



CHINA: HOW TO TEMPORARILY SUSPEND COMPANY OPERATIONS

Welcome to our new **ADVANT Beiten** edition on certain questions and answers on how and in which circumstances an enterprise can be put dormant under the Chinese corporate legal system! With this publication, we aim to provide you with essential information about this topic. We do this intentionally in a way which seeks to draw your attention to some important issues regarding when and how to transfer operational enterprises to a temporarily dormant status. Hence, what we set out in this publication deals with some of the most common questions on that topic that we came across in our advisory services. Thus, please read this publication to get a first understanding on what aspects to pay attention to when a company wants to suspend its operation temporarily and for any specific questions, please contact us anytime!

1. What are the different forms of enterprise registration and what does the status "suspended" mean in that context?

Under Chinese laws, the enterprise business license is the documentary proof that a company is legally registered and qualified to conduct business operations. Business licenses are issued, supervised and cancelled by the locally in-charge Market Supervision Administration (**MSA**).

MSA organises the enterprise registration status into the following categories: existence, revocation, deregistration, moving in/out, **suspension**, liquidation and annulment. While the applications for existence, deregistration, moving in/out and liquidation require active measures by the company/its shareholders, a revocation and annulment is imposed by MSA as a penalty. The meaning of these different forms of enterprise status can be briefly summarised as follows:

- *Existence* means that the enterprise subsists and operates normally. Depending on the actual administrative practice of MSAs across China, this status is also referred to as *open* (开业, kaiye), *in business* (在业, zaiye), *normal* (正常, zhengchang), *registered* (登记, dengji), *recorded* (在册, zaice), *in operation* (在营, zaiying), *valid* (有效, youxiao) or similar.
- *Revocation* of business license is an administrative penalty imposed by MSA for material violations of the enterprise (see below Sec. 2 for details) and means that the company must stop to be operative and shall be liquidated and deregistered according to law.

- *Suspension* is a status where the shareholders of the company decided to keep the company dormant for a certain limited period of time and to decide during such period whether to eventually resume operations or to liquidate and deregister the company.
- *Moving in/out* is the status of a company that decided to relocate from the jurisdictional reach of one MSA to another. During such relocation period, the company remains legally existing and operational.
- *Liquidation* refers to the stage of the company where the shareholders (or in case of bankruptcy the courts/administrators) decided to liquidate the assets of the company, settle all debts and creditor's rights with the goal to deregister the company.
- *Deregistration* is the last step in winding up a company and occurs either based on a corresponding shareholder resolution or in case of bankruptcy based on a decision of the court/administrator. Completion of the deregistration process means that the company legally ceases to exist, even if after such step certain other formalities are required (see below Sec. 4 for details).

Besides the above, there is also the possibility of an *annulment* of company by MSA, if MSA finds that a company was illegally established. This can e.g. result from the illegal usage of others' information to set up a company.

2. What is the legal basis for business suspensions and what are its benefits?

Effective since 1 March 2022, the "*PRC Administrative Regulations for Enterprise Registration*" (中华人民共和国市场主体登记管理条例) ("**Registration Regulations**") are on a national level the guiding piece of legislation concerning all PRC enterprise registration matters. These national level Registration Regulations are further supplemented by local rules and regulations issued by the locally in-charge MSAs. In Beijing for example, the "*Measures of Beijing Municipality for the Administration of the Filing of Suspension of Business of Enterprises (Trial Implementation)*" (北京市市场主体歇业备案管理办法(试行)) supplement the Registration Regulations and stipulate that enterprises may suspend their business upon application with MSA, provided they do not endanger national security, damage social public interests and legitimate rights and interests of third parties.

Prior to the Registration Regulations having entered into effect, enterprises that wanted to operate in an orderly manner and that had suspended operations for more than six months were required to liquidate and deregister their enterprises or otherwise faced the risk of having their business licenses revoked by MSA.

With the Registration Regulations having entered into effect (and having been also now supplemented by many local MSA regulations across China), enterprises now have the opportunity to suspend their operations for a longer time and in a legally sound manner.

This option may help companies who face serious operational challenges (e.g. because of natural disasters, accidents, public health crisis, public security incidents, etc.) by giving them time to decide whether to eventually liquidate and deregister the enterprise or to continue operations, while during such decision making time maintaining their legal registrations and qualifications while saving operating costs. During the suspension period, the company still enjoys the rights to its company name, to all licenses and qualifications it has obtained, all assets that are registered in its name (tangible and intangible) while having the opportunity to drastically decrease the cost base of its operations.

Given that the business suspension system in China is still in its infancy, some implementation issues need to be further clarified and thus companies considering to apply for suspension shall closely monitor any related novel legal developments.

3. Which entities are eligible to apply for suspension of business?

From the perspective of legal forms of entities, basically every kind of legally established units are eligible to apply with its locally in-charge MSA for business suspension if it finds itself in a situation of objective operational challenges that have been ongoing for a certain period, including but not limited to legal persons enterprises and their branches, sole proprietorships, partnerships and their branches, etc.

