 2011 catalogue provides major focus on the new-energy related and environmentally friendly industries, such as new-energy automobile, recycling, and water treatment. The "green" focus is in line with the 12th 5-year plan development commitment, and foreign investments that qualify in the encouraged category may receive preferential tax treatment.

Moreover, the new draft catalogue reflects China's plan to participate in a more global role by encouraging industries such as aviation, automobile, and information & communications technologies. Service industries, which were not emphasized in the 2007 catalogue, are now encouraged.

Industries that are considered less green, such as chemical products, machinery products, and textile will now be required to use modified environmentally friendly equipment in order to qualify as encouraged. Manufacturing industries that are highly polluting and energy consuming were taken out of the encouraged list, while some, such as those that use nuclear fuel, and paint manufacturers, have been placed in the restricted section.

Industries related to processing, research, and development of genetically modified plant seeds, which were previously prohibited, have been extended to cover any genetically modified organism. In addition, villa construction and management were added to the list of prohibited industries.

The draft will also clarify the vagueness that was created between the 2007 catalogue and later policies appearing in the Catalogue of Industrial Structure Adjustment, which goes into effect on June 1st 2011 with its latest updates.

For more information about the Industry Catalogue for Foreign Investment, please contact andrea.cristancho@iljgroup.com.

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The JLJ Group

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