

Structuring Issues for Chinese HNW Clients in view of China Agreeing to AEOI / CRS

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■ PART 1

Common Reporting Standards reaches the PRC

Common Reporting Standard reaches the PRC

- China enters AEOI and CRS in 2018
(reporting on account status for 2017 depending on Jurisdiction)
- Many UHNW individuals in China worry about invasion of privacy
- Security is often more a concern than tax issues
- Or questions about how wealth moved out of the Mainland, or was accumulated offshore

■ PART 2

Related Hong Kong Developments

Registry of Beneficial Ownership

- Consultation papers released 6 Jan 2017
- Public consultation stage pending FATF visit to HK later this year
- Proposal to require all HK companies to keep register of people with significant control (“PSC register”)
- Unlike other PSC registers in other countries (e.g. UK), HK considering to make its register publicly accessible

Registry of Beneficial Ownership

- To facilitate the cooperation with law enforcement agencies, company may be required to nominate an authorised person responsible for providing information and assistance to enforcement agencies
- Under consideration: will companies be able to choose to nominate either (1) a natural person resident in Hong Kong or (2) a local regulated professional (solicitor, accountant, or trust and company service provider)
- Companies and responsible persons will be liable for criminal sanctions
- Exemption for Listed Companies

Regulation of Trust and Corporate Service Providers

- Simultaneous release of consultation paper under AML regime to:
 - a) prescribe statutory customer due diligence (“CDD”) and record-keeping requirements for (i) solicitors, (ii) accountants, (iii) real estate agents and (iv) trust or company service providers (“TCSPs”) when these professionals engage in specified transactions with clients; and
 - b) introduce a licensing regime for TCSPs, requiring license from Registrar of Companies and satisfying “fit-and-proper” test

Regulation of Trust and Corporate Service Providers

- Obligation to verify a customer identity, beneficial owners and monitor business relationship continuously
- Six-year record-keeping period
- Sanctions and penalties apply for non-compliance
- A 90-day transitional period for existing TCSPs to migrate to the new licensing regime
- TCSP licence will be valid for a period of 3 years, renewable on application

■ PART 3

Structuring and Solutions

Structuring and Solutions

- CRS reporting is based on tax residency. In China tax residency is closely linked to the concept of domicile
- Many Chinese emigrants drop off their families in their new homes and return to China to continue business
- Can an entrepreneur give up Passport and Household Registration and still function the same way in China?
- E.g., he returns holding a foreign passport, and he still owns his PRC enterprise, that enterprise would technically require approval from authorities to convert into WFOE
- Or if he is a “foreigner”, he may not be able to buy PRC property?

Structuring and Solutions

- Some clients seek a replacement travel document (eg. Caribbean / EU)
- By itself this may not address CRS reporting, but can be part of solution
- What are the client's realistic relocation options?
- PR or Citizenship by investment?
- Or PR by Entrepreneurial Restructuring?
- Related issue is how to export capital from China



PART 4

Capital Outflows

Ways of Moving Capital Offshore

- Different types of capital outflow:
 - a) China's outbound direct investment (ODI)
 - b) Inter-company loans
 - c) Overseas acquisition

- ODI continued to surge in 2016 - a 55.3% increase on a year-on-year basis compared to 2015

Ways of Moving Capital Offshore

- Recent widespread media coverage of China's new restrictions on outbound investments by Chinese companies
- Although no new laws or regulations so far, public statements by PRC government officials and our recent transactional experiences suggest that new measures have in practice been implemented

New Restrictions on Outbound Direct Investment

- Press conference on December 6, 2016: officials from the People's Bank of China (PBOC), the State Administration of Foreign Exchange (SAFE), the National Development and Reform Commission (NDRC) and the Ministry of Commerce (MOFCOM) reiterated the Chinese Government's continued support for "One Belt, One Road" initiative
- But emphasized importance of monitoring "irrational outbound investments" by Chinese companies

New Restrictions on Outbound Direct Investment

- Based on various reports as an interim measure to stem capital outflow, the Chinese Government is effectively implementing stricter scrutiny over these types of outbound investments:
 1. Outbound investments into these sectors:
 - a) real estate
 - b) hotels and hospitality
 - c) cinemas
 - d) entertainment
 - e) sports clubs

New Restrictions on Outbound Direct Investment

2. Extra-large outbound investments, including:
 - a) Outbound real property acquisitions or developments by state-owned enterprises with an investment value of US\$1bn or above;
 - b) Outbound investments of more than US\$1bn outside of the core business of a Chinese buyer; and
 - c) Extra-large outbound investments valued at US\$10bn or more

New Restrictions on Outbound Direct Investment

3. ODI by limited partnership
4. Minority investments in listed companies: ODI involving the acquisition of 10% or less of the shares in an overseas listed company
5. “Small parent, big subsidiary”: ODI where the size of the target is substantially larger than the size of the Chinese buyer or where the Chinese buyer makes the investment shortly after its establishment

