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Regional Headquarters Schemes by China’s Ministry of Commerce and the Shanghai Municipal Government: Differences, Limitations, and Possible Combinations

BENJAMIN KROYMANN

I. INTRODUCTION

As large multinational companies (“MNCs”) are continuously extending their Chinese market presence, many are considering moving their Asian-Pacific Headquarters to China. In an attempt to attract MNCs’ Regional Headquarters to Mainland China, the Chinese central government is not only faced with competition from regional hubs, such as Singapore and Hong Kong, but also from internal rivals, such as the Shanghai and Beijing municipal governments.

This article analyzes recently passed regulations on the establishment of Regional Headquarters by MNCs in China at the national and the municipal level. The focus will be on Shanghai’s set of regulations, issued in 2002 and 2003, as well as on the People’s Republic of China (“PRC”) Ministry of Commerce’s Holding Company Provisions, which introduced Regional Headquarters as a new investment vehicle at the national level in February 2004. Particular emphasis will be placed on the November 2004 revisions of the national rules, the difference in approval requirements and business scope of national and municipal Regional Headquarters and the two distinct forms of Regional Headquarters (Investment/Management Company) in Shanghai Municipality.

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II. REGIONAL HEADQUARTERS AT NATIONAL LEVEL

A. Legal Antecedents: Holding Company Structures in China since the 1980s

Soon after Deng Xiaoping had proclaimed China’s new Open Door Policy in 1978, foreign direct investment began to soar in China despite initial setbacks such as the Baoshan steel plant controversy and other disputes involving technology import contracts. By the mid-1980s, some MNCs had already established a number of foreign-invested enterprises (“FIEs”) in the Chinese market. As the existence of such multiple investments created a need for coordination and centralization of respective business activities, foreign investors began to experiment with different Holding Company structures and subsequently sought approval of these structures from the Ministry of Foreign Economic Relations and Trade (“MOFERT”) and from its successor, the Ministry of Foreign Trade and Economic Cooperation (“MOFTEC”).

Although the concept of Holding Companies was alien to PRC Law at the time, some foreign investors were able to obtain approval for their Holding Company structures on the basis of late 1980s and early 1990s internal ministry regulations. Such approvals were granted by labeling said company structures with various designations such as umbrella enterprise [伞形企业], group company [集团公司], holding company [控股公司] or investment company [投资公司].

A legal framework for the establishment of foreign-invested Holding Companies was eventually put into place in 1995, when MOFTEC issued the Establishment of Companies with an Investment Nature by Foreign Investors Tentative Provisions (“Tentative HC Provisions”). Various supplementary regulations were enacted in the following years, with the original Holding Company rules undergoing revisions in March and June of 2003, as well as in February and November of 2004. Since 1995, over 300

foreign-invested Holding Companies have been established under the national regulations, most of them in Beijing and Shanghai.

(a) In June 2003, the title of the Holding Company regulations changed to Provisions on the Establishment of Investment Companies by Foreign Investors (“HC Provisions”), but it was only in February 2004 that the Ministry of Commerce (“MOFCOM”) introduced Regional Headquarters as a new investment vehicle. As Regional Headquarters provisions had already been in place for some time at the municipal level in Beijing and Shanghai, the new national rules appeared to be an attempt by MOFCOM to profit from the large success of this new investment vehicle among foreign investors.

B. Regional Headquarters under MOFCOM’s Holding Company Provisions

Despite the difference in name, Regional Headquarters established under the MOFCOM rules are essentially a qualified form of Holding Companies. Accordingly, MOFCOM did not issue a separate set of regulations governing the approval of Regional Headquarters, but instead added the relevant norms to the existing provisions on Holding Companies. Hence, in order to establish a Regional Headquarters, foreign investors must first go through the approval process for Holding Companies before applying for the Regional Headquarters status. In view of this correlation, the following analysis will cover several aspects that apply to both Holding Companies and Regional Headquarters.

1. Legal Form

Holding Companies and Regional Headquarters can take the form of a Wholly Foreign-Owned Enterprise (“WFOE”) or an Equity Joint Venture (“EJV”). Nevertheless, most MNCs have refrained from setting up EJV Holding Companies and have chosen to centralize their business activities in China through WFOE Holding Companies. The strong preference for WFOE Holding Companies can partly be explained by the initial absence

8. Howson & Li, supra n. 4, at 25.
of Chinese companies with a truly nationwide reach, market presence, and acceptance across the country’s varied regions.\textsuperscript{9} Another reason, is that many foreign investors will avoid joint venture structures on the basis of strategic considerations when it comes to establishing a Holding Company abroad. The rationale behind setting up a Holding Company usually consists of a need to create a centralized management structure for existing joint ventures and WFOEs in order to generate economies in management, distribution, advertisement, etc. As the incorporation and management of different Sino-foreign joint ventures already provides for potential conflicts with the different Chinese joint venture partners, establishing an EJV Holding Company would undermine the endeavor even further by creating an additional need for coordination between the Sino-foreign EJV Holding Company partners themselves.

2. Approval Requirements

a. Financial Requirements

The motive for allowing MNCs to set up Holding Companies in China is described in Article 1 of the HC Provisions. The rules are designed to “promote foreign investment”, in particular, the “import of advanced foreign technology and management experience”.\textsuperscript{10} This intention is further highlighted by the title of the HC Provisions; “Investment Company” is used instead of the more common designation, “Holding Company”. In order to establish a Holding Company under the HC Provisions, foreign investors must live up to high requirements regarding their financial strength and prove a strong commitment to investment in China.

According to Article 3 of the HC Provisions, a MNC either has to have a total asset value of no less than US$400 million in the year prior to the application and have already established at least one FIE in China with a capital contribution of more than US$10 million of registered capital actually paid in, or, alternatively, have established more than ten FIEs in China with a capital contribution of more than US$30 million of registered capital actually paid in. If a Holding Company is set up by more than one foreign investor, at least one of them has to satisfy said requirements.\textsuperscript{11} In the rare case of an EJV Holding Company, the Chinese partner has to meet the criteria of a total asset value of RMB100 million in the year prior to the application.\textsuperscript{12}

\textsuperscript{9} Id.
\textsuperscript{10} HC Provisions, supra n. 7, at art. 1.
\textsuperscript{11} Id. at art. 3.
\textsuperscript{12} Id. at art. 3(2).
The latest revision of the HC Provisions in November 2004 has brought about a slight attenuation of the approval benchmarks described above. With respect to the first alternative of an asset value of US$400 million and the establishment of at least one FIE, MOFCOM has dropped the prerequisite that requires the foreign investor have proposed three or more investment projects prior to the application.\textsuperscript{13} This deletion reduces the market entry barriers to foreign investors with the necessary financial resources, but without immediate and concrete large-scale investment plans at the time of setting up their PRC Holding Company.

