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PRESIDENT'S FOREWORD

Investing in Influence: is your company doing enough?

Mats Harborn

President

European Union Chamber of Commerce in China

With the 'Two Sessions' now behind us, the European business community in China is looking at the rest of the year and evaluating how the many laws passed during the meetings will affect us. Several pieces of legislation that were approved are foundational documents that will spawn further policies, regulations and interpretive documents, which in turn will form the new frameworks that will shape the conditions under which firms operate in this country. China should seize this opportunity to examine just how it can reform the policies and regulations that need to be rewritten, and how to begin drafting those that are urgently required, to facilitate its shift from the growth-at-all-costs model to a more sustainable and balanced approach to development.

There are many avenues of influence that European companies can make use of to help steer policy in this direction, with the European Chamber standing at the centre, along with various member-state chambers and relevant industrial associations.

As China's economy and regulatory environment become more mature and complex, the challenges to developing the right framework multiply, demanding input from all stakeholders to find the best way forward. In line with this idea, our various working groups have made hugely successful contributions over the past year, attending 231 meetings at all levels of the Chinese government, and submitting 81 responses to calls for comments and 23 lobby letters to the authorities. Advocacy successes have ranged from changes to regulations that have streamlined procedures or removed unnecessary burdens, to clarifications from officials on policy interpretation to help ensure that companies reach compliance.

However, as the government begins to pour over the new legislation passed in the Two Sessions, we must now ask the question: are we doing enough to influence the next steps in the process?

I worry that, currently, the answer to that question is a "no". While some European companies have large and effective government advocacy teams in China, far too many do not. Larger firms should compare the resources they dedicate to advocacy in Brussels, in Washington DC and in Beijing, and realise that now is the time to dedicate more to China, where we can be part of shaping the business environment of the future. At the same time, while smaller companies may not be able to dedicate many precious resources to such efforts, they can examine how to contribute to advocacy organisations and what sort of expertise they can bring to the table.

Rather than merely reacting to existing draft regulations, what we now need to do is define the roles our respective industries currently play, and proactively put forward concrete proposals as to how they can be expanded to contribute more towards China's social and economic development. In last year's *Position Paper* we attempted to introduce this idea. For example, the financial industry is not only about lending or borrowing money – it is ultimately about optimising resource allocation in society to promote efficient development. This year I hope to improve this part of each paper, because this is how successful advocacy work starts.

Now China's key political season is over, the hard work begins. It is time for us to roll up our sleeves and enhance our role in shaping the environment we operate in.

THREE BATTLES

A Two Sessions Scorecard

By Wang Jing, Yang Yuchen and Lu Zhizhen

2019 is a year of major significance for China, marking a string of anniversaries, not least the 70th of the founding of the PRC. National legislative delegates and political advisors held their annual plenary sessions in Beijing in March, where they read reports, set out targets and policies for the times ahead and heard the occasional frank complaint. **Wang Jing**, **Yang Yuchen** and **Lu Zhizhen** of **China Policy** set out what the 'Two Sessions' revealed of the steadfast central policy focus on Xi Jinping's Three Battles.

Xi Jinping's 'three battles' have dominated domestic policy since the 19th Party Congress of October 2017. Framed in heroic terms, the focus is essentially corrective, addressing failings in the system. While its elements—ending poverty, cleaning up the environment and reining in debt risk—are treated as nearing completion, the commentary shows that doubts remain, and that the sheer scale of China's national government can force top-down policy into qualifications and reversals.

Ending poverty: moving on from low targets

Poverty alleviation offers a quicker win than the environment and debt, with the rural economy now being held up as a bulwark against the domestic downturn and external pressures. The commitment to prioritise it over urban and industrial interests has become a mantra among top leaders, with issues related to land rights and capital allocation and distribution also in focus at the 2019 Two Sessions.

Set at Chinese yuan (CNY) 2,300 per person per year (about United States dollars (USD) 0.95 daily), China's poverty line is around 50 per cent lower than the World Bank's definition of extreme poverty (USD 1.90 a day). Pledging to raise remnant rural poor up to this line by 2020, Xi has made the campaign a whole-of-government priority.

Xi has visited "deep poverty areas" (深度贫困地区) over 30 times since assuming office. An official biography stresses Xi's empathy with poor peasants is due to his experiences as a sent-down youth in Shaanxi during the Cultural Revolution. His thoughts and practice on poverty alleviation are an important part of his *Thought on Socialism with Chinese Characteristics*.

Though policy-makers expect to hit 2020 targets, inter-agency and centre–local cooperation are needed to cross the final hurdle. The upgraded Ministry of Agriculture and Rural Affairs (MARA) has gained the authority and budget to improve infrastructure and develop rural industry. The Ministry of Housing and Urban–Rural Development is tasked with renovating rural housing, the National Health Commission (formerly National Health and Family Planning Commission) is to address high healthcare costs, and the Ministry of Education is to provide funds for children in all families recognised as poor.

> *"While...ending poverty, cleaning up the environment and reining in debt risk – are treated as nearing completion, the commentary shows that doubts remain..."*

Concluding that making over some localities is too challenging, policy-makers plan to relocate 9.8 million poor people between 2016 and 2020. Where geography is the fundamental cause of poverty, says Liu Yongfu, director of the State Council Leading Group Office of Poverty Alleviation, people have to move whatever the cost.

Beijing now pairs each eastern province with a western one, encouraging investment and professionals to flow from east to west and cheaper labour from west to east. Farmland swaps, where major cities buy urbanisation quotas from underdeveloped areas, allow poor regions to earn money from distant urbanisation, with a March 2018 State Council policy loosening those rules.[1]

Some see the 2020 poverty line goal as misguided. The existing standard is inadequate, says Li Xiaoyun, a professor at the China Agricultural University in Beijing. The state, he insists, should adopt a qualitative metric, as specified in its *Rural Area Poverty Alleviation Outline 2011-20*. Whereas Wang Sangui of Renmin University warns that quantitative targets have led to unsustainable practices that fiddle the figures.

Post-2020 planning has already started. China will start to focus on alleviating relative poverty through multidimensional solutions and targeting both rural and urban areas.

Relative poverty will linger long after 2020, says Liu Yongfu. Success in ending poverty will not mean that huge cohorts will suddenly become urban consumers or major players in the national economy. That goal is likely another generation away.

Cleaning up the environment

The state continued to prioritise the anti-pollution fight, while foreseeing that room for improvement is shrinking. More is now expected on addressing water, soil and solid waste pollution. The state is also attempting to shift away from heavy-handed measures to more responsive and less disruptive ones. Stricter environmental regulations are also expected to drive China's green and low-carbon energy transition.

Falsified and superficial responses turned up in first-round checks on local implementation of environmental regulations and pollution cleanup completed between 2015

1. *China's Policy of Alleviating Poverty and Relocation*, National Development and Reform Commission, March 2018, viewed 20th March 2019, < http://www.ndrc.gov.cn/gzdt/201803/t20180330_881743.html>

and 2017. Those checks showed improvement in central regulations, and reflected the former Ministry for Environmental Protection's strengthening profile.

On 21st March 2019, a major explosion occurred at a chemical plant in Xiangshui County, Jiangsu Province. According to the Jiangsu Environmental Protection Bureau, the monitored levels of benzene, toluene and xylene in the area were not abnormal.
Photo: *Li Bo, Xinhua News Agency.*

As environmental conservation has risen in the Xi administration's priorities, centrally-led inspections have emerged as a distinctive governance paradigm. Now going after local authorities who tolerate pollution rather than the polluters, the centre is holding Party and government officials equally accountable.

Updating environmental law is also high on the agenda and experts recommend drafting new "environmental inspection guidelines". Meanwhile, the People's Bank of China (PBoC) estimates CNY 2 to CNY 4 trillion must be invested annually over the next five years to address environmental issues.[2] Market-based regulations, including an ecological compensation scheme, environmental protection tax and carbon market, have also been rolled out. The government is also pushing reform that makes local environmental regulators independent of city and county governments.

Although the state is cracking down harder than ever, considerable challenges remain to break up entrenched vested interests. Xi, meanwhile, is laying siege to the superstructure that enables pollution.

Reining in debt

The call for financial reform at the Two Sessions was dominated by the need to balance economic stimulus with debt management. Along with macroeconomic expansion strategies, the Sessions restated the need for financial sector supply-side structural reform to better service the real economy without adding more risks. Besides tax and fee cuts, "employment first" also continues to be a priority.

The battle against financial risk has moved from deleveraging to safeguarding growth. In early 2018, Beijing targeted making "significant progress" in preventing such risk,[3] emphasising internal controls, regulations and local borrowing discipline. By 31st October, the Q3 Politburo meeting fretted over the economic slowdown, removing references to deleveraging and housing prices. While the 2018 Central Economic Work Conference in December confirmed Beijing was softening its stance on implicit government debt and financial risks.

Loosening credit controls reflects the tug-of-war between growth at-all-costs and long-term sustainability. While structural adjustments and demand stabilisation policies are not mutually exclusive, points out China Finance 40 Forum senior researcher Zhang Bin, balancing them is tough.

China is entering a "downward cycle",[4] says PBoC Governor Yi Gang: monetary easing is needed to reassure firms and investors who overreact to cyclical shocks. The worst-case scenario is a vicious cycle where pessimistic investors escape the asset bubble altogether and trigger mass unemployment. Stock market fire sales in H2 2018 gave early warnings of such risk.

While justifiable, the monetary expansion could roll back gains made in deleveraging, and strengthen the state-led growth model. The PBoC struggles to direct commercial banks in targeted easing: banks still perceive state-owned enterprises (SOEs) as better investments and remain reluctant to finance private firms. Recognising this, the Politburo has resorted to expanding infrastructure investment and boosting local government spending.

In the near-term, the central government will relax deleveraging and focus on reorienting institutions slow to respond to top-level emphasis on quality over speed. In the longer term, Beijing is betting on industry upgrading and market reforms; unlike poverty alleviation and pollution control, the debt problem is being temporarily shelved to buy time for gradual reforms. Eb

***China Policy** is a research and strategic advisory group based in Beijing. Working with clients at the leadership, executive and research levels, they deliver clear insight into China's policy world as it affects strategic and operational decision-making not only in China but around the world.*

2. *Zhou Xiao: Promoting Sustainable Development with Green Finance*, Xinhua, 2nd July 2018, viewed 18th March 2019, <http://greenfinance.xinhua08.com/a/20180702/1767363.shtml>

3. *Report on the Work of the Government*, Xinhua, 22nd March 2018, viewed 18th March 2019, <http://www.xinhuanet.com/politics/2018lh/2018-03/22/c_1122575588.htm>

4. *China's Monetary Policy Framework: Supporting the Real Economy and Dealing with the Balance Between Internal Equilibrium and External Equilibrium*, Chinese Economists 50 Forum, 13th December 2018, viewed 20th March 2019, <http://www.50forum.org.cn/home/article/detail/id/7498.html>

LIANGHUI 2019: A HELPING HAND FOR MANUFACTURERS

By Samuel Sabasteanski and Mike Denison

This year's 'Two Sessions' followed months of sobering economic results that reignited fears of a significant slowdown in the Chinese economy. As such, it is no surprise that the government used the political meetings to lay out a plan to invigorate industries. In this article, **Samuel Sabasteanski** and **Mike Denison** from **North Head** look at how the policies announced will affect the manufacturing industry.

The 2019 economic stabilisation plan revealed at the 'Two Sessions' will cut burdens for manufacturers as part of efforts to support the economy and protect employment. The government's strategy will be a shot in the arm for the sector, but many multinational corporations (MNCs) are waiting to see how effective the measures will be in turning the economy around. MNCs will also need to align with policy objectives to make the most of China's latest plan to galvanise growth.

Background: private enterprises hurting in a slowing economy

Unlike 2018's political spectacle, this year's Two Sessions were all about the economy. And with good reason: the government aims for GDP growth as low as 6.0 per cent—the weakest since 1990; February exports dropped 20.7 per cent in USD terms year-on-year; and the official February manufacturing Purchasing Managers' Index (PMI) contracted below the 50 benchmark to 49.2, the lowest in three years. Some of this malaise is down to the US-China trade dispute; much can be attributed to private sector difficulties in accessing financing. Deleveraging efforts have reined in the debt and ballooning off-the-books financing vehicles that resulted from the post-2008 stimulus, but have also dried up financing for the private sector, which relies on unconventional 'shadow' banking.

In response, the government this year will focus on making life easier for private enterprises, tightening government budgets, and increasing the private sector's access to financing. Manufacturing remains crucial to trade and employment and as such will be a key beneficiary of government policies.

What policy measures from the Two Sessions do manufacturers need to know about?

Beyond broad measures to support the private sector, a series of policies to strengthen the manufacturing sector were revealed at the Two Sessions:

- Cutting the VAT rate for manufacturers from 16 per cent to 13 per cent and for transportation from 10 per cent to 9 per cent in 2019.

- Reducing taxes and fees by Chinese yuan (CNY) 2 trillion (although this will be tempered by more thorough tax collection by authorities).
- Allowing localities to cut corporate pension contribution rates from 20 per cent to 16 per cent and preventing increases in social insurance contributions by SMEs.
- Protecting foreign investors by passing the *Foreign Investment Law*.
- Pushing large state-owned commercial banks to increase their loans to small and micro enterprises (SMEs) by 30 per cent.

