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Doing Business In... 2022

China: Law & Practice

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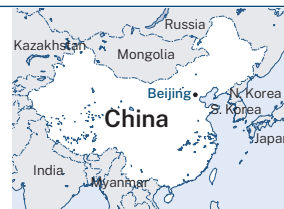
China: Trends & Developments

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Law and Practice

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1. LEGAL SYSTEM

1.1 Legal System

China is governed under a socialist legal system with Chinese characteristics that is based on the civil law system. The legal system is founded on a written constitution and the laws and decisions adopted by the National People's Congress and its standing committee. The State Council is China's top administrative authority, which is empowered to promulgate administrative regulations and whose constituent departments and sub-agencies are authorised to promulgate legally binding administrative measures, rules, decisions, and directives. At the provincial and municipal levels, people's congresses and local counterparts of the nation's administrative authorities also hold legislative and administrative powers, respectively, within their jurisdictions. Local laws and administrative documents must not conflict with their superior national-level counterparts.

The Chinese judicial system is composed of different levels of courts, including the following.

- The Supreme People's Court.
- Local people's courts:
 - (a) higher people's courts at the provincial level;
 - (b) intermediate people's courts at the municipal level; and
 - (c) basic people's courts at the district or lower level.
- Special courts:
 - (a) intellectual property courts in Beijing, Shanghai, and Guangzhou;
 - (b) financial courts in Beijing, Shanghai, and Chongqing;
 - (c) internet courts in Beijing, Guangzhou, and Hangzhou and;

- (d) other special courts (such as military courts, railway courts, and maritime courts).

The Supreme People's Court is the highest authority in China's judicial system and exercises supervisory power over the activities of lower courts. Court rulings in China generally do not serve as binding precedent, although certain cases have important referential value.

China has adopted a "two instances" trial system. Cases are first heard by a court that has jurisdiction over the dispute. If a litigant does not accept the judgment of first instance, it can generally appeal to the court at the next higher level before the judgment takes effect.

The people's procuratorates are divided into levels similar to the people's courts and undertake the role of public prosecutors during criminal proceedings. The procuratorates approve arrests made by the public security organs; carry out investigations of, institute, and prosecute criminal cases; and supervise the enforcement of sentences. The Supreme People's Procuratorate exercises supervisory power over the activities of procuratorates at each level.

The Supreme People's Court and the Supreme People's Procuratorate have the power to interpret the application of laws arising in judicial practice.

2. RESTRICTIONS TO FOREIGN INVESTMENTS

2.1 Approval of Foreign Investments

China has adopted a negative list approach to foreign investment. Foreign investment is generally permitted without approval in industries that are not prohibited or restricted from foreign

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investment under the Special Administrative Measures for Foreign Investment Access (the “Negative List”). Restricted industries currently include telecommunications, education, and healthcare, while prohibited industries include broadcasting and publishing, among others.

Restricted industries are subject to special administrative measures that typically include shareholding limitations and nationality requirements for the legal representative and senior executives, among others. To ensure compliance with the Negative List, foreign investors seeking to invest in restricted industries should obtain a pre-investment permit from the competent industry regulator or, if none exists, apply for a review by the local counterpart of the State Administration for Market Regulation (SAMR).

Besides the Negative List regime, foreign investors may be subject to other pre-investment administrative approvals or permits applicable to all investors, such as anti-monopoly review, national security review, and industry-specific permits.

2.2 Procedure and Sanctions in the Event of Non-compliance

The Foreign Investment Law of the PRC, effective as of 1 Jan 2020, provides a general framework for authority approvals and permits for foreign investors, which include the following.

- Anti-monopoly review – a pre-closing clearance applicable to cross-border acquisitions resulting in a change of control or, in certain cases, the establishment of a joint venture that meets certain thresholds.
- National security review – a pre-closing clearance applicable to foreign investments with national security implications.
- Foreign investment project approval or record-filing – applicable to foreign invest-

ment projects involving fixed asset investments, which must be completed before the commencement of the project.

- Industry-specific permits – applicable to certain business activities that require industry regulatory approval and, in most cases, can be obtained after the foreign-invested company has obtained its business licence.

The timing of the foregoing approvals and permits often varies, depending on the extent and depth of the review process.

Failure to comply with authority approvals and permits may result in adverse consequences for foreign investors and their investments. If a foreign investor makes an investment in a restricted industry without approval, the foreign investor will first be ordered to make corrections and take necessary measures to meet the requirements. Failure to do so could result in the unwinding of the investment. Compliance issues may also negatively impact the investor’s social credit status, which could make it more difficult to obtain financing and to qualify for preferential government policies, among other adverse consequences.

2.3 Commitments Required From Foreign Investors

Chinese authorities generally do not require investors to make commitments prior to investing in China beyond a general undertaking to comply with Chinese laws. Exceptions exist. For example, SAMR may impose restrictive conditions when granting anti-monopoly clearance, such as requiring divestiture of assets, reduction of ownership, or the undertaking of certain other actions.

2.4 Right to Appeal

In principle, an investor may challenge adverse administrative decisions through a complaint

mechanism, administrative reconsideration with the authority, or administrative litigation before a court. However, in practice, it is highly uncommon for investors to challenge an authority's decision not to provide necessary approvals because taking legal action against the authority would be time-consuming and unpredictable.

3. CORPORATE VEHICLES

3.1 Most Common Forms of Legal Entities

The two most common forms of legal entity in China are the limited liability company (LLC) and the company limited by shares (the "joint stock company"). Foreign investors currently favour the LLC form, principally due to its flexible governance structure – a closely held LLC requires only a single equity holder and one executive director, and equity holders enjoy greater flexibility in formulating corporate governance policies. By contrast, a joint stock company requires at least two shareholders and a board of directors, and it must primarily abide by statutory procedural requirements for shareholder and board meetings. Both LLCs and joint stock companies afford limited liability to their investors. In general, LLCs and joint stock companies are not subject to minimum capital requirements, although specific industry rules may impose such requirements.

LLCs are more favourable for greenfield projects, wholly foreign-owned enterprises, and joint ventures. In this regard, the primary advantages of joint stock companies are that they offer access to the resources of local Chinese partners and may be listed on Chinese stock exchanges, thereby providing another exit for investors.

3.2 Incorporation Process

Establishing an LLC in China that will not engage in activities stipulated in the Negative List generally involves the following steps:

- registration for establishment with the local counterpart of SAMR; and
- post-establishment formalities with other local authorities in the LLC's jurisdiction of establishment, including the making of company seals, registration with the tax authority, and registering with the foreign exchange authority through a bank.

LLCs can formally commence operations only upon completion of all post-establishment formalities.

Establishing an LLC that will engage in activities stipulated in the Negative List generally requires obtaining approval from the competent industry regulator or clearance by SAMR that the relevant terms of the special administrative measures have been satisfied.

3.3 Ongoing Reporting and Disclosure Obligations

Chinese law requires private companies to report certain corporate matters to SAMR and the Ministry of Commerce (MOFCOM).

- SAMR filing – private companies are required to file annual reports with SAMR and to report to SAMR on an interim basis any changes to basic information of the LLC, such as a change of shareholder, corporate name, legal representative, directors, etc.
- MOFCOM FDI reporting – private companies with foreign ownership are also required to report to MOFCOM in the event of ownership changes involving the company's ultimate beneficial owner.

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3.4 Management Structures

LLCs in China are required to have a three-tiered governance structure under the Company Law of the PRC (the “Company Law”):

- a board of shareholders or sole shareholder;
- a board of directors or executive director; and
- a board of supervisors or supervisor(s).

For a more detailed discussion of this topic, see Han Kun Law Offices China Law & Practice chapter in **Chambers Global Practice Guide to Shareholders’ Rights & Shareholder Activism 2021**.

Shareholder(s)

Power over an LLC is vested in its shareholder or board of shareholders, which is actively empowered to decide on major corporate matters. Under the Company Law, LLC shareholders are mainly entitled to the following rights:

- to attend and vote at shareholders’ meetings in proportion to their capital contributions;
- to appoint or remove non-employee representative directors/supervisors;
- to be entitled to dividends and to approve the payment of dividends;
- to inspect the company’s articles of association, minutes of shareholders’ meetings, board resolutions, resolutions of the supervisory board and financial accounting reports;
- to inspect the company’s accounting records for legitimate purposes;
- to participate in any liquidation and share proceeds therefrom;
- the right of first refusal for equity transfers to non-shareholders; and
- the right of pre-emption for capital increases.

Under the Company Law, certain rights are exercisable only by shareholders who meet shareholding threshold requirements. LLC sharehold-

ers holding at least 10% of the voting rights may exercise their rights:

- to propose to convene an interim shareholders’ meeting;
- to convene and preside over a shareholders’ meeting if the board of directors (or executive director) and the board of supervisors (or sole supervisor) fails to do so; and
- to request a court to dissolve the company where the company experiences serious difficulties in its business and the shareholders would suffer serious losses if the company were to continue to operate.

