



China Covid-19 Outbreak Snippets

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Policies which you need to know to do business in China

With the recent outbreak in Beijing gradually coming under control, businesses in China are working tirelessly to making sure every employee is safe. However, flights have been reduced thwarting the flow of foreign business managers, annual auditors, investors and staff coming to China to resume business. Not all is lost; LehmanBrown continues to take care of businesses in any way possible to overcome remote business management issues.

Negotiate, Reduce, or Terminate

Struggling businesses who are fraught with cashflow problems and left with no other choice but to look at reducing staff costs have three options to consider, negotiating a reduced pay for everyone, reducing pay temporarily, or terminating the labour contracts.

Negotiating involves discussing with all staff members from the board or partner levels to the employee level to agree on an arrangement which would reduce salaries across the business to ensure the burden is shared equally. This should be seen as fair and equal to all, not discriminating against any positions or levels in the organization.

The Reducing method would mean for employees to agree to a reduced salary for a few months with the promise to pay back staff later with interest. Or more senior management take a reduction in remuneration to save the company costs and cashflow. Any adjustments would have to be in writing, and often the question of the severance base comes up, or the base for bonus calculations. These can be addressed in an agreement on the deal, which should be signed by all of these affected.

Finally terminating would be the last and least appealing option as it may cause more troubles than benefits in the long run. Labour contracts in China have clear criteria which can prohibit the termination of a contract or terminate with 30 days with compensation or for a business to terminate a labour contract immediately without compensation. There are also clear labour laws which must be followed for mass layoffs of 10 people or 20% of the workforce. Severance pay is one month's salary for every year worked, to a maximum of 12 months for 12 years with a cap of monthly salary for the formula at three times city's average. Other criteria can lead to the base being the actual salary if higher than the salary, and also to regulations surrounding unfair dismissal.

Recommendations

With the current covid-19 situation, the best option is to negotiate for a reduction of pay or reduce the salaries significantly and then to pay back later with interest once the demand is back. This solution also allows the businesses to benefit from China's policies to relieve financial burdens to business which do not reduce their staff numbers.

However, if a business needs to terminate it should do so by terminating labour contracts by the priority of each staff member looking at their contract type, family unit and age group, date of joining etc. A business should also avoid mass layoffs which would include the Labour Bureau and having to deal

with potential legal risks or unexpected internal disarray. Instead, a business seeking to terminate labour contracts might consider doing so gradually, while negotiating the severance pay with each employee.

Managing the Cashflow

Countless businesses are having to deal with the sudden drop in demand for their services or products as outbreaks re-appear, are affected by the global ongoing Covid situation and how their own markets are affected, affecting their cashflow and their planning for the future.

For a business to plan, it will need to create cashflow forecasts taking into consideration all known information, and where unknown then making assumptions based upon other sources of data, and combining the gutt feel of management. The devil is always in the detail, and also during a crisis in timeliness. If the detail is not accurate in direction, e.g. over optimism of sales and collection timing of receivables, then the cashflow is not a true reflection of where the business is going, or its future cashflows and possible lack of cash in the future.

In order to shore up cashflows businesses should do a number of things:

1. Move to regularly forecasting of cashflows, eg.. weekly, and monitor movements in forecast to actual, and last weeks forecast to this weeks forecast.
2. Incorporate the cashflow into the payment process, E.g. cut out adhoc requests, all payments needs to be planned as best as possible. Prioritising payments and planning purchases and payments all form part of the planning.
3. Look at all scenarios of revenue and collections, the good, the bad and the ugly, to perform sensitivity analysis on the future cashflow projections. Is the business still okay with the ugly, or does other steps need to be taken in this scenario, e.g. cutting costs, raising capital, selling or leasing assets etc.
4. Create a cashflow culture internally, and have senior management behind this. When a mid level manager demands that finance pay a supplier, the accountant needs to know that they have support when they push back and say "this is scheduled for next week, come back then or talk to senior management". It is about changing the culture and improving planning.

Recommendations

During the crisis, cashflow forecasts must be on a short-term basis e.g. weekly, by weekly, and monthly, looking at all possible situations, developments and running sensitivity analysis under what-if scenarios. Such forecasts allow decision-makers to make informed decisions and regulate their cashflow according to the likely and unlikely risks which may impact their business.

However, a cashflow forecast can only be as effective as senior management's ability to help collect receivables, work closely with clients and suppliers, and to maintain cash sufficiency.



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LehmanBrown is a licensed China-focused accounting, taxation and business advisory firm, operating dedicated offices in Beijing, Tianjin, Shanghai, Shenzhen, Guangzhou, Hong Kong and Macau, and with an extensive affiliate network throughout China and in over 100 countries worldwide.

LehmanBrown combines years of international expertise with practical China experience and knowledge, offering expert advice and support to both local and international clients. We are committed to providing individually tailored financial and business solutions for each of our clients, recognizing that each client is different. Through offering “whole of life” services, LehmanBrown offers clients assistance throughout every step of their business life cycle, from pre-conception to afterlife. LehmanBrown is registered with the PCAOB in the US and is able to conduct SEC work, as well as being accredited by accounting bodies in the UK and Australia.

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