Reductions in VAT will provide a quick boost to manufacturers' bottom lines. For MNCs, VAT reform should alleviate pressure on some suppliers, especially SMEs facing cash flow constraints. But a 13 per cent VAT rate is still higher than in other Asian economies. If the manufacturing sector remains weak, the government could cut manufacturing VAT even further, for example by merging it into the new nine per cent bracket. However, VAT reductions may not have a significant impact on some manufacturing firms' operations if they have already reduced their effective VAT rate through deductions.

Some manufacturing segments will also benefit from the government's plan to expand infrastructure and construction in 2019. CNY 800 billion has been allocated for railway construction, 10 per cent above the 2018 target. Local governments will be allowed to issue CNY 2.15 trillion in special purpose bonds to support infrastructure and construction projects, though it will take months for these bonds to translate into real economic activity and new orders for manufacturers.

For financing, Premier Li Keqiang acknowledged at the Two Sessions that private firms and SMEs face difficulties in accessing affordable options. This comes despite moves in 2018 by the People's Bank of China (PBoC) to pressure banks to lend more to the private sector. To rectify this, the government will push banks for a 30 per cent increase in lending to private enterprises, which should create breathing room for their supply chains. However, work is needed to wean commercial banks from their habit of favouring relatively safe state-owned enterprises.

"With tighter budgets, local authorities will be more selective in offering incentives to enterprises."

How to make the most of these measures

The government leadership has offered extra support for the manufacturing sector and hopes to maintain employment levels. As beneficiaries of the stimulus, manufacturers are expected to support the government's goals. However, reduced taxes and fees will put pressure on local revenues. Slowing economic growth will also increase the risk of negative reactions by local governments to MNCs' business decisions. Here are a few points to consider:

- As employment is a key government concern, MNCs can expect extra sensitivity to large-scale layoffs or plant closures.
- With tighter budgets, local authorities will be more selective in offering incentives to enterprises. There has also been a trend towards greater scrutiny of cadres' performance. Enterprises should be prepared to clearly demonstrate the positive impact of their operations and investments on tax revenue and local businesses.
- The government is eager for feedback on how to improve the business environment, and calls in the Foreign Investment Law for better complaint-handling mechanisms. MNCs should proactively communicate with government stakeholders, both to highlight their priorities and to help regulators improve the local business environment.
- The health of SMEs is a priority. Industry associations could be useful forums for sharing best practices for helping SME partners or customers weather the slowing economy.
- General business sentiment is a sensitive subject. Communications plans should avoid adopting an overly pessimistic tone in media interviews, op-eds, press releases, or other materials.

The policies laid out at the Two Sessions will mitigate the pressure on manufacturers created by China's slowing economy, especially for enterprises that align themselves with government policy priorities. But it will take time for these reforms to take effect. Balancing risks and opportunities in 2019 will require careful analysis of the government's policy goals and using the insights to inform business units. Eb

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CHINA'S POLITICAL SEASON

AND WHAT IT MIGHT MEAN FOR EUROPEAN BUSINESS

By Jacob Gunter

The 'Two Sessions' compose the most important legislative event of the year in China. Two different bodies meet, the legislative—National People's Congress—and the political advisory – the Chinese People's Political Consultative Congress, to review and vote on a variety of laws proposed prior to the event. **Jacob Gunter**, Policy and Communications Coordinator at the **European Chamber**, brings us some of the highlights from the 2019 gathering.

Premier Li Keqiang's Work Report

On 5th March, Premier Li Keqiang delivered the annual work report at the 2019 'Two Sessions'. His speech began with a summary of the work completed over the previous year before expounding on the ten-point agenda set for 2019.

Among the more anticipated contents of the speech was the annual GDP growth rate target, which at 6 to 6.5 per cent was slightly lowered from the previous year's goal.

To help drive that growth, a series of broad reforms were announced. Regulatory improvements to improve the ease of doing business while also pushing down administrative costs were covered, as were several taxes expected to be lowered over the coming year.

However, as important as the plans to spur growth were the commitments on what the government will *not* do to hit its GDP target. Key among these, it was made clear that the focus on resolving structural risks and addressing the overleveraged and debt-ridden economy would not be sacrificed to artificially spur growth rates.

Focusing so much on regulatory and administrative reforms is a positive sign in the eyes of European companies, which remain ready to consult with the Chinese Government to improve the business environment.

However, the business community also recognises that many of these commitments have also been made in the past few years. While progress has been made in several areas, the pace of reform continues to lag behind expectations foreign companies have for the developed and mature economic power China has become. Advancing these commitments more rapidly is thus critical moving forward.

The Foreign Investment Law

Prior to December 2018, the most recent draft of the Foreign Investment Law (FIL) was released in January 2015. The 2018 draft FIL was significantly less detailed than the 2015 one, and read much more like a list of policy intentions than a proper law, sparking some concerns within the international business community.

"Lowering taxes will necessitate the government to either tighten its belt, or take on greater debt, both of which run contrary to other goals."

In response to the 2018 draft, the European Chamber prepared feedback to submit to the government. Comments were collected from members and organised into an article by article submission, but the draft FIL was also commented on more generally. The top concern of European businesses was, and continues to be, the very existence of a separate legal framework to govern foreign investment. Beyond that, the generally vague language and broad nature of most articles leaves far too much room for interpretation. For example, the FIL prohibits administrative bodies from using administrative means to force a foreign investor to transfer technology. This leaves considerable room for interpretation, and should instead simply be a prohibition on forced technology transfer from foreign investors.

The process for the revisions of the draft FIL unfortunately fell outside of commonly accepted procedures for legislation in China, undoubtedly due to a desire to push the law through to reassure negotiators seeking a deal to end the US-China trade conflict. After the December 2018 draft was released, a call for comments went out with a deadline in February. However, the draft was unexpectedly rushed forward, and reviewed and altered in late January, meaning that comments being collected by stakeholders that had not yet been submitted were not taken into consideration.

The final version of the law that was passed included several changes suggested by the European Chamber, specifically to articles 4, 9, 16, 24 and 26. However, the much more significant changes that were called for were not made. For example, Article 40, which gives the government sweeping and unilateral rights to respond to discriminatory actions against Chinese investors in other markets with negative reciprocity. This creates significant uncertainty and also runs contrary to the rules and ideals of the WTO, which is the appropriate place to address such disputes.

In the coming months, a wide variety of follow-up regulations, directives and interpretive documents. are expected to be released. The European business community hopes that they provide clarity and sufficient specificity so that the FIL can fulfill the commitments surrounding it.

Stimulus or no stimulus?

With the economic slowdown driving concerns, many have asked whether China will revert to the heavy stimulus strategy it employed following the 2008 financial crisis. While the agrarian-themed idea of "flood irrigation" that was employed then may have averted a deepening of the crisis, it may also have planted the seeds of the next one.

Monetary easing and massive government spending flooded the market with quick growth, but like its namesake, it left pools of wasted water in the lowlands and did nothing for elevated areas. As a result, China was spared the effects of the financial crisis, but left with underutilised infrastructure, industrial overcapacity, bloated state-owned enterprises and a mountain of debt.

Based on the mantra-like insistence from top leaders that the government will not resort to such a strategy again, coupled with the patterns that have been seen over the past year, businesses should not expect the floodwaters to rise again. Instead, more targeted tools are being applied, and any broad solutions being used are done so more conservatively than before.

As was made clear throughout the Two Sessions, efforts are being made to improve the business environment and cut back on administrative burdens and fees. Those amount to small improvements and savings for each step, but with many areas in which progress can be made, the sum of each improvement may prove meaningful. Additionally, the government is cutting away at taxes across the board. VAT, for example, will go from 16 to 13 per cent for most industries. As stated in Premier Li's work report, these cuts should total roughly CNY 2 trillion.

To free up more money in the market, the government has progressively lowered the reserve requirement ratio (RRR) over the past year. Since 2015, China's RRR rate has dropped by 6.5 percentage points, 3.5 of this in the last 14 months. That acceleration freed up considerable amounts of cash, but it makes China play a card from its policy hand that is difficult to get back. However, there is still room for further dropping this rate if needed, as many countries have set their RRR in the low single digits.

However, these measures certainly bring challenges. Lowering taxes will necessitate the government to either tighten its belt, or take on greater debt, both of which run contrary to other goals. Additionally, dropping RRR rates raises systemic risk in the banking system, which would contradict efforts to tackle risk throughout the economy.

With no easy answer to these challenges, Chinese leaders will have to strike an appropriate balance between competing goals. However, barring drastic changes on the ground, there are few indicators that imply a return to the wasteful stimulus approaches of the past. Eb

CHINA'S DRAFT FOREIGN INVESTMENT LAW

FOUNDATION FOR FURTHER IMPROVEMENT OF THE FOREIGN BUSINESS LANDSCAPE?

By Richard van Ostende

In 2018, China celebrated 40 years of opening up and reform, and vowed the policy will continue. As part of this drive, a draft Foreign Investment Law (FIL) was submitted to the National People's Congress (NPC) during the 2019 Two Sessions. In this first installment of a two-part series, **Richard van Ostende** of the **Netherlands Business Support Office** looks at how the draft law developed, and its reception among the foreign business community.

On 8th March 2019, during the second session of the 13th National People's Congress, the vice chairman of the Standing Committee of the National People's Congress, Wang Chen, made a statement on the draft Foreign Investment Law in Beijing.
Photo: *Zhang Ling, Xinhua News Agency.*

The NPC published its first draft of the FIL on 27th December 2018, with 24th February 2019 the deadline for soliciting public comments. Then, on 29th and 30th January 2019, nearly one month before the deadline for comments, the Standing Committee of the National People's Congress (NPCSC) hosted a special session to conduct a review of the silently released second draft of the law. After this review, the draft was submitted to the NPC for deliberation.

The NPC took place from 5th to 15th March 2019. At the time of writing, the NPC was still in session, and the vote on all resolutions and the draft FIL had not yet taken place. Therefore, this article is the first of a series of two. This article will discuss the developments leading up to the draft version of the law that was submitted to the NPC, as well as major points of concern among foreign industry leaders. The second article will discuss the content of the enacted law in detail, and its implications for foreign businesses.

Deviation from standard legislative processes

Ordinarily, laws issued by the NPC undergo three rounds of review, with public consultation taking place after the first and second rounds. Consultation periods are usually 30 days long. For the new FIL to be implemented following the regular legislative process, the NPCSC would review the draft a few more times during 2019 and submit it to the 2020 NPC session for adoption.

The fact that a second draft has been released before the first consultation period ended, without explanation for the increased urgency, combined with the fact that it has been submitted to the NPC, raises concerns that foreign companies' comments will not be taken into consideration in the final draft. The move further raises questions over China's overall progress in implementing rule of law. Many foreign news outlets suggest proceedings have been rushed because a longer legislative process would not help show China's willingness to comply with certain demands the United States made during trade negotiations.

Streamlining legislation vs more level playing field

The new draft law indicates the Chinese Government's willingness to further open its markets to foreign businesses. Regulators envision the new law as a "basic law for the field of foreign investment".[1] With its implementation. the Chinese-Foreign Equity Joint Ventures Law, Wholly Foreign-Owned Enterprises Law and Chinese-Foreign Contractual Joint Ventures Law will be abolished, further streamlining legislation. However, a legal distinction between foreign and local companies seemingly remains. In order to create a level playing field for foreign and local companies alike, this distinction should be abolished, with the exception being when legitimate reasons such as specific national security concerns can be provided.

Vaguely defined provisions

The current version of the draft law is comprised of six chapters with only 41 articles, significantly shorter than the 170 articles included in the first 2015 version of the draft law. The State Council has removed most of the detailed rules, possibly to allow more maneuvering space to draft them after enactment. This approach would make the detailed implementing rules subject to laxer public consultation requirements. Further, most of the 41 articles appear to be aspirational, unenforceable policy statements. The compressed size of the bill has resulted in the current draft law becoming less transparent, as its regulations and herewith its impact on business are not well defined.

1. Liu, Zhihua, *Foreign Investment Draft Levels the Field*, *China Daily*, 5th March 2019, viewed 22nd March 2019, <http://global.chinadaily.com.cn/a/201903/05/WS5c7db882a3106c65c34ecb69.html>

Foreign investment defined

The draft law defines "foreign investors" as any "natural person, enterprise, or other organization of a foreign country", and "foreign-invested enterprises" (FIEs) as any enterprise established under Chinese law that is wholly or partially invested in by foreign investors. "Foreign investment" is further defined as any foreign investor's direct or indirect investment in mainland China, including:

- Investing in new projects, establishing FIEs, or increasing investment, either individually or jointly with other investors;
- Obtaining stock shares, equity, property shares, or other similar interests in Chinese domestic enterprises through mergers or acquisitions; and
- Investing in Mainland China through other means provided by laws, administrative regulations, or State Council provisions.