In dropping said prerequisite, MOFCOM yielded to criticism regarding the old wording of Article 3 of the HC Provisions. In its previous version, Article 3 of the HC Provisions required foreign investors to have established at least three investment projects prior to the application for establishing a Holding Company. The reference to “investment projects” was noteworthy, insofar as, MOFCOM also used the term “foreign-invested enterprise” twice in the same Article. Hence, it was unclear whether a foreign investor could actually satisfy this criterion by proposing three investment projects with a foreign equity investment of less than the general 25% benchmark of foreign ownership for FIEs.\textsuperscript{14} As MOFCOM silently deleted the relevant passage in the latest version of the HC Provisions, it appears that the ambiguous wording had indeed been the result of neglectful drafting rather than a deliberate differentiation between FIEs and investment projects.

\textbf{b. Registered Capital Requirements}

Article 3 of the HC Provisions set the minimum registered capital for Holding Companies at US$30 million. The US$30 million threshold constituted a considerable shift from the relatively low minimum registered capital requirement of US$10 million, which MOFTEC had previously applied to Holding Company structures on the basis of its internal approval guidelines.\textsuperscript{15} Despite the wording of Article 3 of the HC Provisions, the actual amount of paid in registered capital will eventually be even higher for foreign investors. The increase will come from Article 8 of the HC Provisions, requiring that the Holding Company use at least US$30 million of its registered capital for investments in China and for acquisitions from domestic shareholders.\textsuperscript{16}

\textsuperscript{13} Id. at art. 3.
\textsuperscript{14} See Howson & Li, supra n. 4, at 26.
\textsuperscript{15} See id. at 25.
\textsuperscript{16} Chow, supra n. 2, at 170.
c. Regional Headquarters Status

In order to transform a Holding Company into a Regional Headquarters, the parent company has to live up to even higher standards. The parent company must either have paid in registered capital of at least US$100 million or, alternatively, have paid in registered capital of at least US$50 million with the total sum of assets of its invested enterprise amounting to no less than RMB3 billion and the profits amounting to no less than RMB100 million as of the year prior to the application. Furthermore, the Holding Company is required to have established at least one research and development center and must have used at least US$30 million of its registered capital for investments in China and acquisitions from domestic shareholders in accordance with Article 8 of the HC Provisions. The November 2004 revision of the HC Provisions has brought a partial relaxation, insofar as, foreign investors now only have to establish one research and development center instead of two as previously required.

3. Business Scope

Regional Headquarters are entitled to the business scope available to Holding Companies and to a range of additional business activities only open to Regional Headquarters.

a. Permitted Activities for Holding Companies

Among the long list of permitted activities for Holding Companies, the following items appear to bear the greatest significance for foreign investors:

- Investing in sectors in which foreign investment is permitted in general;\(^\text{18}\)
- Balancing foreign exchange among invested enterprises with the consent of, and under the supervision of, an administration of foreign exchange for an invested enterprise when appointed in writing (subject to the unanimous resolution of the board of directors) by such enterprise;\(^\text{19}\)
- Acting as a distributor in the domestic and foreign markets for the products produced by an invested enterprise when ap-

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\(^{17}\) HC Provisions, supra n. 7, at art. 22(1).
\(^{18}\) Id. at art. 10(1).
\(^{19}\) Id. at art. 10(2)(2).
pointed in writing (subject to the unanimous resolution of the board of directors) by said invested enterprise,°°

- Acting as an agent or distributor in or by way of establishing an export procurement organization (including an internal unit) exporting domestic goods in accordance with relevant state provisions and applying for tax rebates in accordance with relevant provisions,°°
- Purchasing the products of an invested enterprise and, after effecting system integration, selling such products domestically and abroad,°°
- Providing after-sale services to products produced by its parent company.°°

b. Permitted Activities for Regional Headquarters

Once the Regional Headquarters status has been awarded, a company may also engage in the following activities:
- Import and sale of products of multinational companies and their controlled affiliates,°°
- Import of raw and supplementary materials, spare parts and components,°°
- Providing outsourcing services for enterprises inside and outside China,°°
- Providing logistics and distribution services,°°
- Subject to the approval of the China Banking Regulatory Commission ("CBRC"), establishing finance companies to provide relevant finance services for Holding Companies and their invested enterprises,°°
- Subject to the approval of the Ministry of Commerce, engaging in overseas project contracting and overseas investment, establishing leasing companies and providing related services,°°

°° Id. at art. 15(1)(1).
°° Id. at art. 15(2).
°° Id. at art. 15(3).
°° Id. at art. 10(2)(1).
°° Id. at art. 22(2)(2).
°° Id. at art. 22(2)(3).
°° Id. at art. 22(2)(4).
°° Id. at art. 22(2)(5).
°° Id. at art. 22(2)(6).
°° Id. at art. 22(2)(7).
c. Import and Distribution Rights

Since the promulgation of the first Holding Company rules in 1995, the ability of Holding Companies has always been limited to acting as a trading agent for their subsidiary FIEs. By restricting Holding Companies’ business scope to such services, Chinese lawmakers were apparently attempting to prevent a Holding Company from engaging in transactions with unrelated entities.32 One possible explanation for this limitation is the fact that if a Holding Company could import and sell products from offshore, such competition could harm the Chinese partners of its subsidiary FIEs engaged in manufacturing the same kind of product.33 Having caused much disappointment among foreign investors over the years, said restrictions have finally been lifted, but only for Holding Companies meeting the strict requirements for Regional Headquarters. Pursuant to Article 22 of the HC Provisions, a Regional Headquarters may now import and sell products of a MNC. When MOFCOM introduced Regional Headquarters as a new investment vehicle in February 2004, the wording of the HC Provisions appeared to suggest that a Regional Headquarters may sell those products in China without having to apply for a business license with explicit reference to wholesale or retail activities.34 In order to clarify the extent of Regional Headquarters’ distribution rights and to bring the HC Provisions in line with the recently promulgated Administration of Foreign Investment in the Commercial Sector Procedures (“Commercial Sector Procedures”),35 MOFCOM amended the HC Provisions in November 2004 to explicitly rule out any retail activities by Holding Companies or Regional Headquarters.36 According to Article 11 of the HC Provisions, Holding Companies and Regional Headquarters now have to comply with the Commercial Sector Procedures and shall amend their business scope to include specific distribution activities if they wish to engage in such fields.