Some of the rights above can be modified if all shareholders so agree or if provided for in the LLC’s articles of association, such as in respect of voting, dividend payments, and first refusal for equity transfers.

Board of Directors or Executive Director

LLCs are also required to have a board of directors or an executive director, which reports to the shareholder or board of shareholders. Under the Company Law, a board of directors or an executive director exercises powers for overall management of the company, including matters such as operational strategy; business and investment plans; internal management systems; and formulating plans for shareholder approval regarding budgets, financial accounts, and profit distributions.

The Company Law provides that each director is entitled to one vote. In practice, companies with multiple shareholders or with a relatively large board of directors provide in their articles of association more detailed rules on the quorum for the meeting and voting requirements over certain matters for board resolutions.

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Board of Supervisors or Supervisor(s)

The Company Law requires that LLCs have a board of supervisors or a supervisor, whose duty is to supervise financing and operating activities. A supervisor must be an individual and cannot be one of the directors or senior officers (including the general manager).

Other LLC Management Structures

The executive director or board of directors may appoint a general manager that manages the LLC's daily operations.

LLCs are also required to have a legal representative, who must be a natural person and who may concurrently serve as the LLC's board chairman, executive director, or general manager. The legal representative is responsible for engaging in civil acts on behalf of the LLC in accordance with law or the LLC's articles of association.

3.5 Directors', Officers' and Shareholders' Liability

Directors', Supervisors' and Officers' Liability

Liability to the company

The Company Law contains the principal legal provisions governing the liability of directors, supervisors, and officers in the execution of their duties for a company. These individuals may be held liable to the company where, for example, in executing their duties they cause a loss to the company in violation of provisions of law, administrative regulations, or the company's articles of association.

Liability to the shareholders

Directors, supervisors, and officers may also be liable to the shareholders where they violate provisions of law, administrative regulations, or the company's articles of association and cause a loss to the shareholders, particularly the loss of shareholders' rights such as the right to know, to vote, and to receive dividends. In these events,

shareholders are entitled to bring direct suits against the directors, supervisors, and officers.

Shareholders' Liability

Liability to the company's creditors

Companies in China are deemed independent legal persons that own assets and assume debts separately from their owners. Shareholders are generally not held liable for the debts of their companies beyond their subscribed and contributed capital. This "corporate veil" is qualified and may be pierced where, for example, it is shown that a shareholder has abused its limited liability status at the expense of creditors in violation of provisions of law, administrative regulations, or the company's articles of association.

Liability to the company and other shareholders

Shareholders that infringe the legal rights and interests of the company may be held liable to the company and other shareholders through an action brought by the company or a derivative action brought by the shareholders. Common instances where shareholders may be held liable include the following:

- controlling shareholders and ultimate controllers who infringe the company's interests through abuse of related-party transactions may be held liable for damages caused to the company or other shareholders; and
- shareholders who withdraw capital contributions from the company or fail to fulfill their capital contribution obligations may be ordered by the company or other shareholders to make remedy.

4. EMPLOYMENT LAW

4.1 Nature of Applicable Regulations

Employment relationships in China are governed by two foundational laws, the Labour Law and the Labour Contract Law. In addition to these two laws, it is important for foreign investors in China to become familiar with local and provincial regulations, as well as to maintain a positive relationship with the local labour bureau, which handles employment issues on a day-to-day basis.

Employers in China are required to enter employment contracts with each individual employee. Chinese law also encourages employees to enter into collective agreements with their employers that set out matters generally applicable to all employees, such as remuneration, working hours, days off, holidays, health and work safety, insurance, and welfare.

4.2 Characteristics of Employment Contracts

By law, employment contracts entered between employers and employees must be in writing, with the exception of part-time work. If an employer fails to sign a contract with an employee within one month after the employee starts work, the employee is entitled to receive double their normal wages until a contract is signed.

Employment contracts are required to include certain material provisions, such as:

- parties to the contract;
- term of the contract;
- job description and place of work;
- working hours;
- rest and leave;
- labour compensation;
- social insurance;
- labour protection; and

- working conditions and protections against occupational hazards.

According to the Labour Contract Law, an employer and an employee may choose to execute a fixed-term, open-ended, or project-based employment contract. Under certain circumstances, an employer must enter into an open-ended employment contract with an employee at their request, such as the employee having worked for the employer for more than ten consecutive years or it being the third time that the employee has entered into an employment contract with the employer. Local rules and regulations may require the inclusion of additional contractual provisions and recommend the use of standard contracts.

4.3 Working Time

Chinese law implements three types of working hour systems. These systems are the standard working hour system, the comprehensive working hour system, and the flexible working hour system. Each working hour system permits different arrangements for working hours, rest periods, and overtime pay.

Standard Working Hour System

Employees may work up to eight hours each day and work an average of 40 hours per week. Employers may temporarily adjust working hours and workdays in accordance with actual conditions, but employees must have at least one day off each week.

Flexible Working Hour System

This system is usually applied to senior management personnel, field staff, salespersons, and others whose work cannot be measured under the standard working hour system. Prior approval from the local labour authority is required before this system can be implemented.

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Comprehensive Working Hour System

This system allows for employee working hours to be calculated per week, month, quarter, or year. However, the average working hours per day and per month must be similar to those under the standard working hour system. Prior approval from the local labour authority is required before an employer can implement the comprehensive working hour system.

Employees under the standard and comprehensive working hour systems are entitled to overtime pay according to the following standards:

- for overtime worked during normal working days – no less than 150% of the hourly salary for each overtime hour worked;
- for overtime worked during any day off (generally Saturday and Sunday) and if no extra time off could be arranged in lieu thereof – no less than 200% of the hourly salary for each overtime hour worked, which does not apply to the comprehensive working hour system; and
- for overtime worked during public holidays – no less than 300% of the hourly salary for each overtime hour worked.

Generally, employees under the flexible working hour system are not entitled to overtime pay. However, local practice may differ in this respect and should be referenced as necessary. For instance, in Shanghai, employees under the flexible working hour system are eligible for overtime pay on public holidays, which should be paid at 300% of the employee's normal wage.

4.4 Termination of Employment Contracts

Chinese law does not generally recognise an employer's right to at-will employment. Termination by employers is strictly regulated and must rely on a statutory basis and adhere to certain procedural requirements.

Mutual Termination

Employers and employees may terminate the employment relationship based on mutual agreement. Employees who agree to mutual termination are entitled to severance.

Unilateral Termination by an Employee

Chinese law generally permits an employee to unilaterally terminate their employment relationship by resigning at will, provided that 30 days' advance written notice is given to the employer. Employees are also entitled to immediate termination in instances where the employer has acted in violation of laws or the employment contract. The employer is required to pay severance to the employee for such termination subject to the Labour Contract Law.

Unilateral Termination by an Employer

Employers can unilaterally terminate their employees in three ways: (i) summary dismissal, (ii) termination with prior notice or payment of salary in lieu of notice, and (iii) lay-offs.

Summary dismissal

Employers are entitled to terminate employees with immediate effect without severance in the case of the following:

- failure to satisfy conditions during the probationary period;
- serious violation of the employer's policies and rules;
- breach of duty or misconduct resulting in material loss to the employer;
- existence of seriously conflicting employment relationships or refusal to rectify upon request;
- the contract was concluded by fraud, threat, force, or coercion; and
- the employee is investigated for criminal liability.

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Termination with prior notice

Employers may also unilaterally terminate employees with prior notice of not less than 30 days (or payment of one months' salary in lieu of notice) on any of the following grounds:

- the employee suffers from a disease or non-work-related injury and is unable to perform their original duties after the statutory medical treatment period or any other duties arranged by the employer;
- the employee is found to be unqualified and the employee remains unqualified after receiving training or an adjustment of their duties; and
- a major change in objective circumstances that hinders continued fulfilment of the original contract and, upon consultation, the employer and employee are unable to amend the employment agreement.

Employees so terminated are entitled to severance in accordance with the Labour Contract Law.

Lay-offs

Chinese law permits employers to conduct "economic lay-offs" of 20 or more employees or over 10% of an employer's total workforce due to the following severe economic difficulties:

- bankruptcy restructuring;
- serious difficulties in production and/or business operations;
- switching production, introducing major technological innovations, or changing business models, and workforce reduction is still necessary after amending employment contracts; and
- other significant changes to the objective economic circumstances relied upon at the time of execution of the employment contracts.

Note that, before implementing an economic lay-off plan, the employer must first give 30 days' advance notice to the trade union or all employees and then report the plan to the local labour bureau. Employees terminated in a lay-off are entitled to severance.

Other Statutory Bases for Termination

The employment relationship may also terminate upon the expiry of the employment contract or upon any of the following circumstances:

- the employee reaches their statutory retirement age;
- the employee dies or is declared dead or missing by a people's court;
- the employer is lawfully declared bankrupt;
- the employer's business licence is revoked, the employer is ordered to close or is closed down, or the employer decides to dissolve; and
- certain other circumstances specified by law or administrative regulations.