Final version

As stated earlier, the NPC was still in session at the time of writing and the vote on the Draft FIL had not taken place, so the exact content of the legislation and its implications for foreign businesses could not be confirmed. These will be discussed in the second article of this series in the May/June edition of *EURObiz*. Eb

***Richard van Ostende** is Chief Representative of the **Netherlands Business Support Office (NBSO)** located in Nanjing. The NBSOs are an integral part of the Dutch Government's network in China and support Dutch companies in doing business in and with China. Richard is a Doctor of Literature Candidate at Monarch Business School. Subject of research is "Foreign Direct Investment into China: Determinants of the Strategic Decision-Making Process by Dutch Companies".*

ENVIRONMENTAL HIGHLIGHTS FROM THE TWO SESSIONS

By Johnny Browaeys and Ma Liqiang

China has invested a lot in recent years in improving its environment. However, those gains have often come at the expense of companies' bottom lines. **Johnny Browaeys** and **Ma Liqiang** of **Greenment Environment** look at just how the environmental protection policies may develop in the wake of the 2019 Two Sessions.

The Two Sessions repeated China's endeavor to become an eco-civilization, in line with what was written in the country's constitution last year. The battles for "blue sky" and "clear water" continue. Focus will be on objective and accurate monitoring of environmental data, and on regional supervision of key industries.

The business environment will also improve as environmental enforcement matures. The "one-cut" approach—sometimes used by local governments to meet their environmental objectives, and which impacted companies across the board without distinction—is no longer allowed.

In general, 2019 is expected to bring less uncertainty to companies that comply with environmental regulations. But also anticipated is continued supervision and strict enforcement of preventing key pollutant discharges. This will especially be seen in regions with poor environmental quality, where severe air quality alerts are frequent, or where river quality is particularly poor. Regions with high environmental public scrutiny or previous environmental problems will also be a focus.

Listed below are some highlights to give a heads up of what can be expected of environmental governance after the Two Sessions.

Integration of environmental battles

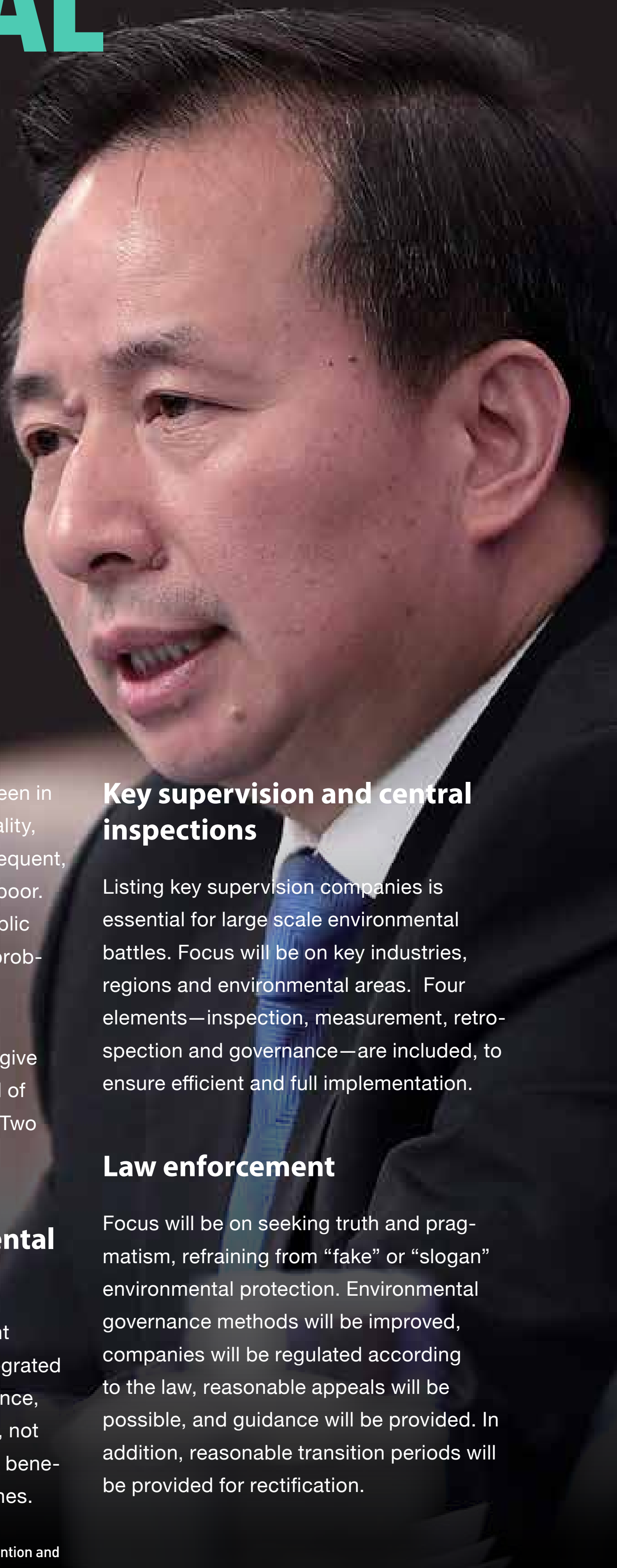
Environmental battles shall be fought steadily and progressively, in an integrated way, with determination and confidence, but also patience and perseverance, not only for the pursuit of environmental benefits, but also economic and social ones.

Key supervision and central inspections

Listing key supervision companies is essential for large scale environmental battles. Focus will be on key industries, regions and environmental areas. Four elements—inspection, measurement, retrospection and governance—are included, to ensure efficient and full implementation.

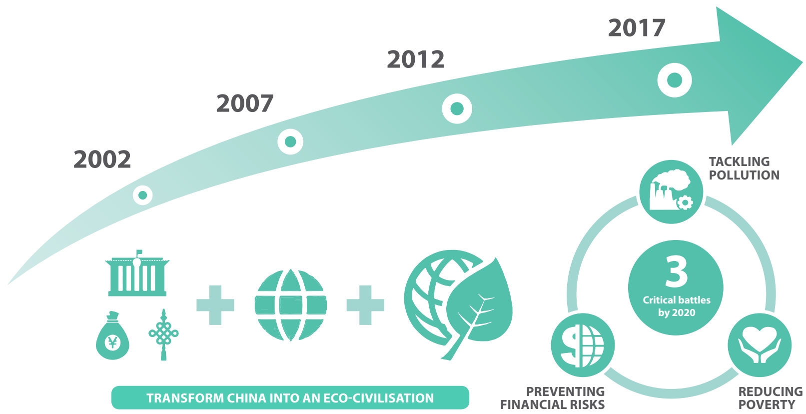
Law enforcement

Focus will be on seeking truth and pragmatism, refraining from "fake" or "slogan" environmental protection. Environmental governance methods will be improved, companies will be regulated according to the law, reasonable appeals will be possible, and guidance will be provided. In addition, reasonable transition periods will be provided for rectification.



On 11th March 2019, Minister of Ecology and Environment, Li Ganjie, answered questions on issues related to the prevention and control of pollution in the press conference of the Second Session of the 13th National People's Congress.
Photo: *Wang Peng, Xinhua News Agency.*

China 5-year Planning Places Strategic Priority on Environmental Protection of European Companies



Source: *Greenment Environment*

Perfection of standards

Standards for volatile organic compound (VOC) content, fugitive emission control and industry emissions, among others, will be upgraded.

Environmental data

Digitisation of environmental data will continue, including automatic monitoring and disclosure of air quality in districts and counties, and key pollution sources. It will be ensured that the monitoring data is true, accurate and comprehensive to provide a foundation for building environmental protection.

Rehabilitation of the Yangtze River Economic Belt

The ecological environment of the Yangtze River will be rehabilitated, utilising economic and market means so that ecological environmental protection adds economical value while realising ecological value.

Self-accountability

Companies' self-accountability will continue to be strengthened, and information disclosure and self-certification will be legally normalised.

Understanding China's environmental storm

China's 'environmental storm' is not only meant to clean up the country's environmental pollution or to address historical environmental non-compliances. It also aims to reshape the national industrial landscape in line with urban and industrial planning, addressing industrial overcapacity, moving and upgrading old factories, and transforming old industries into new ones. We have seen this happen before – in the West.

It took Europe about 150 years to industrialise and about 35 years to develop environmental governance. It took China about 35 years to reach its current industrial level, and Beijing knows it doesn't have another 35 years to develop environmental governance.

When a child grows too fast, it can face growing pains. The environmental enforcement we have witnessed has been drastic and has caused pain. It is hard to predict how long the growing pain of transformation will last, but it is part of China's reality.

Final considerations

Finally, one should remember that China uses a long-term central planning approach, which consecutively and consistently builds five-year plan upon five-year plan. We have seen the focus of the five-year plans over time move from politics, to economy, culture, social stability, environmental quality, and most recently to "battling environmental pollution, poverty and financial risk".[1]

There are several big differences with Europe, some of which are important for Europe to contemplate: China does not lose time by yoyoing political programmes between elections in the way we increasingly have seen happening in Europe over the recent years, with opposition politics aiming at winning votes by extrapolating rather than consolidating public opinion.

As a result, China currently is leapfrogging Europe in digitising environmental information and leveraging public governance to install a real-time policy implementation the world has not seen before; and that is allowing China to move beyond lightning speed in transforming its industrial and urban landscape.

Anyone operating or sourcing from China, who is not considering the impact of the country's environmental storm/industrial transformation on its operations over the next three years, is sailing blind. Eb

Greenment Environment *is the largest independent environmental consulting firm in China. Greenment works for 80% of Fortune 100 companies. Greenment's services include environmental management consulting, engineering and technology services and project implementation. Greenment now has offices in Shanghai, Beijing and Guangzhou in China, Sacramento in the US and Belgium in Europe.*

1. *China to Fight Major Risks, Poverty, Pollution in Next 3 years*, Xinhua, 20th December 2017, viewed 20th March 2019, < http://www.xinhuanet.com/english/2017-12/20/c_136840941.htm>

TWO SESSIONS 2019: THROUGH THE LENSES OF EUROPEAN SMALL BUSINESSES

By Ester Cañada Amela

The annual meetings of the National People's Congress (NPC) and the Chinese People's Political Consultative Conference (CPPCC)—also known as the Two Sessions—are widely followed by governments, media, political pundits, economics analysts and China watchers around the world. They are also closely monitored by those with 'skin in the game': parties with a business already set up in China or investors looking to get involved in the world's second biggest economy. **Ester Cañada Amela** of the **EU SME Centre** examines how the outcomes of this year's Two Sessions could impact European small and medium-sized enterprises (SMEs).

Yi Gang, Governor of the People's Bank of China, answered questions on financial reform and development in a press conference on 10th March 2019.
Photo: *Li Ran, Xinhua News Agency.*

The Two Sessions are usually fraught with newsworthy content and, while typically announcements on GDP growth targets, further opening up on foreign investment, or political declarations tend to be the topics that always make the headlines, these meetings can also offer some insight on the leadership's strategy on other less limelight-stealing issues. Even though this latter group includes the promotion of SME development, one should not make the mistake of thinking that no attention whatsoever is paid to the issue. After all, SMEs in China do represent 99.6 per cent of companies, comprise more than 60 per cent of its GDP and play a key role in fostering innovation and creating employment.[1]

In view of the multiple challenges that arose in 2018 and the first quarter of 2019—from the slowing down of China's economy to the US-China trade tensions—the Chinese leadership has been stepping up its efforts towards supporting the development of businesses. Thus, while showcasing the progress made in the past year on a variety of issues, the 2019 government work report also recognised that there was room for improvement in areas like the upgrading of the business environment in general and access to affordable financing for SMEs.[2]

1. Guo, Linmao, and Ma, Xianghui (Eds), *People's Republic of China Small and Medium-sized Enterprises Promotion Law: Guidebook*, China Democracy and Legal System Publishing House, Beijing, 2017, pp. 15–19.

What is the big news coming out of the 2019 Two Sessions for SMEs?

In terms of macro policies, it was made clear in the work report—and subsequently by high-level officials like the People's Bank of China's PBoC Yi Gang—that a "prudent monetary policy"[3] would be carried out. This means that, although the likelihood of any large stimulus package being rolled out anytime soon is low, monetary policy

2. *Report on the Work of the Government (Delivered at the Second Session of the 13th National People's Congress of the People's Republic of China on March 5, 2019)*, State Council, 5th March 2019, viewed 18th March 2019, <http://english.gov.cn/premier/speeches/2019/03/16/content_281476565265580.htm>
3. *Report on the Work of the Government (Delivered at the Second Session of the 13th National People's Congress of the People's Republic of China on March 5, 2019)*, State Council, 5th March 2019, viewed 18th March 2019, <http://english.gov.cn/premier/speeches/2019/03/16/content_281476565265580.htm>

instruments will still be used to—among other things—decrease the difficulty for small businesses in accessing financing. Measures announced include more targeted cuts to required reserve ratios for medium and small banks, the released funds of which will be lent to private enterprises and small and micro businesses. Also, the work report set a target of a 30 per cent increase in loans granted to small and micro businesses by state-owned commercial banks.

