

China and Colombia

Together Towards a Brighter Future

Patrick Yip

National M&A Leader, Deloitte China
Senior International Advisor, Shanghai Qin Li Law Firm

4 June 2015



Agenda

- Overview of M&A/trade relations between China and Colombia
- Doing Business with China
- Fraud Prevention
- Foreign Investment in China
- Pilot Free Trade Zone
- Considerations before Investing in China
- FOREX rules related to Foreign Investment
- Key Success Factors for Doing Business in China
- Intellectual Property Rights Protection
- Tax Considerations
- Ten Rules for Doing Business in China



Chinese Government Work Report (March 2015)

Highlights

Increase GDP by approximately 7 percent

Increase imports and exports by around 6 percent

M2 money supply is forecasted to grow by around 12 percent, but actual supply may be slightly higher

Create over 10 million jobs in urban areas

China to reduce foreign investment restrictions

China to invest 1.6 trillion yuan in railway, water projects

Chinese Outbound M&A Activities

- **Deal Volume** in 2014: **213**
- **Deal Value** in 2014: **US\$50B**
- **Americas**
Past 5 years: **27%** of deal volume
40% of deal value
- **Latin America**
Past 5 years: **17%** of deal volume of Americas
36% of deal value of Americas

Chinese Outbound M&A Activities

Past 5 years by Country

2014

<u>Deal Volume</u>	<u>Deal Value</u>
1. Brazil	1. Jamaica
2. Chile/ Jamaica	2. Brazil
	3. Chile

2013

<u>Deal Volume</u>
1. Brazil/ Chile/ Peru
2. Argentina/ Ecuador/ Mexico/ Suriname

<u>Deal Value</u>
1. Peru
2. Brazil
3. Ecuador

2012

<u>Deal Volume</u>	<u>Deal Value</u>
1. Brazil	1. Brazil
2. Colombia / Ecuador	2. Colombia
	3. Ecuador

2011

<u>Deal Volume</u>	<u>Deal Value</u>
1. Brazil	1. Brazil
2. Peru	2. Argentina
3. Argentina	3. Peru

2010

<u>Deal Volume</u>	<u>Deal Value</u>
1. Brazil	1. Brazil
2. Argentina	2. Argentina
3. Chile/ Colombia / Jamaica	3. Colombia

Chinese Outbound M&A Activities

Past 5 years by Sector

2014		2013		2012	
<u>Deal Volume</u>	<u>Deal Value</u>	<u>Deal Volume</u>	<u>Deal Value</u>	<u>Deal Volume</u>	<u>Deal Value</u>
1.E&R	1.E&R	1.CB/ E&R	1.E&R	1.E&R	1.E&R
2.CB/ Manufacturing /TMT	Manufacturing 2.CB/TMT	2.FS	2.CB 3.FS	2.CB/FS	2.CB 3.FS
2011		2010			
<u>Deal Volume</u>	<u>Deal Value</u>	<u>Deal Volume</u>	<u>Deal Value</u>		
1.CB/ E&R	1.E&R	1.ER	1.E&R		
2.FS/ Manufacturing	2.FS 3.Manufacturing	2.CB 3.FS	2.FS 3.CB		

Notes:

CB - Consumer Business

E&R - Energy & Resources

FS - Financial Services

TMT - Technology, Media & Telecommunication

Chinese Outbound M&A Activities

Two Chinese outbound M&A deals in Colombia

- In 2012, **Sinochem Group** acquired **TEPMA BV**, a Colombia-based oil and gas producer and a manager of pipeline systems for US\$438 million, from a French company **Total**.



Chinese Outbound M&A Activities

- In 2010, **China Petroleum & Chemical Corporation** acquired **Hupecol**, a Colombia's owner and operator of oil and gas blocks, for US\$281 million