30. Id. at art. 22(2)(8).
31. Id. at art. 22(2)(9).
32. Pitman B. Potter, MOFTEC’s New Regulations on Holding Companies: They Open up New Opportunities (But Only to Very Large Players), 178 E. Asian Exec. Reports 7, 8 (May 15, 1995).
33. Rapp, supra n. 3, at II-4.11 to II-4.12.
35. Issued by MOFCOM on April 16, 2004 with effect from July 1, 2004.
36. See HC Provisions, supra n. 7, at art. 15 (9).
The latest modification of the HC Provisions has also shed more light on the limitations of Regional Headquarters’ import rights. In its February 2004 version, the wording of Article 22 of the HC Provisions left room for interpretation as to whether Regional Headquarters could import products only from their respective parent company, or also from offshore affiliates and other MNCs. The expression “跨国公司的产品” was sometimes translated as “products of the multinational company” and sometimes as “products of multinational companies.”

In order to prevent any misunderstanding, the HC Provisions stipulated that the term was referring to the “parent company of the group to which the foreign investor establishing the Holding Company” belonged.

Despite a partial relaxation of import restrictions, the February 2004 version of the HC Provisions still barred Regional Headquarters from performing the function that Holding Companies in western countries perform for their corporate group. Such functions consist of using Regional Headquarters as single trading agents for the centralized purchasing of raw materials and the centralized selling of products from different FIEs and offshore subsidiaries of the group. Employing common sales personnel through their Regional Headquarters to sell the group’s products allows MNCs to enjoy significant economic benefit. In response to the widespread criticism of said import restrictions, MOFCOM eventually changed the relevant provisions in November 2004. Under the latest version of the HC Provisions, Regional Headquarters are granted import and distribution rights not only for products of their parent company, but also for products of offshore affiliates controlled by the respective parent.

d. **Central Treasury Functions**

MNCs in western economies use Holding Companies to lend to subsidiary FIEs and to transfer funds among subsidiaries in the form of intra-company loans, thereby avoiding the need for incurring outside debts to finance their operations when surpluses exist within the group. When MOFTEC issued its first set of Holding Company regulations, the wording of Article 7 of the Tentative HC Provisions seemed to herald the introduc-
tion of similar functions for Holding Companies in China. The initial euphoria soon gave way to a more realistic evaluation, however, as the “providing of financial support” proved to be conditioned by an additional approval of the People’s Bank of China (“PBOC”). The PBOC was quick in promulgating its *Interim Measures for the Administration of Group Finance Companies* in September 1996, which stipulated the requirements for Holding Companies to establish a separate Group Finance Company when engaging in financial services.

Despite the fact that the name of the regulations changed to *Administration of Finance Companies of Enterprise Groups Procedures* in June 2000 and that the authority for approving such Group Finance Companies now lies with CBRC, the requirement for establishing a separate Finance Company remains unchanged, even after the latest revision of the procedures in July 2004. Due to the very high capital benchmarks for establishing such Group Finance Companies, few foreign investors have so far been able to obtain the necessary approval from CBRC.

Regional Headquarters are now granted the option of establishing finance companies to provide central treasury functions to the group in China. Although it has been suggested that such finance companies will be subject to leaner regulations by CBRC in the future, there is no indication, so far, that Regional Headquarters will be able to avoid the high approval requirements set by the *Administration of Finance Companies of Enterprise Groups Procedures*. CBRC’s latest revision of the procedures in July 2004 has broken very little new ground, particularly with respect to the stringent financial requirements.

C. Conclusion

The introduction of Regional Headquarters as a new investment vehicle at the national level has opened new possibilities for foreign investors to coordinate and centralize their business activities in China. The most significant new business activity among the list of new items introduced in February 2004, was the possibility for a Regional Headquarters to import and sell products from its parent company. The November 2004 revision of the HC Provisions has removed another major obstacle, in this regard, by extending Regional Headquarters import rights to offshore affiliates con-
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trolled by the parent company. A factor which will continue to deter for-
eign investors from establishing a Regional Headquarters at the national
level, however, are the high capital requirements set by MOFCOM, which
make this new investment vehicle only available to very large MNCs.

III. REGIONAL HEADQUARTERS IN SHANGHAI MUNICIPALITY

A. Legal Antecedents: Regional Headquarters Structures in Beijing and
Shanghai Since the 1990s

Many years before MOFCOM launched its Regional Headquarters ini-
tiative in 2004, local governments in Shanghai and Beijing had already
introduced the Regional Headquarters scheme at the municipal level. 48
This time lag can partly be explained by the fact that pressure for issuing
such legislation was much higher on local governments than on
MOFTEC/MOFCOM, due to the strong competition between the two mu-
nicipalities and the other major cities in the area, such as Hong Kong and
Singapore. 49

First attempts were made in Shanghai in the early 1990s, when the
Shanghai government experimented with the concept of a so-called Group
Company (集团公司). 50 Such Group Companies were designed to perform
management functions without actually holding any investments them-
selves, and were conceived to act as a kind of dragon head for foreign in-
vestors in the Chinese market. However, due to strong resistance from the
central government in Beijing, this first experiment soon came to an end.

The Beijing government went ahead with its own set of rules in January
1999, when it issued the Beijing Municipality, Encouragement for Mul-
tinational Companies Establishing Regional Headquarters in Beijing Sev-
eral Provisions. 51 The Provisions put forward some preferential policies,
such as an exemption from local income tax, support for import and export
rights and support for the establishment of sales agencies and finance com-
panies. Despite their innovative character, the Beijing Regulations were
criticized for falling short of legislative standards. 52 The rules remain un-
clear with respect to several fundamental issues, such as the exact precon-

49. Winston Zhao & Lucy Li, Issues in Shanghai’s Regional HQs Legislation, 17 China L. & Prac.
70, 70 (Sept. 2003).
50. Bernd-Uwe Stucken, Address Before the German Chamber of Commerce in China, Establish-
ment of Real and Virtual Holding Company Structures (Shanghai, China, Apr. 20, 2004).
& Practice Publishing Ltd. 2003).
52. See e.g. Guo, supra n. 48, at 44-45.
ditions for establishing a Regional Headquarters and the performance of services for affiliate companies outside of China.53

In order to position itself as a regional hub for corporate headquarters against Beijing, on the one hand, and Singapore and Hong Kong, on the other hand, the Shanghai Municipality issued an equivalent version of regulations in July 2002, the Shanghai Municipality, Encouraging the Establishment of Regional Headquarters by Foreign Multinational Corporations Tentative Provisions (“RHQ Tentative Provisions”).54 Unlike the Beijing government, the Shanghai municipal government was quick to issue Implementing Rules to its RHQ Tentative Provisions in March 2003,55 which provided guidance with respect to various issues left open for interpretation in the RHQ Tentative Provisions. The Shanghai legislation appeared to be the result of a rather well prepared legislative effort. Prior to issuing the RHQ Tentative Provisions, the Shanghai government had apparently set up a special task force in charge of assessing the various legislative alternatives for Regional Headquarters regulations and had sent out delegations overseas, including to Singapore.56

