CEPA – YOUR **SPRINGBOARD** TO CHINA

CLOSER ECONOMIC PARTNERSHIP ARRANGEMENT

WHAT IS CEPA?

- A free trade agreement between **Hong Kong** and **mainland China**
- Effective from 1 January 2004
- Preferential access to China's market from Hong Kong
- Significant China market liberalisation
- Goes further than China's WTO commitments

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CEPA – A SIMPLE GUIDE

WHAT DOES CEPA OFFER?

- Zero tariffs on 90% of Hong Kong exports to China
- Faster/easier China market access for 18 service sectors
- Lower entry thresholds for smaller players (capital/trading history requirements)
- 100% ownership of many China ventures
- Manufacturers in China able to use Hong Kong services
- Makes Hong Kong the easiest route into/out of China

WHO BENEFITS FROM CEPA?

Hong Kong-based service providers *(in 18 sectors)*:

- *Company* must be incorporated in Hong Kong
- Doing business in Hong Kong for past 3-5 years
- Liable for Hong Kong profits tax
- Employing 50% of staff in Hong Kong
- Any nationality

Manufacturers/distributors of goods *(for 273 categories)*:

- *Goods* must qualify as 'made in Hong Kong'
- Not necessary for *company* to be based in Hong Kong
- To qualify, goods must be'substantially transformed' – 30% of value must be added in Hong Kong (includes R&D, design costs)

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HOW CAN OVERSEAS COMPANIES BENEFIT?

Service companies

- *Partner* with, *invest* in, or *buy* into a Cepa-qualified firm in Hong Kong

Manufacturers or traders of goods

- *Partner* with, or *outsource* to, a Hong Kong manufacturer
  (no need for your company to have a base in Hong Kong)

HOW CAN COMPANIES APPLY?

- Hong Kong-based service companies must apply for a Cepa certificate
- Manufacturers must apply for a Cepa certificate for their products

Easy application procedure through Hong Kong's Trade and Industry Department

MORE INFORMATION?

www.tid.gov.hk/cepa/eng – detailed information from Hong Kong's Trade and Industry Department

www.tdctrade.com/cepa – Hong Kong Trade Development Council's Cepa section

www.hktrader.net – e-newsletter with Cepa section for overseas companies

HOW CEPA CAN HELP YOU

1 What is Cepa?

Cepa stands for Closer Economic Partnership Arrangement. It is a free trade deal, operating from 1 January 2004, between Hong Kong and the Chinese mainland. It is the first bilateral free trade deal signed by China.

2 What are the main provisions of Cepa?

Cepa is broadly divided into three sections:

Trade in goods

Any company (Hong Kong-based or from outside Hong Kong) can benefit from zero tariffs on 273 categories of products exported from Hong Kong into the Chinese mainland, as long as the products are classified as 'Made in Hong Kong'.

Your company does not have to have an office in Hong Kong, but your products must satisfy 'Rules of Origin' to classify as 'Made in Hong Kong'.

Trade in services

Under Cepa provisions, the Chinese mainland has opened up its market to Hong Kong-based service providers in 18 sectors.

Advertising, accountancy, audiovisual, banking, construction and real estate, convention and exhibition services, distribution services, freight forwarding, insurance, legal, logistics, management consultancy, medical and dental, securities, storage and warehouse services, telecommunications, tourism and transport.

Trade and investment facilitation

The main provisions relate to liberalising customs clearance, business regulations and the standardisation of e-commerce.

3 How does Cepa add to Hong Kong's position as Asia's business centre?

Cepa offers preferential access to China's markets, over and above commitments made by China under WTO. Cepa adds to the long list of reasons why international businesses choose Hong Kong as a base for their China and Asia operations.

Three broad groups stand to benefit:

- Companies already based in Hong Kong (of any nationality)
- Overseas companies interested in developing their China business strategy through Hong Kong
- Chinese mainland enterprises that wish to use Hong Kong services to streamline and expand their businesses overseas

Section 1

TRADE IN GOODS – HOW CEPA CAN HELP YOUR BUSINESS

4 What products are eligible for zero tariffs?

273 product categories have been selected to be tariff free from 1 January 2004. This covers 90 percent of Hong Kong products. The majority of remaining products will be tariff free by 2006, at the latest.

