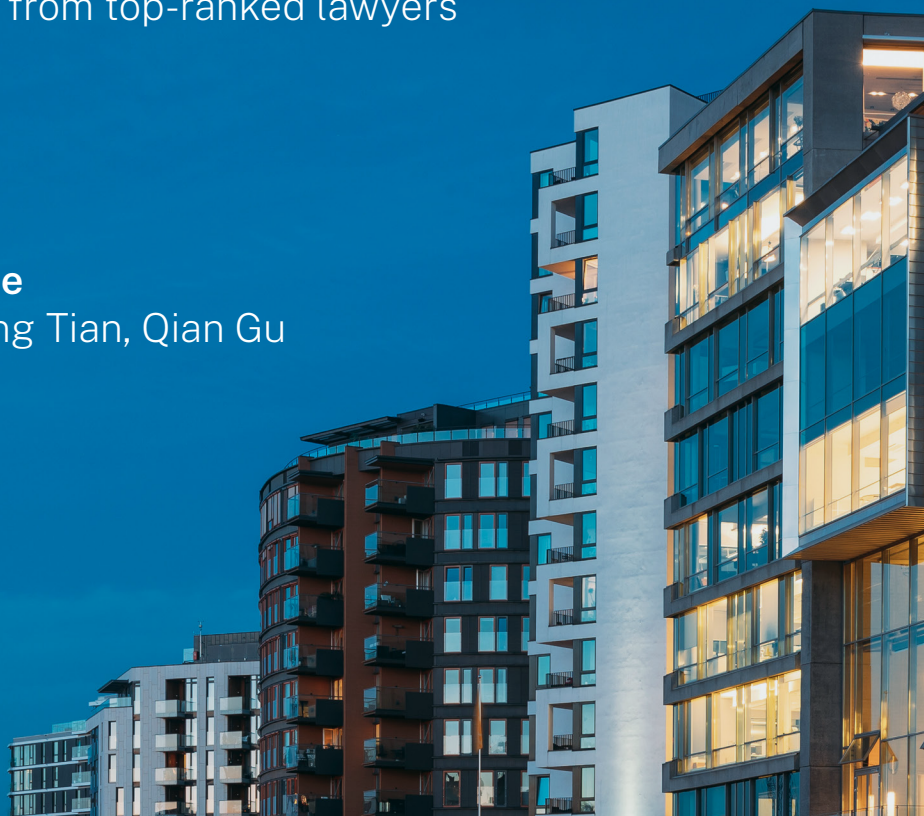

CHAMBERS GLOBAL PRACTICE GUIDES

Real Estate 2023

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China: Law & Practice

Nancy Zhang, Xiaoying Tian, Qian Gu
and Wang Wanjun
JunHe



CHINA

Law and Practice

Contributed by:

Nancy Zhang, Xiaoying Tian, Qian Gu and Wang Wanjun
JunHe

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JunHe was founded in Beijing in 1989 and is one of the first private partnership law firms in China. Since then, the firm has become one of the largest and most widely recognised Chinese law firms. It has 13 offices worldwide and a team of more than 800 professionals, including over 240 partners and legal counsel, as well as over 560 associates and legal translators. JunHe is committed to providing top-tier legal services in commercial transactions and litigation, and is

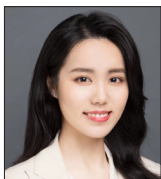
well known as a pioneer, innovator and leader in the re-establishment and development of the modern legal profession in China. The firm has experience in advising international clients on China's constantly changing legal environment affecting their investments and operations. In addition, the lawyers often concurrently hold high posts in international organisations, government agencies, trade associations and arbitration tribunals.

Authors



Nancy Zhang joined as a partner at JunHe in 2016. Her practice includes mergers and acquisitions, corporate restructuring and real estate, and she has extensive

experience in advising offshore clients in M&A and real estate investments in China. Her real estate expertise includes real estate development, sales, acquisition of existing or unfinished buildings, joint ventures, acquisition of existing project companies, lease transactions, finance structures, real estate-backed non-performing assets, management and operation of finished projects, and other related matters. She is an arbitrator of the China International Economic and Trade Arbitration Commission and a member of the All China Lawyers Association.



Wang Wanjun is an associate at JunHe whose practice encompasses mergers and acquisitions, real estate, general corporate and special situation/opportunity investment.



Xiaoying Tian is a senior associate at JunHe. Her main practice areas include real estate, mergers and acquisitions, and foreign investment. She represents

well-known commercial real estate companies, offshore real estate funds and hotel management groups involved in real estate development and acquisition, incorporation of joint venture companies, reviewing of lease documentation and management of real estate-related disputes. Xiaoying also provides legal advice to real estate companies concerning general company matters. She is a member of the All China Lawyers Association.



Qian Gu is an associate at JunHe. He specialises in mergers and acquisitions, general corporate law, foreign direct investments and special situation/opportunity investment

with a special focus on the real estate and financial sectors. He has extensive experience in advising both international and Chinese clients on a broad range of legal matters.

JunHe

25/F, China Resources Building
8 Jianguomenbei Avenue
Beijing 100005
PRC

Tel: +86 10 8519 1300
Fax: +86 10 8519 1350
Email: zhanglp@junhe.com
Web: www.junhe.com



1. General

1.1 Main Sources of Law

The main sources of real estate law in the People's Republic of China (PRC) include the laws, administrative regulations, ministerial rules, local regulations and other normative documents promulgated by the national and local governments. Among these, the laws promulgated at the national level include the Civil Code, the Land Administration Law of the PRC, the Urban and Rural Planning Law of the PRC, the Construction Law of the PRC and the Urban Real Estate Administration Law of the PRC.

1.2 Main Market Trends and Deals

During 2022, office space remained the most sought-after asset class in terms of transaction value in the real estate market of the PRC. However, an upward trend in the acquisitions of other asset types, such as business parks, logistics and industrial properties, apartments and hotels, has been observed (Source: Colliers International Group Inc, Annual Analysis for Real Estate Transactions in China, 13 January 2023). Specifically, business parks, and logistics and industrial properties accounted for 26.8% of the total transaction value, representing a significant increase of approximately 9.8% compared to

the previous year. In contrast, the transaction value of apartments and hotels accounted for 10.1%, with a moderate increase of about 3.1%.

In 2022, factors such as pandemic uncertainty, geopolitical tensions, sluggish economic performance and weak leasing fundamentals, contributed to a decline in the total transaction value of bulk properties. The majority of transactions continue to be driven by domestic demand, accounting for a staggering 80% of all transactions.

Notable transactions in 2022 include China Resources Land (CR Land) acquiring a portfolio of office, commercial and residential assets in Wuhan and Nanjing from China Fortune Land for a discounted price of RMB12.4 billion. This acquisition sought to alleviate liquidity stress following China Fortune Land's default last year. Additionally, ESR Cayman Limited (ESR) purchased a portfolio of logistics and industrial assets in the Greater Shanghai area, comprising 11 completed logistics and industrial properties with a gross floor area exceeding 550,000 square metres. This acquisition represents the largest logistics and industrial portfolio ever sold in the area.