New Restrictions on Outbound Direct Investment

6. Privatisation: participation in the delisting of overseas listed companies which are ultimately controlled by Chinese companies or individuals
7. High risk/low return transactions: ODI into an overseas target resulting in a high-debt to asset ratio and a low return on equity

Other Restrictions by SAFE re ODI

a) Current Operations of Banks

- From November, 2016, PRC banks now required to report to SAFE any overseas transfer of US\$5m or more (both foreign currency and RMB) per transaction
- Such overseas transfers can only be made after the Chinese regulators have re-examined the underlying transaction of the requested transfer to verify its authenticity and compliance with relevant regulations

Other Restrictions by SAFE re ODI

b) Other SAFE Restrictions

- Also SAFE has tightened controls over ODI with capital outflow of US\$50m or more
- Such fund transfers will only be permitted after re-examination of the underlying transaction for authenticity and compliance with relevant regulations

Other Restrictions by SAFE re ODI

c) No Official Rules

- So far no official rules have yet been promulgated by the regulators in relation to the measures outlined above
- However, various sources suggest that PBOC and SAFE have given so-called “window guidance” to local foreign exchange bureaus and local banks to implement such measures
- Such measures have already affected a number of cross-border transactions

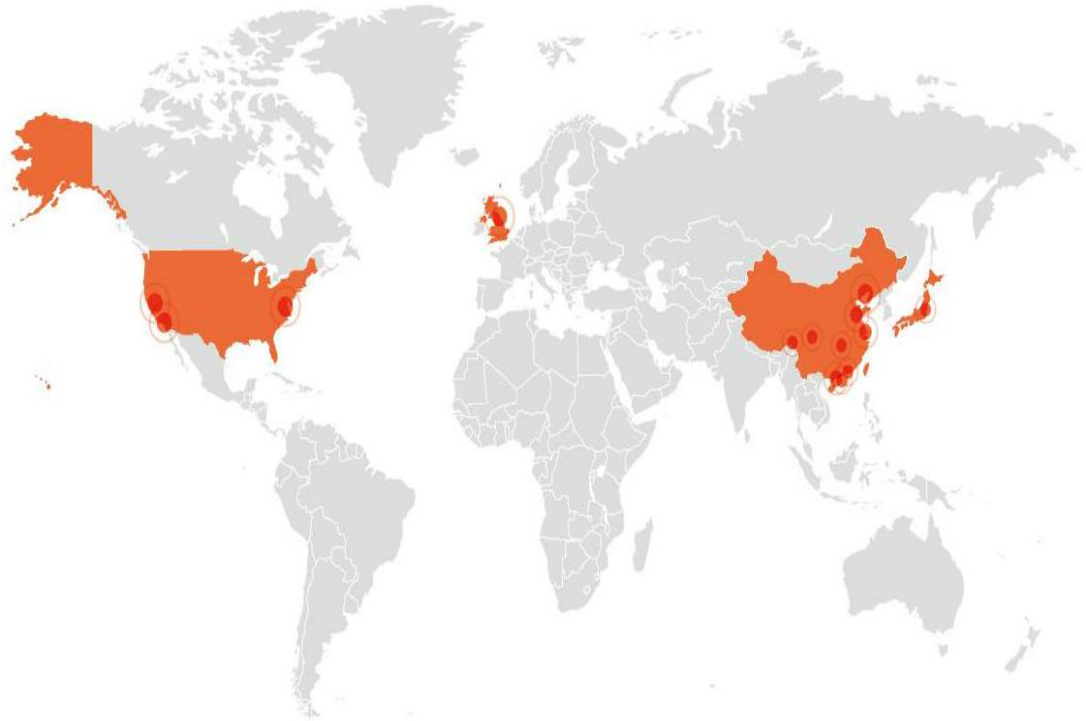
Thank you!
Q&A

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Presenter

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Kevin heads Zhong Lun's private client practice. He specializes in succession planning, trusts, and tax planning for high net worth individuals, and he is also experienced in corporate and commercial law, mergers and acquisitions, private equity, as well as charitable and non-profit structures. Kevin is recognized by Chambers, Citywealth, Who's Who Legal and Spear's Asia as one of the leading private client lawyers in Hong Kong/China. He is also one of the few practitioners in Asia Pacific who advises on Canadian tax.

Background

Kevin is a solicitor in Hong Kong, England and Wales and a barrister and solicitor in British Columbia, Canada. Kevin graduated with a Bachelor of arts degree from the University of British Columbia and obtained his LL.B from Dalhousie University, Canada. Kevin has been practicing in Hong Kong since 1989.

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About Zhong Lun Hong Kong

Zhong Lun's Hong Kong office has a history of over 30 years in Hong Kong. We serve a broad range of local and international clients including financial institutions, manufacturers in various industries, private equity funds, real estate developers, listed and private companies, as well as high net worth individuals and families.

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