Employees subject to termination on any of these bases are entitled to severance.

Severance

An employee whose employment is terminated unilaterally, by mutual agreement, or for other reasons may be entitled to severance from their employer. Severance payments are typically calculated at the rate of one month's salary for each full year of employment; for this purpose, a period of employment greater than six months counts as one year and a period of less than six months counts as one half year.

In principle, each month of severance payable is determined based on the employee's average monthly salary over the previous 12 months. Limitations apply. An employee's average monthly salary is capped at three times the local monthly average wage; where this cap applies, the eligi-

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ble years of employment occurring after 2008 are also capped at 12 years.

4.5 Employee Representations

Chinese law does not require employees to be formally represented, either by a trade union or an employee representative congress. Foreign-invested companies do not typically form these representative bodies. An employer is required to consult with its employees or their representatives in instances where the employer seeks to adopt or amend the employee manual, handbook, or other sets of rules, or change substantial matters that involve the interests of employees, such as remuneration, working hours, days off and personal leave, work safety and health, insurance and benefits, training, and discipline. In addition, an employer is required to consult with the relevant trade union or all employees before implementing an economic lay-off plan.

5. TAX LAW

5.1 Taxes Applicable to Employees/Employers

Chinese law generally requires employers to withhold income taxes and social benefits contributions from wages, salaries, bonuses, and other amounts payable to their employees.

Individual Income Tax

Employees are subject to individual income tax on their wages and salaries, which is levied at graduated rates ranging from 3% to 45%. Employees are allowed a general deduction from taxable income each year of CNY60,000 as well as deductions for certain social benefits contributions and applicable special deductions.

Social Benefits Contributions

Employers and their employees who work in China are generally required to contribute to the country's social benefits scheme, which is

composed of the housing provident fund and mandatory social insurances – ie, medical insurance, unemployment insurance, maternity insurance, work-related injury insurance, and pension insurance.

Social benefits contribution rates vary by locality, with the employee's and the employer's share being approximately 10% and 35%, respectively, of the contribution base. The contribution base is set at a minimum of 60% and a maximum of 300% of the local average monthly salary.

5.2 Taxes Applicable to Businesses

China primarily taxes economic activity by levying corporate income and value-added taxes. Other taxes include consumption tax, customs duties, land appreciation tax, real estate tax, stamp duty, and local surcharges.

Corporate Income Tax

Chinese tax resident companies are subject to a corporate income tax (CIT) on worldwide taxable profits at a uniform rate of 25%. Tax resident companies include companies that are established under Chinese law and companies that are established in another jurisdiction but have their effective management located inside China.

Non-Chinese tax resident companies are subject to 25% CIT on taxable profits attributable to their permanent establishments within China. China-sourced income that non-resident companies receive that is not attributable to a permanent establishment is generally subject to a 10% CIT withholding tax. Withholding taxes are generally imposed on passive income, such as dividends, interest, royalties, and capital gains, and may be reduced under tax treaties or other arrangements.

Value-Added Tax

China imposes a value-added tax on the business-related provision of goods, intangible and

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immovable properties, and taxable services, and on the importation of goods into China. Applicable rates are as follows:

- 13% for the sale and importation of most goods, the provision of repairs, replacement and processing services, and the leasing of tangible movable properties;
- 9% for the sale and importation of exceptional goods, the provision of transportation services, postal services, basic telecommunication services and construction services, the leasing and sale of immovable property, and the transfer of land use rights;
- 6% for the provision of value-added telecommunication services, financial services, modern services (eg, information services) and consumer services, and sales of other intangible properties; and
- 0% for the exportation of goods and certain services.

Small-scale VAT taxpayers are usually taxed at a levy rate of 3%, unless otherwise stipulated. From 1 April 2022 to 31 December 2022, certain small-scale VAT taxpayers (with annual taxable sales of less than CNY5 million) are exempt from paying or prepaying the 3% levy.

General VAT taxpayers are entitled to a credit against output VAT for input VAT that has been levied on purchased goods and services. Taxpayers may be entitled to a credit or refund of input VAT on exported goods and zero-rated services.

5.3 Available Tax Credits/Incentives

CIT Incentives

Certain tax resident companies may be eligible for a preferential 15% CIT rate. Eligible companies include qualified hi-tech enterprises, advanced services enterprises, small and thin-profit enterprises, enterprises that are active in encouraged industries in China's central, west-

ern, or north-eastern regions, and enterprises that are active in specified regions that encourage investment, such as the Hainan Free Trade Port.

From 1 January 2022 to 31 December 2024, small thin-profit enterprises are subject to a reduced 20% CIT rate on only 12.5% of their annual taxable income up to CNY1 million (ie, the effective CIT rate is 2.5%). For the portion of annual taxable income between CNY1 million and CNY3 million, only 50% of the income is taxable at the reduced 20% rate (ie, the effective CIT rate is 10%).

Tax resident companies may also qualify for super deductions of R&D expenses, accelerated depreciation, and foreign tax credits.

VAT Incentives

VAT exemptions may be granted for the provision of qualified services, such as educational, medical, religious, or culture-related services; certain financial services; technology-related services; and certain exported services.

Qualified general VAT taxpayers engaging in four specified industries may receive a 10% or 15% weighted deduction for creditable input VAT from 1 April 2019 to 31 December 2022, these industries are postal services, telecommunications services, modern services (eg, information services), and livelihood services.

5.4 Tax Consolidation

Consolidated tax filings are generally permissible only for a company and its branches, which are considered dependent legal entities. Besides branch consolidations, tax consolidations are allowed on a limited basis for specified wholly owned holding companies of large corporate groups, upon approval and announcement by the national tax authority.

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5.5 Thin Capitalisation Rules and Other Limitations

Related-party loans are subject to thin capitalisation rules, which state that a borrower's debt-to-equity ratio in China cannot exceed 5:1 for financial companies and 2:1 for other companies. A borrower whose debt-equity ratio exceeds the relevant threshold may be unable to deduct interest payments for CIT purposes, unless the borrower establishes with the tax authority that the lending is made at arm's length.

5.6 Transfer Pricing

In China, transfer pricing rules apply to related-party transactions based on the arm's-length principle, which means related parties to a transaction are expected to undertake that transaction as if they were independent and not subject to undue influence. Parties can be considered related by shareholding or "control" through, for example, loans, IP licensing, business operations, or management.

Chinese law requires contemporaneous documentation of related-party transactions upon reaching a specified value threshold. This documentation includes a detailed analysis of the functions and risks of the related parties and prices in comparable transactions. Companies may apply to the authorities for advance pricing arrangements to mitigate transfer pricing risk.

5.7 Anti-evasion Rules

CIT provisions contain broad anti-evasion measures, including for thin capitalisation, transfer pricing, and controlled foreign corporations. Notably, the tax authorities tend to scrutinise the indirect offshore transfer of assets taxable in China, which include equity in Chinese companies, China situs real estate, and assets connected to Chinese permanent establishments.

If a Chinese tax authority deems an indirect transfer by an offshore company to be an

attempt to evade CIT without a bona fide business purpose, the authority can levy taxes on the domestic transferor based on the substance-over-form principle.

6. COMPETITION LAW

6.1 Merger Control Notification

Under the Anti-monopoly Law of the PRC (AML) a merger filing to SAMR is generally required when an underlying transaction qualifies as a "concentration" and either of the two relevant business turnover thresholds is met. Such transactions may not be completed before SAMR issues a clearance decision. Offshore transactions can also be subject to the merger control rules.

The essence of a "concentration" is the possession or acquisition of control. This control may be through positive control, such as shareholder voting rights, or through negative control, such as veto rights over certain critical matters. The business turnover thresholds are as follows.

- Worldwide turnover – the combined worldwide turnover of all the undertakings participating in the concentration exceeds CNY10 billion in the previous fiscal year, and at least two of the undertakings participating in the concentration each has turnover in China in excess of CNY400 million in the previous fiscal year.
- China turnover – the combined turnover in China of all the undertakings participating in the concentration exceeds CNY2 billion in the previous fiscal year, and at least two of the undertakings participating in the concentration each has turnover in China in excess of CNY400 million in the previous fiscal year.

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6.2 Merger Control Procedure

Merger filings may be made under either normal or simple filing procedures. The simple filing procedure is available for transactions that do not raise competition concerns based on market share thresholds and certain other criteria. Simple procedure filings are typically cleared within 30 calendar days of case establishment. For normal procedure filings, the entire process is 180 days (30 days for Phase I review, 90 days for Phase II review, and 60 days for Phase III review).

If SAMR identifies competition concerns during the review process, SAMR may request the parties to propose remedies to address such concerns. The remedy proposal is subject to negotiations with SAMR and comments from key stakeholders. SAMR will conditionally approve the transaction with remedies if the remedies can address the competition concerns. If not, SAMR is authorised to block the transaction.