This emphasis on continuing to carry out a prudential monetary policy means that, conversely, more weight will be put on fiscal policy, which for SMEs essentially implies further tax cuts. The reduction of financial burdens for SMEs through tax cuts and preferential tax policies is not new, however. In fact, it was a recurrent theme throughout 2017 and 2018. For instance, in October 2017, the State Administration of Taxation announced that, in order to support micro and small enterprises, businesses with a monthly sales volume of between Chinese yuan (CNY) 20,000 and CNY 30,000 would be exempted from value-added tax (VAT),[4] a threshold that was increased to CNY 100,000 in a January 2019 announcement by the State Council.[5] During that same meeting, the State Council also announced that for SMEs with taxable income below CNY 1 million/year, only 25 per cent of income would be considered taxable. Furthermore, in the case of enterprises with between CNY 1 to 3 million/year of taxable income, only 50 per cent of this income would be considered taxable. Preferential task policies for innovative or high-tech enterprises are also a recurrent theme and part of the wider push to encourage innovation.

The improvement of the business environment was another of the key issues addressed in the 2019 government work report. In 2018, a number of measures to improve the business environment were introduced in various Chinese cities (prompting the country's considerable rise in ranks in the World Bank's index on ease of doing business).[6] This commitment to continue this development trend was renewed throughout the 2019 Two Sessions. Some of the measures envisioned include reducing and simplifying approval procedures, making it easier to obtain licences, developing online services and establishing a government service evaluation system.

What are the implications of these moves for European SMEs?

If one thing has become clear in recent years, it is that it is in the best interests of the Chinese Government to improve the operating conditions of SMEs, both domestic and foreign. The measures and policies outlined here are proof that a degree of willingness to support the development of SMEs is indeed present within leadership circles. Nonetheless, there are a couple of aspects to take into account when analysing these announcements and measures.

To begin with, it is important to note that while fiscal policy-related measures such as tax reduction and VAT reform are certainly beneficial to all SMEs, their trickle-down effects tend to become noticeable in the longer term. Furthermore, in the short term (crucial for SMEs), the key issue of financing is still very much shrouded in uncertainty. Although the Chinese Government's intention to address this challenge has been clearly expressed in numerous occasions, the fact is that SMEs in general (and more so foreign SMEs) are still regarded by financial institutions as high-risk, low-return investments, and therefore cannot compete against the security offered by state-owned enterprises (SOEs). This situation is not likely to change unless some major reforms and effective measures are developed and carried out.

Finally, as mentioned, the improvement of the business environment seems to be a priority for the government this year. If implemented effectively, this can potentially reduce the burden of SMEs and bring considerable benefits to them. According to the feedback provided by European SMEs to the EU SME Centre and the European Chamber, the impact of the past years' efforts towards improving the business environment has, in some cases, been noticed. However, a number of European SMEs have also reported encountering issues related to the implementation of these measures and to the equal treatment between domestic and foreign companies – especially when it comes to business registration procedures.

In conclusion, from the outcomes of the Two Sessions it can be surmised that China is earnest when it comes to supporting the development of private enterprises, and more concretely SMEs. This is why it is all the more important for the European SME community in China to come together through platforms like the EU SME Centre in order to properly convey their feedback and their recommendations to the Chinese leadership. Eb

***The EU SME Centre** is a European Union initiative that provides a comprehensive range of hands-on support services to European small and medium-sized enterprises (SMEs), getting them ready to do business in China. Our team of experts provides advice and support in four areas – business development, law, standards and conformity and human resources. Collaborating with external experts worldwide, the Centre converts valuable knowledge and experience into practical business tools and services easily accessible online at http://www.eusmecentre.org.cn/.*

4. *Notice on Continuing the VAT Policy of Micro and Small Enterprises*, State Administration of Taxation, 20th October 2017, viewed 12th March 2019, <http://www.chinatax.gov.cn/n810341/n810755/c2897233/content.html>
5. *Li Keqiang Presided over the State Council Executive Meeting and Decided to Introduce a Number of Inclusive Tax Cuts for Small and Micro Enterprises*, State Council, 9th January 2019, viewed 12th March 2019, <http://www.gov.cn/xinwen/2019-01/09/content_5356305.htm>
6. *Doing Business 2019, Training for Reform*, World Bank, 31st October 2018, viewed 12th March 2019 <http://www.doingbusiness.org/content/dam/doingBusiness/media/Annual-Reports/English/DB2019-report_web-version.pdf>

THE BROADER SPECTRUM

By Yvonne Yu

China's Path Towards 5G Commercialisation

At this year's Two Sessions, tech industry leaders such as Pony Ma from Tencent and Lei Jun from Xiaomi expressed optimism about 5G empowering sectors such as industrial Internet of Things (IoT), new media, smart agriculture, autonomous vehicles and healthcare.[1] But just how far are we from realising 5G's full potential? **Yvonne Yu**, CEO of **Politech**, seeks to demystify 5G by providing a brief but comprehensive overview of its development in China.

Path to 5G commercialisation

5G commercialisation requires three prerequisites:

1. Allocating 5G spectrum (frequency bands) to telecom carriers. Different companies use different parts of the spectrum to transmit 5G data. Using one part over another impacts both the speed of the connection and the distance it can cover. Without first knowing which 5G spectrums are allocated, telecom carriers cannot build 5G network infrastructure, and manufacturers cannot produce 5G phones.

2. With 5G spectrum allocated, telecom carriers are able to build the network infrastructure in accordance with standards set by 3GPP, the key standardisation body for global mobile communication systems. Telecom carriers will purchase equipment, such as 5G core network and base stations, developed by network equipment suppliers like Huawei.

3. With the right network infrastructure, data can be transmitted at a faster speed and lower latency. To realise commercialisation however, there's one last missing piece – terminals. The most common are 5G smartphones, autonomous vehicles, smart watches and 5G virtual reality/augmented reality (VR/AR) headsets.

5G spectrum: allocated

On 6th December 2018, the Ministry of Industry and Information Technology issued China Telecom and China Unicom licences for the 3.5 GHz band of the global standard, and China Mobile the suboptimal 2.6GHz and 4.9GHz bands. This puts

1. *5G Communication Services, Two Sessions, Operators to Accelerate the 5G Commercial Process*, Sohu, 12th March 2019, viewed 19th March 2019, <http://www.sohu.com/a/300726940_565998?sec=wd>

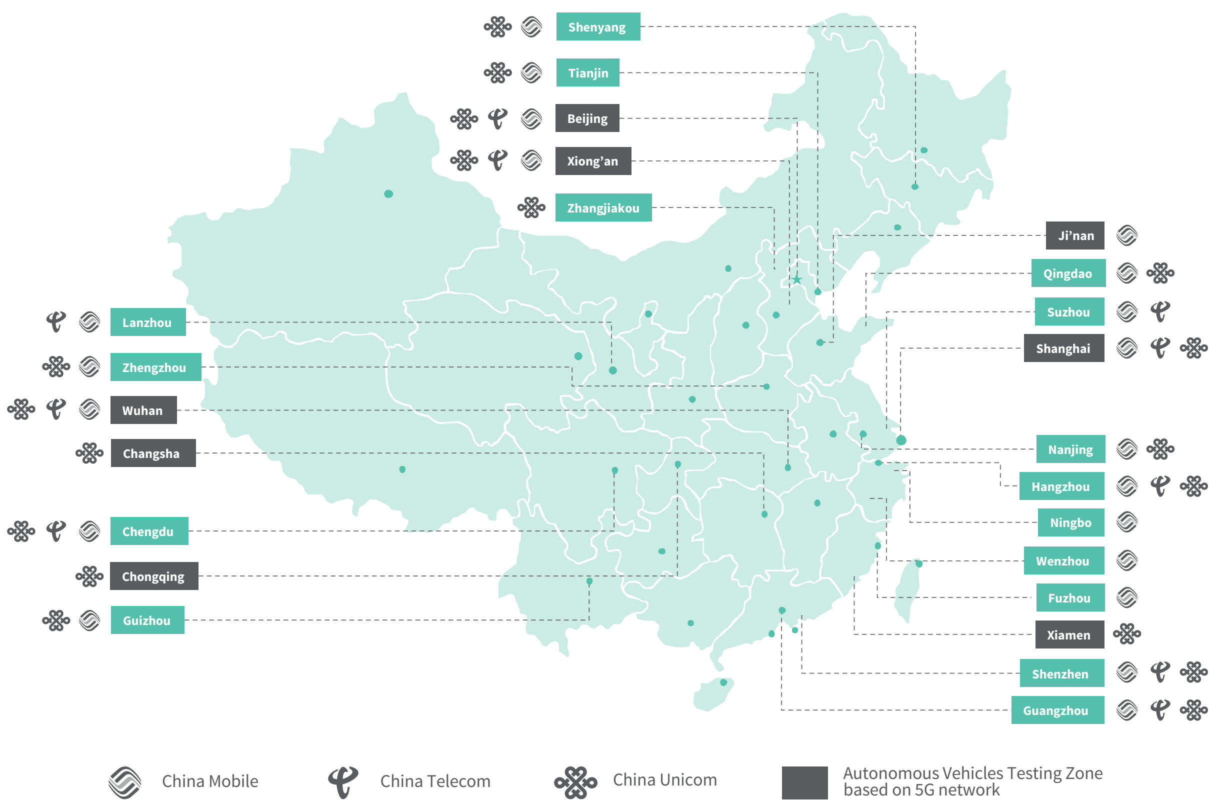
China Mobile at a disadvantage, as network equipment and commercial 5G products will need to be modified to receive signals from the different bandwidth. An upside for China Mobile is that the 2.6GHz band was

(see map), aiming for 500-1,000 base stations in each city per carrier in 2019.[3] This will enable subways, entertainment spaces, sports halls and commercial buildings to be covered by 5G. Further, the three carriers

Phone manufacturers from around the world showcased their 5G phone prototypes at the Mobile World Congress in Barcelona in February. They included Huawei's Mate X – a foldable phone that runs

Network Infrastructure: Testing in 26 Cities

5G pilot cities by the three telecom carriers. All three are testing in Beijing, Xiong'an, Shanghai, Hangzhou, Shenzhen, Guangzhou and Chengdu



Source: *Yi'ou and various Chinese media, Politech*

used in the 4G era, so it can reuse some of its current network infrastructure.[2]

Network infrastructure: testing in 26 cities, mass deployment in 2020

With government support and equipment provided by Huawei and ZTE, the three telecom carriers are piloting 5G in 26 cities

are devoted to investing tens of billions in 5G deployment in 2019 as shown in the table.

Though China's plan to build 5G infrastructure is very impressive, full nationwide coverage is not possible till at least late 2020.

Terminal: release by Q2 2019

Terminals are smart devices able to receive 5G signals, such as phones, cars and watches. 5G smart phones are by far the most developed terminal.

on Huawei's self-developed 5G chipset, the Balong 5000 – and ZTE's Axon 10 Pro 5G, both expected to enter the market by mid-2019.[4]

Though phone manufacturers are eager to launch their 5G product, the unavailability of the 5G network, high pricing of the phones, and a lack of killer applications will continue to hinder their mass adoption.

2. *5G Ready, Set and Go!*, *Caixin*, 17th December 2018, viewed 19th March 2019, <http://weekly.caixin.com/2018-12-15/101359513.html?p0#page2>
3. *Three Operators' 5G Networking Strategy is Becoming Clearer, Investment will Reach Tens of Billions Next Year*, *Xinhua*, 18th December 2018, viewed 19th March 2019, <http://www.xinhuanet.com/finance/2018-12/18/c_1210017745.htm>

4. *35.4 trillion! Hopeful Speeches of 5G at the 'Two Sessions'*, iyiou.com,
5. *Three Operators' 2019 5G Plan Released*, cww.net, 19th December 2018, viewed 19th March 2019, <http://www.cww.net.cn/article?id=444331>
6th March 2019, viewed 19th March 2019, <https://www.iyiou.com/p/94105.html>

Current commercialisation status

5G's commercialisation is aimed at more than just boosting speeds for consumers and selling handsets. 5G is about creating a network optimised for connecting billions of new devices to the Internet. This requires the support of different sectors, and presents a unique business-to-business (B2B) opportunity to telecom carriers, alongside the traditional business-to-consumer (B2C) model.

Three Carriers' 5G Deployment in 2019

	CHINA MOBILE	CHINA TELECOM	CHINA UNICOM
5G INVESTMENT	To establish a "5G Co-Venture Industry Fund" of **CNY 10 billion** for the initial launch. Total value at **CNY 30 billion**. To promote the maturity of the 5G telecom industry chain.	Hasn't published their initial investment amount.	From 2019 to 2020, will invest **CNY 21 billion** to develop terminals.
5G FIELD TEST	Network field test of 5G service in **17 cities**. Already completed 100 5G base stations in Hangzhou.	Network field test of 5G service in **17 cities**.	Network field test of 5G service in **17 cities**.
5G NETWORK TECHNOLOGY	Non-Standalone (NSA) architecture at first, and gradually move to Standalone (SA) network.	Prioritize SA deployment.	Believes SA and NSA are both important. Sources show Unicom leaning more towards SA.[5]

Source: *Politech*

B2C model: launch in major cities in late 2019

So far, telecom carriers are able to deploy 5G network coverage at a few key facilities, including Tiananmen and the Palace Museum in Beijing, the Canton Tower in Guangzhou, Lukou International Airport in Nanjing and Hongqiao Railway Station in Shanghai. The goal in 2019 is to expand 5G coverage in the 26 cities identified on the map.