The real estate industry in China is gradually recovering, thanks to adjustments in epidemic prevention policies and the introduction of favourable policies for the sector at the end of 2022. In 2022, China's inflation rate remained relatively low compared to other countries. Further contributing to this recovery are decreases in interest rates throughout 2022 and cuts in the reserve requirement ratio until March 2023.

1.3 Impact of Disruptive Technologies

No significant changes have been seen.

1.4 Proposals for Reform

On 26 January 2022, the Ministry of Finance and the State Taxation Administration jointly issued Bulletin (2022) No 3, which introduced pilot tax policies for real estate investment trusts (REITs) in the infrastructure sector. The pilot tax policies include both corporate income tax exemption prior to the establishment of infrastructure REITs and deferral of corporate income tax during the establishment stage of these REITs. It is anticipated that implementing tax rules will be introduced, which will effectively boost asset supply and growth of the REITs market.

2. Sale and Purchase

2.1 Categories of Property Rights

There are two main categories of property rights under PRC laws.

- Ownership right is the right to possess, use, receive proceeds from and dispose of the properties of the owner. A typical example is ownership of the title to buildings and structures. Under PRC law, land may only be owned by the state or collectively owned by farmers.

- Usufructuary right is the right to possess, use and receive proceeds from the properties owned by other persons, such as land use rights, contracting rights for farmland, farmer's rights to homestead land, rights of habitation and easement rights.

2.2 Laws Applicable to Transfer of Title

National laws and regulations governing the transfer of title to real estate mainly include the Civil Code, Urban Real Estate Administration Law, the Interim Regulations of the PRC Concerning the Assignment and Transfer of the Right to the Use of State-Owned Land in Urban Areas, and the Interim Regulation on Real Estate Registration.

2.3 Effecting Lawful and Proper Transfer of Title

The effectiveness of the transfer of real estate is subject to registration with competent real estate authorities, and no transfer is valid unless it is duly registered or otherwise provided by law. For example, a court judgment, arbitration award or, in the event of government taking or expropriation, an administrative decision of government, may serve to effect a title transfer if the same is effectively issued.

Title insurance is not common in the PRC.

The COVID-19 pandemic has, to some extent, propelled the government's ongoing digitalisation reform of the real estate registration system relying on the internet and blockchain technology. In certain localities (such as Guangzhou and Shenzhen), the process of second-hand non-residential properties transfers between enterprises can be completed online.

2.4 Real Estate Due Diligence

A buyer typically performs due diligence investigations on various aspects, such as legal, tax, financial, environmental and technical.

Asset Deal

In terms of legal due diligence, the scope for an asset deal focuses more on the property, such as title, existing encumbrances, zoning and licence requirements, environmental compliance, leasing, operation and management status, but also covers verification of key aspects of the seller, which may prevent or materially affect the sale of the property, such as the corporate governance structure and legal capacity of the seller, restrictions under financing obligations, and ongoing or pending material litigation, arbitration and administrative penalties involving the property.

Equity Deal

The scope for an equity deal is generally a comprehensive investigation, subject to the client's specific instruction, of the target company and the target property. The investigation of the target company generally covers the corporate history, corporate governance structure, business operation, material contracts (including financing contracts), environmental compliance, material litigation, arbitration and administrative penalty, intellectual property, labour and employment, taxes, subsidiaries and investment into other entities. The investigation of the target property is similar to that of an asset deal if not already covered in the part on the target company in the due diligence report.

Impact of the COVID-19 Pandemic

Due diligence investigations have been affected by the COVID-19 pandemic. On-site due diligence investigations and verifications are more difficult, if not completely impossible, and conference calls, database verification and virtual

interviews have been used more often in due diligence practices.

2.5 Typical Representations and Warranties

A buyer generally requests the seller to make representations and warranties on itself and on the target (ie, the target property in an asset deal, and the target property, the target company and the target equity/shares in the target company in the event of an equity deal). Typical representations and warranties on the seller include capacity, power, authority, solvency of the seller, all authorisations, consents and approvals obtained, the binding effect of the contract and the sale of the target without contravention or claim by third parties or other contracts.

In spite of the COVID-19 pandemic, specific coronavirus-related representations and warranties are uncommon in practice.

Target Property

Typical representation and warranties on the target property in an asset deal include clean title to the target property (free from encumbrances or, as the case might be, with disclosed existing encumbrances), the state of the target property, leasing status, no pending fees and no knowledge of taking, seizure or expropriation.

Target Equity/Shares

In an equity deal, sellers are often requested to make additional representations and warranties on the clean title to the target equity/shares (free from encumbrances or, as the case might be, with disclosed existing encumbrances), legal capacity and status, financial condition, tax matters, compliance with laws, environmental matters, indebtedness and loans, leases and other material contracts, employees, intellectual prop-

erty and no pending litigation in respect of the target company.

Coverage of Representation and Warranties

The coverage of representation and warranties is subject to business negotiations between the parties to a transaction. In general, parties to cross-border transactions are more comfortable with standard broad representation and warranties provisions, while domestic players tend to welcome a shorter version of an asset or equity transfer agreement; ie, a more condensed coverage of representation and warranties.

Breach of Representations and Warranties

If the seller is in breach of the relevant representations and warranties, the buyer is generally entitled, in accordance with the contract or relevant PRC laws, to claim for damages, refuse to proceed with the closing or even terminate the contract.

A sophisticated seller may insist that the buyer may only refuse to proceed with the closing or terminate the contract when the seller is in breach of fundamental representations and warranties, and otherwise only claim for damages in the event of breach of general representations and warranties.

Breach of certain representations and warranties is articulately regulated by the relevant PRC laws to protect the interests of buyers when purchasing property from real estate developers. For instance, the failure of a seller, being a developer, to have a pre-sale permit for a building under construction might lead to the invalidity of a strata title property sales contract.

Seller's representations and warranties apply primarily to the facts and circumstances existing at the time of contract execution and are deemed

to have been remade on and as of the closing date. A sophisticated seller may insist on adding a time limit for bringing claims for breach of such representations or warranties and capping the seller's liability for breach of the same. A typical cap for the aggregate of all the claims is 100% of the total contract price, while a sophisticated seller generally sets different sub-caps for different categories of claims.

Representation and warranty insurance is more often seen in cross-border transactions involving international players, mostly taken out by purchasers in cross-border transactions. Although pure domestic transactions involving local parties taking out representation and warranty insurance are still uncommon, local parties, particularly state-owned enterprises, are becoming increasingly aware of and interested in such insurance.

2.6 Important Areas of Law for Investors

See 1.1 Main Sources of Law, 2.2 Laws Applicable to Transfer of Title, 2.11 Legal Restrictions on Foreign Investors and 5.4 Applicable Governance Requirements.