Under current law, the statutory period for a merger review case does not stop after SAMR officially accepts the case. SAMR will, in practice, sometimes require undertakings to withdraw a notification to technically extend the period of review. A recent amendment to the AML provides for a stop-clock mechanism in the merger review process (see **9. Looking Forward** for further discussion).

6.3 Cartels

Chinese law prohibits undertakings with a competitive relationship from concluding anti-competitive agreements. These agreements are classified either as horizontal monopoly agreements or vertical monopoly agreements. Certain exemptions and a leniency programme exist with respect to anti-competitive agreements and practices.

Horizontal Monopoly Agreements

Undertakings are prohibited from reaching monopoly agreements with their competitors concerning prices, production or sales volumes, allocation of markets, restrictions on R&D, joint boycotts, and other matters.

Vertical Monopoly Agreements

Undertakings are prohibited from reaching monopoly agreements with transaction counterparties such as suppliers, distributors, and customers concerning fixing resale prices and restricting minimum resale prices (RPMs). The lawfulness of agreements with transaction counterparties concerning other matters requires additional analysis as to their impact on competition. In civil litigation (as opposed to administrative litigation), courts also tend to closely analyse the competitive impact of RPMs rather than prohibiting them outright. For future changes to RPMs, see **9. Looking Forward**.

Exemptions

Agreements falling into the scope of prohibited monopoly agreements can be exempted from the general prohibition on monopoly agreements if specific conditions are met, including:

- the agreement has a qualifying purpose, such as technological advancement and/or product development, improvement of product quality, increases in efficiency and reductions in cost;
- the agreement will not substantially restrict competition in the relevant market(s); and
- consumers can receive a fair share of the resulting benefits.

Agreements entered by undertakings to safeguard legitimate interests in foreign trade and foreign economic co-operation can be exempted from meeting the conditions above.

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Leniency

Undertakings that conclude monopoly agreements in China are entitled to come forward and apply for leniency with SAMR, a mechanism similar to those in the European Union and the USA. Penalty waivers or reductions may be available to an applicant based on multiple factors, including the timing of the voluntary reporting and the importance of the inculpatory evidence the applicant provides. Generally, the first party to come forward is eligible for waived or significantly reduced fines (over 80%), provided that it offers important evidence proving the existence of the anti-competitive practices. Likely, the second and third parties to report themselves may also be rewarded reduced fines on a progressively decreasing basis.

Commitments

Undertakings being investigated for concluding or implementing monopoly agreements (excluding horizontal agreements concerning prices, volumes, and market division) may make commitments and offer detailed plans to correct their wrongdoings in exchange for the suspension, and eventual closing, of the investigation. This mechanism also applies to investigations into abuse of market dominance.

6.4 Abuse of Dominant Position

A number of factors are taken into consideration when assessing the market dominance of an undertaking, including its market share, its ability to control sales or procurement market(s), its financial and technological strength, the degree to which it is relied upon by other undertakings, and the ease of other undertakings to enter the relevant market. Market dominance is rebuttably presumed to exist if the market share thresholds are met. For example, an undertaking is presumed to hold market dominance if its market share reaches or exceeds 50%. In making assessments, SAMR and the courts have shown

a clear preference for official Chinese government data and third-party data.

An undertaking with market dominance is prohibited from engaging in abusive conduct without justification, which includes selling at unfairly high prices, predatory pricing, refusing to deal, exclusive dealing, bundling, or imposing discriminatory or other unreasonable conditions.

Unfair Competition

The Anti-unfair Competition Law of the PRC (AUCL) has been one of the most frequently enforced laws in China in the past decade, particularly in respect of commercial bribery and advertising violations. China relies on the AUCL to regulate unfair competition behaviours separately from the specialised AML. The AUCL, however, retains certain provisions that address competition among digital and other undertakings that possibly overlap with anti-monopoly provisions, such as technical measures that harm competition or otherwise hinder or damage the products or services of competitors.

The AUCL initially came into force in 1993 and has since been revised and amended, effective 1 January 2018 and 23 April 2019, respectively. The 2019 amendment mainly enhanced trade secret protections and increased fines and damages for unfair competition behaviours.

The AUCL mainly regulates the following types of unfair competition behaviours:

- causing an undertaking's products to be confused with the well-known products of another undertaking;
- seeking transaction opportunities or competitive advantage by using monies, assets, or other means to bribe the employees of a transaction counterparty, organisations or individuals that are entrusted by the transaction counterparty, or organisations or indi-

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viduals likely to use power of authority or influence to affect the transaction;

- misrepresentation of products;
- infringement of trade secrets;
- disallowed prize-attached sales;
- fabricating or disseminating false or misleading information to harm the goodwill or product reputation of competitors; and
- the disruption of the normal operation of cyber products or services provided legitimately by other undertakings in specified ways.

SAMR and its local counterparts have the authority to investigate violations of the AUCL and to impose administrative penalties, which include monetary fines, the confiscation of illegal gains, orders to cease violations, the revocation of business licences, and recording enterprises' violations in the social credit system.

The AUCL is also widely cited in civil proceedings in China and the Supreme People's Court has issued multiple judicial interpretations to clarify the application of the law. In addition to the above-mentioned unfair competition behaviours, in a civil proceeding, any behaviour may be deemed wrongful if it breaches any of the principles of voluntariness, equality, fairness, and good faith or fails to abide by business ethics.

7. INTELLECTUAL PROPERTY

7.1 Patents

Invention-Creations in China

The Patent Law of the PRC (the "Patent Law") came into effect in the 1980s and has since been periodically amended to more closely conform to international standards, most recently in 2020. The Patent Law affords patent right protections for invention-creations, which include

inventions, utility models, and designs. The law defines these concepts as follows.

- Inventions – new technical solutions proposed for a product, a process or the improvement thereof.
- Utility models – new technical solutions proposed for the shape and structure of a product, or the combination thereof, which are fit for practical use.
- Designs – with respect to a product, new designs of the shape, pattern, or the combination thereof, or the combination of colour with shape and pattern of the overall product or a part thereof, which are rich in an aesthetic appeal and are fit for industrial application.

Patent Filings

The China National Intellectual Property Administration (CNIPA) Patent Office is the designated authority for the acceptance, publication, and examination of patent applications and the granting of patent rights. The CNIPA Patent Office also reconsiders rejected patent applications and grants patent invalidation requests.

Patent applications in China can be made in the following three ways.

- Direct filing – an applicant may directly file with the CNIPA Patent Office through a Chinese patent agent; the application must be in Chinese.
- Paris Convention – within 12 months of an invention or utility model patent being filed for outside of China (or six months for a design patent), the applicant can file the same in China and claim priority to the overseas application.
- Patent Cooperation Treaty (PCT) application – a foreign applicant can file a PCT application in its home country and select China as one of the designated countries for the application to enter the national phase in China.

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Patent Terms

Patent grants are valid beginning from the date of application. Invention patents are valid for 20 years, utility model patents are valid for ten years, and design patents are valid for 15 years.

Invention patentees may now request protection period compensation for unreasonable delays during the examination process. Specifically, an invention patentee may request CNIPA to grant protection period compensation if an invention patent is granted at least four years from the filing date and at least three years from the date of the substantive examination request, except where such delays are caused by the patentee.

Patent Enforcement and Compensation

In cases of infringement, a patent owner can choose to file an administrative complaint with SAMR or initiate a lawsuit with a competent court. In either case, the patent owner can obtain injunctive relief if infringement is found to exist. Patent owners tend to favour litigation to enforce their rights because SAMR administrative actions are not final and may be appealed to a competent court for judicial review.

Courts can award patent owners compensatory damages and up to quintuple punitive damages in cases of wilful and severe infringement. Damages are calculated based on the right owner's actual losses, the infringer's gains, or reference to multiples of the patent licensing fee where actual infringement losses and gains are difficult to calculate. Statutory damages for patent infringement are between CNY30,000 and CNY5 million.

7.2 Trade Marks

Trade Marks in China

Registered trade marks in China include trade marks for goods and services, collective marks, and certification marks. A mark is generally registrable where it distinguishes the goods or

services of one seller or provider from those of others, including any word, device, letter, number, 3D mark, colour combination, sound, or any combination of these elements.

Trade Mark Registrations

The CNIPA Trade Mark Office is the designated trade mark approval and registration authority. Trade mark applications generally require one year for approval. An applicant can claim priority within six months after the same application is filed outside of China or if the mark is used in an exhibition recognised by the Chinese authorities. A trade mark may be registered in China in two ways:

- direct filing – direct filings with the Trade Mark Office must be made through a Chinese trade mark agent, the application must be prepared in Chinese; or
- Madrid System – foreign applicants can file a Madrid application in their home country (if applicable) and select China as one of the designated countries for the application.

Trade Mark Terms

A trade mark registration is valid for ten years from the date it is approved. The registrant can file a renewal application within 12 months before the end of each successive ten-year period following the date of registration, or within a grace period of six months thereafter.

