

大成 DENTONS

Hotel Investment Guide China

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China hotel business prospects are on the rise as China has made significant progress in the control of Covid-19. China is the first country in the world that has the economy back to normal track since the first quarter of 2021 and among which, the hotel business has on its fast track of recovery. Certain Chinese provinces have put the hotel business in the list of the encouraged category for foreign investment, which will attract the investment to the development of high end hotels and holiday resorts in China.

China has gained popularity as one of the best MICE (Meetings, Incentives, Conferences, Exhibitions) destinations over the forthcoming years¹. Although the international travel ban is still not released for the temporary reasons, we expect the resume of the international travel and the number of Chinese inbound visitors who are travelling more within the country will continue to boost the growth of China hotel market.

With an estimated nearly 130 million of annual tourists arrival by the year 2021, the People's Republic of China will be the world's number one tourist destination; offering significant opportunities to the China Hotel Industry².

1 China hotel market & forecast to 2023 by hotel type 1st July 2019. Source: ResearchAndMarkets.com

2 Same as above.

1. Can Foreign Investors Wholly Own and Operate Hotels in PR. China?

Although there is no restriction on the foreign ownership of hotels in mainland China under the latest real estate related laws and rules, the entry of foreign investment in real estate industry has been subject to heavy regulatory review since 2006 pursuant to *Opinions on Regulating the Entry and Administration of Foreign Investors on Real Estate Market* (Jianzhufang [2006]No.171) (“Decree No. 171”) which set forth the primary restrictions include the followings, and other implementing rules issued by related authorities during the 2006-2015 are still applicable up to today:

- **PRESENCE OF BUSINESS ENTITY.** A foreign investor must set up a business entity with the scope of business in the built-up and operation of hotels, or land development (or tracts of land) for the purpose of building and operating the hotels.
- **ONE PROJECT ONE COMPANY.** Project companies need to be set up on project base, but prior to the establishment of a project company, a foreign investor needs to obtain the land use right, ownership of the buildings or enter into agreements to obtain such rights.
- **REGISTERED CAPITAL AND TOTAL INVESTMENT.** The registered capital and total investment, and the ratio is a special concept in Chinese foreign invested area, as this has particular implication to the financing capacity of the foreign invested entity (see Q4). Generally, the ratio of the registered capital varies from 7/10, 1/2 or 2/5 of the total investment depending on the level the total investment falls in, i.e., below 3 million, 10 million, or 30 million.

Note that a foreign entity with a branch office or representative office in China or a foreign citizen can purchase commercial residential property for its own use or residential purpose, provided the local restrictions on the purchase of commercial residential property are satisfied.



2. What are the Major Market Supervision Departments for Foreign Investors in P.R. China?

- Ministry of Commerce (“**MOFCOM**”) and State Administration for Market Regulation (originally called Administration of Industry and Commerce, and still commonly used in practice “**AIC**”) and their local competent counterparts, responsible for the company set-up respectively from the entry of foreign investor and administrative company registration procedure. Since the *Foreign Investment Law* became effective from January 1, 2020, a foreign investor only needs to submit the set-up documents to AIC and no longer needs to obtain a prior approval certificate from MOFCOM on the foreign investment.
- National Development and Reform Committee (NDRC) and its local competent counterpart in charge of the approval of the hotel projects as such project typically involves the construction of the fixed assets. If a foreign investor only provides the management skill and service, but not own the hotels, then NDRC approval is not triggered in such service provision.
- State Administration of Foreign Exchange (SAFE), and its local counterpart are the key gatekeeper of the government agency in control the flow of the foreign capital in or out of China.

3. How do foreign investors normally structure their investment in hotels in P.R. China?

An entity 100% owed by foreign investor or a joint venture with local partner are all seen in China. For greenfield investment, normally a foreign investor will choose to cooperate with a local partner in order to secure the land use right or ownership of the buildings on the land.

It is also commonly seen that a foreign investor acquires a domestic real estate company with the license or permits of the lands or buildings on the land.

However, the above structure must follow the restrictions as addressed in the Q1, and you may wish to note a foreign invested company for the sole purpose of making investment, is not allowed to invest in real estate. However, there are still alternatives for a real estate investor to set up or participate in certain real estate fund in China, as we have seen in the current practice for the last 3 years.



4. How do foreign investors typically finance hotel investments in PRC?

The hotel financing by foreign investors is very limited. Based on our recent confirmation with SAFE on this practice, the restrictions applicable over a decade still apply today.

- (i) For the entities set up after June 1, 2007, the financing of the entities, e.g., loan borrowings from foreign shareholder or a foreign financing institution, are not allowed.
- (ii) For the entities set up prior to June 1, 2007, the financing of the entities is subject to the following restrictions:
 - within the difference of registered capital and total investment; and
 - financing is not allowed if the registered capital not fully paid up, or land use right certificate not obtained, or the capital injected in the project development not reaching 35% of the total investment.

5. Are there any specific concerns when acquiring hotels in China?

Round trip investment should be avoided when structuring the acquisition of hotels in China. Round trip investment refers to overseas entities controlled by a mainland Chinese entity acquiring the domestic Chinese entities related to the same Chinese entity. Furthermore, the shareholders of the entities should also prove that they are not under the same control. If an acquisition falls into the round trip investment, the approval of the MOFCOM will be triggered, and so far, there has no such case precedent based on the published information.

6. What is the common operating structure in the market?

The operating modes are more or less similar in the other developed countries, i.e., either, the owner will operate or engage a professional hotel service provider.



7. What key taxes should foreign investors consider when acquiring or operating hotels in PR. China?

Enterprise income tax are levied at 25%. The VAT of the sale of the land or hotels are in a range of 30%- 60%.

8. Are there any other key legal concerns for foreign investor before market entry in PR. China?

In certain areas of China, such as Jilin province or Hainan province, the hotels are listed in the encouraged category for foreign investment, which means the foreign investor could receive certain preferential treatment, such as reduced enterprise income tax at 15% in middle-western area, or reduced price of land use, or customs duty free for equipment imported for its own use by the entity.

KEY CONTACT



Susan (Xiaona) Wang

Beijing Partner

+86 10 58131279

+86 18910573469

xiaona.wang@dentons.cn

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