2.7 Soil Pollution or Environmental Contamination

The Environmental Protection Law of the PRC and Soil Pollution Prevention and Control Law of the PRC provide that the person causing the soil pollution (the "causing person") is responsible for managing the soil pollution risks and the remediation of the soil pollution it caused. However, if the causing person cannot be identified, the land use right owner (eventually the buyer, unfortunately) is responsible for managing the soil pollution risks and remediation of the same, even if the land use right owner did not cause the pollution or contamination.

2.8 Permitted Uses of Real Estate Under Zoning or Planning Law

A buyer can ascertain the permitted use of a parcel of real estate by viewing the construction land planning permit (建设用地规划许可证 in Chinese), land grant contract (土地出让合同 in Chinese), the construction works planning permit (建设工程规划许可证 in Chinese), other relevant zoning documents and the title certificate. In addition, a buyer may make further verification by accessing, with the authorisation of the seller, the relevant files of the real estate at the competent planning and natural resources authority (the Planning and Natural Resources Commission or PNRC) or the competent local urban construction archives.

2.9 Condemnation, Expropriation or Compulsory Purchase

The state may, in the public interest:

- expropriate real estate, including land collectively owned by farmers and buildings or other real estate owned by any entities or individuals, with appropriate compensation; or
- temporarily requisition the real estate of any entities and individuals which will be returned to the said entities and individuals after such use.

The power of expropriation and temporary requisition must be exercised with due authority and legitimate process.

Compensation

The compensation must be fair and reasonable in case of expropriation and temporary requisition. Where the land to be expropriated is collectively owned by farmers, they shall be compensated according to the principle that their living standard is not negatively affected; while the

land user, in respect of land under a land grant contract to be taken back by the government for public interest, shall be compensated, considering the actual elapsed term of the land use and the status and condition of the developments made on the land. In the case of requisition, compensation shall be made for any damage to or destruction of the requisitioned real estate.

2.10 Taxes Applicable to a Transaction

In respect of the purchase and sale of real estate, taxes payable may differ depending on the different transaction structures.

Asset Deal

In an asset deal, taxes payable include:

- enterprise income tax/individual income tax;
- VAT and surcharges; and
- land appreciation tax, stamp duty and deed tax.

Of these:

- the seller is obliged to pay enterprise income tax/individual income tax, value added tax and surcharges, land appreciation tax, and stamp duty; and
- the buyer is obliged to pay deed tax and stamp duty.

Equity Deal

In an equity deal (regardless of whether to purchase all or a portion of the equity/shares), taxes payable include:

- enterprise income tax/individual income tax, which the seller is obliged to pay; and
- stamp duty, which the seller and the buyer are obliged to pay.

In addition, see **7.2 Assigning Responsibility for the Design and Construction of a Project** for the potential exposure to land appreciation tax in an equity deal.

Tax Rates

Enterprise income tax

The rate ranges from 10% to 25%. The individual income tax rate is generally 20%, but an individual who transfers their sole residential housing after holding it for more than five years is exempt from individual income tax payment.

VAT

The rate ranges from 5% to 9%. Surcharges imposed on the VAT payable include tax for maintenance and construction of cities at an applicable rate ranging from 1% to 7%; education surtax at an applicable rate of 3%; and local education surtax, the rate of which varies in different localities. See **7.1 Common Structures Used to Price Construction Projects** for more detailed analysis.

Land appreciation tax

The rate for this is progressive, ranging from 30% to 60%, but an individual who transfers their residential housing is exempt from paying this tax.

Deed tax

This generally ranges from 3% to 5%, but an individual who purchases a sole residence for their family (including their spouse and underage children) with a gross floor area of more than 90 square metres is eligible for a reduced rate of 1.5% and with a gross floor area of less than 90 square metres, of 1%.

Stamp duty

The rate is generally 0.05% for the seller and the buyer. Currently, an individual who purchases or

transfers residential housing is exempt from paying this tax.

2.11 Legal Restrictions on Foreign Investors

A major restriction on foreign investors acquiring real estate in the PRC is the “commercial presence” requirement; ie, offshore entities or individuals cannot acquire real estate in the PRC for non-personal use unless a foreign-invested enterprise is established or has been established in the PRC to own and operate the real property. The following restrictions also apply to foreign investors:

- a foreign individual is only allowed to purchase one housing unit (in practice, one title certificate represents one unit of housing) for their own use, subject to the requirement of residing or studying in China for more than one year; and
- a branch or representative office of an offshore entity in China is allowed to purchase non-residential real estate for its office use in the city where such branch or representative office is registered.

In addition, no real estate companies are currently allowed to acquire offshore loans except for foreign-invested real estate companies incorporated prior to 1 June 2007.

3. Real Estate Finance

3.1 Financing Acquisitions of Commercial Real Estate

If commercial real estate is acquired by an onshore entity (including a foreign-invested enterprise), generally the onshore entity may seek financing from banks within the PRC, subject to certain restrictions required by the China

Banking Regulatory Commission. For instance, the facility amount shall not exceed 60% of the total acquisition price, and the term of the loan shall not exceed seven years. If the onshore entity intends to arrange loans from offshore bank(s) or offshore entities, including shareholder(s), to acquire a commercial real estate, it must meet the requirements and restraints in relation to foreign debt under the PRC laws. Currently, no real estate companies are allowed to arrange loans from offshore, except for foreign-invested real estate companies incorporated prior to 1 June 2007. In cases where the onshore entity acquires equity in a target company engaged in real estate, obtaining loans from offshore banks or entities may still be practically unattainable.

Offshore Acquisition and Onshore Fixed-Asset Loans

Where a foreign investor acquires commercial real estate through an equity deal (by acquiring equity interest in the onshore company holding the real estate), the most common financing structure is an offshore acquisition loan accompanied by an onshore fixed-asset loan in renminbi. The offshore acquisition loan is extended by an offshore bank to the offshore buyer to pay for the equity/share purchase price in the same currency as that of the equity/share purchase price, secured by a pledge over the equity interest in the onshore target company acquired by the buyer. The onshore fixed-asset loan is generally extended to the onshore target company by an onshore subsidiary of the offshore bank, secured by a mortgage over the real estate owned by the onshore target company. Nowadays, we are seeing more onshore domestic banks directly extending foreign-currency acquisition loans to offshore buyers to finance the purchase price payment.

3.2 Typical Security Created by Commercial Investors

Where a commercial real estate investor that intends to acquire or develop real estate, acquires a loan from a lender, it will usually be required to provide the following forms of security:

- the mortgage over the real estate;
- the pledge of the equity interest of the target or project company by such investor;
- the guarantee made by the investor;
- the pledge of the account receivables, which are usually the rental proceeds generated from the real estate; and
- the agreement for the transfer of interests in material contracts, which generally include material lease contracts, the property management contract, asset management contract and insurance policies in relation to the real estate.

3.3 Restrictions on Granting Security Over Real Estate to Foreign Lenders

Although the PRC laws do not prohibit an offshore lender from being the mortgagee of real estate collateral, in practice, certain local real estate registration centres, which serve as the competent authority in charge of real estate mortgage registration, such as in Xiamen, refuse to register an offshore entity (including offshore banks) as the mortgagee. Therefore, in terms of practicality, it may not be possible to register a mortgage in favour of offshore lenders in certain localities, resulting in a failure to create an effective mortgage.