For example, China Mobile plans to cover Beijing (within the 5th Ring Road) by the end of 2019. It will also build "thousands" of base stations in Shanghai by May 2019.[6] It is expected that commercial 5G will roll out in major cities by the end of 2019.

B2B model: operators eager to find compelling use cases for 5G

Compared to the B2C model, commercialising with the B2B model is inherently more difficult because industry leaders are cautious of investing too much in 5G, as they cannot rely on its profitability. Nonetheless, they are keen to partner with telecom carriers to explore different user scenarios on a small scale. Some sectors piloting 5G applications include:

- **New Media:** 5G was used for ultra-high definition video transmissions from this year's Two Sessions.
- **Healthcare:** on 16th March 2019, China conducted the first 5G-based long-distance human surgery to successfully complete a "brain pacemaker" implantation for Parkinson's disease. A neurosurgeon in Hainan used China Mobile's 5G network to receive high definition video images in real time and operate surgical instruments remotely.[7]
- **Industrial IoT:** China Unicom is to provide a 5G smart harbour system at the Port of Qingdao, Shandong.[8]
- **Autonomous Vehicle:** test drives in Wuhan, Changsha, Chongqing, Beijing, Xiong'an, Ji'nan, Shanghai and Xiamen by telecom carriers.

The National Development and Reform Commission (NDRC), the top policy planning body, also promised to speed up the process of issuing licenses for commercial use of 5G technologies in 2019.

It is unclear yet which sectors will benefit the most from 5G. What is clear though, is that the various pilots and trials happening in 2019 will certainly lay the groundwork for mature B2B use of 5G scenarios in late 2020. Eb

__Politech__ is a boutique strategic consulting firm serving foreign companies and local governments in China. Officially established in 2018, Politech is incubated by the University of Tsinghua and Innoway, a prestige state-owned enterprise. Politech's investors include industrial IoT leader ProudSmart, and ex-CTO of IT Juzi. It has developed its own proprietary database with 80 million+ company data, and is currently serving two Chinese local governments.

6. *35.4 trillion! Hopeful Speeches of 5G at the 'Two Sessions'*, iyiou.com, 6th March 2019, viewed 19th March 2019, <https://www.iyiou.com/p/94105.html>
7. *Chinese Enterprises Speed up Efforts to Test the Water with 5G Innovative Application*, tech.163.com, 17th March 2019, viewed 19th March 2019, <http://tech.163.com/19/0317/08/EAF6N1EE00097U7S.html>
8. *Ericsson and China Unicom Announce 5G Smart Harbor at the Port of Qingdao*, Ericsson, 26th February 2019, viewed 19th March 2019, <https://www.ericsson.com/en/press-releases/2019/2/ericsson-and-china-unicom-announce-5g-smart-harbor-at-the-port-of-qingdao>

EUROPEAN CHAMBER ADVOCACY HIGHLIGHTS

4 FEB

BRUSSELS

Chamber President Mats Harborn meets with key stakeholders in Brussels

President Harborn with European Commissioner for Trade, Cecilia Malmstrom.

President Harborn with Ann Mettler (centre), director general of the European Political Strategy Centre and staff.

President Harborn (R) meets former German Ambassador to China Michael Clauss.

President Harborn with Chinese Ambassador to the EU, Zhang Ming (centre L), and staff.

On 4th February, European Chamber President Mats Harborn had a series of meetings with top leaders in Brussels. The diverse round of meetings included discussions with European Commissioner for Trade, Cecilia Malmstrom; former German Ambassador to China, Michael Clauss; Chinese Ambassador to the EU, Zhang Ming; and Ann Mettler, head of the European Political Strategy Centre, the in-house think tank of the European Commission. President Harborn briefed all parties on the most recent findings and views of the European Chamber before inquiring on their own views. Each meeting ended with plans to follow-up on any further information that was needed by each party and to stay in touch in the future.

17 JAN
SHANGHAI

Second Shanghai Government Dialogue gives voice to European companies

On 17th January, the European Chamber's Shanghai Chapter held its second Shanghai Government Dialogue. The Shanghai Government delegation was led by Mr Xu Kunlin, Vice Mayor of Shanghai Municipal People's Government, who headed a group of 16 representatives from various municipal government departments whom also participated in the discussion. The European Chamber's delegation, which included 10 working group chairs and vice chairs, was led by Carlo D'Andrea, Vice President of the European Chamber and Chairman of the Shanghai Board. The European Chamber delegation presented their recommendations on how to improve Shanghai's business environment and create a level playing field between local and foreign companies. At the end of the conversation, both sides committed to following up on the agreed action points and meet twice a year.

12 MAR
NANJING

The Nanjing Chapter Government Dialogue brings together business leaders and officials

Nanjing Chapter holds annual Government Dialogue with local government leaders.

On 12th March, the Nanjing Chapter held its annual Government Dialogue with local government leaders. Kong Qiuyun, Director of the Nanjing Bureau of Commerce, led representatives from multiple government departments to the meeting with the Nanjing Chapter, led by Nanjing Chapter Chair Bernhard Weber. Members were first updated on key policies that had recently been promulgated before separating into a variety of round-table discussions with government representatives. In the subsequent meetings, members were able to raise detailed and specific concerns with officials. A variety of topics were covered, including ways to improve specific regulatory challenges, how to better attract investment from European SMEs, approaches to boost the quality of vocational school graduates and how to develop a compliance-based approach to environmental protection enforcement.

22 FEB
TIANJIN

Tianjin Chapter hosts the Tianjin Municipal Commerce Bureau

Catherine Guo, general manager of the Tianjin Chapter, welcomed Yan Zeng, the new Deputy Director General (DDG) of the Tianjin Municipal Commerce Bureau, as well as representatives from the bureau's various relevant divisions, to the Chapter's offices on 22nd February. What ensued was a fruitful discussion on the new structure of the Commerce Bureau as well as topics as varied as the US-China trade conflict's impact on European companies in China, the development of SMEs and the local free trade zone. In conclusion, DDG Zeng expressed strong interest in organising further high-level dialogues with the Tianjin Chapter and fostering a close relationship with European business. Eb

Fresh Horizons

Prospects for Growth in China's Cruise Shipbuilding Industry

By Davide Cucino

Cruise holidays have long been popular among European and North American travellers, but Chinese tourists are now increasingly getting on board with the passion for 'floating cities'. But the industry may miss out on this golden opportunity due to a shortage of ships and backlogs in the building yards. **Davide Cucino** of **Fincantieri** argues that China is best placed to benefit from this situation, with a little help from European stakeholders.

An article published in the November/December issue of *EURObiz* highlighted the tremendous shift the Chinese shipbuilding industry is taking toward a high-end, value-added technology context. This represents a challenge for European business as well as an opportunity, given the huge gap that still exists between the industries of our continent and those of China in this sector.

To meet its ambitious expectations, China is determined to build a domestic cruise shipbuilding industry. Partnership with some major European stakeholders, such as Fincantieri among others, will enable the country to improve its technical knowledge when it comes to the shipbuilding high tech sector. It will also help to set up a proven supply chain, increasing the opportunities for all those companies in Europe which are looking for expansion in new markets. In fact, at least 70 per cent of a cruise ship is composed of systems and components, therefore the interests at stake for many of the SMEs in the sector are self-evident.

Production backlogs

As a matter of fact, the European cruise shipbuilding industry is now booming. There are only a few large shipyards in the region, and they have an orders backlog that means many new cruise ships cannot be delivered until 2027. By 2019, the global cruise ship order portfolio (including memorandums of understanding and letters of intent) amounted to 103 units, corresponding to 252,000 lower berth (LB). That figure alone is equal to 45 per cent of the world's currently available fleet. Even the ferries segment is showing strong signals of market recovery right now.

"In fact, at least 70 per cent of a cruise ship is composed of systems and components, therefore the interests at stake for many of the SMEs in the sector are self-evident."

In this ideal context, the only possible solution to the production backlog is to find new suitable locations for large shipbuilding yards around the world. China seems to be the best option in terms of large facilities, talent availability and market demand share. New propulsion technology developments (LNG and hybrid) as well as more stringent international environment requirements are also reasons for operators to look toward a new generation of vessels.

Finally, AI innovative solutions to better operate and maintain the newly-built intelligent cruise ships are changing both shipbuilders' and ship-owners' approaches toward the construction of such floating cities. China has highlighted through measures introduced in recent years its interest of working in these innovative fields, such as by providing R&D funds to develop technical skills. European business is requesting to be involved more in such initiatives and demanding equal access to financial incentives.

Costa Venezia Cruise Ship.
Photo: *Filippo Vinardi*

Cruise ship tourism

In China, around 200 million consumers now belong to the middle class. They are looking for new modes of entertainment they believe will improve their quality of life, including tourism and leisure. This is an ideal foundation on which to create the world's largest high-class cruise industry. Since 2012, the number of Chinese tourists going on cruises has been increasing, reaching 2.8 million passengers by the end of 2017. The target for 2020 is 4.5 million, even though there are still a number of hurdles to overcome before that goal becomes achievable.

In any case, China has already overtaken Germany to become the world's second largest cruise market after the United States. China is seeing a double-digit annual increase that may allow it to reach 10 million customers by 2026. This result, however, is still marginal if we compare it with the penetration rate of cruises in the industry's traditional markets of Europe and North America. Chinese cruise tourist numbers still represent only 0.5 per cent to 1 per cent of travelers globally, compared with 3.5 per cent for both Europe and North America. Meanwhile, Chinese tourists have also developed a sophisticated demand for services that do not necessarily match with how cruise ships have so far been built: among those are more digital connectivity, different type of cuisines, more gaming and karaoke facilities, cabin configurations to accomodate larger families, and enhanced shopping choices. Chinese passengers' expectations will be the driver for a 'revolution' in the concept of cruise ships.

"In China. around 200 million consumers now belong to the middle class. They are looking for new modes of entertainment they believe will improve their quality of life, including tourism and leisure. This is an ideal foundation on which to create the world's largest high-class cruise industry. "

The Chinese shipbuilding market

China has focused in recent years on supporting the development of high-tech shipbuilding. Many European manufacturers of vessels and components have stayed away from the Chinese market as the country's overcapacity in some segments was caused global crises, especially regarding traditional oil and gas vessels and low-end merchant vessels.

However, in recent months, China has put new policies into effect in order to allow foreign business to invest directly in the domestic industry. Further, the restrictions on "Design, manufacturing and repair of ships (including sections)" in *The Special Administrative Measures on Access to Foreign Investment (Negative List)* have been removed in the 2018 version of the document. The attention of industry stakeholders has been caught by the new Foreign Investment Law approved during the recent Two Sessions—in which it was indicated that technology transfer cannot be imposed on foreign investors—as well as the publication of the draft of the *MOFCOM Encouraged Industry Catalogue*, where further opening is foreseen in the sector.

More opportunities may come from the recovery of the global oil and gas sector, especially in the domains of deep-sea mining and renewable energies exploitation. New and innovative vessels are needed to access resources located in harsh marine environments while also keeping the marine eco-system intact as much as possible.

Even in this context, China has a lot to learn, and potential collaboration with shipbuilders as well as in systems and components could create win-win situations. Under the framework of collaboration between China and the EU Member States' companies in third countries, parties will have the chance to intensify the implementation of projects along the maritime Silk Road.

"China has a lot to learn, and potential collaboration with shipbuilders as well as in systems and components could create win-win situations."

To conclude, despite the complexity of the shipbuilding industry in China and difficulties that European companies have met in the past, a new era of opportunities is taking shape. There is a need for China to further open up its market so that both Chinese and foreign companies in the sector can equally benefit from those chances and introduce innovative technologies and solutions.

***Fincantieri** is one of the world's largest shipbuilding groups and number one for diversification and innovation, with over 230 years of history and more than 7,000 vessels built. It is a leader in cruise ship design and construction and a reference player in all high-tech shipbuilding industry sectors, from naval to offshore vessels, from high-complexity special vessels and ferries to mega yachts, as well as in ship repairs and conversions, production of systems and mechanical and electrical component equipment and after-sales services.*

PLANNING NEW E-VENTURES

China's Funding Strategy for Artificial Intelligence

By Alessio Petino

2018 appeared to be a turning point for the European Union (EU) in terms of artificial intelligence (AI). In December, the European Commission released a *Coordinated Plan on Artificial Intelligence* with EU member states. This followed the EU's earlier decision last year[1] to increase investment in AI by at least euro (EUR) 20 billion under its research and innovation programme Horizon 2020. Meanwhile, China has become a key player on the global AI scene. Since 2015, the Chinese Government has been extremely proactive in establishing AI initiatives. The State Council released a national strategy on AI in July 2017, with the aim of making China the industry's world leader by 2030. **Alessio Petino** from **DEVELOPMENT Solutions (DS)**, tells us more about China's plans for funding its AI industry.