For a full list, see www.tid.gov.hk/english/cepa

5 Do you have to have an office in Hong Kong for your products to qualify as 'Made in Hong Kong'?

No. Cepa provisions that a company be based in Hong Kong for three to five years; be liable to pay tax; and employ 50 percent of its workforce locally, *only* applies to service companies.

For goods to qualify as 'Made in Hong Kong' they simply have to qualify under the Cepa 'Rules of Origin'.

6 Do your products have to be manufactured in Hong Kong to enjoy zero tariffs? What are the Rules of Origin (ROO)?

Products must be classified as 'Made in Hong Kong' under Cepa 'Rules of Origin' (ROOs). For goods to qualify as made in Hong Kong, they must have been substantially transformed in Hong Kong.

Currently 273 product codes are covered by Cepa.

- 187 of these will adopt Hong Kong's existing origin rules (these include textiles and clothing, jewellery, cosmetics, pharmaceutical products, and plastic and paper articles).
- 46 products (such as some chemical and metal products, some electronic products and electronic components) will adopt a 'Change in Tariff Heading' (CTH) approach. CTH is widely used by most WTO members.
- The remaining 40 products (electrical and optical components, watches and clocks) will adopt a 30% value added requirement. R&D and design will be counted under this value adding requirement.

7 Will you need a Certificate of Origin to benefit from zero tariffs?

Yes. Hong Kong's Trade and Industry Department has set up a new unit to administer certification. Companies do not have to wait until 1 January 2004 to seek certification. Please click on www.tid.gov.hk for details.

8 Do the zero tariffs apply to taxes levied by the Chinese government?

Cepa only covers import tariffs. VAT and other domestic taxes in China are not exempt.

9 Will Cepa help you to source products efficiently from the Chinese mainland?

Yes. Cepa opens up the Chinese mainland to more Hong Kong companies working in the trade support industries.

In particular, Cepa looks set to further integerate the economies of Hong Kong and the Pearl River Delta region of southern China.

The economy of the Pearl River Delta is dominated by manufacturing, while Hong Kong excels in trade services, such as sourcing, financing, logistics and transportation. The combination of these two regions (often called the *Greater* Pearl River Delta) offers a compelling and competitive way to do business.

10 If you want to sell products into China, how can Hong Kong and Cepa help?

Under Cepa, Hong Kong-based companies can set up wholly-owned distribution ventures to manage the full process of getting your products to retailers and consumers.

Working with a Hong Kong partner, you can find suitable markets, better understand local consumers and distribute to all regions on the mainland.

Please note that your products will still be subject to mainland Chinese import tariffs, *unless* they have Cepa certification.

11 What are the advantages of manufacturing in Hong Kong – and how can you satisfy the 'Rules of Origin'?

Cepa establishes Hong Kong as a competitive manufacturing location for *high-value goods*, especially those with strong design content, or valuable trademarks. Hong Kong's strict intellectual property legislation and strong service sectors support the manufacture and distribution of high value products.

Using Hong Kong's free port system, raw materials or semi-made products can be imported into Hong Kong tariff free. 'Boutique' factories in Hong Kong can manage the specialised stages of the design, manufacturing and IP protection of the product. Your products can then be exported tariff free to China (i) for further mass production (ii) for China-wide distribution, or (iii) exported to the rest of the world.

You can either invest in your own production lines, or license/outsource to Hong Kong factories to satisfy the Rules of Origin.

Section 2

TRADE IN SERVICES – HOW CEPA CAN HELP YOUR BUSINESS

12 If you have a services company, can you take advantage of Cepa provisions to enter the China market?

Cepa provisions cover 18 service areas. You must also qualify as a 'Hong Kong company'. To satisfy these criteria, your company must:

- Be incorporated in Hong Kong for three to five years (depending on the sector)
- Be liable to pay profits tax
- Employ at least 50% of staff in Hong Kong

Any company, regardless of nationality, which satisfies this criteria, can benefit from Cepa provisions.