By the end of 2004, already eighty-six MNCs had opted for setting up their Regional Headquarters under the Shanghai rules.57 General Electric and Unilever were among the first companies to establish a Regional Headquarters in Shanghai58 and many of the big MNCs have followed suit, including Exxon Mobil, Kodak, Honeywell and Johnson & Johnson.59 In order to take advantage of available tax rebates, most foreign investors have chosen Shanghai’s Pudong New Area as their Regional Headquarters’ place of registration.60

While Beijing has traditionally been the main target for MNCs wanting to establish a Regional Headquarters in Mainland China, Shanghai has now overtaken Beijing in attracting the highest number of MNCs’ Regional Headquarters. In 2004, thirty new Regional Headquarters were approved in

53. Wong, supra n. 6, at 17.
57. Ross & Chen, supra n. 5, at 48.
59. Cheung & Leng, supra n. 6, at 279; Mitchell Dudek & Alex Feng Wang, FDI in Shanghai, 18 China L. & Prac. 71, 71 (Dec. 2004).
60. Shanghai Welcomes Regional Headquarters, EuroBiz: J. European Union Chamber Commerce China 66, 66 (June 2004).
Shanghai compared to a mere seven in Beijing. Nevertheless, despite the relative popularity of Shanghai’s RHQ Provisions among foreign investors, the city cannot match the success of its competitors, Hong Kong and Singapore. The more favorable investment climate and lower legal requirements for Holding Companies in these two cities are still keeping many foreign investors from moving their Regional Headquarters in Asia to Mainland China.

B. Regional Headquarters under Shanghai’s RHQ Regulations

1. Legal Form

a. WFOE or EJV

Unlike its national counterpart, the Shanghai RHQ Provisions only appear to provide for the possibility of a Regional Headquarters to be established as a Wholly Foreign-Owned Enterprise without making any explicit reference to an (Equity) Joint Venture structure. This comes as a surprise insofar as China has traditionally preferred foreign direct investment through joint ventures rather than through WFOEs. Since the beginning of the Open Door Policy, China has striven to obtain greater access to advanced science, technology, management skills and international distribution channels. Considering that such skills and knowledge are only transferred to Chinese companies if they are a partner in a Sino-foreign joint venture, the preference for joint venture structures on the Chinese side appears as a natural choice. The reluctance of Chinese lawmakers to accept WFOE structures is also reflected in the development of PRC legislation in general. Only in recent years, and only as a result of the WTO accession requisites, have many areas of the Chinese economy been made accessible for WFOEs through a revision of the Foreign Investment Industrial Guidance Catalogue and other relevant laws and regulations.

There are several possible explanations for the omission of EJVs in Article 2 of the RHQ Tentative Provisions. Firstly, a Regional Headquarters usually serves a different purpose than a regular FIE. While standard FIEs are established to function as manufacturing, retailing/wholesaling or trading vehicles, a Regional Headquarter’s main purpose consists of performing a coordinating and centralizing function for the MNC’s multiple in-
vestments in China. Therefore, the prospect of a transfer of technology or advanced science to the Chinese joint venture partner does not come into play when forming a Regional Headquarters.

Secondly, the exclusive reference to WFOE structures may simply emanate from practical considerations on the part of the Shanghai municipal government. As mentioned above, very few investors opt for joint venture structures when establishing a Holding Company at the national level, highlighting a general preference for WFOE Holding Companies among MNCs. As Article 2 of the RHQ Tentative Provisions stipulates, enterprise forms other than WFOEs may be approved by the Shanghai government on a case to case basis. The unlikely scenario of a foreign investor wanting to establish a Regional Headquarters as an EJV also appears to be provided for.

b. **Holding Company, Management Company, Other FIE Forms**

Regional Headquarters in Shanghai may be established in the form of Holding Companies or Management Companies. As the wording of Article 2 of the RHQ Tentative Provisions ("may take such corporate forms as [. . .] etc.") seems to indicate, these two forms are mere examples of the legal structures available for Regional Headquarters. The question arises as to whether foreign investors could establish Regional Headquarters in forms other than Holding or Management Companies, and whether it would even be possible to transform an existing FIE into a Regional Headquarters. Transforming an existing FIE into a Regional Headquarters could prove to be an attractive option for foreign investors as such Regional Headquarters could presumably continue to engage in the same business activities as the original FIE (e.g., manufacturing, trading, etc.), while at the same time assuming the role of a Regional Headquarters for the corporate group.

With respect to the first question of whether a Regional Headquarters could be established in a legal form other than a Holding or Management Company, the wording of the RHQ Tentative Provisions points to part of the answer. Article 5 of the RHQ Tentative Provisions names only two ways of establishing a Regional Headquarters: (1) an existing Holding Company applies for the Regional Headquarters status, or (2) a foreign investor who has not yet established a Holding Company applies for the establishment of a Regional Headquarters in the form of a Management Company.
Company. Although this seems to contradict the exemplary character of the enumeration in Article 2 of the RHQ Tentative Provisions, it has to be taken into account that there are different possible interpretations of Article 2 of the RHQ Tentative Provisions. One interpretation could be that Regional Headquarters may be established in forms other than Holding and Management Companies. However, rather than suggesting a different basic structure, the wording could equally be understood to merely mean that, in addition to taking the form of WFOE Holding and WFOE Management Companies, Regional Headquarters may also be established as EJV Holding and EJV Management Companies. This interpretation is supported by the fact that while Article 2 of the RHQ Tentative Provisions makes reference to “wholly-owned investment companies” and “wholly-owned management companies,” Article 5 refers only to “investment companies” and to a “management company,” while omitting the denomination “wholly-owned.” As mentioned above,70 this interpretation would also be more in line with the interests of Chinese lawmakers by providing a possibility for granting approval to the traditionally preferred investment structure of Sino-foreign joint ventures. Articles 2 and 5 of the RHQ Tentative Provisions are therefore mostly understood as only giving MNCs the choice between establishing a Regional Headquarters as a Holding or Management Company.71

With respect to the second question of whether foreign investors could transform an existing FIE into a Regional Headquarters in the form of a Management Company, the wording of the RHQ Tentative Provisions is not entirely clear. Article 2 of the RHQ Tentative Provisions stipulates that, in order to exercise their management and service functions, Regional Headquarters must be established in the Shanghai Municipality. This appears to rule out the possibility for any FIE established elsewhere in China to fall inside the scope of the Shanghai rules.72 Besides this geographical containment, however, there is no explicit guidance provided as to whether the Management Company must be a newly established FIE. Article 5 of the RHQ Tentative Provisions simply stipulates that an “application may be made for the establishment of Regional Headquarters in the form of a management company.” However, when read in combination with the preceding sentence of Article 5 of the RHQ Tentative Provisions, the term

