After Earning Cash in China, The Trick Is Getting It Out

BY VIPAL MONGA

U.S. companies have plowed billions into China with high hopes of capitalizing on the country's fast-growing economy. Few of them, however, contemplate the flip side: getting that money back out.

Big corporate investors such as General Motors Co., industrial-gear maker Emerson Electric Co. and fast-food restaurant operator Yum Brands Inc. have long counted on China to fuel their growth. The country now is GM's biggest market, and the car maker plans to invest as much as $7 billion more there by 2016.

But, as their Chinese profits accumulate, some companies are finding that bringing that money home is a costly and time-consuming process. "It's like the 'Hotel California,'" said Daniel Blumen, co-founder of consulting firm Treasury Alliance Group. "Everybody goes into China in a hurry, but then they find it's not so easy to get out."

Most countries regulate big movements of corporate cash. But in countries with a freely convertible currency that often means little more than routine approval from tax authorities. In China, which closely regulates the conversion of its yuan into dollars or euros, the hurdles to withdrawing profits include an array of taxes and regulatory gray areas.

The process can be especially frustrating for those who might need the money most urgently. Cash-strapped Eastman Kodak Co., which recently filed for protection under Chapter 11 of the U.S. Bankruptcy Code, has about $320 million in China, and it is likely to need at least some of it to pay its creditors.

The company declined to comment for this article. But Antoinette McCorvey, Kodak's chief financial officer, said during a conference call in November that the photography icon wanted to remove as much of its China cash as it could "once various government requirements are met," according to a transcript of the call from FactSet. Ms. McCorvey said it would take several months for Kodak to repatriate its money.

That is because China, which has gradually been deregulating foreign investment since the 1980s, has put up barriers to...
Continued from page B1

limit the sort of capital flight that occurred in countries such as Thailand, Indonesia and Malaysia during the Asian currency crisis of the late 1990s.

“Trapped cash will always be a concern,” said Sam Xu, executive director in J.P. Morgan Chase & Co’s treasury-services group, which advises companies on cash management. He added that recent steps China has taken to loosen its currency controls, aimed at promoting the yuan as a global currency, haven’t made it easier for foreign companies to extract their profits.

“It is very likely that it will take a long time before China’s capital account is completely open,” Mr. Xu said.

In fact, the problem could get worse. China’s slowing economy might encourage authorities there to make it more difficult for companies to take out profits, said Wei Shu, lead economist of Deloitte Touche Tohmatsu’s transfer-pricing practice in China, which advises companies about cross-border transactions.

“If the economy is not as good as it was in the past, the Chinese tax authorities could get more tax revenues from foreign companies,” he said.

Corporations that want access to their China cash have a few options, according to several experts. None is very straightforward, but the least complex is for a company’s Chinese unit to pay dividends directly to its foreign parent.

First the subsidiary has to put aside about 10% of its profits in a so-called enterprise reserve, capped at 50% of a company’s total investment in the country, to protect against future losses. That can be a substantial sum for a company such as GM, which has invested billions in China.

Then, the company must set aside another, unspecified percentage of profit for employee welfare. The sum is based on a number of factors, some of them murky. “It’s a little bit of a gray area,” said Alvin Chan, a director at tax and accounting advisory firm Nair & Co. The rest, already taxed at China’s corporate rate of 15% to 25%, is subject to an additional 10% withholding tax.

A company also can lend money from a Chinese-incorporated unit to an overseas affiliate by using a registered bank as a broker. That can help the company use its Chinese profits to manage cash flow but ultimately keeps the money in China.

China’s State Administration of Foreign Exchange, which oversees foreign-currency activity, regulates such transactions and requires they be treated as true loans, paid back at interest rates comparable with similar loans by banks. Cross-border loans out of China generally are made in U.S. dollars, so the rate is based on the London Interbank offer rate, said J.P. Morgan’s Mr. Xu.

Another way to move money: Foreign companies can charge their Chinese unit royalty fees or charge them for services. China also taxes those payments, and it insists that they have a legitimate business purpose that is supported by documentation.

“It’s a cumbersome process and not exactly tax-efficient,” said Herbert Parker, chief financial officer of stereo-equipment manufacturer Harman International Industries, which has been investing in China since 2000. He said the process is manageable, but that companies need to plan in advance.

One reason why is that the rules companies must follow to get government approval to repatriate Chinese funds can be a bit of a moving target.

“There’s a difference between the regulations as written and the laws and regulations as they are practiced,” said George Kelakos of Kelakos Advisors LLC.