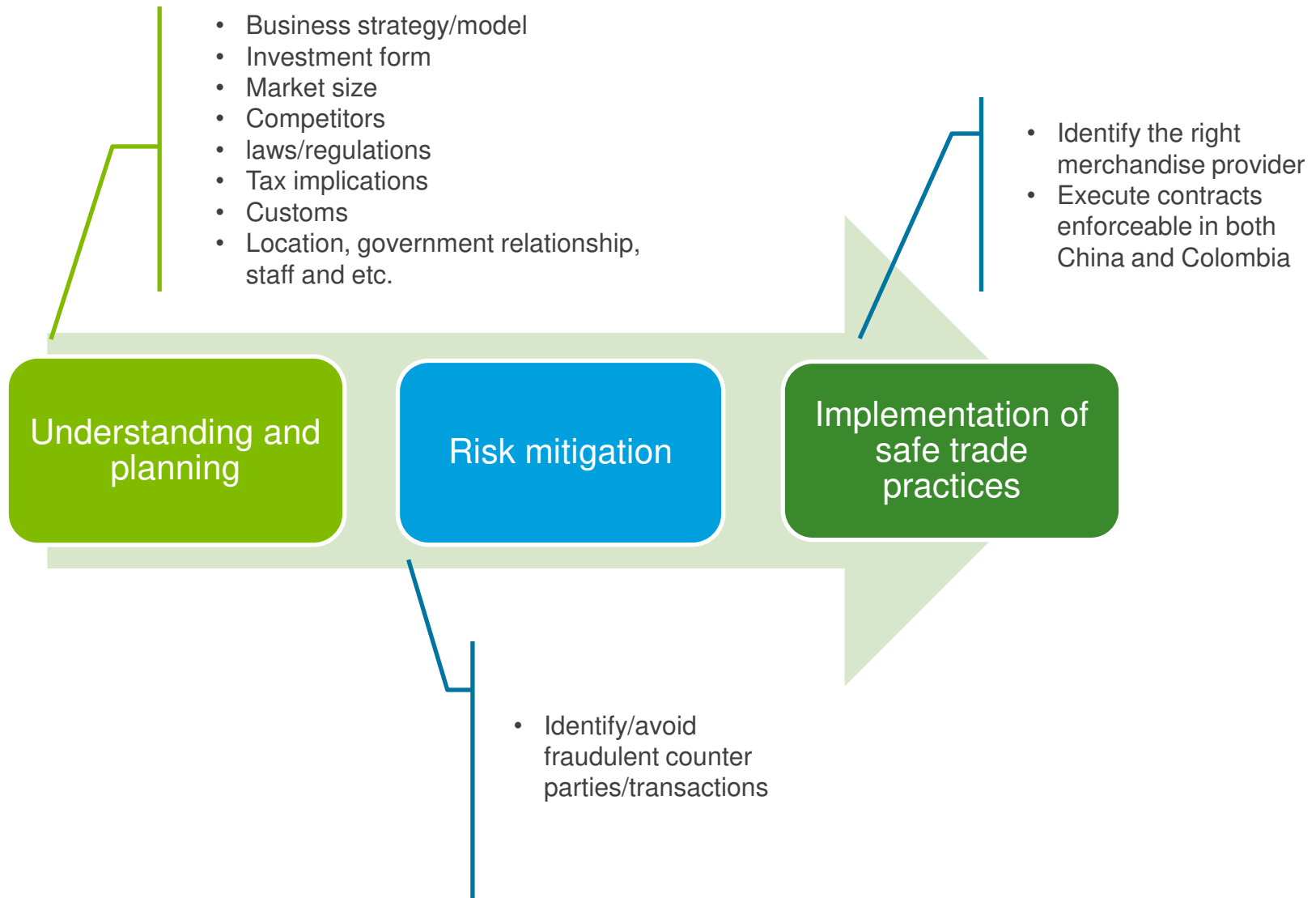
Bilateral trade between China and Colombia

Trade volumes

- **China is Colombia's second-largest trade partner.** The value of the bilateral trade between China and Colombia received US\$15.6 billion in 2014. In 2013, China purchased 5.9% (US\$3.5B) of Colombia's total exports while 16.3% (US\$9.7B) of Colombia's total imports was from China. (Source: Trade statistics of United Nations)



Doing Business with China



Fraud Prevention

- ❑ Good standing verification
 - Online company notice system
 - Company registration records
- ❑ Qualification check
- ❑ Credit and background screening
- ❑ Court enforcement search
- ❑ Reliable e-commerce platform
- ❑ Protective payment method (e.g. L/C)
- ❑ Professional due diligence

Fraud Prevention — Case Sharing

❑ Background

- Importer in Colombia deals with exporter in China
- An email from exporter's email account requesting an upfront payment to a designated bank account other than the one agreed in contract
- Second email requesting the upfront payment for 2nd batch of goods
- Paid as requested but goods never received
- Suspected fraud by export's staff or email hacker