A borrower is generally able to make repayments to its offshore lender without further restrictions, provided that they have completed the relevant foreign exchange regulatory formalities for the cross-border loan (including, but not limited to,

the registration of such cross-border loan) in accordance with the PRC laws.

3.4 Taxes or Fees Relating to the Granting and Enforcement of Security

If a mortgage is created over real estate, both the mortgagor and the mortgagee are obliged to pay stamp duty for the mortgage contract at a tax rate of 0.05% each of the secured debt. A minimal registration fee for a real estate mortgage (CNY80 for residential property and CNY550 for non-residential property, per registration) is charged by the registration authority and often borne by the mortgagee.

Furthermore, if the mortgagor and mortgagee agree in the mortgage contract to an enforcement notarisation, a fee for enforcement notarisation may be incurred, which is usually borne by the mortgagor. Such fee is charged by the notary public office at a rate equal to an agreed percentage of the amount of the secured debt, which may vary at different localities.

3.5 Legal Requirements Before an Entity Can Give Valid Security

Under PRC laws, certain real estate may not be used as collateral to secure a debt, such as:

- land ownership (other than land use rights that can be a valid collateral), land use right to certain collectively-owned land such as farmers' homestead land (other than collectively-owned construction land), educational, medical and other public welfare facilities owned by non-profit schools, nurseries and/or medical institutions, real estate subject to title dispute or without clear title, real estate under attachment, detainment or custody orders; and
- as mentioned in 3.3 Restrictions on Granting Security over Real Estate to Foreign Lend-

ers, although the PRC laws do not prohibit an offshore lender from being the mortgagee of real estate collateral, in practice, certain local real estate registration centres, which serve as the competent authority in charge of real estate mortgage registration, such as in Xiamen, refuse to register an offshore entity (including offshore banks) as the mortgagee.

3.6 Formalities When a Borrower Is in Default

When a lender enforces its security over real estate against a defaulting borrower, if the lender and the mortgagor have explicitly agreed in the mortgage contract to apply the enforcement notarisation approach, the lender may directly apply to the competent court for enforcement by presenting the duly notarised mortgage contract and the enforcement certificate issued by the notary public's office. If the lender and the mortgagor have not explicitly agreed in the mortgage contract to apply the enforcement notarisation approach, the lender may, by agreement with the mortgagor, dispose of the collateral by negotiating a purchase price, by auction or sale of the collateral, and the lender may claim its senior debt against the proceeds from such a negotiated purchase price for auction or sale of the collateral. Failing an agreement between the mortgagor and the mortgagee on the means of disposal of the collateral, the lender may apply to the local court to auction or sell the collateral. In either case, the sale or negotiated purchase price of the collateral shall be based upon market price.

The time frame required for the aforesaid enforcement varies, and typically ranges from 6 to 12 months.

There is no restriction on the lender's ability to foreclose or realise on collateral in real estate

lending implemented by governmental entities in response to the COVID-19 pandemic.

3.7 Subordinating Existing Debt to Newly Created Debt

An existing mortgage debt may become subordinated to a newly created mortgage debt, the mortgage interest of which has been duly registered, only if the mortgage over such existing debt has not been duly registered. But if the mortgage over the newly created debt has also not been duly registered, the existing debt will rank *pari passu* with the newly created debt.

3.8 Lenders' Liability Under Environmental Laws

Given the principle that whoever causes the pollution shall be responsible for remediation, the party causing the pollution shall be held liable. Therefore, the lender, being the mortgagee of the real estate, will not generally be held liable. However, if the lender becomes the land use right owner in respect of such real estate as a result of foreclosure (or enforcement) of the mortgage, the lender may be held liable for such non-compliance if the party that caused the pollution cannot be identified.

3.9 Effects of a Borrower Becoming Insolvent

The security interests created by a borrower in favour of a lender will not be made void if the borrower becomes insolvent, and the lender may continue to claim its senior debt against the collateral, although this will be subordinated to the contractor's lien. In the event of restructuring during the bankruptcy proceedings, the lender will have to temporarily suspend its enforcement of the mortgage (unless damage to the collateral or a situation is likely to decrease the value of the collateral and might endanger the mortgagee's interests). If the borrower enters into reconcilia-

tion or a liquidation procedure, the lender may continue to enforce the mortgage.

3.10 Consequences of LIBOR Index Expiry

In response to the discontinuation of LIBOR at the end of 2021, lenders and borrowers frequently agree, mostly in cross-border facility agreements, to use an alternative interest rate (such as the interest rate published by the relevant reference banks) where there is no applicable LIBOR.

4. Planning and Zoning

4.1 Legislative and Governmental Controls Applicable to Strategic Planning and Zoning

The PRC laws applicable to strategic planning and zoning at state level mainly include the Land Administration Law, and the Urban and Rural Planning Law.

Local governments shall, in accordance with these laws, prepare the urban planning and zoning, and reasonably determine the development scale, steps and construction standards of the urban locality.

4.2 Legislative and Governmental Controls Applicable to Design, Appearance and Method of Construction

In addition to the relevant laws and regulations, such as the Construction Law of the PRC and Regulation on the Quality Management of Construction Projects, the design, appearance and method of construction are governed by the national standards promulgated by the relevant authorities of the state council, such as the:

- General Standard for Civil Building;

- Unified Standard for Energy-Saving Design of Industrial Buildings;
- Code for Fire-Protection Design of Buildings; and
- General Standard of Quality Control in the Construction of Buildings and Municipal Projects.

Generally, these regulations and rules apply to both the construction of a new building and the refurbishment of an existing building. Local governments may promulgate detailed implementing rules according to the relevant national regulations and policies.

4.3 Regulatory Authorities

The development and designated use of real estate are generally governed by the competent authorities of the state and local governments, such as:

- the competent development and reform commission (DRC) for the approval or filing of the project initiation;
- the PNRG for planning and zoning approval, grant of land use right and issuance of land use right certificate; and
- the housing and urban-rural development authority (HUDA) for preliminary design approval, issuance of the construction works construction permit (建筑工程施工许可证) and filing for completion acceptance.

4.4 Obtaining Entitlements to Develop a New Project

The approval process for development of a new building and/or infrastructure project can be divided into four phases:

- phase 1 for project initiation and land-planning permission, which includes approval or filing of the project, and issuance of the

construction land planning permit (建设用地规划许可证);

- phase 2 for engineering and project permission, which includes project design examination, and issuance of the construction works planning permit (建设工程规划许可证);
- phase 3 for construction permission, which includes design confirmation of fire-protection and civil air defence, and issuance of the construction works construction permit (建筑工程施工许可证); and
- phase 4 for completion acceptance, which includes completion acceptance of zoning, land, fire protection, civil air defence and other relevant matters, and the completion acceptance filing.