70. See supra pt. III(B)(1)(a).
72. See Yuping Wang, Establishing a Regional Headquarters in Shanghai, 17 China L. & Prac. 65, 66 (June 2003).
“establishment” appears to be delivering an indication regarding the correct interpretation of the Article. In the preceding sentence of Article 5, it is stipulated that a Holding Company may apply for “recognition” as a Regional Headquarters. This implies that Holding Companies must have already been established when applying for the Regional Headquarters status. The deliberate distinction between the “recognition” and the “establishment” of a Regional Headquarters provides a strong indication for the conclusion that a Management Company may not be set up by transforming an already existing FIE into a Regional Headquarters. Hence, it seems that the only FIEs that may be transformed into a Regional Headquarters are Holding Companies registered in the Shanghai Municipality.73

2. Definition

Article 2 of the RHQ Tentative Provisions defines a Regional Headquarters as a MNC’s only head office that, through investment or by authorization, exercises management and service functions for enterprises in a region consisting of more than one country. The requirement that a Regional Headquarters be the MNC’s only head office in a region consisting of more than one country highlights the intention of the Shanghai Municipal Government to position Shanghai in direct competition with other Chinese cities as well as with non-Chinese cities in the Asian-Pacific region.74 Said precondition constitutes a clear deviation from the benchmarks set by MOFCOM’s HC Provisions which provide for the possibility of a Regional Headquarters being established even in cases where a MNC has already set up another Regional Headquarters in the Asia-Pacific region or where a MNC’s Asian-Pacific investments are limited to China.

The RHQ Tentative Provisions do not provide further guidance as to which forms of enterprises fall into the scope of the term “head office.” It is thus unclear whether MNCs that have established a Holding Company in other cities would be considered as already having set up a head office in a place other than Shanghai. To begin with, it is obvious that a foreign investor that has set up a Holding Company under MOFCOM’s HC Provisions will not be granted approval for establishing a Regional Headquarters in the form of a Management Company in Shanghai given that Article 5 of the RHQ Tentative Provisions limits the options for such Holding Companies to being recognized as a Regional Headquarters in the form of Holding Company.

73. Id. at 66.
74. Id. at 65.
It is less apparent, however, whether Article 2 of the RHQ Tentative Provisions would allow a foreign investor that has set up a Holding Company in a municipality or city other than Shanghai to establish an additional Regional Headquarters as a Management Company in Shanghai. Although this is sometimes referred to as a feasible option under the Shanghai rules, the rationale behind Articles 2 and 5 of the RHQ Tentative Provisions seems to point to a different interpretation. As mentioned above, Article 5 of the RHQ Tentative Provisions only gives foreign investors the choice between setting up a Regional Headquarters directly in Shanghai and transferring an existing Holding Company to the Shanghai Municipality to be recognized as a Regional Headquarters. As this highlights the Shanghai government’s intention to prevent foreign investors from keeping an additional Holding Company elsewhere in China and in the entire Asia-Pacific region, it seems unlikely that the Shanghai Municipal Commission of Foreign Economic Relations and Trade ("SMERT") would grant approval for the establishment of a Management Company in such cases. Hence, the option of setting up a Regional Headquarters in the form of a Management Company only appears to be available for MNCs that have not yet set up a Holding Company anywhere in China.

The RHQ Tentative Provisions do not address the question of whether Hong Kong, Macao, and Taiwan are considered parts of China for the purpose of determining if an enterprise has been established inside or outside of China. Hong Kong, Macao, and Taiwan are mentioned only in Article 15 of the RHQ Tentative Provisions which stipulates that the establishment of Regional Headquarters by MNCs from said areas shall be handled with reference to the RHQ Tentative Provisions. In view of Article 15 and the absence of any explicit reference or classification in Articles 2 and 5 of the RHQ Tentative Provisions, some authors have come to the conclusion that MNCs’ enterprises in Hong Kong, Macao, or Taiwan would not be counted for the purpose of the provisions.

It is not entirely clear, however, in what way Article 15 of the RHQ Tentative Provisions could support this interpretation. The rationale expressed in Article 15 is that investors from said areas shall be treated as foreign investors if they choose to establish a Regional Headquarters in Shanghai. Since MNCs from Hong Kong, Macao, or Taiwan are thus treated as companies from abroad, it seems more coherent to assume that a foreign investor’s enterprise established in one of these areas would also be

75. Id. at 66.
76. See supra pt. III(B)(1)(b).
77. Zhao & Li, supra n. 49, at 70.
78. E.g. Cai, supra n. 56, at 87.
considered as a foreign enterprise for the purpose of the provisions. Moreover, the wording of Article 15 coincides with many other PRC laws on foreign investment that usually treat Hong Kong, Macao, and Taiwan as regions abroad. It therefore appears likely that the requirement of enterprises established outside of China will be satisfied even if a MNC’s only Asian-Pacific FIE outside of Mainland China has been established in Hong Kong, Macao, or Taiwan.

3. Approval Requirements

a. Approval Authority

All required documents must be submitted to SMERT for approval and a decision shall be rendered within thirty days after the date SMERT receives the application documents. Article 4 of the RHQ Tentative Provisions stipulates that SMERT shall be in charge of the examination and approval of Regional Headquarters and shall coordinate the administrative work of the relevant departments. In practice, however, SMERT has delegated this authority to the Shanghai Foreign Investment Committee (“SFIC”) which has general approval authority over foreign-invested enterprises in Shanghai. As some companies have already experienced a swift approval process of as little as seven days instead of the legally prescribed thirty days, the delegation of approval authority to SFIC has apparently helped to streamline the approval process.

b. Additional Approval by MOFCOM

After the RHQ Tentative Provisions were issued in July 2002, there was initial confusion regarding the need for central government approval of Regional Headquarters set up in Shanghai in the form of Holding Companies. Article 5 of the RHQ Tentative Provisions was seen by some as being unclear about the question of whether such Regional Headquarters should also satisfy the requirements laid down in the national Holding Company rules. However, the wording of the RHQ Tentative Provisions does not appear to leave much room for interpretation in this regard. According to Article 5, foreign-invested Holding Companies may apply for

79. E.g. HC Provisions, supra n. 7, at art. 29.
80. RHQ Tentative Provisions, supra n. 54, at arts. 7 and 8; RHQ Implementing Rules, supra n. 55, at arts. 1 and 2.
81. Zhang, Grobowski & Wilson, supra n. 71, at 3.
82. Shanghai Welcomes Regional Headquarters, supra n. 60, at 66.
83. Cai, supra n. 56, at 87.
“recognition” as Regional Headquarters. Since the Article evidently refers to already existing Holding Companies, a prior approval by MOFCOM for the establishment of a Holding Company under the national HC Provisions seems to be indispensable for obtaining the status of Regional Headquarters under the Shanghai rules. A Holding Company established in a city other than Shanghai presumably could not apply for “recognition” as a Regional Headquarters as the RHQ Tentative Provisions clearly stipulate that the place of establishment for the Holding Company must be Shanghai Municipality.