❑ Suggestions

- Verify bank account information before wiring payment
- Use L/C instead of TT
- Engage PRC lawyers to perform due diligence and review contract

Foreign Investment in China

❑ Foreign Investment Vehicle

- Wholly Foreign Owned Entity (WFOE)
- Joint Venture (JV)
- Representative Office

❑ Foreign Investment Catalogue

- Prohibited (e.g. ivory carving, wholesale/retail of cigarette)
- Restricted (e.g. wholesale of cotton, telecom, shipping agency)
- Permitted (e.g. general manufacturing sector, e-commerce)
- Encouraged (e.g. production of organic vegetable, planting of coffee)

❑ Pilot Free Trade Zone and Negative List

❑ Merger Control Review

❑ National Security Review

Pilot Free Trade Zone (PFTZ)

❑ China (Shanghai) PFTZ — First trial in China

- Professional and financial services
- Shipping
- Bonded maintenance

❑ Guangdong PFTZ

- Guangzhou Nansha: transportation, logistics, high-end manufacturing
- Shenzhen Qianhai: science service, IT service, modern finance
- Zhuhai Hengqing: tourism and health, culture and education

❑ Tianjin PFTZ

- Parallel import of cars
- Finance lease

❑ Xiamen PFTZ

- Outsourcing services (e.g. ITO, BPO, KPO)
- Cold-chain logistics

Considerations before Investing in China

- ❑ What should the business strategy / model be?
 - Should it be a WOFE or a JV with partner(s)?
 - What is my business model – manufacturing, distribution, services, etc.?
 - What licenses do I need to operate in China?

- ❑ How / where should I set up the business entity in a manner which is flexible and cost-effective?

Forex Control Rules for Foreign Investment

❑ New SAFE rules governing forex capital

- SAFE delegated banks to handle forex registration for foreign investors' capital contribution to China
- Foreign investors are allowed to convert forex capital to RMB at will

❑ Foreign debt quota

Registered capital (USD)	Foreign debt quota (USD)
0 – 2.1 million (including 3 million)	Roughly 40% of registered capital
2.1 - 5 million (including 10 million)	1 time of registered capital
5 - 12 million (including 30 million)	1.5 times of registered capital
Over 12 million	2 times of registered capital

Key Success Factors for Doing Business in China

- ❑ Thorough knowledge of local business environment
 - Laws/regulations
 - Market size (customers)
 - Competitors
 - Business customs
- ❑ Local partners that could help overcome barriers in tapping into local market
- ❑ “Guanxi” or connections, especially with government
- ❑ Localized management team

