Expanding to China? Don’t Make These 6 Mistakes.

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According to the American Chamber of Commerce in South China’s 2022 report, foreign companies are quite optimistic about their China expansion plans. As many as 72% of the companies surveyed intended to expand their China operations over the next three years.

However, even with a large number of companies interested, foreign investments in China were down by 2.1% in 2022. This can be attributed to restrictions imposed for Covid shutdowns, along with the complexity of expanding into a huge and complex market such as China for small and large enterprises alike.

Not being aware of the laws of the land can result in serious complications along with loss of money and time. For instance, AstraZeneca, the global pharma giant, found out the hard way that it needed government permission to transfer citizens’ genetic material to third parties even within China’s borders, resulting in criminal arrests of the company’s employees.

Avoid these six mistakes to ensure you don’t fall victim to a similar unfortunate incident when venturing into the Chinese market:

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1. Not researching business

registration laws

Building a subsidiary in a new country, especially one as legally complex as China, is a massive undertaking both in terms of time and money. You can either choose to hire individual consultants and law firms to guide you in different steps or complete the entire process on your own.

While the government incorporation costs to register a Wholly Foreign-Owned Enterprise or WFOE isn't much, and you'd be tempted to do it yourself, a single mistake can set you back thousands of dollars in legal fees.

For instance, when registering a WFOE, you need to ensure that the scope of your business is broadly defined in the application to accommodate future changes but specific enough to be approved by the authorities. Getting this crucial element wrong can create legal issues for your company down the road.

On the other hand, Professional Employer Organization (PEO) services allow you to have a legally approved presence in the country without getting bogged down by protracted registration cycles. This is because a global PEO such as INS Global deals with legal compliance, payroll administration and other legal benefits globally on your behalf.

2. Missing essential certificates and licenses

China has strict laws regarding the products and services that can be sold within its borders. Multiple government departments require your products to be certified and licensed before distribution.

Your business and products should also be compliant with the Foreign Investment Negative List, Market Access Negative List,

and the Unreliable Entity List. Correctly completing these additional requirements is time-consuming. Thus, many companies partner with a local entity well-versed with all the necessary certificates and licenses to reduce these legal hassles.

3. Not studying local tax regulations

Tax laws for businesses in China can differ from those in many western countries. Enterprise income tax, business tax, import duties, value-added tax and more need to be closely studied before commencing operations in the country.

Legal and tax advisors can help you assess the impact of all relevant taxes on your China operation. Hence, it’s essential to know them in-depth during the initial phase of your expansion.

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4. Ignoring local labor laws

Chinese labor laws can differ significantly from what you might be used to in your home country. Strict employment contracts are required by law, and they’re limited to only fixed-term, open-ended and project-based contracts.

When hiring in China, additional clauses like a non-compete can also differ from, say, American contracts. For instance, compensation is required to be paid to an employee during the non-competition period.

Severance pay calculation in China is also something you should be aware of. In short, companies owe employees one month’s salary for every completed year of service.

Employment contracts can be tricky if you’re unfamiliar with

China’s labor landscape. Leveraging the services of a local PEO can ease the process for you.

5. Not having airtight dispute resolution contracts

Dispute resolution clauses are heavily negotiated when doing business with Chinese entities. Companies need to get into airtight arbitration clauses when partnering with local vendors. The U.S. and China are both parties to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the “New York” Convention).

But the arbitration clause needs to be properly drafted: deciding which arbitration institution and rules to choose, the location of the arbitration, the language to be used and the governing law that’ll govern any disputes.

Arbitration clauses have the potential to drag your company into years-long court cases and huge financial losses. Hence, it’s always better to consult with a trusted partner that knows the ins and outs of dispute resolution in the Chinese context.

6. Not protecting your intellectual property

China’s IP protection laws have improved drastically over the years, offering foreign companies much more legal protection to safeguard their IP. But the onus still lies on the company to obtain copyright protection before launching operations in the country. Global trademarks are not automatically protected in China, so you’ll need to register them again. And with the first-to-file trademark system, it needs to be done as soon as possible.

China’s National Intelligence Law also affects how you manage your core IP. Moreover, China’s Cybersecurity Law determines how your organization can collect, store and transfer customer data.

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Flexibility and partnerships to unlock success in China

Companies mulling expansion to China stand to unlock increased and sustainable growth in one of the largest economies on the globe. But diving headfirst without the necessary homework can quickly kill your expansion dreams and tarnish your brand for years to come.

Besides legal compliance, it’s also incredibly important to take your time to study China’s cultural and socio-political landscape to be able to adapt your products effectively to the market. Chinese businesses also differ from their western counterparts in terms of corporate hierarchies, compensation structures, distribution channels, advertising laws and more. Being flexible and open to partnerships is the way to go if you want to tame the Chinese dragon.

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