Refurbishment and expansion of an existing building also require the relevant approval and permits, which generally include the construction works planning permit (建设工程规划许可证), the construction works construction permit (建筑工程施工许可证), and the completion acceptance filing. Local authorities may also issue detailed implementation orders.

In addition, for any modification to urban and rural zoning, the relevant authorities that prepared such urban and rural zoning shall solicit public opinion by holding hearings or using other methods. In the event of any modification to the approved detailed construction plan or master plan of a project design, the relevant zoning authorities shall solicit the interested parties' opinions by holding hearings or using other methods. Also, any entity or individual is entitled to report any zoning non-compliance to the competent zoning or other relevant authorities.

4.5 Right of Appeal Against an Authority's Decision

If a real estate developer objects to the approval decision of the competent authority, generally such developer may submit applications for administrative review to the local government or the administrative department at the higher level. If such developer further objects to the administrative review decision, it may file an administrative lawsuit to the court, unless such administrative review decision is, as provided by law, a final decision.

4.6 Agreements With Local or Governmental Authorities

A developer or investor may enter into an investment or joint development agreement with the competent subdivision of the local government, specifying, among other things, local regulatory requirements upon construction, progress and the investment intensity, and the fiscal preferential treatment offered by the local government. The specific contents of such agreement vary from project to project and are subject to local policies and negotiations.

4.7 Enforcement of Restrictions on Development and Designated Use

The regulatory authorities may enforce restrictions on the development and designated use of a piece of land in various ways.

- If any entity occupies land without due approval or with approval obtained by deception, such entity shall be ordered to return the land, and any building and other structures newly constructed on the land may be ordered to be confiscated or dismantled. In addition, a fine may be imposed concurrently, and the relevant persons responsible for the illegitimate occupation may also be subject to criminal liability.

- In the event of any illegitimate land transfer, the income gained by the transferor from such transfer shall be confiscated, and the newly constructed buildings on the land may be ordered to be confiscated or dismantled.
- If construction work is carried out without a permit or the approval of the competent authorities (including failure to obtain permission or failure to carry out construction in compliance with the construction works planning permit), the project owner or developer may be ordered to correct the violation and dismantle the building or structures, they may be liable to pay a fine and the illegitimate properties may also be confiscated.

5. Investment Vehicles

5.1 Types of Entities Available to Investors to Hold Real Estate Assets

Investors generally set up companies to hold real estate assets, unless an individual prefers to own a real estate asset directly. Under the Company Law, the types of companies include limited liability companies (有限责任公司) and limited companies by shares (股份有限公司). The liability of each shareholder of either a limited liability company or a limited company by shares is limited to its respective subscribed capital contribution to the company. Limited liability companies are the most common choice for acquiring real estate assets among both domestic and offshore investors.

5.2 Main Features of the Constitution of Each Type of Entity

Both limited liability companies and limited companies by shares are formed and governed by their articles of association (章程), which also govern their shareholders, directors, supervisors and officers, in addition to the companies them-

selves. These provide for, among other things, capital contributions, shareholding percentage, governance rights, distribution rights, dissolution and liquidation matters.

5.3 Minimum Capital Requirement

The minimum capital for companies engaging in real estate development may not be less than CNY1 million.

5.4 Applicable Governance Requirements

A Limited Liability Company

Pursuant to the Company Law, a limited liability company shall have:

- less than 50 shareholders and a shareholders' assembly consisting of all the shareholders (or sole shareholder), which is the highest authority of the company;
- a board of directors consisting of three to 13 directors (or one executive director in lieu of a board of directors if there is a limited number of shareholders or the company is small), which reports to the shareholders' assembly (or shareholder); and
- a board of supervisors of no less than three supervisors (or one or two supervisor(s) in lieu of a board of supervisors if there is a limited number of shareholders or the company is small).

Board directors are appointed by the shareholders' assembly (or shareholder). A limited liability company may have a general manager, who reports to the board, to be appointed or dismissed by decision of the board.

A Limited Company by Shares

A limited company by shares is incorporated by two to 200 sponsors, with at least half of them having residence in the PRC, and has:

- a general assembly of shareholders consisting of all shareholders, which is the highest authority of the company;
- a board of directors consisting of five to 19 directors, which reports to the general assembly of shareholders;
- a board of supervisors of no less than three supervisors; and
- a general manager.

As in the limited liability company, board directors are appointed by the general assembly of shareholders, and the general manager is appointed or dismissed by decision of the board of directors.

5.5 Annual Entity Maintenance and Accounting Compliance

Upon incorporation, a company must submit the annual report for the preceding year to the administration for market regulation through the corporate credit information disclosure system between 1 January and 30 June each year. No fees are required for the submission of such report.

Companies are also required to prepare financial accounting reports at the end of each fiscal year, which are audited by an accounting firm. In addition to such accounting expenses, additional fees may be incurred for other financial matters as agreed in a company's articles of association. Such fees vary depending on the location of the accounting firm and the company's assets and financial condition.

6. Commercial Leases

6.1 Types of Arrangements Allowing the Use of Real Estate for a Limited Period of Time

Leasing is the most common method to obtain the right to occupy and use any or all of a building for a limited period of time. In addition, the habitation right, if duly registered, is another method to occupy and use another person's dwellings, generally free of charge unless otherwise agreed. The habitation right is a newly created right under the Civil Code.

Methods to obtain the use right to a piece of land vary depending on the type of land. According to the Land Administration Law, land is classified into farmland, construction land and unused land:

- farmland means land that is directly used for agricultural production, including cultivated land, forest land, grassland, etc;
- construction land mainly includes land zoned for the construction of buildings and other structures; and
- unused land refers to land other than farmland and construction land.

The use right to farmland may be obtained through a contracting arrangement, whereby contractors may enter into an agreement with a landowner or other entities with delegated authority to engage in agricultural production such as planting, forestry, animal husbandry, and fishery on the land, and benefit from such production.

The use right to construction land may be obtained by entering into a land grant contract (with land premiums to be paid) or a land allocation contract (no land premiums to be paid)

with the competent local land authorities if it is stated-owned or the relevant collective if it is collectively owned.

In addition, real estate owners are entitled, under the PRC laws, to use the land or buildings adjacent to their own real estate for the purpose of obtaining and draining water, passage, ventilation and lighting, etc that are necessary for their life or production. Such neighbouring right is mandatory and no agreement between the parties is required. Parties may also create easement through execution of agreements to obtain the right to use another party's real estate.

6.2 Types of Commercial Leases

In practice, commercial leases may be divided into the following categories depending on the different rent payment methods:

- lease with a fixed rent, often seen in office leases, under which the rent is a fixed amount as agreed by the parties;
- lease with a turnover rent, under which the rent is calculated at an agreed percentage of the tenant's gross turnover generated from the leased property; or
- lease under which the rent is the higher of a fixed base rent or a turnover rent.