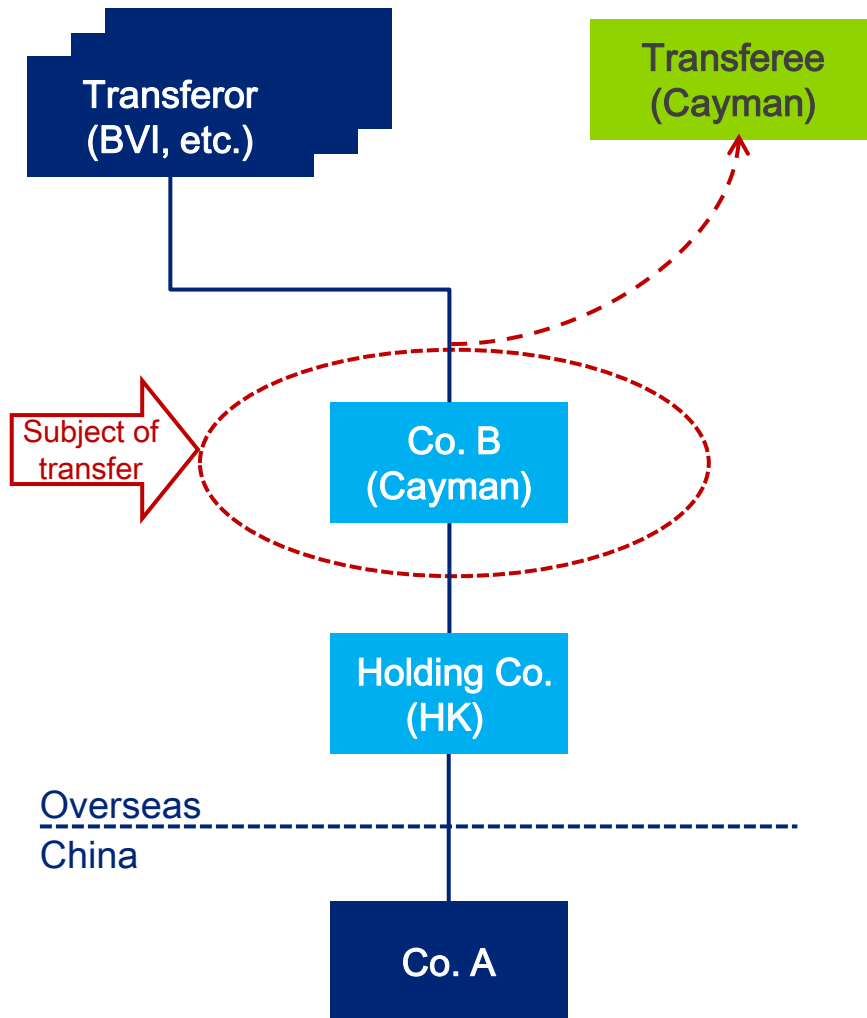
Intellectual Property Rights Protection

- ❑ China has a legal system for IP registration and protection
 - Patent
 - Trademark
 - Copyright
 - Trade secret

- ❑ Important to establish Intellectual Property rights protection strategies

- ❑ Remedies for infringement
 - Law enforcement agencies: Administration of Industry and Commerce, patent office and trademark office
 - Judicial system: civil lawsuit or criminal action

A recent Case: Indirect Share Transfer of Non-resident Company



Background

- Co.A is - leading IT company Beijing
- Sellers – BVI Co and other offshore Cos.
- Buyer - Cayman Islands Co.
- Co. B - Cayman Islands. Co holds 100% of Co. A via HK Holdco
- Total consideration - USD775million.
- Consideration – onshore vs offshore.
- No allocation was allowed - matching principle of tax revenue and real economic activities of BEPS,
- Tax bureau's argument - overseas users and offshore income are sourced from onshore investment in R&D.

