



Doing Business in Hong Kong and Mainland China

29 August 2008

ERNST & YOUNG
Quality In Everything We Do

Doing Business in Hong Kong and Mainland China

- ▶ Hong Kong – A Tax Perspective
- ▶ Mainland China – A Tax Perspective
- ▶ Australia – Commercial / Tax Considerations

Hong Kong – A Tax Perspective

- ▶ Under the “One Country Two Systems” principle, HK has its own separate tax system different and independent from that of the Mainland China
- ▶ No tax holidays and incentives for any particular industries
- ▶ Simple, low and territorial-based tax systems; only HK sourced profits
- ▶ Foreign-sourced income not taxed even remitted back
- ▶ No capital gains, dividends and interest withholding tax

Hong Kong – A Tax Perspective

- ▶ Tax laws generally well organised and transparent
- ▶ Supported by explanation notes from Revenue, published advance ruling; Board of Review Cases and Court Decisions (including UK and Australia)
- ▶ Adoption of OECD principles eg royalty v product sale; activities which cause a Permanent Establishment
- ▶ Not covered by PRC: tax treaties; HK has tax treaties with Belgium, Thailand, Luxembourg and PRC
- ▶ Favourable treaty with PRC: lower withholding tax rates on dividend, royalty and interest from mainland China to HK, potential capital gain exemption

Hong Kong – A Tax Perspective

- ▶ Taxes limited to:
 - (i) Profits Tax – 16.5% flat
 - (ii) Salaries Tax – 15%
 - (iii) Property Tax – 15%

- ▶ Stamp duties are of limited scope: 0.2% on shares and 3.75% on assets/property transfers in HK

- ▶ No GST

Mainland China – A Tax Perspective

I) Corporate Tax regime changed beginning 1 January 2008

- ▶ Single tax rate of 25%
- ▶ Withdrawal of preferential tax treatment for most foreign owned companies under old law, ie increase from 15% to 25% over time; refer to HNTE rules later
- ▶ Withholding tax of 20% on dividends distributed offshore; possible treaty reduction to 10% or less; tax clearance certificate required

Mainland China – A Tax Perspective

II) Other Important Developments

A. Tax residency of PRC companies

- ▶ If PRC resident, subject to tax on worldwide income
- ▶ If non-PRC resident, profits effectively connected to a permanent Establishment ('PE') taxed in PRC
- ▶ Factors which could influence residency include:
 - ▶ Key management and strategic decisions made in the PRC
 - ▶ Directors meeting held in PRC at which activities such as strategic policies, business decisions, evaluation of business performance, implementation of management decisions are performed
- ▶ A PE includes,
 - ▶ "... a place of management, business office, factory and business agents..."
 - ▶ Treaty exclusions for "bona fide" agents may apply

Mainland China – A Tax Perspective

B. Transfer Pricing

- ▶ Very comprehensive draft rules were circulated to selective groups, if released, will be effective from 1 January 2008
- ▶ Contemporaneous documentation (in Chinese) will be compulsory
- ▶ Need to be submitted to authorities when requested, potentially within 15 days
- ▶ Numerous forms to be completed depending on the nature of cross border dealings – comprehensive and detailed
- ▶ New penalty (interest) regime

Mainland China – A Tax Perspective

C. High-new technology enterprises (HNTE) Guidelines

- ▶ Companies which qualify as a HNTE will enjoy a tax rate of 15% (compared with normal rate of 25%)
- ▶ Prospect of tax holiday for HNTE set up in SEZ or Shanghai Pudong New Areas after January, 2008
- ▶ Existing HNTE's under old regulations are not automatically entitled to new preferential tax treatment; qualifying companies are required to be accredited with new HNTE status
- ▶ A HNTE status certificate valid for 3 years – emphasis on R&D expenditure spend/IP retention in PRC/majority of R&D spend in PRC (personnel in PRC) having scientific/R&D skills

Mainland China – A Tax Perspective

D. Exchange Control

- ▶ Relaxation of foreign exchange controls on a trial basis in certain service type sectors (remittances exceeding US\$50,000 - through a designated bank)
- ▶ Avoids seeking tax clearance
 - withholding tax, if any still to be determined
- ▶ Requires contracts/forms to be filed prior to actual remittance
- ▶ Six Regions are Tianjin, Shanghai, Jianjsu, Sichuan, Fujian and Hunan
- ▶ Possible extension of rules to other regions/nationwide if trial run is effective
- ▶ Example of Services covered appear to be:
 - ▶ Travel, communications, construction, insurance, computer technology, sport, cultural and entertainment services, licensing and royalty etc.