Funding is a central part of China's State Council's national AI strategy. The 2017 plan proposed a "forward-looking '1+N' funding project cluster strategy" for AI –establishing '1' new megaproject focusing exclusively on new generation AI; and including several 'N' tasks and topics relating to AI in pre-existing national funding programmes. The strategy aims to create a synergic funding support mechanism linking together basic research with application, demonstration and commercialisation of AI technologies. This means it will be government-guided but market-driven, with each actor having a precise role.

Implementation of the '1+N' funding strategy for AI

Eighteen months later, the '1+N' funding strategy has already led to noteworthy developments within the five main pillars at the core of China's national innovation funding system. These five areas are as follows:

1. The *New Generation Artificial Intelligence* 'megaproject'

In October 2018 the first annual call for the *New Generation Artificial Intelligence* 'megaproject' was made. A total of Chinese yuan (CNY) 870 million will be allocated to support up to 39 projects in the areas of new generation AI, key technologies and smart chips and systems.

2. National Natural Science Fund (NSFC)

Basic and applied research proposals in AI in 2018 (in areas such as machine learning, pattern recognition, cognitive neurosciences, as well as cross-disciplinary studies in mathematics and education) became eligible for funding from the National Natural Science Fund. The NSFC also launched a major research project the same year on *Fundamental Theories and Key Technologies for Coexisting-Cooperative-Cognitive Robots* ('Tri-Co Robots'). This explicitly encourages joint proposals with internationally-leading scientists in the field of robotics.

3. National Key R&D Programmes

Four new National Key R&D Programmes (NKPs)—China's largest programme supporting commercialisation-oriented R&D—were established in AI-related areas in 2018, bringing the total number to 10. Many NKPs in other fields also started to design an increased number of AI-related subtopics—such as AI-based diagnostic medical imaging, financial risk calculation methods, and garbage sorting and transportation.

4. Development of AI technologies and talent

Infrastructure and platforms for develop-

1. *Artificial Intelligence: Commission Outlines a European Approach to Boost Investment and Set Ethical Guidelines*, European Commission, 25th April 2018, viewed 26th February, <http://europa.eu/rapid/press-release_IP-18-3362_en.htm>

CHART 1

New Generation Artificial Intelligence 'megaproject'

FUNDAMENTAL THEORIES OF NEW GENERATION AI	KEY TECHNOLOGIES SERVING MAJOR NEEDS	SMART CHIPS AND SYSTEMS
1. New generation neural network models	1. Knowledge learning and computing engines	1. New types of sensory devices and chips
2. Adaptive sensing for open environments	2. Cross-medium analytical reasoning technology systems	2. Key standards and validation chips for neural network processors
3. Cross-medium causal interference	3. Scene active sensing technologies during cognitive tasks	
4. Game theory-based decision-making under scenarios of incomplete information	4. Stimulation and convergence of collective intelligence for group software	
5. Emerging mechanisms and calculation methods of collective intelligence	5. Software and hardware technologies for human-machine coordination	
6. Man-in-the-loop hybrid enhanced intelligence	6. Autonomous intelligent perception and operation in unmanned systems	
7. Human-machine integrated control methods in complex manufacturing environments	7. Autonomous smart agents' dexterous and precise operation and learning	

ing AI technologies and talent started to appear across the country. These were concentrated in three main directions:

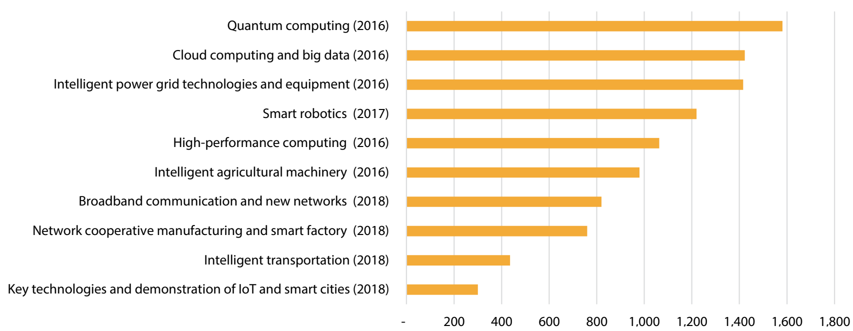
- Universities and research structures (with at least 10 State, Ministry or Engineering Key Laboratories).
- Hundreds of industry-university joint structures and degree programmes (focusing on industrial experimentation and application of fundamental AI theories and results, and directly hiring new graduates every year).
- Pure industry bases (with five national AI champions—Baidu, Alibaba, Tencent (BAT), iFLYTEK, and SenseTime—selected by the Ministry of Science and Technology (MOST) to host open innovation platforms. The five saw such benefits as local administrations offering strong regulatory support to test their technologies).

5. Investments in tech start-ups

Finally, China's '1+N' funding strategy for AI is also backed by vast investments in tech start-ups, both by government-guided funds (e.g. the Technology Innovation Guiding Fund, with CNY 290 billion) and by private actors. These are led by BAT, and followed by extremely active PE/VC firms, both Chinese—such as Sinovation Ventures, Cash Capital, Legend Star, Zhenfund—and foreign, such as Sequoia Capital and Intel Capital.

CHART 2

National Key R&D Programme



Source: *National S&T Information Service Platform*

Replication of the '1+N' AI funding strategy at the local level

Several local administrations across China are replicating the central government efforts. By the end of 2018, 13 out of 31 provinces, direct municipalities, autonomous regions in Mainland China had released their own strategies and policies for the development of AI. The provinces roughly correspond to the areas where the majority of AI companies (light yellow bars in Chart 3) and talent (yellow bars) are concentrated.

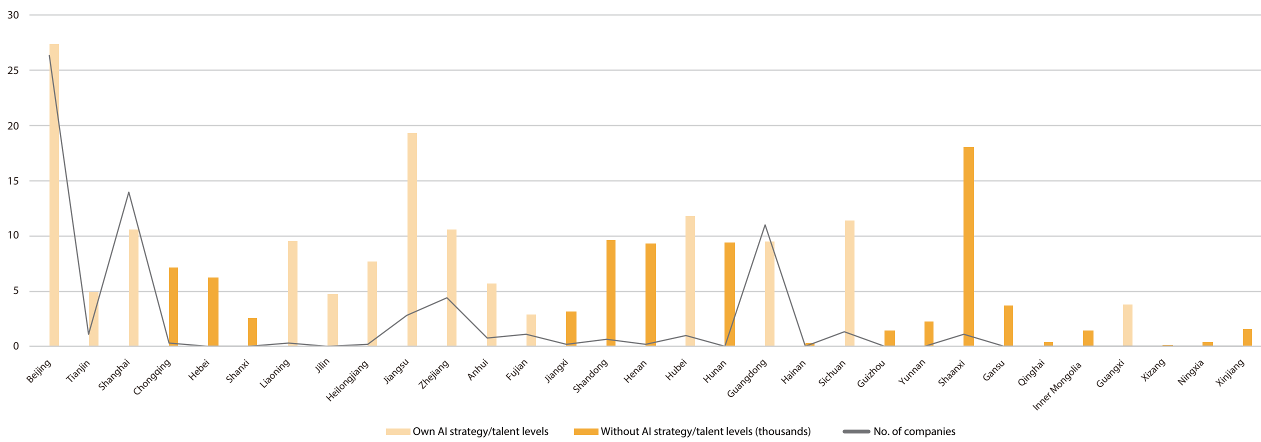
Even more notably, three main clusters now dominate China's AI scene: Beijing; Shanghai and the Yangtze River delta; and the Pearl River delta led by Shenzhen.

Beijing's published policy, the *Guiding Opinions on Accelerating Science, Technology and Innovation to Nurture Artificial Intelligence Industries in Beijing*, outlined how the country's undisputed leader in AI plans to invest nearly CNY 14 billion on an AI technology park in Mentougou suburb district. In February 2019, the Beijing New Generation Artificial Intelligence Development National Experimental Zone—the first of its kind in China—was officially announced, to focus on AI talent growth and industry development, and act as a pilot base for institutional reform. It will set up series of 'no man's lands' where innovators will be able to experiment, test and integrate new AI-related technologies and prototypes – with very few regulatory restrictions.

The Yangtze River delta region—with Shanghai at its heart—is also aiming to become a global hub for AI. The *Implementation Measures for Accelerating the High-Quality Development of Artificial Intelligence in Shanghai* (September 2018) policy discusses significant increases in support for enterprises that conduct R&D

CHART 3

Released Strategies and Policies for AI Development



Source: *Data related to provinces with AI-related strategies was collected from websites of relevant provincial-level governments.*
Data related to the distribution of companies and talent was extracted from the China Artificial Intelligence Development Report 2018.

and related activities on AI. This will be mainly done through a CNY 100 billion guiding fund, and credit funds by local financial institutions. All these 'N' measures complement the Shanghai AI Innovation Development Special Programme, which annually funds dozens of R&D, application and commercialisation projects (83 projects were funded in 2018—including three to Sino-foreign joint ventures—each receiving around CNY 3 million).

The Pearl River delta, led by Shenzhen, is also emerging as a key AI hub in China, though lacking the pools of talent, institutional knowledge and start-ups Beijing and the Yangtze River Delta enjoy. In line with the *Plan for the Development of New Generation AI in Guangdong Province* (August 2018), the provincial government established its own version of the '1+N' funding strategy: the Provincial Key R&D Programme in New Generation AI will grant CNY 5 to 10 million to around 20 projects in 2019, while other existing programmes (e.g. the Guangdong Industry Development Fund) will add other 'N' AI-related tasks. These will complement incentives and subsidies offered by local municipal administrations, e.g. Shenzhen subsidies for enterprises replacing their equipment with robots.

Opportunities for international actors

In the State Council's national strategy, there is no mention of opportunities for international enterprises or research structures to participate in Chinese funding programmes. Only a few world-renowned international talent and teams stood to benefit from national funding through the 'Thousand Talents Plan', in particular in the fields of neurocognition, robot learning and auto-piloting vehicles.

What the strategy does encourage is the establishment of AI R&D facilities in China, and cooperation with Chinese domestic actors on AI research (Microsoft probably offers the best example, with joint key laboratories established with the Ministry of Education and the Harbin Institute of Technology, and with Shanghai Jiaotong University).

At the local level, several municipalities and provinces have established ad hoc funds for this purpose. One example is the Shanghai Special Fund for Encouraging the Development of Foreign-invested R&D Centres and Regional Headquarters, which offers several types of financial support to MNCs establishing (or upgrading) a base in Shanghai.

Chinese incubators and accelerators are also starting to target foreign AI start-ups. In December 2017, COMB+ (known for its joint accelerator with Finnish Pivot5) announced the establishment of a 65 million EUR fund for AI start-ups wishing to enter China.

European companies and innovators, therefore, in addition to a large and growing pool of AI talent, can also benefit from several funding programmes and incentive schemes offered by Chinese administrations – though those at the local level currently appear more accessible. Eb

Alessio Petino *is a Senior Project Manager at* ***DEVELOPMENT Solutions (DS)*** *– a European consultancy with a primary focus on supporting EU external policies and cooperation strategies towards strategic partner countries. Petino currently also serves as project expert on the EU-funded Improving EU Access to National and Regional Financial Incentives in China, which has the objective of increasing framework conditions for boosting European participation in Chinese innovation funding programmes.*

WTO Appellate Body Crisis

By Shane Farrelly

Stuck Between a Rock and a Hard Place

Thirteen members of the World Trade Organization—including the European Union—met in Ottawa in October to discuss the increasing need for reform of the international body. The 'Ottawa 13' proposed focusing primarily on reforming the body's monitoring function, strengthening its dispute settlement system and updating trade rules: in summation, modernising the WTO. However, the most pressing of these issues seems to be the current dispute resolution system. The process once was a source of reliable and predictable rules, but has since been stripped down to its bare bones. For the WTO to be able to guide global commerce in the rapidly evolving economies of the 21st century, immediate action must be taken. **Shane Farrelly** of **D'Andrea & Partners** identifies what the proposed reforms could mean for the international business community.

Appellate body in crisis

It is no secret that, at the time of writing, the WTO's main arbitration body of trade disputes is in difficulties. The WTO's highest court is set to have only three judges on its roster (it is designed to have a roster of seven), which is considered the minimum number required to sign off on any dispute resolution. Meanwhile, appeals continue to pile up amid international scrutiny of the WTO. The Appellate Body may even soon be rendered inoperable, as the four-year terms of two of these judges (Ujal Singh Bhatia from India and Thomas Graham from the US) will run out on 10th December 2019. If new judges are not appointed before then, the global trade body will become incapable of adopting decisions. To add further pressure, the remaining judge, China's Hong Zhao, is set to finish her term on 30th November 2020.

The crisis has been aggravated by the United States repeatedly vetoing the initiation of a process to nominate and appoint Appellate Body members, citing various criticisms. This is a long-standing thorn in the side of the Appellate Body, as multiple US administrations have levied critiques towards it, such as over its perceived judicial overreach and frequent failure to meet the 90-day deadline for reports provided for in the WTO's Dispute Settlement Understanding (DSU). These concerns of the US are no doubt heightened by ongoing trade tensions with China.