Nevertheless, the prerequisite of prior central government approval applies only to Regional Headquarters in the form of Holding Companies. With respect to Management Companies, Article 5 of the RHQ Tentative Provisions stipulates that in a case where no Holding Company has been established, application may be made for the establishment of a Regional Headquarters in the form of a Management Company.

Hence, foreign investors wishing to set up their China/Asia Regional Headquarters in Shanghai can choose between two options: (1) to first establish a Holding Company under MOFCOM’s HC Provisions and subsequently apply to SMERT for the status of Regional Headquarters in the form of a Holding Company under the RHQ Tentative Provisions, or (2) to turn directly to SMERT and establish a Regional Headquarters in the form of a Management Company under the RHQ Tentative Provisions without obtaining prior approval by MOFCOM.

c. Common Requirements

Regardless of whether a Regional Headquarters is established as a Holding or a Management Company, a foreign investor must comply with the following requirements:84

- The Regional Headquarters must have independent legal person status;
- Its parent company’s total assets must be no less than US$400 million;
- Its parent company’s total investment in China shall be no less than US$30 million; and
- The Regional Headquarters must invest in, or be authorized to manage, no less than three enterprises in China or abroad, and should have management and service authorities over such managed enterprises.

84. See RHQ Tentative Provisions, supra n. 54, at art. 5.
In order to provide evidence of its total assets, the parent company may submit a copy of its financial statement.\textsuperscript{85} As to the parent company’s total investment figure, it is not clear whether reference is made to registered capital or total investment. The PRC laws on foreign investment distinguish between these two forms with the registered capital equaling the equity investment. For the purpose of EJVs, the total investment is defined as the sum of capital construction funds and the circulating funds needed for the EJV’s production scale.\textsuperscript{86} On a more general level, total investment is commonly referred to as equaling the equity investment plus any shareholder loans or third party debts that are typically guaranteed pro rata by shareholders.\textsuperscript{87} Although neither of these two terms is used in Article 5 of the RHQ Tentative Provisions, it appears that the provisions are referring to the total investment of the parent company.\textsuperscript{88}

Of the three enterprises required under Article 5 RHQ Tentative Provisions, only one has to be established outside of Mainland China.\textsuperscript{89} It appears, however, that this requirement is currently not enforced by SMERT.\textsuperscript{90} Article 5 of the RHQ Tentative Provisions further stipulates that MNCs which do not meet the conditions described above may nevertheless obtain approval for setting up a Regional Headquarters if the foreign investment is made in a targeted area (such as high technology\textsuperscript{91}) and if the MNC has made “outstanding contributions” to the region’s economic development. Given the vague wording of the latter condition, SMERT wields considerable discretion, which thereby adds a degree of legal uncertainty for MNCs that do not meet the legal requirements. It appears that providing advanced technology, management expertise or new products is not necessarily sufficient to qualify as “outstanding” in the eyes of SMERT.\textsuperscript{92} In order to go beyond the normal contribution of a FIE and meet the prerequisite of an “outstanding” contribution to the region’s economy, a MNC will presumably have to provide evidence of large-scale investments in Shanghai.\textsuperscript{93}

\textsuperscript{85} Cai, \textit{supra} n. 56, at 87.
\textsuperscript{87} Cai, \textit{supra} n. 56, at 87.
\textsuperscript{88} Id.
\textsuperscript{89} Zhang, Grobowski & Wilson, \textit{supra} n. 71, at 1; Wong, \textit{supra} n. 6, at 65.
\textsuperscript{90} Wang, \textit{supra} n. 72, at 65.
\textsuperscript{91} Zhang, Grobowski & Wilson, \textit{supra} n. 71, at 2.
\textsuperscript{92} Wang, \textit{supra} n. 72, at 66.
\textsuperscript{93} Zhang, Grobowski & Wilson, \textit{supra} n. 71, at 2.
d. Registered Capital Requirement

For Management Companies there is an additional requirement of a minimum registered capital of US$2 million. Since Regional Headquarters in the form of Holding Companies may only be set up by Holding Companies established under the national HC Provisions, the minimum registered capital for Holding Companies in Shanghai is set by Article 3 of the HC Provisions at US$30 million. This difference in registered capital constitutes a remarkable divergence from the national rules for Regional Headquarters. Especially smaller and medium-sized MNCs that have previously been hindered from establishing a Holding Company or Regional Headquarters in China due to the high capital requirements involved are now provided with an alternative corporate investment structure. As Management Companies require only local approval, this investment vehicle also offers the advantage of a swifter approval procedure.

4. Business Scope

Regional Headquarters in Shanghai may engage in the following business activities:

- Investment and operational decision making;
- Marketing services;
- Capital operations (i.e., treasury functions) and financial management (i.e., accounting functions);
- Technical support and research and development;
- Information services;
- Employee training and management; and
- Other operational, management and service activities permitted under other laws and regulations.

Those Regional Headquarters that exercise investment management functions may establish centralized internal fund management systems to centrally manage their own funds. For this purpose, Regional Headquarters may enter into a three-party agreement with a commercial bank and the controlled enterprises.

The RHQ Tentative Provisions and the RHQ Implementing Rules do not explicitly limit the business scope of Regional Headquarters for either Holding Companies or Management Companies. Nevertheless, there are several indications that the actual business scope for Regional Headquar-

94. See RHQ Tentative Provisions, supra n. 54, at art. 5.
95. See id. at art. 6.
96. RHQ Tentative Provisions, supra n. 54, at art. 13.
97. RHQ Implementing Rules, supra n. 55, at art. 4.
ters in the form of Management Companies will turn out to be narrower than the one for Regional Headquarters in the form of Holding Companies. To begin with, the considerable difference in capital requirements of US$2 million on the one hand and US$30 million on the other hand makes it rather unlikely that both enterprise forms will indeed be able to engage in exactly the same business activities. 98 Adding to this is the fact that Holding Companies will have the approval of both MOFCOM and SMERT, whereas Management Companies will only be authorized by the Shanghai regulations without meeting the requirements set by the national HC Provisions. In view of these differences, it can be expected that SMERT would come under pressure from the central government if it issued identical business licenses for both enterprise forms, given that this would undermine the national requirements for exercising the complete range of Regional Headquarters functions.