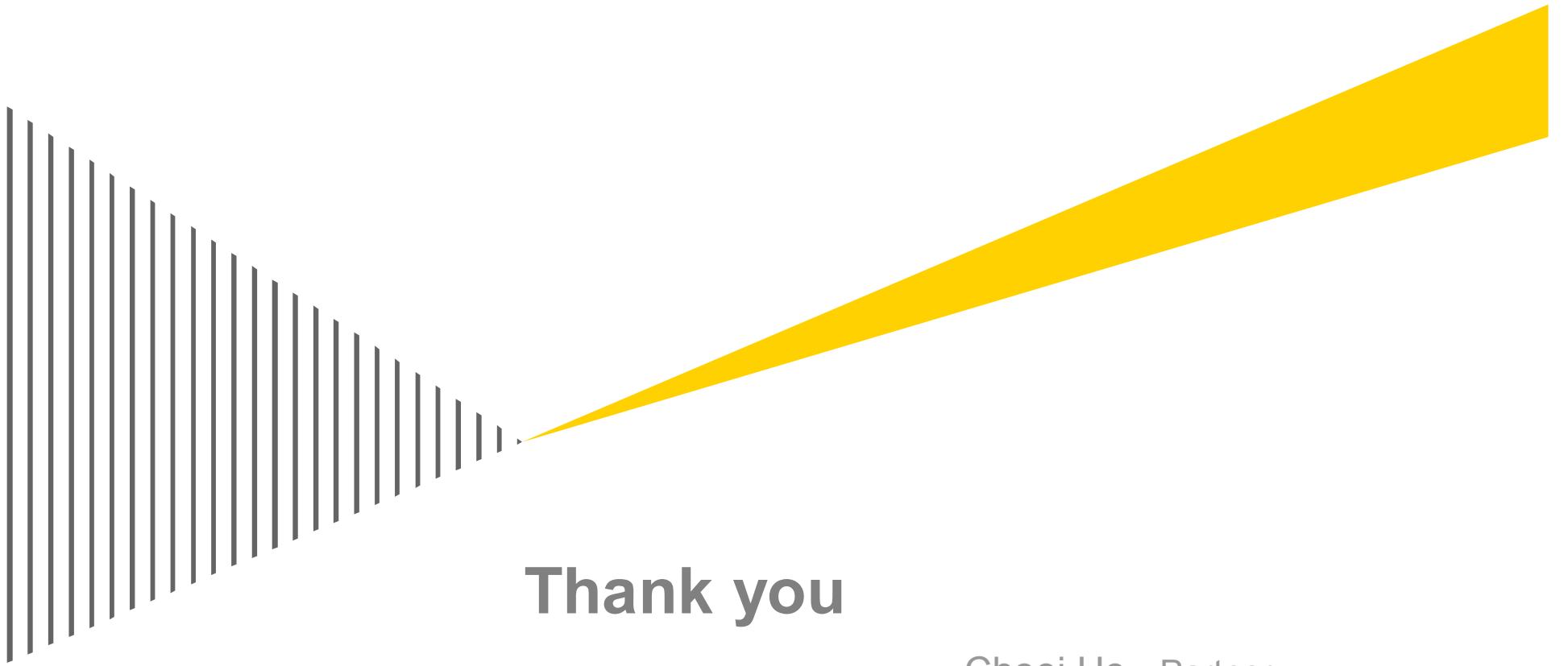
Australia – Commercial/Tax Considerations

Australian investment into Hong Kong or mainland China

- ▶ Different investment decisions depending on whether the Australian entity is:
 - ▶ Foreign owned OR Australian owned
 - ▶ If Australian investment entity is foreign owned – consider a “management” oversight role instead of shareholder role.
 - ▶ If owned by Australian residents, different tax and commercial considerations apply e.g.. maximising dividend franking capacity may be important, as would be centralising of IP/key functions in Australia.

Australia – Commercial/Tax Considerations

- ▶ To operate in Hong Kong or mainland China, what is required from a business perspective
 - ▶ A representative Office (RO) acting in a liaison/marketing capacity
 - ▶ An operating branch
 - ▶ A local company
 - ▶ Structure can be managed once business needs identified
 - ▶ Other considerations include funding, exchange control, ease of repatriation, personnel issues



Thank you

Chooi Ho - Partner
Rose Wen - Senior Manager
Sydney

29 August 2008

ERNST & YOUNG
Quality In Everything We Do