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China Representative Office Registration and Maintenance Guide (4)- Scope of Business of a China Representative Office

1. Scope of Business of Representative Offices

The business scope of a Permanent Representative Office (RO, also known as Resident Representative Office) should be clearly stated in the application document prepared by the applying foreign enterprise. After approval by the relevant authority and registration with the AIC, the business scope will be stated in the Registration Certificate of the Permanent Representative Office (RO). A Representative Office (RO) can only engage in business activities which are within the business scope as set forth in the Registration Certificate (business registration certificate).

Normally, ROs can only engage in non-operational activities in China, such as liaison, product promotion, market research and technology exchange. However, if a bilateral treaty between China and the home country of the foreign enterprise provides that Permanent Representative Office (RO) established by enterprises of both countries should have the authority to engage in direct operational activities, such provisions should prevail.

ROs will have the authority to engage in economic activities and sign economic contracts which are necessary to maintain the existence and function of the Permanent Representative Offices (RO). For example, a Representative Office (RO) enters into a purchase contract with a computer company, whereby the Permanent Representative Office (RO) will purchase a computer for office use. This contract for the purchase of computer contract should be valid because the purpose of this contract is to satisfy the basic needs of its operation.

The right to engage in activities to maintain its operations is an intrinsic right of a Permanent Representative Office. Such activities are not business activities. Examples include engaging the services of Chinese personnel, renting permanent office space, using a company chop, importing personal and office goods, opening a bank account in the name of the office, obtaining resident visas and other permits for expatriate employees.

2. Allowable Activities for a Permanent Representative Office

On approval, a RO will only be granted with a Permanent Representative Office Registration Certificate (BRC) rather than a Business License. The Implementation Rules for the Approval and Supervision of Representative Offices of Foreign Enterprises in China, announced by the Ministry of Foreign Trade and Economic Co-operation in February 1995, states that a Permanent Representative Office of a foreign enterprise (FE) (i.e. an entity incorporated or established outside China) is only allowed to engage in non-direct business activities for its head office and represent the FE to undertake activities such as:

- product liaison and promotion
- market research and technology exchange.

A Permanent Representative Office is prohibited from doing direct business with, or rendering services to, any other persons. Any violation of this restriction could result in a fine and even nullification of the Permanent representative Office's business registration in China. In addition, such direct business activities may result in the head office being considered as carrying on a taxable activity in China and hence may be subject to taxes in China.

Although there is no official definition of direct business, the following are the allowable activities for a Permanent representative Office in China:

- performing liaison, promotional and co-ordination functions for its head office
- buying or leasing its own office premises
- importation of reasonable amounts of normal office equipment (note: the imported commodities are subject to import customs duty and import taxes)
- importation of personal effects in reasonable amounts
- helping to obtain working visa and related applications in respect of expatriate employees
- contracting with an approved employment service organization in China for the provision of local staff to work for the Permanent Representative Office
- opening necessary bank accounts in the name of the Permanent Representative Office.

3. Restricted activities of a China Representative Office

- rendering services to any persons other than its head office (e.g. suppliers or customers of the head office, fellow subsidiaries or associated undertakings of the head office)
- soliciting, concluding or signing business contracts with any customers in China
- determining prices of goods or offering any sales discounts to customers
- issuing bills or invoices to customers
- collecting money from customers or issuing business receipts to customers
- warehousing and managing inventory in China for trading purposes
- hiring local staff directly without the use of an approved employment service organization in China
- any activities other than of a liaison nature (e.g. quality control services and installation and testing services) not specified in the BRC of the RO.

4. Complying with Limitations on Activities

The apparent intention of limiting representative offices to "non-direct business activities" is to ensure that representative offices act on behalf of the foreign-based companies they represent and not on their own behalf as separate business entities. Thus contracts signed by the representative office (other than those relating to its own administration, such as its office lease) should be signed in the name of its parent enterprise or one of its affiliates, not in the name of the representative office itself. Such contracts should also show an address outside of China for the relevant foreign party. Any sale and subsequent billing and collection of money for technical, consulting, inspection, or other services should similarly be carried out by the parent enterprise or one of its affiliates, not the representative office. Based on the regulations, representative offices should not perform the functions of a "service center".

5. Consequences of Exceeding the Limitation on Activities

If an established representative office is found to be "directly engaging in business activities", the Registration Procedures provide for penalties including fines of up to RMB20,000 and suspension of business activities. In practice, actual fines and sanctions are somewhat discretionary and determined on a case-by-case basis. It is possible that the representative office may be allowed to remedy the situation without sanction or that appropriate penalties will be determined on the basis of the amount invested in such activities and/or income generated through such business activities.

If you wish to obtain more information or assistance, please visit the official website of Kaizen CPA Limited at www.kaizencpa.com or contact us through the following and talk to our professionals:

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