Trade Mark Enforcement and Compensation

In cases of infringement, a trade mark owner can choose to file an administrative complaint with SAMR or initiate a lawsuit with a competent court. Administrative penalties include no more than five times the illegal turnover or no more than CNY250,000 in fines if the illegal turnover is less than CNY50,000.

Courts can award trade mark owners compensatory damages and up to quintuple punitive

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damages in cases of wilful and severe infringement. Damages are calculated based on the right owner's actual losses, the infringer's gains, or by reference to multiples of the trade mark licensing fee where actual infringement losses and gains are difficult to calculate. The maximum statutory damages for trade mark infringement are CNY5 million.

7.3 Industrial Design

Industrial designs are eligible for protection in China under the Patent Law, the Trade Mark Law of the PRC (the "Trade Mark Law"), the Copyright Law of the PRC (the "Copyright Law"), and the AUCL as described below.

- Patent Law – industrial designs are expressly eligible for patent protection as designs.
- Copyright Law – given their creative and aesthetic nature, industrial designs can be regarded as protectable works under the Copyright Law with respect to their device, shape, colour, or combination thereof.
- Trade Mark Law – industrial designs may be registrable as trade marks where they can identify the source of a product or distinguish the seller or provider, or can be used for such purpose.
- AUCL – industrial designs can be considered a packaging or trade dress; in which case they may enjoy protection under the AUCL if they are sufficiently known to the public.

Terms of protection, enforcement, and remedies with respect to industrial design rights are the same as those described in the sections on patents, trade marks, and copyright.

7.4 Copyright Copyright in China

Copyright is the exclusive right of authors in literary, artistic, and scientific works. In China, copyright protectable works include the following:

- written works;
- oral works;
- musical, dramatic, operatic, dance or acrobatic artistic works;
- art or architectural works;
- photographic works;
- audio-visual works;
- graphic and model works, such as engineering design plans, product design plans, maps, schematic diagrams;
- computer software; and
- other intellectual achievements that have the characteristics of works.

Copyright Terms

Authors are not time-limited with respect to their rights of authorship, revision, and integrity. The right of publication and other statutory copyrights of an individual are valid for the individual's life span plus 50 years. If it is a work of a legal person, these rights are valid for 50 years after the first publication. In the case of audio-visual works, the right of publication and other statutory copyrights are valid for 50 years after the first publication.

Copyright arises upon the creation of a work and need not be registered. Nevertheless, authors may register their copyrights with the National Copyright Administration of China (NCAC), which can be used as evidence of ownership in cases of enforcement. In the case of a commissioned work, the commissioned party owns the copyright, unless agreed otherwise.

Copyright Enforcement and Compensation

In cases of infringement, a copyright owner can choose to file an administrative complaint with NCAC or initiate a lawsuit with a competent court. Administrative penalties include no more than five times the illegal turnover or no more than CNY250,000 in fines if the illegal turnover is less than CNY50,000.

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Courts can award copyright owners compensatory damages and up to quintuple punitive damages in cases of wilful and severe infringement. Damages are calculated based on the right owner's actual losses, the infringer's gains, or by reference to multiples of the copyright licensing fee where actual infringement losses and gains are difficult to calculate. The maximum statutory damages for copyright infringement are CNY5 million.

7.5 Others

Software is generally protected by copyright. Software can also be patentable, such as industrial control software, internal performance enhancement software, and external data processing software. Software may also be protected as a trade secret.

Databases are principally protected by copyright, particularly where the compiling of data is considered an "intellectual achievement". Databases may also be protectable under the AUCL and the Civil Code of the PRC.

Trade secrets are protected principally under the AUCL, among other legal provisions. Trade secrets are commercial information, such as technical information and business information, that is not known to the public and that has commercial value, and which the right-holder has taken measures to keep secret. The misappropriation of trade secrets is subject to civil and/or criminal liabilities.

Lay-out designs are protected in China under the Regulations on Protection of Integrated Circuit Layout Design. A right-holder may file an application for registration with the CNIPA within two years from the date of the first commercial use of the layout design anywhere in the world. The regulations give a protection period of ten years for integrated circuit lay-out designs, from

the date of application for registration or the date of first commercial use.

Plant variety rights are protected in China under the Regulations of the PRC on Protection of New Varieties of Plants, which protect artificially cultivated plant varieties or those developed from discovered wild plants that possess novelty, distinctness, consistency and stability, and are duly named. The regulations provide a protection period from the date of grant of 20 years for vines, forest trees, fruit trees, and ornamental trees; and 15 years for other plants.

8. DATA PROTECTION

8.1 Applicable Regulations

Overview

China has strengthened its data protection laws in recent years, beginning in 2016 with the adoption of the Cybersecurity Law of the PRC (CSL), which stipulates principled personal information and data protection requirements for operators in the digital economy. Following this development, administrative departments issued a series of draft rules and voluntary national standards in this area, principally the Personal Information Security Specification (GB/T 35273-2020).

These administrative efforts were made in advance of specialised laws on data and personal information protection, namely the Data Security Law of the PRC (DSL), adopted on 10 June 2021, and the Personal Information Protection Law of the PRC (PIPL), adopted on 20 August 2021. 2021 thus proved to be a milestone for data protection in China – the CSL, the DSL, and the PIPL together represent "three pillars" of China's data protection framework and enable a broader regulatory architecture governing data processing and cybersecurity issues.

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China's data protection framework also comprises legal and regulatory provisions specific to certain industries and contexts. These include sensitive industries such as connected vehicles, telecoms, banking, healthcare, e-commerce, postal services, cloud services, online payments, online mapping, and ride-sharing platforms, among others. Provisions of laws also govern data protection in the contexts of privacy and personal information protection (eg, the Criminal Law of the PRC and the Civil Code of the PRC) and State secrets (eg, the Law of the PRC on Guarding State Secrets), among others.

Principal Data Protection Laws

The CSL serves as the foundational data protection law in China, firstly establishing a legal framework for cyber-sovereignty, network security, and personal information and data protection. The CSL imposes various requirements and obligations on network operators and more stringent requirements on operators of critical information infrastructure ("CII operators"), which include data localisation and security assessments of cross-border data transfers.

The DSL principally governs data processing activities and security supervision of such activities within China, reiterating the main requirements under the CSL and calling for enhanced protection of certain sensitive types of data. The DSL also imposes more severe penalties on organisations and individuals that violate important data protection requirements, increases risk monitoring and reporting requirements, and further regulates cross-border data transfers.

Unlike the security-centric provisions of the CSL and the DSL, the PIPL principally governs personal information protection. The PIPL provides in law for the first time a comprehensive set of rules around the collection and use of personal information, which to a certain extent is influenced by and modelled after the EU's General

Data Protection Regulation. The PIPL introduces several legal bases for personal information collection and processing, specifies lawful means of transferring personal information across borders, and offers personal information subjects a greater level of protection and control over their personal information. In addition, the PIPL imposes high penalties for violations, capping penalties at CNY50 million or 5% of the annual turnover in the prior year.

Data Classification Scheme

China's data protection framework envisions a data classification scheme that has significant implications for foreign investment and multinational business operations in China. These data classifications remain under development and include the following.

- State secrets.
- Sensitive data comprising:
 - (a) national core data;
 - (b) important data; and
 - (c) specified industrial, healthcare, and other data (eg, online mapping, human genetic resources).
- Personal data comprising:
 - (a) sensitive personal information; and
 - (b) personal information.

Note that these classifications are presumed not to be mutually exclusive; eg, specified forms of data could also be classed as important data or national core data.

Entity Classification Scheme

China's data classification scheme underlies a related entity classification scheme that primarily comprises two classes: CII operator and large personal information handler ("large PI handler"). These are defined as follows.

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- CII operators are generally defined as entities that operate network infrastructures and important information systems:
 - (a) in important industries and fields such as public telecoms and information systems, energy, transportation, water resources, finance, public services, e-government, and national defence science and technology; or
 - (b) which, if damaged, disrupted, or subject to a data leak, may seriously threaten national security, people's livelihood, or the public interest.
- Large PI handlers are considered those entities that hold personal information in excess of a specified quantity. The competent administrative department has yet to announce this quantity.

In general, these entities are imposed with more stringent data protection obligations, as they are considered important to the nation and the public.

Appointment of Personnel for Data Protection and Compliance

The CSL, the DSL, and the PIPL, impose the mandatory requirements for appointing appropriate persons responsible for data protection and compliance, specifically:

- the CSL requires domestic entities to appoint an officer with the general responsibility of overseeing cybersecurity matters;
- furthermore, the DSL sets out that domestic entities that process important data must appoint a data security officer to be in charge of data security; and
- the PIPL requires domestic entities appoint a personal information protection officer if they handle personal information in a quantity reaching a specified threshold, responsible for conducting supervision of personal information handling activities – in addition, offshore

entities, subject to the PIPL, are required to set up a dedicated entity or appoint a representative in China to be responsible for personal information protection matters and report to supervisory authorities.

For now, no clear rules have been issued specifying (i) the relationship between the above officers and the qualification standards and experience requirements for such officers, or (ii) the thresholds for triggering the officer requirement under the PIPL.