Proposals for reformation

A number of WTO members—principally China, the European Union and some of its member states—have put forward several proposals via joint communications for the body to consider. These include requiring the Appellate Body to: consult with parties involved in disputes if it anticipates exceeding the 90-day deadline; limiting the body's findings to those "necessary for the resolution of the dispute,";[1] and allowing Appellate Body members to serve one single longer term instead of the two four-year terms under current rules.[2] However, despite the United States being one of the main advocates for WTO reform, it does not acknowledge that these proposals often run contrary to the US' own standards.

If the WTO's formal appeals process and its ability to issue binding rulings becomes paralysed, countries may abandon the multilateral system altogether and resort to unilateral retaliatory measures to settle trade disputes.

Possible solutions already in place?

While the Appellate Body crisis continues to loom over the WTO, there are alternative dispute resolution methods available to members. According to Article 25 of the DSU, "expeditious arbitration within the WTO as an alternative means of dispute settlement [...] of certain disputes that concern issues that are clearly defined by both parties [...] which shall agree on the procedures to be followed." This allows parties to a dispute to vaguely define what aspects they wish to solve via arbitration proceedings, and what rules to follow thereof, seemingly providing a parallel dispute settlement structure within the WTO framework.

The procedures of such arbitration could mirror those of the Appellate Body but, instead of appointing judges, parties outside of the dispute would have no involvement unless with prior consent of the parties involved. The parties involved would also be able to appoint personnel to hear appeals of any judgement, thus preventing the United States from further impeding dispute resolution procedures.

1. *Communication from the European Union, China, Canada, India, Norway, New Zealand, Switzerland, Australia, Republic of Korea, Iceland, Singapore and Mexico to the General Council*, World Trade Organization, 26th November 2018, viewed 7th March 2019, <http://trade.ec.europa.eu/doclib/docs/2018/november/tradoc_157514.pdf>
2. *Communication from the European Union, China and India to the General Council*, World Trade Organization, 26th November 2018, viewed 7th March 2019, <http://trade.ec.europa.eu/doclib/docs/2018/november/tradoc_157514.pdf>

Concluding thoughts

In utilising Article 25, parties to the dispute would need to sign an agreement that they will be bound by the decisions of the arbitration. However, this option is merely a short-term solution to a very large problem in the WTO. While reform proposals are being presented, replacing the function fulfilled by the Appellate Body through a system based around Article 25 may ensure that trade conflicts will continue to be resolved within the multilateral WTO framework. If the vacant seats in the Appellate Body are not filled by the end of the year, the WTO's dispute settlement system will essentially be incapacitated, its rules will be unenforceable and members may abandon it altogether in favour of bilateral and regional trade agreements. The hope is that a comprehensive reform of the WTO prevails, to provide a multilateral solution that will allow world trade to prosper under new rules.

As an aside, it should be noted that the EU and China are already collaborating on establishing a working group to reform the WTO as a whole, and not only the Appellate Body. These efforts aim to modernise trade rules, especially for new and emerging industries such as the e-commerce sector. The move reflects the cooperative approach between the EU and China. As two members that have benefitted enormously from the WTO, their combined efforts may lead to an overhaul of the global trade body in a more progressive way. Eb

***D'Andrea & Partners Legal Counsel**, DP Group was founded in 2013 by Carlo Diego D'Andrea and Matteo Hanbin Zhi, both of whom have extensive backgrounds in Chinese and EU law. DP Group currently has four service entities: D'Andrea & Partners Legal Counsel, PHC Tax & Accounting Advisory, Eastant Communication and Events, and Chance & Better Education Consulting. DP Group has a variety of branches around the world, with locations in several major developing economies.*

Spotlight on China's Individual Income Tax Reform

By Melody Ma and Rachel Yao

How Taxpayers Will Be Impacted and the Steps They Should Take

China's amendment of its Individual Income Tax (IIT) Law in 2018 was a new landmark in tax development in the country. **Melody Ma** and **Rachel Yao** of **Deloitte Tax China** outline for us the details of the reform, the challenges it has brought and the actions that should be taken, particularly by foreign taxpayers.

Background/objectives of the IIT reform, and where it leaves us now

Having significantly reformed the corporate tax system and introduced VAT in previous years, China continued its pursuit of a major transformation of its tax system in 2018. This reform saw the individual income tax system overhauled. The resulting 7th amendment to the Individual Income Tax Law was approved by the Standing Committee of the People's National Congress in August 2018. In contrast with previous amendments, this change has caught the attention of the public, as it materially changes the original IIT Law system. The reform is intended to ease the tax burden for low-income earners in particular, enhance the taxation equity principle and boost consumption while combating the effects of rising living costs under the fast economic growth in China.

The new IIT Law became effective on 1st January 2019, after a series of relevant regulations and rules were unveiled in late 2018. Following rules and regulations with practical guidance on taxation and filings will be released gradually.

On 12th March 2019, the Second Session of the 13th National People's Congress held its third plenary meeting in the Great Hall of the People in Beijing. This is the interview with Wang Jun, director of the State Administration of Taxation, in the "Ministerial Channel".
Photo: *Yin Gang, Xinhua News Agency.*

Key changes to all tax payers

The amended IIT Law introduces a basket of fundamental changes that affect the tax system at its calculation, application and enforcement stages, for both Chinese and foreign nationals. The key amendments can be summarised as follows:

- **Tax residence rule** – introduction of a 183-day test to define tax residence for non-domiciled individuals.

- **Tax categories** – consolidation of four categories of income (salaries and wages, remuneration for independent services, author's remuneration, and income from royalties) into a single new category called "comprehensive income".

- **Tax rates and brackets** – broadening of the three lowest tax brackets.

- **Standard deduction** – increasing the standard tax-free deduction from Chinese yuan (CNY) 3,500 per month to CNY 5,000 per month, repealing the additional deduction of CNY 1,300 per month available for foreign individuals.

- **Additional itemised deductions** – resident taxpayers will be allowed to deduct certain additional items from their comprehensive income. These items include education expenses for children, expenses for further self-education, health care costs for serious illnesses, housing loan interest/housing rent, and expenses for taking care of elderly parents.

- **Tax assessment, collection and filing** – introduction of a new annual assessment and filing requirement for the comprehensive income of resident individuals.

- **Tax clearance requirements upon emigration** – taxpayers must settle their IIT liabilities before they can deregister their Chinese household registration (户口, or hukou in Chinese) if they plan to emigrate.

- **Anti-avoidance rules for individuals** – the introduction of anti-avoidance rules into individual income tax will give the authorities additional powers to enforce tax adjustments on non-arm's length transactions (where two or more parties involved have some vested interest in helping each other, e.g. family members, affiliated businesses) among related parties, offshore tax avoidance schemes, and commercial arrangements from which inappropriate tax benefits are derived.

Interpretations of the relevant rules for foreign individuals

From a China IIT perspective, foreigners (including Hong Kong, Macau and Taiwanese citizens) working in China are generally considered non-domiciled taxpayers, since they are not deemed as habitually residing in China due to their main family and business interests, unless under special situations.

Spend 183 days or more in a calendar year in China, become a tax resident

Under the 2018 amendment, non-domiciled individuals, such as foreigners, who live and work in China will now be subject to the 183-day test - a rule that draws upon recognised international practices. A foreign individual who resides in China for 183 or more days in a year is considered a resident for the tax year concerned.

Five-year rule becomes six-year rule

The old IIT law provided a five-year rule on tax residency. Non-domiciled individuals working or living in China did not have to pay tax on their worldwide income before spending five full consecutive years in China.

Under the new IIT law, the five-year period has been extended to six years. If the non-domiciled individual has not been a tax resident in any calendar year during a six-consecutive-year period, the individual will be exempt from Chinese IIT on income that is nether sourced in China nor paid by a Chinese enterprise or individual. The six-year clock will also be restarted if someone stays outside China for more than 30 days in a single trip in a calendar year in which they stay in China for 183 days or more. A tax registration is required to qualify for the six-year rule; the tax authority will provide guidance on the registration requirements. China days/years spent prior to 2019 will not be counted for the six-year rule.

Tax-exempted fringe benefits – continued or not?

In tax years 2019, 2020 and 2021, eligible foreign individuals can still enjoy non-taxable fringe benefits. Once a foreigner becomes a resident taxpayer, they can either avail of the additional itemised deductions outlined under the new IIT Law for that tax year, or enjoy the non-taxable fringe benefits that are only applicable to foreigners. From 2022 onward, fringe benefits on housing, children's tuition and language training could become taxable.

Taxation on comprehensive compensation – resident vs non-resident

Tax implications are quite different for residents and non-residents when it comes to comprehensive income, with respect to areas such as tax calculations and withholding methods, monthly and annual filing procedures, rules on the tax-exempted items/benefits and tax treatment on annual bonus and equity incentive income, etc.

Major impacts for foreign individuals in China

Compared to the old IIT Law, all the changes mentioned above will have significant impacts for foreign individuals in China. Foreigners and their employers should definitely take appropriate actions to cope with these changes to the new IIT Law.

Meanwhile, under the new IIT Law, a unique tax code will be assigned to each taxpayer, including foreign individuals. This allows the government to scrutinise and control the social credit of each taxpayer, including foreigners.

Practical considerations for companies and foreign individuals

Foreign taxpayers should acknowledge the key changes as well as the impacts under the new IIT regime, to properly manage their tax issues.

With the changes such as the residency definition and six-year rule provided under the new IIT Law, foreigners should review their residence status, and pre-plan any travel in a tax year to meet their compliance obligations.

Since certain fringe benefits provided to foreigners will become taxable after 2022, foreign taxpayers should review their compensation package, quantify their net pay and tax burden and monitor their cash flow.

Companies wishing to follow the developments and face the challenges brought by the new IIT regime should consider:

- Arranging sufficient communication among employees of the IIT reform changes and impacts;
- Reviewing internal policies and procedures to ensure the new compliance requirements can be accommodated;
- Assessing how different groups of foreign employees are impacted by the amended law; and
- Leveraging technologies to upgrade existing internal financial and tax systems to fulfil their withholding obligations and achieve administration efficiency. Eb

Deloitte China Tax and Business Advisory *is the only 'Big Four' practice that works As One across the Greater China Region, including the Chinese Mainland, HK, Macau and Taiwan, to advise and assist clients on tax and business issues. Melody Ma (Tax Director) focuses on PR China IIT services to multinational companies, domestic companies, and individuals, and has extensive experience on tax compliance, tax and business advisory and tax planning. Rachel Yao (Senior Tax Manager) specialises in PR China IIT compliance and consulting services.*

EUROPEAN CHAMBER IN THE MEDIA

European Chamber's Stance and President Mats Harborn's interview on the Foreign Investment Law

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《外商投资法》全文公布 务实修法获称赞

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随着正式文本公布，不少人发现，他们曾经通过公开渠道提交的意见，在最终版本得到体现。中国欧盟商会主席何墨池（Mats Harborn）对第一财经记者称，《外商投资法》最终版本考虑到了中国欧盟商会的一些建议（体现在第4、9、16、23、24和26条），意味着这些反馈得到了关注。


South China Morning Post

China Economy

Chinese Premier Li Keqiang says foreign investment law shows Beijing is serious about opening economy further

The European Union Chamber of Commerce, which represents EU firms doing business in China, welcomed the enactment of the foreign investment law, saying the approval increases the likelihood that Beijing's promises regarding opening up "will become a reality".

However, it repeated its concerns that the ambiguous wording of some clauses raise the possibility of problems with implementation.

> More than anything else, foreign companies want equal treatment and opportunities.
> Mats Harborn, EU Chamber of Commerce, China

The chamber said that despite two rounds of public consultation, the law still contains "vague" clauses that would give China the power to take unilateral action against trading and investment partners if the government felt it was being treated unfairly in a foreign country.

In that regard, the new law creates further uncertainty for foreign companies, the chamber said.

On 15th March 2019, The National People's Congress passed the new Foreign Investment Law. The European Chamber released an official stance on the final draft, to follow up on its earlier stance on the draft law during the public consultation process.

Please find the stances on the European Chamber's website, under 'Press Release' in the 'News' column.

On the same day, President Mats Harborn was interviewed by *CGTN* and *ARD*, and shared European businesses' view on the impact of the law. During the interviews, President Mats Harborn highlighted that there should be no legal distinction between foreign and local companies, unless it is to provide exceptions for legitimate reasons such as specific national security concerns. He added that now the Foreign Investment Law law has been passed, the Chamber will closely monitor its implementation to ensure it is fully respected at all levels of government and in all corners of this country.

European Chamber's Stance on the Government Work Report

Economic Observer


eeo 经济观察网 .com.cn

欧盟中国商会主席积极建言献策，他怎么看政府工作报告?

