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Solutions for China Entry & Growth

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Market Insights

Commercial Due Diligence for M&A Target

Entering or consolidating in the Chinese market can be achieved through several means, one being mergers and acquisitions (M&A).

Although M&As can be a relatively fast way to consolidate or gain market share and knowledge, there are a number of uncertainties involved, especially in a market like China. Because of these uncertainties, it is important for companies to conduct not only Financial Due Diligence (executed by an accounting firm), but also Commercial Due Diligence.



Commercial due diligence can help companies gain a better understanding of the target's growth potential, through investigating several areas:

- **Business Assumptions** – especially in China where growth outlooks can be highly optimistic, but changes are also unpredictable; it is important to challenge and validate business assumptions built into the target's growth projection through proper investigation
- **Market Dynamics & Growth Potential** - understanding the market, including potential opportunities

and challenges, as well as the target company's positioning is crucial for validating business assumptions and developing post M&A strategies

- **Human Resources** – target company's organizational structure, HR practices, working culture, and succession plans are often overlooked; however, these areas are vital to the company's long-term growth

It can be difficult to anticipate potential challenges when merging with or acquiring companies in China; proper Commercial Due Diligence combines market research, benchmarking, internal assessment, and other techniques necessary to support the M&A process, increasing the chances of a successful venture.

For inquiries about this article and how The JLJ Group can assist your company, or other work of our consulting division, at mark.ray@jljgroup.com

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Tax Updates

Shanghai Local Tax Bureau Released New Measures on Business Tax



Effective from September 1st 2010, businesses in Shanghai may be able to first deduct business expenditures from business income for business tax calculation, according to the newly released measures by Shanghai Local Tax Bureau. The scope of the new measures covers almost every business type in Shanghai.

Previously, business tax was determined directly from taxable amount of business income. Only a few industries such as transportation and tourism were able to deduct business expenditures from revenue before business tax was applied.

The new measures affect companies engaged in 9 main business categories and 60 sub-categories, 24 of which are service industry activities. The main categories are transportation, construction, post and telecommunications services, banking and insurance, service, culture and sports, intangible asset assignment, sale of immovable property, and other circumstances approved by regulations.

The strengthening management of business tax, in the form of measures and tentative regulations, is aimed to better administrate taxation and to promote the development of service industries by regulating deductible items subjected to business tax. It will bring great tax benefits for service industries conducting their operations in China.

For more information about business levied for business tax, please email to vicky.xu@jljgroup.com

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Human Resources

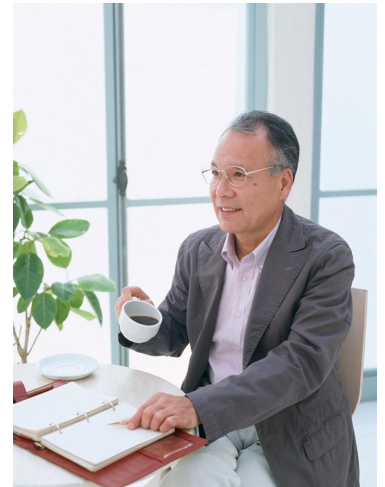
There is Work After Retirement Age

As of October 1st 2010, Shanghai local residents, excluding government employees, can apply to draw their pension later than retirement age if they choose to keep their jobs and the employers agree to keep paying their social insurances. The policy, announced on September 6th 2010 by the Shanghai Human Resources and Social Security Bureau ('Bureau'), is aimed at alleviating the growing pressure on the city's pension pool, given the rapid growth of Shanghai's aging population.

In China, the retirement age, which was fixed 50 years ago, is 60 years old for men and 55 or 50 years old for women, depending on the type of job. The new city policy says men can retire as late as 65, while the age for women is 60 years old. The bureau said people delaying retirement would enjoy a higher monthly income when their contract eventually finished, due to their growing personal pension account.

The policy hopefully will create a positive impact, especially when the number of young people entering the job market does not outpace the number of people reaching retirement each year.

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China FDI

Tax Incentive Policies on R&D Centers



The Ministry of Finance (MOF), General Administration of Customs (GAC) and State Administration of Taxation (SAT) jointly issued a circular (Circular No. 115) in October 2009 that granted an import VAT exemption on equipment imported by R&D centers and a full VAT refund on domestically manufactured equipment purchased by R&D centers. The benefits under Circular No. 115 (import VAT exemption and VAT refund), however, only apply until 31 December 2010.

Affected companies should immediately review and assess whether their R&D departments/branches or legal entities engaged in R&D activities qualify. If possible, documents should be prepared and an application submitted to take full advantage of the VAT incentives during 2010.

Besides tax benefits for purchased equipment from R&D centers, qualified high-tech investments can also take advantage of a 15 percent Corporate Income Tax (CIT) rate which is normally 25 percent, regardless of their location and investment vehicle. What's more, the first RMB 5 million in annual revenue resulting from technology transfer is exempt from CIT and any amount that exceeds RMB five million is subject to a discounted rate of 12.5 percent. In order to qualify for a high-tech investment, business needs to satisfy the following criteria:

- Must be established within China and exist for more than one year
- Continuously conduct R&D activities and do business in a qualifying High-Tech sector
- Own the IPR of its main products core technology in China
- Engage 10 percent of employees on R&D work
- Invest 3 to 6 percent of revenue on R&D with 60 percent of occurring expenses in China
- Earn more than 60 percent of total revenue from high-tech products and services.

For more information about this article, please email andrea.cristancho@jljgroup.com

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The JLJ Group

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