8.2 Geographical Scope Extraterritoriality

The CSL and the DSL are limited in terms of their extraterritorial reach, as they apply principally to domestic networks and data processing activities, respectively. However, the laws reserve the right to investigate and impose liability on offshore actors that harm domestic interests. As a practical matter, the Chinese authorities are empowered to block domestic access to foreign networks and websites that are deemed to be in violation of Chinese law.

By contrast, the PIPL applies extraterritorially to offshore individuals and entities that process personal information of Chinese residents for the purpose of:

- providing products or services to such persons within China;
- analysing or evaluating the behaviours of such persons within China; or
- other circumstances provided by any law or regulation.

Data Localisation and Cross-Border Transfer Restrictions

China imposes requirements for data localisation and cross-border data transfers, which have become an increasing concern especially among multinationals. In general, “data localisa-

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tion” refers to the local storage of data collected or generated within China; this localised data is then subject to restrictions on their cross-border transfer, which range from a security assessment to outright prohibition.

Under China’s data protection framework, CII operators are required to localise the important data and personal information they collect or generate in China. Large PI handlers are required to localise the personal information they collect or generate in China. The departmental rules intended to implement these requirements have not been formally promulgated.

Provision of Data to Foreign Authorities

According to the DSL, a request for data made by a foreign law enforcement or judicial authority is subject to the approval of the Chinese competent authorities (i) in accordance with relevant laws and international treaties or agreements concluded or acceded to by China, or (ii) in accordance with the principles of equality and reciprocity. This provision underscores China’s position that approval is required to submit data to foreign authorities, such as in response to subpoenas as part of a foreign judicial proceeding or regulatory investigation.

Similar provisions exist in other laws, including the PIPL, the Civil Procedure Law of the PRC, the Securities Law of the PRC, and the Law of the PRC on International Judicial Assistance in Criminal Matters.

8.3 Role and Authority of the Data Protection Agency

In general, four major administrative departments are in charge of enforcing data protection rules in China:

- the Cyberspace Administration of China (CAC);
- the Ministry of Public Security (MPS);

- the Ministry of Industry and Information Technology (MIIT); and
- the State Administration for Market Regulation (SAMR).

Among these, CAC is responsible for overall planning with regard to data protection and cybersecurity, and co-ordinates with other competent departments, while MIIT, MPS, SAMR, and others are responsible for the supervision and administration of data protection within their respective scopes of authority.

CAC

CAC was established on 4 May 2011 and later empowered by the State Council on 26 August 2014 “to be in charge of the administration of Internet-based information content nationwide and of regulatory enforcement.” CAC implements the policies of the Office of the Central Cyberspace Affairs Commission, which shares the same administrative organisation as CAC and is under common leadership.

MPS

MPS “directs and supervises local public security organs in security monitoring work related to public information networks,” and is responsible for handling cyber and information-related crimes. Local MPS counterparts also serve as the registration authorities for information systems record-filings.

MIIT

MIIT, a department under the State Council, together with telecoms administrations at the provincial level, is responsible for:

- the administration of the internet industry, including of personal information;
- safeguarding cybersecurity and emergency management and resolution;
- the supervision, administration and security examination of telecommunications networks,

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- the internet and industrial control system networks;
- the establishment of telecommunications networks and information security systems; and
- drafting and organising the implementation of security administration policies, rules, and standards regarding the data security of telecommunications networks and the internet.

SAMR

SAMR is an authority under the State Council established in 2018 following the merger of the former State Administration for Industry and Commerce and several other agencies. SAMR and its local counterparts enforce provisions of the E-Commerce Law of the PRC, the Law of the PRC on the Protection of Consumer Rights and Interests, and the AUCL, among others, which are responsible for the protection of consumer rights (including those related to personal information). SAMR has corresponding power to impose administrative penalties for illegal conduct such as violating personal information protection rules. SAMR is also responsible for standards setting and issues national standards on data protection and other technical matters.

In addition, other industry administrative departments also supervise and manage data protection in accordance with their respective responsibilities.

9. LOOKING FORWARD

9.1 Upcoming Legal Reforms

Legislative changes are expected to occur in the near future, particularly with respect to the Company Law and the AML, according to the 2022 Legislative Work Plan of the Standing Committee of the National People's Congress (the "NPC Standing Committee"). Further administrative rule-making is also expected to implement provisions of the DSL, the PIPL, and the CSL.

Company Law (Draft Amendment)

On 24 December 2021, the NPC Standing Committee issued a draft amendment to the Company Law (2021 CL Draft Amendment), which was open for public comments through 22 January 2022. The draft would add or amend about 70 articles to the current Company Law.

Since the Foreign Investment Law came into effect, foreign-invested enterprises (FIEs) in China are now subject to the Company Law, which is equally applicable to all companies registered in China. According to the Foreign Investment Law, existing FIEs have five years (until December 31, 2024) to convert to the appropriate corporate form and to update their organisational documents to be compliant with the Company Law.

If the 2021 CL Draft Amendment is adopted largely in its current form, it may affect FIEs with respect to company formation, corporate governance, transfer of equity interest, duties of directors and officers, etc. Notable changes in the 2021 CL Draft Amendment with respect to FIEs include the following.

- Audit committee – a company would have the option to set up an audit committee under its board of directors that is responsible for supervising the company's financial and accounting matters; if so, the company would not require a board of supervisors (or a supervisor).
- Employee representative director – a company with 300 or more employees would be required to have at least one director among the board of directors who is selected by the employees and acts as their representative.
- Additional officer and director liability – directors, supervisors, and senior management could be liable to compensate for the company's losses where they knew or should have known that a shareholder failed to fulfil

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its capital contribution obligations and failed to take necessary actions.

- Consent to sale of interest not required – in the case of an equity transfer of an LLC, the selling shareholder would no longer be required to obtain the consent of a majority of the other existing shareholders. The selling shareholder would only need to notify the other shareholders about the price, payment method, and term of the equity transfer and offer them a pre-emption right to purchase the equity. If the other shareholders do not exercise such pre-emption right to purchase the equity within 30 days after the receipt of the notice, the selling shareholder would then be free to proceed to sell the equity to the proposed buyer.

Anti-monopoly Law Amended

On 24 June 2022, the NPC Standing Committee adopted an amendment to the AML (the “Amended AML”), which will enter into force on 1 August 2022. The Amended AML contains many significant changes, the highlights of which include the following.

- Enhanced penalties – the Amended AML will significantly increase penalties, especially for merger filings, to up to 10% of prior year turnover; fines of up to CNY1 million may be imposed on the legal representatives, primary persons responsible, and others directly responsible for the conclusion of monopoly agreements.
- Change of RPM legal status – under the current regime, SAMR takes the view that price-related RPMs are per se illegal, while China’s courts require in-depth analysis as to their anti-competitive effect as opposed to prohibiting them outright in civil litigation where law enforcement is not involved (see **6.3 Cartels**). The Amended AML provides that RPMs are “prohibited in principle”, while also allow-
- ing undertakings to directly establish that an RPM is not anti-competitive.
- Safe harbour – a market share-based safe harbour will be established for less restrictive monopoly agreements.
- Third-party liability – third-party undertakings will be held liable where they organise or substantively assist in reaching a monopoly agreement in the same manner as parties to the agreement. This could help address the dilemma of deterring organisers who contribute to the reach of horizontal monopoly agreements but are not parties thereto.
- Stop-clock rules – the Amended AML will introduce stop-clock rules for merger reviews covering scenarios such as undertakings that fail to submit adequate materials, discovery of significant and new facts, and assessing the necessity of restrictive remedies; this will replace the current withdraw-refile practice upon expiry of the 180-day statutory time limit.
- Mandatory merger review – SAMR will be expressly required to ramp up merger review of filings concerning livelihood, finance, technology, and media.
- Public interest litigation – public procurators will be allowed to institute public-interest litigation where social public interests are harmed by monopoly agreements, abuses of dominant market position, or merger filings; the expansiveness of “social public interests” could significantly increase the risk of litigation to undertakings.
- Criminal liability – the Amended AML provides a stand-alone clause imposing criminal liability in instances where an AML violation constitutes a crime.

In addition to the Amended AML, another recent milestone event was the establishment of the State Anti-monopoly Bureau (SAB) on 18 November 2021. The result of a governmental reorganisation, the SAB ranks higher among

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administrative departments than SAMR's anti-monopoly bureau. The SAB is afforded significantly more law enforcement head count to cope with the increased enforcement needs and is considered to symbolise a new era in China's anti-monopoly regime.

Data Protection – Clarification and Implementation of the PIPL and the DSL

The year 2021 was a milestone for the development of China's data protection framework, and most notable is the promulgation of the PIPL and DSL. The PIPL and DSL respond to pressing issues and challenges in current industry and legal practice. Going forward, the authors expect to see further administrative rule-making and enforcement in respect of data protection, including:

- catalogues that define categories of national core data and important data and the detailed rules for processing such data;
- departmental rules for identifying CII in respective industries and detailed requirements and obligations for CII operators;
- clarification of data localisation thresholds and cross-border transfer requirements;
- rules further specifying the relationship as well as requirements for appointing responsible officer/entities/representatives for data protection and compliance matters; and
- departmental rules that implement specific provisions of the DSL and the PIPL.