With respect to the possibility for Regional Headquarters to perform investment management functions, the wording of Article 13 of the RHQ Tentative Provisions appears to suggest that such functions will only be available to “investment” companies, i.e. for Regional Headquarters in the form of Holding Companies. It is hence expected that Regional Headquarters in the form of Management Companies will not be granted approval for engaging in treasury functions and general investment activities as stipulated in Articles 6(1) and 13 of the RHQ Tentative Provisions and Article 4 of the RHQ Implementing Rules. 99 There has indeed already been a reported case where SMERT has issued a business license for a Management Company without including these services in the business scope. 100

Despite the wording of the Shanghai rules, even Regional Headquarters in the form of Holding Companies may not be able to fully engage in treasury and investment functions. The reference to centralized internal fund management systems in Article 13 of the RHQ Tentative Provisions appears to suggest that Regional Headquarters could allocate funds among enterprises in a way similar to that of a Group Finance Company, but without the requirement to establish a separate legal entity. 101 Such a provision reveals a potential for conflict with CBRC’s Administration of Finance Companies of Enterprise Groups Procedures. 102

In order to circumvent such conflicts, the national HC Provisions stipulate in Article 13 that a Holding Company may only provide financial ser-

98. Zhao & Li, supra n. 49, at 70.
99. Wang, supra n. 72, at 66; Zhao & Li, supra n. 49, at 70.
100. Zhao & Li, supra n. 49, at 70.
vices for its invested enterprises with prior approval of CBRC, which has replaced the PBOC in regulating the banking sector. Similarly, Article 22 of the HC Provisions lays down that a Regional Headquarters may only engage in financial services for its invested enterprises if it establishes a group finance company with the approval of CBRC. In contrast, the Shanghai regulations do not make any reference to the CBRC or the group finance company regulations. As mentioned earlier, such group finance companies are rarely established due to the considerably high capital requirements.  

It is therefore unlikely that CBRC will tolerate Regional Headquarters in Shanghai engaging in financial services without its prior approval.

5. Preferential Treatment

The Shanghai regulations offer a range of additional benefits for Regional Headquarters to enhance the city’s competitiveness:

- Regional Headquarters with research and development functions are eligible for the same preferential treatment as high and new technology enterprises. Such preferential treatment may include a 15% corporate income tax rate and certain tax holidays.

- Regional Headquarters established in Pudong New Area are eligible for the incentives available in that area. The benefits available in Pudong are mostly tax-related and provide for refunds of income tax, business tax, value added tax (“VAT”), and corporate income tax paid during the first few years following the registration. In addition, Article 9 of the Pudong New Area, (Shanghai Municipality, Encouraging the Establishment of Regional Headquarters by Foreign Multinational Corporations Tentative Provisions) Implementing Procedures (2002) stipulates that research centers and technology development centers set up in Pudong by Regional Headquarters may enjoy additional benefits in accordance with the Shanghai Municipality Encouraging the Development of Enterprise Technology Development Institutions in Pudong New Area (promulgated Nov. 1, 2000) (available at http://english.pudong.gov.cn/government/detail.asp?tableid=t_english_pudong_gov_cn_law&articleid=14) [hereinafter Pudong Opinions] at item 4.

103. See supra pt. II(B)(3)(d).
104. RHQ Tentative Provisions, supra n. 54, at arts. 11, 12 and 14; RHQ Implementing Rules, supra n. 55, at arts. 3 and 5.
105. Zhang, Grobowski & Wilson, supra n. 71, at 3.
Technology Development Departments in Pudong New Area
Several Opinions ("Pudong Opinions")\textsuperscript{107}, promulgated in the year 2000. Article 1 of the Pudong Opinions defines Enterprise Technology Development Institutions as institutions dedicated to scientific research, development and testing work and related technical fields, or the development of technology, processes and products and related technical services within an enterprise. Available benefits for such institutions include a lump sum financing ranging from RMB500,000 to RMB1.2 million.\textsuperscript{108} Such institutions will furthermore enjoy preferential tax policies as well as conveniences in staff relocation and overseas travel;\textsuperscript{109}

- Regional Headquarters providing training and education for their employees are eligible for subsidies. In practice, the subsidies will emanate from individual income tax receipts collected from the Regional Headquarters’ personnel;\textsuperscript{110}
- Regional Headquarters are encouraged to set up procurement and logistics centers. Upon approval, such centers may obtain import and export rights, and enjoy VAT rebates on the export of goods. Regional Headquarters will apparently be required to set up separate legal entities and will not be able to establish such centers internally.\textsuperscript{111} It also appears that import and export rights will only be granted to Regional Headquarters in the form of Holding Companies or Regional Headquarters that have set up a purchase or distribution center and not to Regional Headquarters in the form of Management Companies.\textsuperscript{112}

Even for such Regional Headquarters, the import/export benefit may prove to be difficult to obtain in practice as such rights usually require central government approval.\textsuperscript{113} After the promulgation of the national Provisions on the Administration of Establishing Foreign-Invested Export Procurement Centers\textsuperscript{114} in November 2003, Regional Headquarters will now presumably run into even greater complications when applying for import and export rights in Shanghai Municipality; Expa-

\textsuperscript{107} China Law & Practice, September 2003.
\textsuperscript{108} Pudong Opinions, supra n. 106, at item 4.
\textsuperscript{109} Id. at items 6 - 20.
\textsuperscript{110} Shanghai Welcomes Regional Headquarters, supra n. 60, at 66; Wang, supra n. 72, at 67.
\textsuperscript{111} Wang, supra n. 72, at 67.
\textsuperscript{112} Cai, supra n. 54, at 88.
\textsuperscript{113} Zhang, Grobowski & Wilson, supra n. 71, at 3.
triate personnel of the Regional Headquarters may enjoy pref-
ferential treatment in the form of simplified and swifter visa
and entry/exit procedures.\footnote{RHQ Tentative Provisions, supra n. 54, at art. 14; RHQ Implementing Rules, supra n. 55, at art. 5.}

With respect to the tax rebates referred to above, such rebates may be
claimed every three, six or twelve months.\footnote{Shanghai Welcomes Regional Headquarters, supra n. 60, at 66.} The tax bureau will inform
Regional Headquarters about the required documentation for such claims
and will provide Regional Headquarters with special computer software for
drafting the refund claim.\footnote{Id.} Regional Headquarters will furthermore be
able to deduct their payroll as operating costs when calculating their oper-
ating profits, apparently without any restriction on the amount of the de-
duction.\footnote{Wang, supra n. 72, at 67.}

C. Conclusion

The introduction of Shanghai’s Regional Headquarters regulations has
added an attractive new investment vehicle to the options available to for-
eign investors. The various incentives offered in Shanghai combined with
the strategic location of the city will certainly continue to encourage for-
eign investors to set up their Regional Headquarters for China and Asia in
the Shanghai Municipality. Especially for smaller MNCs, the low capital
requirements for Management Companies offer a cheap and simple way to
establish their Regional Headquarters without having to meet the stringent
requirements at national level.