经济观察网 记者 张文扬 于3月5日发布的2019年政府工作报告获得了外资的关注。就在报告发布的当日，欧盟中国商会(European Union Chamber of Commerce in China)主席何墨池(Mats Harborn)表示，他已经关注到了这份工作报告。

"我们希望这份工作报告能够真正推动创建一个公平、监管良好、具有全球特色的中国市场。"何墨池如是说。

何墨池认为，正如预期的那样，政府工作报告涵盖了对中国未来发展至关重要的议题。这些问题包括中国2019年6%至6.5%的增长目标等经济问题，中国的去杠杆化运动，以及在整个经济领域降低税费的计划，以及扶贫、医疗和环境保护等社会问题。

欧盟商会显然注意到了其中的机遇。何墨池指出，在所有这些领域，欧洲企业可以提供高质量的产品和服务，并分享他们的经验，帮助中国实现报告中提出的具体改进目标。但他也指出，前提是他们具备适当的条件。因此，欧盟商会继续敦促中国履行扩大市场准入的承诺。

On 5th March 2019, the annual work report was delivered to the National People's Congress (NPC), during the yearly plenary sessions of the NPC and the Chinese People's Political Consultative Congress. The work report reviewed last year's progress before covering ten main areas of focus for 2019. The European Chamber released its stance on the report, highlighting the areas closely related to foreign companies operating in China. President Mats Harborn also delivered comments to the *Economic Observer*, saying that the comprehensive government work report covers many essential topics relevant to China' s development, and he hopes it can actually promote the process of the Chinese market becoming fair, well-regulated and with global characteristics.

Southwest China Chapter Chair Paul Sives' interview with *Chengdu Daily*

Chengdu Daily


注入强大活力 国际化营商环境建设年动员大会上嘉宾们有话说

On 11th February 2019, Chair of the Southwest China Chapter Paul Sives was invited to attend the Conference of International Business Environment Mobilisation Year. He was interviewed by *Chengdu Daily* at the conference, and introduced the European Chamber and the Southwest China Chapter. He also shared that members of the European Chamber have a strong willingness to invest in southwest China, and that well-functioning logistics and a good business environment created by local governments have demonstrated their efforts to attract foreign investment.

Nanjing Chapter's Innovation Fair and Innovation Week Promotion Event

Nanjing Daily


南报网 njdaily.cn

中德创新企业推介会在宁举办

On 25th February 2019, over 100 German members of a Baden-Württemberg Delegation and 700 representatives of Jiangsu companies met at the Innovation Fair and Innovation Week Promotion Event hosted by the Nanjing Chapter and Messe Nanjing. Media reports briefly introduced this event and the cooperation between Jiangsu and Baden-Württemberg, with the Chamber being mentioned as the organiser of this event.

EVENTS GALLERY BEIJING

European Chamber Hosts 2019 Cybersecurity Conference

Key takeaways:

- Multinationals need to be prepared for the Cybersecurity Law at all levels.
- Predictions for 2019: China's cross-border data regulatory framework unveiled; the Critical Information Infrastructure Protection Regulation promulgated; the Classified Cybersecurity Protection Scheme (CCPS) in place; and law enforcement efforts intensified.
- A variety of factors such as interoperability, maintenance, security and licensing need to be jointly taken into consideration before a decision is made on the issue.
- Novelties of the revised standard include: requirements on prohibiting forced collection of personal information personalised display and opt-out; aggregation and fusion of personal information collected for different services/functions; recording personal information processing activities; and management of access by third parties.

Three Years On: How is China Manufacturing 2025 Rolling Out

Key takeaways:

- The China Manufacturing 2025 initiative has been downplayed in media and government messaging, but is still continuing to progress at all levels of government throughout China.
- Local governments often classify their regional industries as key sectors so as to allocate support to them. This will drive unfair competition in some sectors and is likely to raise overcapacity.
- New government funds are being raised to finance CM2025 projects, but they are struggling to reach their goals and many are sitting on the funds they have secured.

EVENTS GALLERY SHANGHAI

2019 HR Excellence Conference: Upgrade Your Retention Formula

Key takeaways:

- Managing people is the very core of business building.
- Binding people through their common experiences is what a leader should do.
- Understanding the company's cultural approach is essential, whether Chinese, foreign, or hybrid.
- Bottom-up feedback needs to be heard.
- The HR department should be able to push the company to adapt to the new technological age.
- To fill jobs in rural areas, choose the right person: young people want to work in a place where they can grow and develop, and you have to find that person.

Leadership for Digital Transformation: Define the Critical Skills for Digital Success

Key takeaways:

- Many companies have embarked on digital transformation of their business processes to improve efficiency and customer engagement.
- Some management teams are finding the journey challenging and not seeing the expected improvements.

EVENTS GALLERY NANJING

European Chamber Business Dialogue with Nanjing Government to Promote Open and Innovative Development

Key takeaways:

- The EU has been the largest trading partner with Nanjing for the past 5 years.
- Multinational companies encouraged to set up R&D centres, talent teams for entrepreneurship and innovation, technology services, new-energy auto and bio-medicine industries in Nanjing.
- Regulatory reform that expand on Nanjing's strengths to boost economy should be pursued.

EVENTS GALLERY SOUTH CHINA

European Business in China Awards Gala 2019

Key takeaways:

- Winners:
  - Top Performers in China Award: Andritz China Ltd., Siemens Transformer (Guangzhou) Co., Ltd
  - Innovation & Intelligence Award: TÜV Rheinland Greater China, Carl Zeiss Vision (China Ltd)
  - HR Excellence Award: HSBC Electric Data Processing Guangdong Ltd
  - Above & Beyond Award: Dezan Shira & Associates
  - Green Business Award: SHV Energy China
  - Chinese Champion in Europe Award: CITIC Telecom
  - Silk Road Awards: Stäubli
- The awards recognise businesses that have made exceptional contributions to, and act as role models in, the business community in both China and Europe.

EVENTS GALLERY SOUTHWEST CHINA

Speed Business Meetings (Chongqing & Chengdu)

- The speed business meeting is a long-standing event for the Southwest China Chapter
- The Chengdu office is re-starting the event from this year.
- Chongqing event co-organised with the Chongqing Association of Enterprises with Foreign investment, Chongqing Foreign Projects Service Center, Chongqing Overseas Chinese Chamber of Commerce, Youth Federation of Chongqing Overseas Chinese, Chongqing Returnees Club, Chongqing Yubei Returnee Entrepreneurship Association and Chongqing MBA Entrepreneur Association.
- Events provided an opportunity to meet other members of the business community through two-minute-long conversations.
- Guests continued to communicate in cocktail party after the business meeting.

ADVISORY COUNCIL NEWS

Volkswagen Opens Modular Electric Toolkit to Other Manufacturers

The vehicle manufacturer Volkswagen Group is opening its Modular Electric Toolkit (MEB), developed in recent years, to other manufacturers. The purpose is to achieve a significant reduction in the cost of e-mobility through the widest possible deployment of the MEB and the associated economies of scale, thus enabling broad access to individual mobility to continue. The Volkswagen Group is currently projecting a first wave of around 15 million pure electric vehicles based on the MEB. e.GO Mobile AG, based in Aachen, Germany, is to be the first external partner to use the platform to launch further electric vehicles in addition to Volkswagen's model range. A dedicated vehicle project is already being planned. Volkswagen highlighted the MEB's versatility – even for small series – with the ID.BUGGY on display at the Geneva International Motor Show.

BASF and Midea Group to Collaborate on Innovative Solutions

Chemical producer BASF and Midea Group Co Ltd, a leading electrical appliance manufacturer, signed a strategic collaboration agreement. According to the agreement, BASF and Midea will explore the applications of BASF's advanced materials and innovative solutions to Midea's electrical appliances portfolio, which includes refrigerators, air conditioners, washing machines, water purifiers and water heaters. BASF's material solutions offer many advantages for manufacturing partners such as the Midea Group. BASF's innovative polyurethane insulation materials help improve the energy performance and life expectancy of household applicances, and Formaldpure™ filters can reduce indoor formaldehyde pollution and keep indoor air healthy for homeowners. As part of the new partnership, BASF will develop a surface active agent for laundry detergents compatible with Midea's washing machines. This solution also helps protect garments during washing, thus further extending their overall life.

thyssenkrupp System Engineering Honoured at Daimler Supplier Awards

Industrial engineering firm thyssenkrupp System Engineering has been honoured with the Daimler Supplier Award 2018 in the category 'Partnership' (International Procurement Services). The awards were presented to ten outstanding suppliers by Dr. Dieter Zetsche, Chairman of the Board of Management of Daimler AG and Head of Mercedes-Benz Cars, further Daimler Board members and top purchasing managers in Stuttgart on 20th February 2019. thyssenkrupp System Engineering received the award as a longstanding partner that has recently set benchmarks with the development and construction of a battery assembly line for Daimler's first electric vehicle, the EQC.

The annual Daimler Supplier Award honour outstanding performance and partnerships with the vehicle manufacturer's suppliers. Quality, partnership, innovation, cost-efficiency, delivery reliability and sustainable behaviour are key criteria for the award.

Airbus Officially Launches Innovation Centre in Shenzhen, China

Airbus has inaugurated its Innovation Centre in China at an official opening ceremony in Shenzhen, China, one of the world's leading innovation hotspots. The Airbus China Innovation Centre (ACIC) has been operating since early 2018. It currently focuses on designing, testing, and certifying new technologies relating to five areas: Hardware Lab, Cabin Experience, Connectivity, Manufacturing Innovation and Urban Air Mobility (UAM). Airbus also signed a Memorandum of Understanding (MoU) with Shenzhen Municipal Commerce Bureau for close collaboration, acceleration, application and industrialisation of UAM. With extended regional partners, Airbus aims to further develop the local UAM ecosystem and promote solutions that fit local transportation needs. As Airbus' first disruptive innovation centre in Asia, and second worldwide after A3 in Silicon Valley, ACIC's mission is to fully leverage local advantages including talent, enterprises and the ecosystem, and combine them with Airbus' aerospace expertise to identify, explore and accelerate breakthroughs in technologies, business models and new growth opportunities.

Bayer Crop Science and Ministry of Agriculture Sign Green Development Plan

On 27th February, a Green Development Capability Building Action Plan signing ceremony took place at the Ministry of Agriculture and Rural Affairs (MARA). In attendance were Qu Dongyu, Vice Minister and from Bayer Crop Science Jesus Madrazo, Head of Agricultural Affairs and Sustainability, and Weidong Huang, Greater China Cluster Country Head. 'Embracing the Green Program' is a large-scale non-profit training programme jointly by Bayer Crop Science China and the National Agricultural Technology Extension and Service Centre

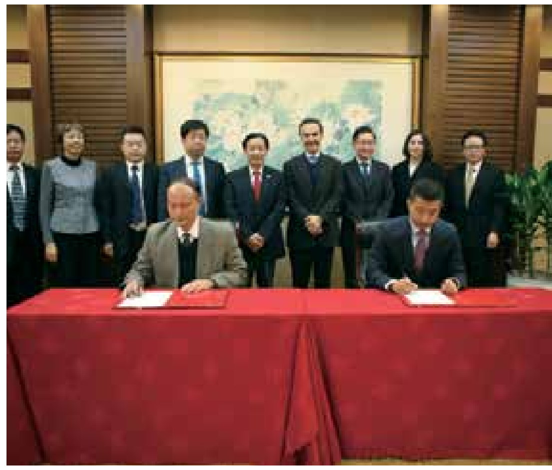
(NATESC), also a key part of Sino-German agricultural cooperation framework. It aims to build green development capacities among key players, i.e. local officials and technicians in agriculture, executives in new types of agribusinesses, service organisations and leads in co-operatives. The program helps improve capacity in green development policies, technologies and individual planning, and also promotes the latest concepts, standards, technologies and international best practices. The program will be implemented in the next five years (2019–2023) and cover all provinces and autonomous regions. Eb

Tell Us Your Big News

Chamber Members are welcome to add news items on their own activities to our website, and share it with all the other 1,600 members. Visit our website to find out more.

Dr. Günther Schuh, CEO of e.GO Mobile AG and Dr. Herbert Diess, CEO of Volkswagen AG in the Volkswagen ID. BUGGY.

Dr. Xu Chengmao, President of Midea Corporate Research Center (front right) and Dr. Zheng Daqing, Senior Vice President, Business and Market Development Greater China, BASF, sign the strategic collaboration agreement on the application of more advanced solutions from BASF to Midea's household appliances.



Bayer Crop Science and Ministry of Agriculture sign green development plan. In attendance were Qu Dongyu, Vice Minister and from Bayer Crop Science Jesus Madrazo, Head of Agricultural Affairs and Sustainability and Weidong Huang, Greater China Cluster Country Head.

Award presentation (from left): Wilfried Porth, Member of the Board of Management of Daimler AG, Human Resources and Director of Labour Relations, Mercedes-Benz Vans, Ingo Steinkrüger, CEO thyssenkrupp System Engineering, moderator Judith Rakers and Andreas Burkhart, Head of International Procurement Services.

Airbus inaugurates its Innovation Centre in China at an office opening ceremony in Shenzhen, China.

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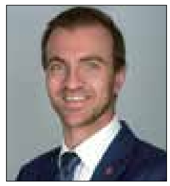

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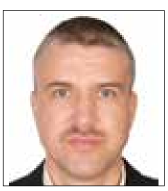

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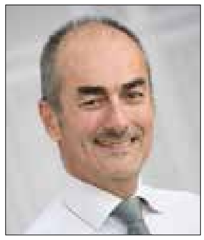
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