Data protection compliance promises to be a critical area for compliance in 2022 and into the future.

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Trends and Developments

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Foreign Direct Investment

China has continued to move forward with its long-term vision of foreign investment liberalisation, as shown by further revisions to the Negative List-related provisions on foreign investment, which act to restrict foreign investment in sensitive areas. Despite this, some foreign investors have expressed concerns lately regarding supply chain disruptions due to the implementation of strict COVID-19 prevention measures.

Company Law to be amended

On 24 December 2021, the Standing Committee of the National People's Congress (the "NPC Standing Committee") issued a draft amendment to the Company Law of the PRC, which was open for public comments until 22 January 2022. The amendment is expected to be adopted sometime in 2022 and may affect, among other things, the corporate governance structure of companies in China, including foreign-invested enterprises. For details of the changes proposed in the current draft amendment, see **9. Looking Forward** in the China Law & Practice chapter in this guide.

Negative List developments

China stipulates industries and economic activities that are subject to foreign investment restrictions in the Special Administrative Measures for the Access of Foreign Investment (the "National Negative List"). The latest version was issued on 27 December 2021 and became effective on 1 January 2022. While the National Negative List is obviously national in its scope, the Chinese authorities also implement negative lists that are regional in scope or applicable in designated economic development zones. Among these

negative lists, the free trade zone negative list (the "FTZ Negative List") applies to the 21 FTZs in China. While the two lists contain generally the same provisions, the FTZ Negative List tends to be more liberal and currently has 27 restricted items compared to 31 in the National Negative List.

Aside from the continuing reduction of restricted items, the most notable development for the 2021 National Negative List was the explanatory notes on overseas listing that appeared for the first time. The 2021 National Negative List provides that Chinese companies operating in fields prohibited to foreign investment are permitted to be listed on overseas stock markets, provided that the listing is pre-approved by the competent authorities. Foreign investors may not participate in the operation and management of such companies and the equity ratio of foreign investors in the company will be governed by the relevant rules, such as under the "qualified foreign institutional investors" (QFII) scheme, the "RMB qualified foreign institutional investors" (RQFII) scheme, and the stock market transaction interconnection mechanism. The rationale for this is that foreign financial investment in prohibited industries appearing on the Negative List is permitted only through the narrow exception of overseas listings.

Since first issuing the National Negative List in 2018, China has excelled at using the negative list approach to manage foreign investment and investor expectations in the context of a gradual, measured opening up. It is reported that the Chinese authorities are revising the Negative Lists to further liberalise the market for foreign invest-

tors, and we expect restrictions to be loosened further, particularly in the services sector.

Hainan Negative List on cross-border trade in services

Chinese authorities issued, on 23 July 2021, the Special Administrative Measures for Cross-Border Trade in Services in Hainan Free Trade Port (Hainan TIS Negative List). The Hainan TIS Negative List is the first negative list published in the field of cross-border trade in services and differs from Hainan's existing negative list, issued in 2020, which focuses on foreign investment access.

The Hainan TIS Negative List stipulates 70 special management measures in 11 categories for overseas service providers. In all areas outside the list, in the Hainan Free Trade Port, domestic and foreign service providers are treated equally and have equal access to cross-border trade in services. According to the Ministry of Commerce, the liberalisation provided by the Hainan TIS Negative List goes beyond China's commitments for WTO accession and its main free trade agreements (including the Regional Comprehensive Economic Partnership Agreement) in corresponding areas.

Amendment to the Provisions on Administration of Foreign-Invested Telecommunications Enterprises

On 7 April 2022, the State Council promulgated its Decision on Amending and Annuling Certain Administrative Regulations (the "Decision"), which took effect on 1 May 2022. The Decision amends, among other regulations, the Provisions on Administration of Foreign-Invested Telecommunications Enterprises (the "Foreign-Funded Telecoms Provisions").

As amended, the Foreign-Funded Telecoms Provisions modify the definition of a foreign-invested telecoms enterprise to conform to the

Foreign Investment Law and remove provisions that have become obsolete since the Foreign Investment Law entered into force.

According to the Foreign-Funded Telecoms Provisions, foreign investors operating value-added telecoms services are no longer required to have a good track record and operational experience in telecoms services, which offers substantial qualification relief to foreign investors in this category.

The Foreign-Funded Telecoms Provisions also simplify the permit application process and shorten the statutory time limit for examination, which will establish a more efficient process for foreign-invested telecoms enterprises to apply for a telecoms operating permit and reduce the uncertainties imposed on the applicants' business operations due to a prolonged examination process.

Data Protection

China's data protection legal framework continues to develop and promises to be a critical area for compliance going forward. Following China's 2016 adoption of the Cybersecurity Law of the PRC (CSL) – the first law in China to specifically call for data protection – administrative authorities have successively issued voluntary national standards and proposed rules in this area. In 2021, these efforts culminated in the adoption and effectiveness of the Data Security Law of the PRC (DSL) and the Personal Information Protection Law of the PRC (PIPL). These laws serve as pillars of China's data protection legal framework.

Data Security Law becomes effective

On 10 June 2021, the NPC Standing Committee formally adopted the DSL, a specialised law in the field of data security that came into effect on 1 September 2021. The law declares China's policy objectives on data security, protection

and use; imposes obligations on data processors; and offers a series of principled framework provisions that will guide future administrative rule-making in this area.

Data policy objectives

The DSL concisely reiterates China's long-held policy objectives with regard to data, namely that it is intended to "regulate data processing activities, guarantee data security, promote the development and utilisation of data, protect the legitimate rights and interests of individuals and organisations, and safeguard the sovereignty, security and development interests of the State."

Data administration

The DSL divides data security responsibilities among the central government, local governments, and industry departments and associations. "Important data" remains loosely defined, but the law calls for the co-ordination of the relevant administrative departments to formulate catalogues of important data and authorises local and industry-competent departments to also formulate catalogues. It is therefore expected that further clarity with respect to defining important data will soon be provided, which will be critical for foreign investors grappling with data-related compliance matters.

Data processor requirements

The DSL sets out principled obligations for data processors to undertake during data-processing activities, such as establishing a comprehensive data security management system, organising data security education and training, and taking corresponding technical measures. Whilst the CSL stipulates such requirements for network operations, further refinement of these requirements for data processing is expected.

Data transaction systems

Data exchanges have been established in China in recent years. These exchanges, and

data transaction partnerships, have become important data sources for market players in fields such as financial risk control and credit investigation, advertising media, map surveying, and healthcare. The DSL recognises these data transactions and service providers and promotes data transaction activities.

Personal Information Protection Law becomes effective

On 20 August 2021, the NPC Standing Committee formally adopted the Personal Information Protection Law of the PRC (PIPL), which entered into force on 1 November 2021. The PIPL is a landmark piece of legislation that governs personal information (PI) in China and has drawn comparisons to the EU's General Data Protection Regulation (GDPR). The PIPL contains many provisions that reiterate existing PI rights and protections stipulated in other laws, administrative regulations, and departmental rules. The following are particular highlights of the PIPL.

Legal bases for PI processing

The PIPL provides a series of legal bases for processing PI and expressly stipulates circumstances under which parties may process PI without the consent of the PI subject, an issue previously unaddressed in the CSL and other laws. According to the PIPL, the legal bases for PI processing are:

- consent of the PI subject;
- the processing being necessary for the conclusion or performance of a contract to which the PI subject is a party, or necessary for human resource management in accordance with lawful labour rules and regulations and lawful contracts;
- the processing being necessary for the performance of statutory duties or obligations;
- the processing being necessary for responding to public health incidents or for the pro-

- tection of life, health, and property safety in an emergency;
- the PI being reasonably processed for news reporting, media supervision, and other activities conducted in the public interest;
 - the PI being disclosed by the subject themselves or otherwise being lawfully disclosed; and
 - other circumstances as provided for by laws and administrative regulations.

Legal bases for cross-border PI transfers

The PIPL provides separate legal bases for the cross-border transfer of PI, which include:

- passing an administrative security assessment;
- obtaining a certification from a specialised institution;
- concluding a contract with an overseas recipient based on a standard contract formulated by the competent department; and
- other conditions stipulated by laws, administrative regulations, or the competent department.

To date, administrative regulations and departmental rules have yet to fully implement these legal bases. In addition, PI subjects must provide their “separate consent” to allow their PI to be transferred across borders and PI handlers must complete a PI protection impact assessment, a type of self-assessment, to evaluate potential risks before transferring PI across borders.

As a consequence, for now, many market players are optimising their internal compliance practices (eg, consent and assessment processes) and taking a wait-and-see approach to the implementation of legal bases for cross-border PI transfers.