Despite these advantages, in practice some of the listed incentives and
business activities do not seem to be obtainable for foreign investors. Im-
portant items, such as import and export rights, require central government
approval or are subject to the authority of the central government admin-
istration.\footnote{Zhang, Grobowski & Wilson, supra n. 71, at 3.} With respect to Management Companies, it appears that the
actual business scope granted by SMERT is considerably narrower than the
one for Holding Companies. This might also explain the relatively low
popularity of the Management Company option compared to the Holding
Company scheme among foreign investors so far.

The continued success of Shanghai’s RHQ Regulations will therefore
depend largely on the cooperation of the various central government au-
torities. Moreover, it remains to be seen how the promulgation of the na-
tional HC Provisions will affect the attitude of the central government towards municipal Regional Headquarters legislation in general.

IV. DUAL REGIONAL HEADQUARTERS STATUS

Considering the differences in business scope conferred by MOFCOM’s HC Provisions and the regulations in Shanghai, a combination of both investment vehicles would certainly be a tempting option for foreign investors. Although the question of blending the two forms has not been addressed in the legal discussion so far, in theory, such a construction does seem to be possible.

In order to reap the full range of benefits offered to Regional Headquarters by MOFCOM and the Shanghai government, a MNC could first establish a Holding Company under MOFCOM’s HC Provisions. As a second step, the newly created Holding Company could apply to be recognized as a Regional Headquarters in the form of a Holding Company under Shanghai’s RHQ Tentative Provisions. In theory, the FIE should then be able to apply for the Regional Headquarters status under MOFCOM’s HC Provisions, thereby obtaining a dual Regional Headquarters status.

The reason why MOFCOM could, in principle, grant a second Regional Headquarters status is the fact that the Regional Headquarters status conferred by the Shanghai rules is not identical with the one granted by the national rules. A FIE established under MOFCOM’s HC Provisions continues to be a simple Holding Company in the eyes of MOFCOM and the national rules even after its transformation to a Regional Headquarters under Shanghai’s RHQ Tentative Provisions. This is due to the fact that a Regional Headquarters status obtained under the Shanghai rules neither enables a Holding Company to engage in business activities offered by the HC Provisions nor indicates that the respective FIE fulfills the financial criteria imposed by the national rules.

In practice, however, it will presumably prove very difficult to obtain a second Regional Headquarters status from MOFCOM. By allowing a MNC to engage in business activities listed in both the national and municipal regulations, MOFCOM would in fact be granting a considerably broader business scope than prescribed by the national rules. As this would contradict MOFCOM’s own legal framework, it is unlikely that investors will succeed in using Shanghai’s RHQ Tentative Provisions as a means to circumvent the national restrictions on Regional Headquarters’ business scope.

In order to avoid resistance by MOFCOM, a Holding Company could first apply for a Regional Headquarters status under the HC Provisions and subsequently request the status of a Regional Headquarters under the
Shanghai rules. Nevertheless, it is equally improbable that the Shanghai government will allow for its RHQ Tentative Provisions to be undermined and for two classes of Regional Headquarters with diverging business scopes to operate under its rules. The Shanghai authorities could further argue that after its transformation from a Holding Company into a Regional Headquarters under the HC Provisions the applying FIE no longer satisfied the prerequisites of a Holding Company as required by Article 5 of the RHQ Tentative Provisions.

In view of the practical hurdles involved, the theoretical option of a dual Regional Headquarters status does not seem to be available as an additional investment vehicle for MNCs.

V. CONCLUSION

In comparison, the national Regional Headquarters scheme provides for a significantly broader business scope than the Regional Headquarters rules in Shanghai where the list of business scope items appears rather short. The national rules have also gained some ground regarding possible interactions between Regional Headquarters and offshore affiliates. As MOFCOM’s February 2004 rules limited Regional Headquarters to business relations with their respective parent company, the Shanghai regulations used to have a comparative advantage by offering foreign investors a way to create a Regional Headquarters for all of their Chinese and offshore subsidiaries in the Asia-Pacific region, although there appeared to be restrictions in practice. By extending Regional Headquarters’ import rights in November 2004, MOFCOM has eliminated one major disincentive for establishing a Regional Headquarters under the national rules. Adding to the appeal of the national rules is the fact that, unlike the Shanghai regulations, they do not require that a MNC’s Regional Headquarters in China be the only one in the entire Asian-Pacific region and that a MNC hold investments elsewhere in the region. With respect to central treasury functions, both schemes appear to be offering the same limitations, given that the requirements for performing such functions continue to be set by the rigid CBRC rules for Group Finance Companies.

One of the biggest shortcomings of the national rules is its high capital requirements, which are contrasted by the low benchmarks for Management Companies in Shanghai. The requirement of a paid in registered capital of US$100 million/US$50 million on the one hand and a registered capital of a mere US$2 million for Management Companies on the other hand will certainly lead many MNCs to consider Shanghai as an alternative place for setting up their Regional Headquarters. However, the cost advantage of the Shanghai rules is partly outweighed by the legal uncertainty
regarding the establishment of Regional Headquarters in the form of Management Companies to engage in the same business activities as Regional Headquarters in the form of Holding Companies and to enjoy all of the benefits listed in the regulations.

Another drawback of the Shanghai scheme is the fact that there is no indication so far as to whether the current legal regime for Regional Headquarters will be maintained. As the incentives and benefits listed in the Shanghai regulations are due to be phased out in the near future, it is unclear whether such benefits will be extended or whether the current regulations will be replaced by another scheme altogether. Despite ongoing rumors that the Shanghai municipal government will be forced to modify its Regional Headquarters scheme to include equally stringent requirements as the national rules, there appears to be no indication of any imminent changes so far.\textsuperscript{120} In the long run, the fate of the Shanghai rules will depend on the degree to which MOFCOM and the central government will tolerate Regional Headquarters schemes at municipal levels and how the relevant authorities will handle the various unclear issues in practice.

\textsuperscript{120} Ross & Chen, \textit{supra} n. 5, at 48.