From the actual circumstances which allow entities to file such applications, in certain situations entities will be barred from such applications, e.g.:

- companies being found in abnormal operations such as being listed on MSA blacklists, being marked as unreliable creditors in the public systems, being under insolvency orders;

- companies which have been established less than six months ago will likely face difficulties as well because for them it may be difficult to establish that they face serious operational challenges for a longer period that would warrant a business suspension;
- companies whose business licenses will soon expire.

Also, it must be understood that business suspensions cannot be decided by shareholders/their companies at will but that there must be well-founded objective circumstances that substantially challenge the business operations for longer periods of time.

4. Is there a maximum time for which an entity can legally suspend its business before deciding to restart operations or to finally liquidate and de-register?

The Registration Regulations allow a maximum period of three years for business suspension, whereby the applicant can initially also apply for a shorter period of e.g. six months or a year and then decide to apply for an extension of the suspension period. Any such extension application shall be made at the latest 30 days prior to the expiration of the ongoing suspension period and the overall continuous time of suspension shall not exceed three years. Legally speaking it is also possible for a company to use the overall three-year period of suspension in uninterrupted installments, provided the overall objective reasons for business suspensions can be established at the given times.

5. What obligations must be met by an enterprise that intends to file for business suspension?

Prior and during the period of suspension of operations, the affected enterprise still has certain obligations it needs to fulfill, while other obligations will be lifted during such period:

- **Human Resources:** Prior to applying for business suspension with MSA, the company and its employees must negotiate how to handle the labour relationships and related matters of the staff of the company. The company (employer) and its employee must consult and agree whether to terminate or keep the labour relationships alive during the suspension period. In case of termination, severance payment and employment settlement procedures need to be conducted. Where the labour relationship maintains, labour compensation and statutory social benefits payments need to be settled on an ongoing basis at least with the minimum amounts legally required. Companies must understand that the suspension of business filing (other than the company liquidation and deregistration) does not establish a unilateral right of labour termination for the employer. Also, companies that have non-PRC nationals on their staff list and wish to maintain the labour relationships with them during the suspension period should check prior to the business suspension application whether they can apply – if necessary – for the extension of foreign national residence and work permits.
- **Civil and Administrative Liabilities:** Since during the period of business suspension the company maintains its legal person status, it remains liable to perform all obligations arising out of civil obligations (e.g. commercial contracts, financing agreements, court/arbitration rulings and alike) as well as it remains liable to settle administrative penalties/decisions, as applicable. Thus, companies are well advised to negotiate with any contractual partners prior to filing the business suspension application on how to suspend/terminate/settle any third-party contracts they have entered into.
- **Taxation:** Enterprises that have suspended their operations with MSA are not required to report to the tax authorities separately about the suspension as such because this will be handled by MSA directly. However, that does not mean that during the suspension period the company has no tax-related obligations altogether. If during the business suspension period taxes still become payable or to be withheld by the company, it is still obliged to pay/withhold such taxes, but it may do so in a simplified quarterly manner (see for details *"SAT Announcement on Simplifying the Handling of Tax-related Matters during Business Suspension and Deregistration of Enterprises"*(国家税务总局关于简化办理市场主体歇业和注销环节涉税事项的公告)).

Also, since in practice the local tax requirements for companies who have suspended their operations may differ among the local in-charge tax authorities across China, companies are well advised to consult with their local in-charge tax authorities on what requirements shall be met for the regular monthly, quarterly and annual tax filings.

- **Annual Recordal:** Despite having filed for business suspension with MSA, companies must file their annual recordal application publicly in the National Enterprise Credit Information Publicity System (**NECIPS**) for the previous year between 1 January to 30 June of the current year.
- **Address for Service of Documents:** During the suspension period enterprises can freely choose an address for service of documents and this address must not necessarily be their usual legal address. If they choose to do so, they must provide a confirmation letter to MSA with the related content and update such information with MSA, if it changes during the suspension period.

6. How to apply for business suspension?

A company that wishes to apply for suspension of business shall file a corresponding application with its locally in-charge MSA prior to suspending the business. The application documents may differ on a case-by-case basis depending on the specific requirements of the locally in-charge MSA and will typically comprise the following documents:

- MSA application form for business suspension;
- commitment letter for suspension of business;
- sealed copies of business license;
- information on address for service of documents;
- other documents as required by MSA on a case-by-case basis.

Once accepted by MSA, MSA will publish the period of business suspension, the address for the service of documents and other relevant information through NECIPS.

7. How and when to resume operations after the business suspension?

In any of the following circumstances, a company is considered to have resumed operations:

- expiry of the business suspension period shown in NECIPS without valid extension thereof or the accumulative period of business suspension has reached three years (if in the aforesaid cases the company has not actually resumed operations, it must apply for liquidation and deregistration without delay);
- actual (decision of) commencement of business activities during the suspension period (in this case, the company shall announce the termination of the business suspension through the NECIPS within 30 days as of actual resumption of business).

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