6.3 Regulation of Rents or Lease Terms

PRC laws stipulate that the term in a lease agreement cannot exceed 20 years. If the term exceeds 20 years, the excess period will be invalid. When the lease term expires, the parties may renew the lease agreement for up to 20 years from the date of renewal of the lease agreement. Lease agreements with a term longer than the remaining term of the land use right to the land located beneath the property may be at risk because it is uncertain whether the landlord will

still have the right to use the land after the land use term expires.

The rent for a commercial lease is generally negotiable and subject to agreement between tenant and landlord. However, rent for affordable housing such as public rental housing (公共租赁住房) and low-rent housing (廉租房) may not exceed the guiding rental rate promulgated by the local government.

In the wake of the COVID-19 pandemic, the Supreme People's Court issued a special guiding opinion on 15 May 2020 and later, ministries and local governments issued various administrative orders to address leases affected by the pandemic. Termination of lease and claims for damages made by a landlord on the basis of a tenant's failure to pay the rent of a commercial lease, where the tenant's business proceeds have significantly declined, or the tenant has encountered working capital difficulties as a result of the pandemic or its control measures, will not be supported by the court. Macro and small businesses, which are tenants of state-owned landlords, are entitled to a rent reduction or exemption for up to three months in most cases. Other tenants of commercial leases may apply to the court to adjust the terms of the lease if the continued performance of the lease becomes inequitable or unfair under the circumstances of the pandemic. The aforesaid rules have since been consistently applied by the courts.

6.4 Typical Terms of a Lease

Generally, the length of a lease term is subject to the agreement between the landlord and the tenant but shall not exceed 20 years (see 6.3 Regulation of Rents or Lease Terms). The landlord and tenant may agree in the lease whether

the term may be renewed and if so, how the lease may be renewed.

PRC law provides that the landlord shall be responsible for the maintenance and repair of the leased premises, unless otherwise agreed by the parties. The tenant has the right to require the landlord to maintain and repair the leased premises within a reasonable time limit when necessary. Where maintenance and repair affect the use of the leased premises, the rent may be reduced, or the lease term extended accordingly.

The frequency of rent payment is, subject to the agreement between the landlord and the tenant, generally on a monthly, quarterly or yearly basis.

6.5 Rent Variation

The tenant shall pay rent in the amount and manner as agreed in the lease agreement. If agreed in the lease, the rental rate may be adjusted based on the agreed adjustment mechanism. For example, the rental rate may be adjusted annually based on the increase or decrease in the consumer price index in the preceding year. Parties are not allowed to unilaterally change rent payments, unless otherwise agreed by the parties or provided for by PRC laws, such as the occurrence of a force majeure, or an unforeseeable material change (other than commercial risks and force majeure) of circumstance.

6.6 Determination of New Rent

When deciding the price adjustment mechanism, a fixed yearly increase rate, the consumer price index or fair market prices are often taken into consideration.

6.7 Payment of VAT

The landlord is responsible for the payment of VAT on the rent income generated from leasing real estate.

6.8 Costs Payable by a Tenant at the Start of a Lease

Generally, in addition to rent, a refundable security deposit, equal to rent plus a management fee of three to six months in most cases for commercial leases (or one to three months for residential leases), is required to be paid to the landlord at the start of a lease. If the tenant wishes to improve or fit out the property, the tenant may be required to pay a security deposit for the fitting-out or improvements, refundable after the completion of the work. Improvements or fitting-out work undertaken by the tenant is usually borne by the tenant, unless otherwise agreed.

6.9 Payment of Maintenance and Repair

Under the PRC laws, unless otherwise agreed by the parties, the landlord is responsible for the maintenance and repair of the leased premises. In practice, small maintenance and repairs of common areas and shared equipment, machinery and facilities are generally conducted by the property manager engaged by the landlord, and covered by the management fees, which are payable to the property manager by either the landlord or the tenant, subject to the lease agreement.

6.10 Payment of Utilities and Telecommunications

In practice, the tenant pays their own utilities and telecommunications fees incurred in respect of, or consumed at, the leased premises. Utilities and telecommunications fees incurred in respect of common areas, and public equipment, machinery and facilities are often shared and charged to the end user (ie, the tenant in most cases, or the landlord if otherwise agreed in the lease, or if the premises are vacant) in proportion to the floor area of the leased premises.

6.11 Insurance Issues

The landlord will usually take out and maintain, at their own cost, property all risks insurance for the leased premises, which covers physical loss of or damage to the insured property arising from any natural hazards or accident. Damages caused or expenses incurred by intentional acts or gross negligence, confiscation, requisition, destruction or damage by any action or order of any government or public authority, war, coup d'état, or strike are generally excluded. On the other hand, the tenant is usually requested by the landlord to take out and maintain through the lease term construction/installation works all risks insurance for the tenant's fitting-out or improvement works, and public liability insurance for the tenant's business operations in the leased premises.

Business interruption insurance, an insurance ancillary to the property all risks insurance, generally only covers losses incurred by business interruption resulting from property damage. In response to the COVID-19 pandemic, certain insurers have developed insurance products that include "Business Interruption Plus Infectious Disease Clause" to cover business losses (eg, gross profits and expenses) resulting from government epidemic prevention measures. Due to the recurrent and sudden outbreaks of coronavirus, insurers in China are becoming less interested in promoting such insurance products.

6.12 Restrictions on the Use of Real Estate

In practice, the landlord commonly imposes various restrictions in the lease agreement on how a tenant shall use the leased property, including but not limited to restrictions on the permitted use, subleasing, assignment, and fitting-out of the leased premises. Applicable PRC laws also require that use of the leased premises shall be

in accordance with the zoned usage, and the tenant shall not change the load-bearing structure or demolish indoor facilities without the landlord's approval.

6.13 Tenant's Ability to Alter and Improve Real Estate

Typically, the tenant must obtain the landlord's prior consent if the tenant intends to improve or fit out the leased premises. A fitting-out plan is typically required in order to obtain the landlord's written consent. To ensure the safety of the leased premises, the landlord usually requires that the tenant takes out insurance for such improvement or fitting-out works and engages qualified contractors. As discussed in 6.12 **Restrictions on the Use of Real Estate**, the tenant may not change the load-bearing structure or other main structure of the leased premises without approval. Furthermore, it is common practice for the landlord to require the tenant to complete all the approval, filing and recording procedures required by the competent authorities (including but not limited to the planning, construction and fire-protection approvals and completion acceptance) for such improvement or fitting-out at the tenant's own cost.

6.14 Specific Regulations

Leasing of various types of real estate are mainly governed by the:

- Civil Code of the PRC;
- Administrative Measures for Commodity Real Estate Leasing; and
- Interpretation of the Supreme People's Court on Certain Issues Concerning Specific Application of Law in the Trial of Contractual Disputes over the Leasing of Urban Housing 2009 (as amended in 2020).

