TTN Conference
Hong Kong 2016

Changes in the use of HK structures involving activities in China

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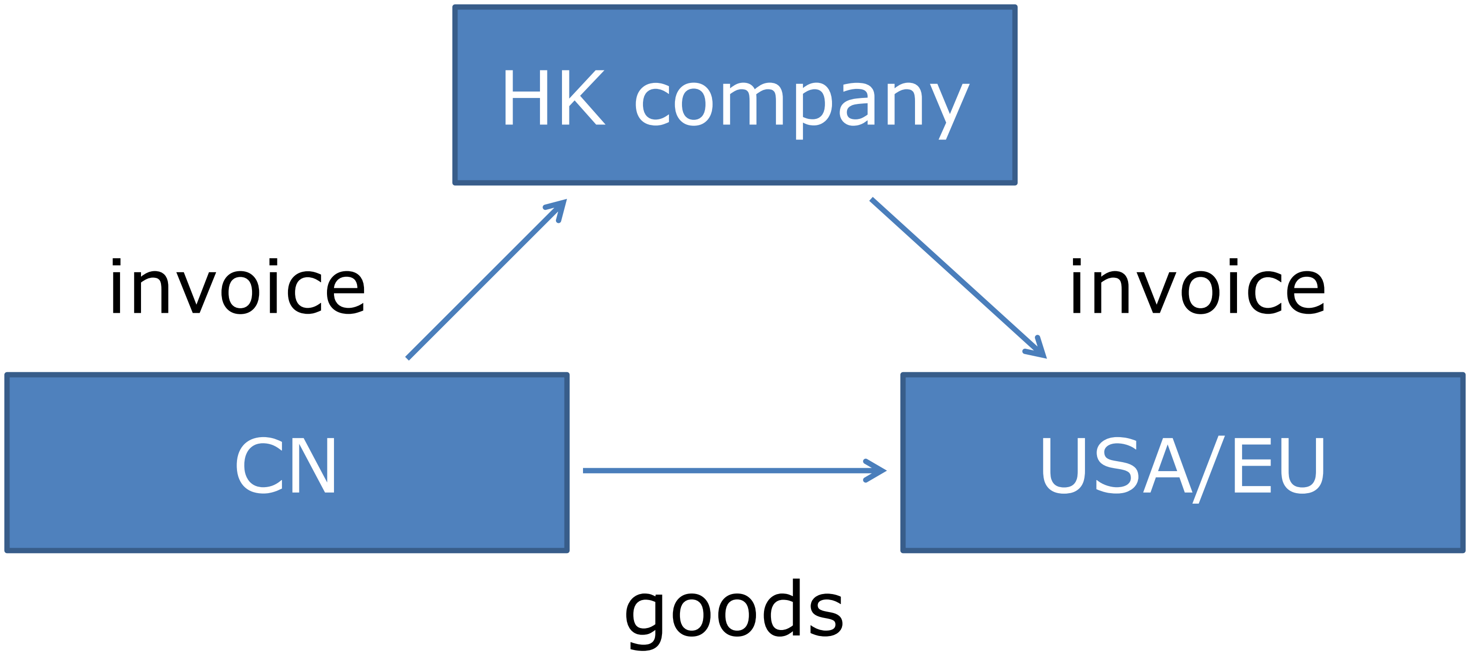
Classical HK-CN structures

1. Trading structure

2. Holding structure

1. Trading structure



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Advantages

- Territorial tax system
  - “Profits arising in or derived from HK”
- No VAT
- Easy setup
- Proximity to mainland CN

Erosion of advantages

- CFC (already from the 1960's in some jurisdictions)
  - Loopholes (nominee director arrangements, non-disclosure and others)

- Black lists (Brazil 2002; Portugal 2004; and also Poland, Greece, Bulgaria, Croatia)
  - Somewhat reversed (Spain 1991-2013; Italy 2010-2015)

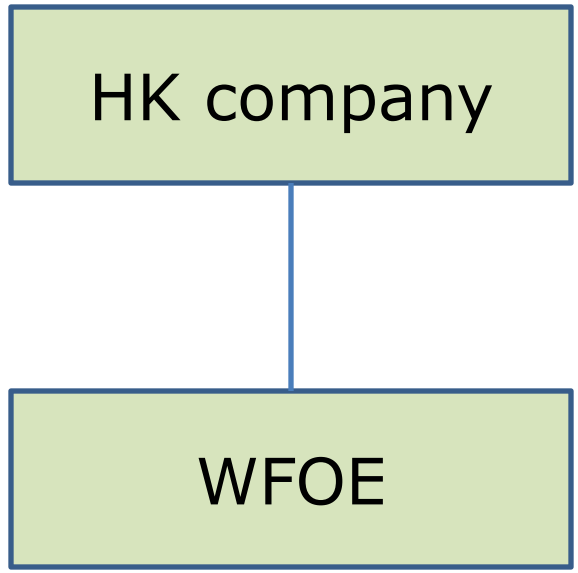
- Anti-Money Laundering and Counter-Terrorist Financing Ordinance (effective since April 2012); and

  New Companies Ordinance (effective since March 2014);

  both discouraging nominee director arrangements

- BEPS (a global effort to close loopholes)
  - Standard for Automatic Exchange of Financial Account Information in Tax Matters (2014)
  - Exchange mechanism in 2017

2. Holding structure



Characteristics of CN/foreign invested enterprises

- Identity of shareholders could change the corporate structure (WFOE, EJV, CJV);

- Long and bureaucratic incorporation process

- Normally, equity not divided into shares (exception: FICLS);

- Normally, transfer of equity requires amendment of articles and approval from several government departments;

- General inflexibility in financial
    - Debt/equity
    - Sweat equity and non-cash contributions problematic
    - Foreign exchange controls

- Difficulty in enforcing exit mechanisms

- Limitations on business scope

HK advantages 1

- Flexibility of corporate structures
- Stable judicial system
- Less bureaucracy
- CEPA – HKSS status (placement of personnel, medical services, tourism, insurance, banking)

HK advantages 2 (tax)

- Dividends not part of tax base in HK
- No capital gains tax (with some exceptions)
- Low withholding tax on dividends from mainland CN (cap of 5% if the HK company owns at least 25% of the CN company)

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Erosion of advantages

Tax treaty network (100+)

1994	Luxembourg	5-10% on dividends
2006	HK	similar arrangement
2007	Singapore	similar arrangement
2011	United Kingdom	similar arrangement
2013	Netherlands	similar arrangement
2013	Switzerland	similar arrangement

Circular 601 (2009)

Sufficient substance needed to benefit from tax treaties

Circular 698 (2009); Bulletin 7 (2015)

Indirect transfer of equity in CN entities through offshore vehicles may be subject to CN tax

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Is HK still attractive?

Bonnard Lawson

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