PI localisation

The PIPL provides that certain parties must localise the PI they collect or generate in China, namely operators of critical information infrastructure and large-quantity PI handlers. Parties subject to localisation are allowed to transfer data across borders only where there are operational needs and upon completion of an administrative security assessment.

Further administrative rule-making is expected in this area to set the PI quantity threshold for large-quantity PI handlers and the details of the administrative security assessment, among other matters.

Extraterritorial effect

The PIPL has extraterritorial effect on offshore PI handlers in a manner considered similar to GDPR. Specifically, the PIPL may apply to offshore PI handlers who provide products or services to Chinese residents, or who analyse or evaluate the behaviours of Chinese residents, as well as in other specified circumstances. The PIPL further requires offshore PI handlers to set up a dedicated entity or appoint a representative in China to be responsible for PI protection matters and to report to supervisory authorities.

Regulations on Security Protection of CII promulgated

The State Council on 30 July 2021 promulgated the Regulations on Security Protection of Critical Information Infrastructure (the “Regulations”), which became effective on 1 September 2021. The Regulations reiterate principled provisions with respect to CII operators provided in the CSL while providing additional detail on, among other things:

- how the CII administrative identification process is intended to take shape;
- inter-departmental reporting functions; and

- the duties of each CII operator’s internal control function.

Revised Measures for Cybersecurity Review become effective

The Cyberspace Administration of China and 12 other departments and commissions jointly promulgated, on 28 December 2021, a revision to the Measures for Cybersecurity Review (Measures), which became effective on 15 February 2022. As revised, the Measures institute a review process for certain business activities that may have national security implications:

- CII operator procurement of network products and services; and
- online platform operator data-processing activities.

Notable among the revisions, online platform operators that handle the PI of more than one million individuals must submit to a cybersecurity review if they plan to publicly list in a foreign country. This provision formalises certain administrative actions taken in July 2021 against online ride hailing platform Didi Chuxing in response to its initial public offering in the United States of America. This requirement eventually caused Didi Chuxing to delist from the USA in the first half of 2022.

Competition Law

Starting in 2020, the Chinese leadership announced its intention to “curb market monopolies and prevent the disorderly expansion of capital.” Industry observers believe that this was a response to the public’s call for government intervention in China’s digital undertakings and the platform economy to curb monopolistic behaviours and to reduce the ubiquitous influence of the country’s internet giants.

This call to action has manifested in both legislative and enforcement fronts, which are addressed in turn below.

Competition law legislative developments

Anti-monopoly Law amended

On 24 June 2022, the NPC Standing Committee adopted an amendment to the Anti-monopoly Law of the PRC (the “Amended AML”), which will become effective on 1 August 2022. For details of the changes in the Amended AML, see **9. Looking Forward** in the China Law & Practice chapter in this guide. Prior to this, various amendment drafts to the AML were proposed by the State Administration for Market Regulation (SAMR), which solicited public comments in several rounds. The Amended AML provides some new mechanisms and systems, such as “stop-the-clock” and “safe harbour”, and it also greatly increases fines for failure to file cases.

Anti-monopoly administrative guidelines

The State Council Anti-monopoly Commission promulgated, on 7 February 2021, the Anti-monopoly Guidelines for the Platform Economy (the “Guidelines”). The Guidelines are intended to assist the Chinese authorities in curbing the abusive practices of major internet platforms. The Guidelines cover questionable behaviours by platform companies, including sales below cost, refusal to deal, tying or attaching unreasonable conditions to transactions, and discriminatory treatment. The Guidelines serve to assist SAMR in its enforcement actions and to warn the platform economy that these abusive practices will not be tolerated. To substantiate the regulation of internet platforms, the Amended AML expressly prescribes as a principle that companies should not engage in monopolistic behaviours while leveraging data, algorithms, technology, capital strength, or platform rules.

State Anti-monopoly Bureau

As a product of the reorganisation of SAMR's Anti-monopoly Bureau, the State Anti-monopoly Bureau (SAB) was officially established on 18 November 2021 and is afforded a higher ranking in the administrative hierarchy and more law enforcement resources, it remains, however, one level below a ministerial department under the PRC State Council.

Anti-monopoly “enforcement storm”

Dubbed the “enforcement storm”, SAMR and provincial AMRs have, since November 2020, engaged in an unprecedented number of anti-monopoly investigation and enforcement actions. By the end of 2021, SAMR has made public 143 decisions, a rate of approximately one decision every three days. These decisions cover monopoly agreements, abuse of market dominance, and merger control notification. Below are selected highlights and insights.

Notable anti-monopoly enforcement actions

The enforcement storm has involved investigations into China's most recognisable digital undertakings and has featured landmark penalty decisions against Alibaba and Meituan. In these two decisions, SAMR cited the undertakings' abuse of dominance, principally by imposing “choose one of two” exclusive dealing restrictions; imposed substantial fines (approximately CNY18.23 billion for Alibaba and approximately CNY3.43 billion for Meituan); and issued detailed guidelines instructing the undertakings' future behaviour.

Illegality of “choose one of two” practices

“Choose one of two” practices, pervasive in China's digital economy and the subject of widespread criticism, were one of the main triggers of the enforcement storm. These practices concerning retail platforms (Alibaba) and online food-delivery platforms (Meituan and Sherpa's) were determined by SAMR to be anti-competitive

and illegal for being a subcategory of transaction restrictions, which refers to an undertaking with market dominance that restricts the transactions of transaction counterparties without justification. Based on these decisions, it can be reasonably expected that fewer undertakings will adopt “choose one of two” policies in future, especially where the undertaking seeks to enforce the policy through disciplinary or penalty arrangements.

VIE-related deals must be notified

As part of its stepped-up enforcement actions, SAMR has issued failure-to-file penalty decisions against many of China's largest digital undertakings, such as Alibaba, Tencent, DiDi, and Meituan. In the past, these undertakings were unable to file their acquisition transactions for merger review because of the ambiguity surrounding the notifiability of variable interest entity (VIE)-structured undertakings. Now, it has become clear that a VIE structure is no longer an obstacle for merger filing.

As of 13 December 2021, SAMR has published 113 non-filing penalty decisions since the start of the enforcement storm, which predominantly concern Chinese internet giants and their use of VIE structures. Coupled with the call to “prevent disorderly expansion of capital,” these decisions involved significantly heavier fines, as 91% of these non-filing cases were given the maximum monetary penalty permitted under the AML (CNY500,000, or approximately USD72,000). Furthermore, the speed with which non-filing investigation cases are handled has also been much faster; the average investigation period during the enforcement storm has been 53.2% shorter compared with those decisions made earlier. The Amended AML gives SAMR more power and authority to stop and investigate a transaction even if the relevant revenue thresholds are not met, as long as such transaction is or may be anti-competitive. This new power

could cause uncertainties for parties structuring transactions.

Increasing sophistication of law enforcement

SAMR and provincial AMRs showcased their expertise and capabilities to make use of more complicated analytical tools. For example, SAMR and the Shanghai AMR, for the first time, defined two-sided platforms in penalty decisions against Alibaba, Meituan, and Sherpa's; furthermore, the Shanghai AMR also deployed the small but significant and non-transitory increase in prices test to predict the critical loss rate based on multiple factors, analysed the actual data from 2015–19 on that model under various assumptions, listed out the daily and monthly average orders, sales, and the number of users as proof of Sherpa's' market share and arranged for a survey to demonstrate users' reliance on the Sherpa's' platform.

Data

Data resources and the use of data have become core factors in assessing an undertaking's market power. SAMR has identified data as a key factor for establishing market dominance. For example, it found that Alibaba accumulated abundant data on transactions, logistics, and payments, which could be utilised based on its advanced algorithms to satisfy consumers' demands; further, it is difficult to transfer data on Alibaba's platform (especially user reviews) to other competing platforms. Therefore, vendors on the platform heavily rely on Alibaba.

The Amended AML prescribes directly that companies should not use to data and algorithms to engage in monopolistic behaviors; in particular, companies holding market dominance should not use data and algorithms to abuse their market dominance. In addition to the Amended AML, China has recently enacted a series of laws to regulate data, such as the CSL, the DSL, and the PIPL to pursue governmental objectives on privacy, national security and sovereignty. SAMR and provincial AMRs may pay more attention to data-based monopolistic behaviours such as algorithm collusion and discrimination based on big data.

A "new normal"?

Enhanced anti-monopoly legislation and tightened enforcement may become a "new normal" in China. That said, as China's economy is expected to come under substantial pressure in 2022 due to a variety of factors, there is speculation that China's top leadership will seek to boost the economy by setting a softer tone for digital undertakings, the platform economy, and private capital. Thus, for now, SAMR and provincial AMRs could tone down their enforcement efforts. Despite this, it is advisable for undertakings doing business in China or in connection with China to improve their anti-monopoly compliance awareness and to keep pace with the updated anti-monopoly regulations in China.

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CHINA TRENDS AND DEVELOPMENTS

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