6.15 Effect of the Tenant's Insolvency

It is common practice to specify in the lease that the landlord is entitled to terminate the lease should the tenant become insolvent. Failing explicit agreement, the Enterprise Bankruptcy Law of the PRC shall govern. If the court accepts the tenant's application for bankruptcy, the tenant's bankruptcy administrator decides whether to rescind or continue to perform the lease agreement. Failure by the bankruptcy administrator to notify the landlord of its decision within two months from the date when the bankruptcy application was accepted, or to reply to the landlord within 30 days after receiving the landlord's exhortation, will result in the rescindment of the lease agreement.

Rescindment of the Lease Agreement

Where the lease agreement is so rescinded, the tenant shall reinstate and return the leased premises, and the landlord is entitled to declare its claims to the court, in accordance with the bankruptcy proceedings, for the damages incurred thereunder. Where the administrator decides to continue the performance of the lease agreement, the landlord must comply. However, the landlord has the right to request the administrator to provide security. The lease agreement will then be deemed rescinded if the administrator fails to provide security.

6.16 Forms of Security to Protect Against a Failure of the Tenant to Meet Its Obligations

It is common practice to specify in the lease that the tenant shall pay a refundable security deposit to secure the performance of its obligations under the lease agreement, and the security deposit may be utilised by the landlord, in whole or in part, to rectify the tenant's default. The security deposit is, in most cases, equal to rent plus a management fee of three to six

months for commercial leases, or one to three months for residential leases.

6.17 Right to Occupy After Termination or Expiry of a Lease

After the expiry or termination of a lease, the tenant generally has no right to continue occupying the leased premises. However, if the tenant continues to use the premises after the expiry of the lease without any objection from the landlord, the original lease shall be deemed as remaining in force but without a fixed term. Under such circumstances, either party can terminate the lease at any time, provided that the landlord gives the tenant reasonable prior notice of such termination. In addition, if the landlord intends to lease the premises after the expiry of the lease, the tenant shall have a right of first refusal under the same terms and conditions.

6.18 Right to Assign a Leasehold Interest

According to the PRC laws, the tenant may sublease part or all of the leased premises to a third party with the prior consent of the landlord. The sublease term should not be longer than the residual lease term of the original lease agreement. In addition, the tenant is liable for any damages caused by such third parties to the leased premises.

6.19 Right to Terminate a Lease

The following circumstances are often seen in a lease as causes for termination by the tenant:

- damage to the leased premises preventing the tenant from using the leased premises;
- insolvency of the landlord; and/or
- frequent interrupted supply of water, electricity, air conditioning or elevators.

The PRC laws also give the tenant the right to terminate the lease in the event of:

- the leased premises endangering the safety or health of the tenant;
- the occurrence of any of the following circumstances for reasons not attributable to the tenant, thus rendering the tenant unable to use the leased premises:
 - (a) the leased premises being attached by judicial or administrative organs;
 - (b) title claim to the leased premises; or
 - (c) violation of the mandatory provisions of laws and administrative regulations in respect of the requirements on the use of the leased premises.

Landlord's Right

The following circumstances are often seen in a lease as causes for termination by the landlord:

- failure by the tenant to pay the rent, management fee, deposit or other amounts due, and the outstanding amounts remain unpaid for a reasonable period after receipt of notice from the landlord;
- insolvency of the tenant;
- unauthorised suspension or close of business operations; and/or
- damage to the main structure or unauthorised fitting-out or improvement of the leased premises by the tenant.

The PRC laws also give the landlord the right to terminate the lease should the tenant sublease the leased premises without the landlord's consent.

6.20 Registration Requirements

The PRC laws provide that a lease agreement shall, within 30 days of its execution, be filed with the competent real estate authority of the

city where the real estate is located, otherwise the parties to the lease will be ordered to comply. Should the parties fail to comply within the prescribed time period, the parties shall be subject to a fine of CNY1,000 (in the case of an individual) or CNY1,000 to CNY10,000 (in the case of a legal entity).

The lease of real estate is not usually reflected in the Land Record.

6.21 Forced Eviction

If the lease is terminated as a result of the tenant's default, the tenant must reinstate and return the leased premises in a timely manner. Should the tenant fail to do so, after the lease has been duly terminated, the landlord may cut off the water or electricity supply to force the eviction of the tenant.

The landlord may file a lawsuit to the court with competent jurisdiction for its confirmation that the lease is duly terminated. If the tenant still occupies the leased premises after the court has found that the lease has been terminated, the landlord may apply for an enforced eviction based on a valid judgment. In practice, the period required for a court to make a judgment and complete the enforcement procedure varies in different localities but is usually longer than a year.

6.22 Termination by a Third Party

A third party who is not a party to the lease cannot generally terminate the lease because it is not a party to the lease. However, under certain circumstances, third parties may make it impossible for the lease to be performed or fulfilled, resulting in early termination of the lease.

7. Construction

7.1 Common Structures Used to Price Construction Projects

The most common pricing structures for construction include:

- fixed quota pricing (工程定额计价);
- bill of quantities pricing (工程量清单计价);
- fixed lump-sum price (固定总价);
- fixed unit price (固定单价);
- cost plus fee (成本加酬金); and
- adjustable price (可调价).

These are not mutually exclusive and sometimes, multiple pricing structures might be included in the same contract.

Fixed Quota Pricing

Fixed quota pricing means that the construction price, in accordance with the bidding documents, is a total of:

- the direct construction cost calculated based on the unit labour price, material price, equipment price and other information formulated by the relevant administrative authorities and the market price for the same during the same period;
- the indirect construction cost (including management salaries, office expenses, employees' insurance, etc);
- profit; and
- taxes.

Bill of Quantities Pricing

Bill of quantities pricing means that the aggregate of the price for each component of the construction work, which is calculated based on the integrated unit price and quantity of such component, is determined based on the construc-

tion drawing and construction management and engineering skills.

Fixed Lump-Sum Price

With a fixed lump-sum price, the total construction price is a fixed amount which is not adjustable within the agreed work scope and conditions.

Fixed Unit Price

This means that the unit price is a fixed amount, which is not adjustable in response to any change in conditions or quantities, and the total construction price is the product of the weighted summation of the fixed unit price multiplied by the quantity required.

Cost Plus Fee

Cost plus fee means that the contractor is paid a fee in the amount agreed between the parties, in addition to reimbursement of the actual construction cost.

Adjustable Price

With an adjustable price, the contract price is adjustable subject to agreed conditions, such as an increase in labour or material costs due to inflation or market change, a change in the order, a change of quantities or other geotechnical conditions.

7.2 Assigning Responsibility for the Design and Construction of a Project

An owner may either enter into an EPC Contract with a general contractor, or separately enter into a design contract and a construction contract with a local design institute and construction contractor, respectively.

EPC Contracts include the following according to market practices:

- an Engineering-Procurement-Construction (EPC) arrangement, under which the contractor is responsible for the engineering, procurement and construction of the project, and is fully accountable for aspects such as quality, safety, schedule and price;
- a Design-Build (DB) arrangement, under which the contractor is responsible for the engineering and construction of the project, and is fully accountable for aspects such as quality, safety, schedule and price;
- an Engineering-Procurement (EP) arrangement, under which the contractor is only responsible for the engineering and procurement of the project, and not the construction thereof;
- a Procurement-Construction (PC) arrangement, under which the contractor is only responsible for the procurement and construction of the project, and not the engineering thereof; and
- a Lump-Sum Turn-Key (LSTK) arrangement, under which the contractor is responsible for the engineering, procurement, construction and installation, commissioning service, and delivery of the project qualified for use.