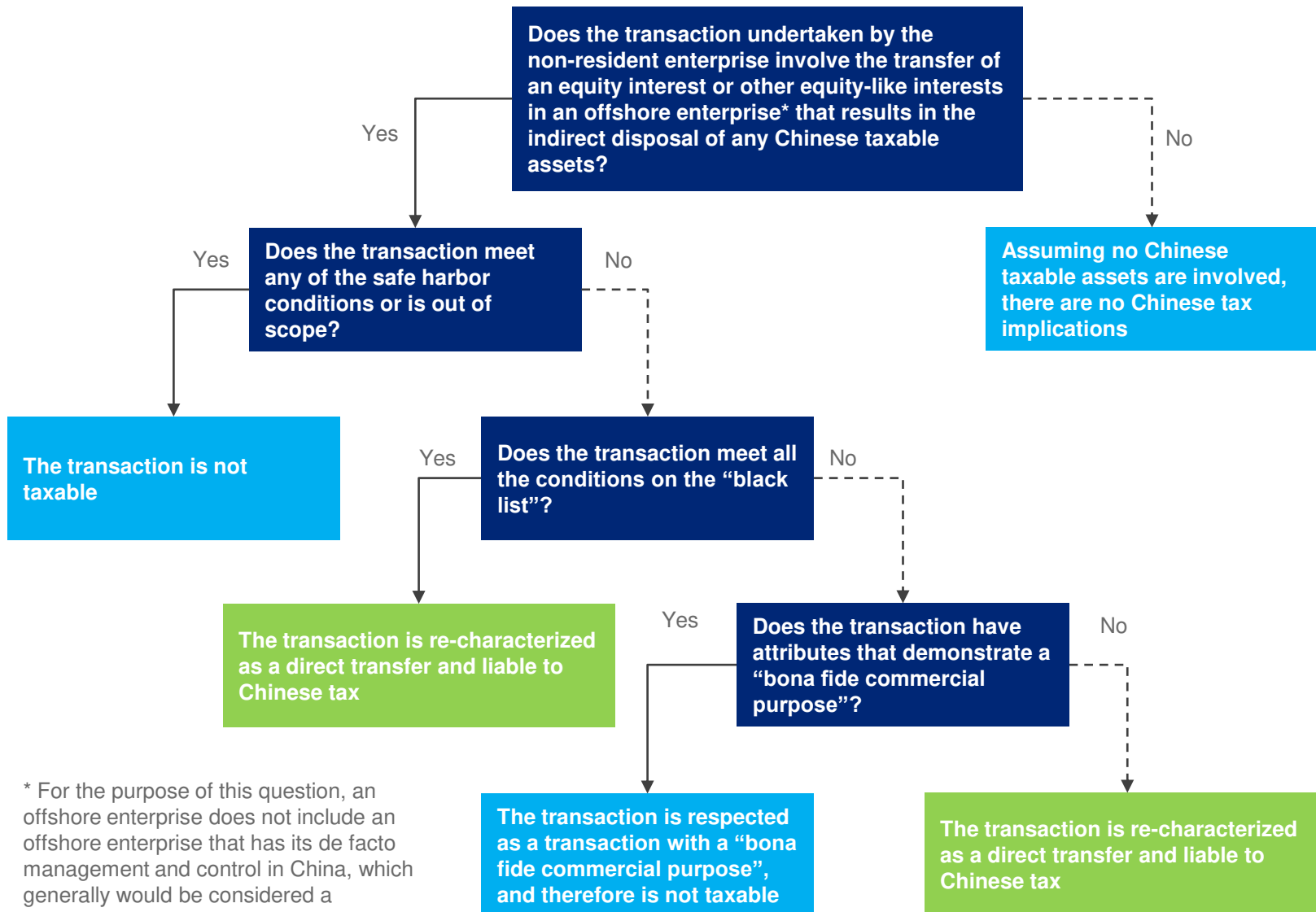
Conclusion

- CIT paid - RMB468million

Implication

- Principle of BEPS adopted by tax bureau

Navigating Bulletin 7



* For the purpose of this question, an offshore enterprise does not include an offshore enterprise that has its de facto management and control in China, which generally would be considered a Chinese tax resident enterprise

Ten Rules for Doing Business in China



1. Everything is possible
2. Nothing is easy
3. Patience is the essence of success
4. The answer “Yes” is not necessarily an indication of agreement or confirmation
5. “You don’t understand our country” means they disagree
6. “Provisional regulations” means they can change the rules anytime they want, even retroactively
7. “Basically, no problem” does not necessarily mean no problem
8. “Drafting a contract” means the beginning of the real negotiation
9. When you are optimistic, think about Rule No. 2
10. When you are discouraged, think about Rule No. 1

Q&A





About Deloitte Global

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL", its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global" does not provide services to clients. Please see www.deloitte.com/cn/en/about for a more detailed description of DTTL and its member firms.

Deloitte provides audit, tax, consulting, and financial advisory services to public and private clients spanning multiple industries. With a globally connected network of member firms in more than 150 countries and territories, Deloitte brings world-class capabilities and high-quality service to clients, delivering the insights they need to address their most complex business challenges. Deloitte's more than 200,000 professionals are committed to becoming the standard of excellence.

About Deloitte in Greater China

We are one of the leading professional services providers with 22 offices in Beijing, Hong Kong, Shanghai, Taipei, Chengdu, Chongqing, Dalian, Guangzhou, Hangzhou, Harbin, Hsinchu, Jinan, Kaohsiung, Macau, Nanjing, Shenzhen, Suzhou, Taichung, Tainan, Tianjin, Wuhan and Xiamen in Greater China. We have nearly 13,500 people working on a collaborative basis to serve clients, subject to local applicable laws.

About Deloitte China

The Deloitte brand first came to China in 1917 when a Deloitte office was opened in Shanghai. Now the Deloitte China network of firms, backed by the global Deloitte network, deliver a full range of audit, tax, consulting and financial advisory services to local, multinational and growth enterprise clients in China. We have considerable experience in China and have been a significant contributor to the development of China's accounting standards, taxation system and local professional accountants.

This communication contains general information only, and none of Deloitte Touche Tohmatsu Limited, its member firms, or their related entities (collectively, the "Deloitte Network" is, by means of this communication, rendering professional advice or services. No entity in the Deloitte network shall be responsible for any loss whatsoever sustained by any person who relies on this communication.