Setting Up a Business - Foreign Invested Enterprise

China offers foreign investors several alternatives in structuring their business in the Chinese market, including registering a representative office (RO), establishing a wholly foreign-owned enterprise (WFOE) or forming a joint venture (JV) with one or more Chinese partners.

A Representative Office represents the interests of the foreign investor in China and may only conduct market research and develop relationships between Chinese customers or suppliers and the foreign parent. All business transactions, including the issuance of invoices, are managed by the parent company and ROs are not allowed to directly engage in any profit-making activities. Furthermore, ROs may not directly hire local employees but must rely on a government-authorized employment agency. The establishment of a RO is the simplest way for a foreign company to set up a legal entity in China and is therefore often the choice for foreign companies with no prior experience in China.

A wholly foreign-owned enterprise is established entirely with foreign capital, under total foreign control and without any Chinese ownership or participation. WFOEs are currently the most popular form of foreign investment in China due both to the increased legal acceptance and support for this type of structure from the Chinese government as well as the low success rate that affects JVs. A WFOE may hire local employees and legally conduct business transactions allowing the foreign company to carry out business and receive payment in RMB within China.

A Joint Venture is a business arrangement or partnership between foreign and Chinese investors, and involves the sharing of expenses, resources, profits and losses. Chinese law stipulates that the

foreign partner contribute no less than 25% of the capital. Foreign investors may set up two different kinds of JVs in China: an equity Joint Venture (EJV) or a Contractual Joint Venture (CJV). In an EJV arrangement, the two partners share the profits, management responsibilities and risks according to the percentage of the capital investment each side has made. In a CJV arrangement the amount of risk and profit shared by each party is not determined by capital investment but rather according to a ratio agreed to at the beginning of the partnership and stipulated in the contract signed by the investors.

The risk associated when entering into partnerships with Chinese companies can sometimes be exacerbated by disparities in culture and business practices between the foreign and local partners. It is only recommended to enter into any kind of JV arrangement when both parties have reached a clear understanding of the business objectives.

For further information on how to structure your foreign investment in China, contact the Shanghai-based JLJ Group, an integrated service provider assisting foreign companies with China entry. www.jljgroup.com