7.3 Management of Construction Risk

Construction risks may be allocated between the parties to a contract, considering factors such as bargaining power, fairness and justice. For instance, the owner may transfer the risk of price increase to the contractor by adopting the fixed lump-sum price contract, or the contractor may agree to indemnify the owner only to the extent of the total contract price. Generally, risk allocation arrangements are valid and recognised by the courts, provided they are not in violation of the mandatory provisions of PRC laws and administrative regulations.

Furthermore, a project owner may require a contractor to take out and maintain project-related insurance (such as contractor's all risks and third-party liability insurance) in favour of the owner.

7.4 Management of Schedule-Related Risk

The owner and contractor generally specify a duration for work, including milestone and completion dates in the contract, and manage the work progress through the following contractual arrangements:

- the contractor is required to make and update the work schedule, report in a timely manner any risks of extension of work duration, take all actions necessary to keep to the agreed schedule and pay the delay damages;
- the owner has the right to terminate the contract in case of severe delay of the schedule; and
- the circumstances under which the owner must agree to extend the duration of the contract must be specified.

Monetary compensation may be claimed by an owner in accordance with the contract or by law, if certain milestone and completion dates are not achieved.

7.5 Additional Forms of Security to Guarantee a Contractor's Performance

In practice, the following forms of security are generally requested by the owner:

- a performance bond, in the form of a bank guarantee or third-party guarantee, which is issued to the owner by the guarantor for the purpose of securing the performance of the contract by the contractor;

- a payment guarantee in the form of a bank guarantee or third-party guarantee, which is issued to the subcontractors, suppliers or construction workers by the guarantor, for the purpose of securing the payment obligations of the contractor under the relevant contract(s); and
- retention money is an amount retained from each progress payment, which is generally released to the contractor after the contractor has fully performed its contract obligations, usually after the expiry of the defect liability period.

7.6 Liens or Encumbrances in the Event of Non-payment

The contractor for construction work has the right of contractor's lien over the construction in the event of non-payment by the owner, which is senior to a mortgage or other debts. Such contractor's lien is valid for up to 18 months, commencing from the date the construction payment becomes due. The contractor's lien may be removed if the overdue payments are made in full by the owner by voluntary payment or offset against the negotiated sale price (between owner and contractor) of the construction, or the proceeds from the auction of the construction, ordered by a competent court.

7.7 Requirements Before Use or Inhabitation

The PRC laws explicitly stipulate that no construction shall be delivered for use unless it passes completion acceptance. The owner must organise the geological survey contractor (勘察), designer, contractor and jianli (监理) (professional supervision engineer mainly responsible for the supervision and management of the construction quality and schedule) to attend the completion acceptance inspection; and, after completion acceptance is passed, the owner must go

through specific completion acceptance filing formalities at the relevant government authorities, and obtain the Completion Verification and Acceptance Filing Certificate for the Construction Project (建设工程竣工验收备案证书), which may be replaced by an electronic notice from HUDA declaring that the completion acceptance has been passed, for certain small-scale non-residential construction works in some localities.

In addition, in the case of a residential housing project, the PRC laws also require the Residential Housing Quality Warranty and Residential Housing Use Manual to be provided by the real estate developer when delivering such housing, and certain localities, such as Shanghai, Shandong province and Tianjin, further require a certificate of delivery and occupancy issued by the local HUDA, to be obtained by the real estate developer before occupation of the newly built residential housing.

8. Tax

8.1 VAT

PRC companies are subject to payment of VAT for the sale of real estate, and the seller is the obliged taxpayer. The taxes payable are equal to the sale price multiplied by the applicable tax rate. Two methods are applied to calculate the sale price:

- under the simplified method, the sale price includes all the costs received by the seller plus the out-of-price expenses; and
- under the general method, the sale price equals the balance of the total amount of the costs received by the seller and the out-of-price expenses after deduction of the expenses incurred during the sale of the real estate.

For a general taxpayer, if the seller acquires the real estate before 30 April 2016, it may choose the simplified method (at an applicable rate of 5%) or the general method (at an applicable rate of 9%). If the real estate is acquired after 1 May 2016, only the general method may be applied (at an applicable rate of 9%).

For a small-scale taxpayer (ie, whose VAT-taxable sales are no more than CNY5 million per year), the simplified method at an applicable rate of 5% will be applied. If VAT-taxable sales are no more than CNY100,000 per month, such taxpayer is exempt from the payment of VAT.

8.2 Mitigation of Tax Liability

An equity deal is often chosen by companies over an asset deal as a way to mitigate tax liabilities. However, the State Administration of Taxation has issued certain official replies on a case-by-case basis to collect land appreciation tax from the seller in equity transfer transactions where the main asset of the target company acquired was the real estate. As a result, there might be potential exposure to land appreciation tax liability in similar equity deals.

8.3 Municipal Taxes

Property tax and urban land use tax are the main municipal taxes paid on the occupation and usage of real estate:

- for property tax, the applicable rate is 1.2% if it is calculated based on the residual value of the real estate (ie, the original price of the real estate reduced by 10% to 30%), and 12% if the tax is calculated based on the rental income from the real estate; and
- the applicable rate of urban land use tax varies from CNY0.6 per square metre to CNY30 per square metre, depending on where the real estate is located.

Exemptions

Preferential policies on property tax and urban land use tax in respect of commercial real estate are available to taxpayers in a less favourable financial situation or in certain specific industries.

8.4 Income Tax Withholding for Foreign Investors

In the case of an offshore entity holding an onshore project company, which, in turn, holds real estate in the PRC, such offshore entity is subject to:

- withholding income tax at an applicable rate of 10% on any dividends received from the onshore project company; and
- withholding income tax at an applicable rate of 10% on the net income generated from the transfer of equity in such onshore project company, if under each circumstance such offshore entity has no establishment in the PRC or such income has no actual connection with such establishment, unless otherwise provided in a more preferential bilateral tax treaty.

In the case of an offshore entity directly holding real estate in the PRC, which existed before July 2006, such foreign investor, if it has no establishment in the PRC or the income generated in the PRC has no actual connection with such establishment, is subject to:

- withholding income tax on the net income generated from the transfer of the real estate at a rate of 10%; and
- withholding income tax at a rate of 10% on the rental proceeds generated by the real estate.

8.5 Tax Benefits

According to the PRC Enterprise Income Tax Law, real estate held by a company is typically treated as fixed assets, which may be depreciated, and the relevant depreciation amounts are allowed to be deducted from taxable income. The land use right held by companies is usually treated as a non-tangible asset, which may be amortised, and the relevant amortised amount may be deducted from taxable income.

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