13 How will Cepa make it easier for you to access the China market?

The exact provisions vary according to the sector. Please see page 9 for an overview, or click on www.tid.gov.hk/english/cepa for a sector-by-sector breakdown.

However, broadly speaking, Cepa helps in four key areas:

- *Earlier market entry* – Under WTO commitments China is gradually making it easier for overseas companies to set up. Cepa offers a one to five year head start to Hong Kong-based companies.
- *Setting up wholly-owned companies* – Currently overseas companies have to partner with Chinese companies. In many cases Cepa allows for the creation of wholly-owned companies.
- *Lower capital thresholds* – Capital requirements to set up in China have been reduced substantially opening up the field to smaller players.
- *Recognition of qualifications* – Many Hong Kong professional qualifications will be recognized in China, and access to sit China professional exams will be broadened.

14 If you would like to take advantage of Cepa provisions, but you do not have an office in Hong Kong, what should you do?

If you do not qualify as a 'Hong Kong company' under the criteria set out in Q12, you can partner with, invest in, or buy into, a Hong Kong-based company that already qualifies. You may then enjoy the advantages offered by Cepa.

15 How does Cepa differ from China's WTO commitments?

Cepa provisions offer two key benefits over and above WTO commitments:

- *Earlier implementation* – in most cases, Cepa advantages will be available to Hong Kong-made products and Hong Kong-based service providers one to five years ahead of WTO benefits.
- *Better benefits* – For 'Made in Hong Kong' products, Cepa provisions offer zero tariffs on 90 percent of goods from 1 January 2004, and will offer zero tariff on all goods by 2006, at the latest. Even under full WTO commitments, tariffs will remain between five and 30 percent.

  Cepa-eligible service companies (of any nationality), benefit from lower capital and asset requirements, no global quota restrictions and being able to set up wholly-owned ventures. WTO commitments have no timetable for wholly-owned ventures in areas such as logistics and exhibition services.

16 What is the difference between a Free Trade Agreement and Cepa?

Normally FTAs are signed between two countries. Because of the 'one country, two systems' between the Chinese mainland and Hong Kong, a different name has been used. In other ways, Cepa is comparable to a FTA.

"Made in Hong Kong" products covered by Cepa

• Electrical and electronic products • Metal products • Chemical products • Pharmaceutical products • Plastic articles • Paper articles • Textiles and clothing • Cosmetics • Clocks and watches • Jewellery

For more detail, check www.tid.gov.hk/english/cepa

Service sectors covered by Cepa

NB. Any company that satisfies Cepa-eligibility can benefit, regardless of nationality.

Accounting: One year permits for Hong Kong companies to conduct auditing services on the mainland. Hong Kong-qualified accountants who have practised on the mainland will be treated as Mainland accountants.

Advertising: Firms from Hong Kong can establish wholly-owned advertising companies on the mainland.

Audiovisual: Hong Kong-produced Chinese language movies will be exempt from the 20 overseas film quota and can be distributed on the mainland. Co-produced movies will be treated as mainland films.

Banking: Asset requirement for banks to establish mainland branches is reduced from US$20 bn to US$6bn.

Conventions: Hong Kong firms can set up wholly owned operations.

Construction and real estate: Hong Kong firms can set up wholly-owned operations.

Distribution (exc tobacco): Hong Kong firms providing distribution services, retailing or franchising can set up wholly-owned operations. Hong Kong car dealers can open up to 30 wholly-owned retail outlets.

Freight forwarding: Hong Kong firms can operate on a wholly-owned basis.

Insurance: Max limit of capital by a Hong Kong insurance firm in a mainland firm is 24.9 per cent. Hong Kong insurance agents can practice with mainland professional qualifications.

Legal: Hong Kong lawyers can work for mainland firms. Minimum requirements are waived for those operating in Shenzhen and Guangzhou and shortened to two months for other areas.

Logistics: Hong Kong companies can set up wholly-owned operations on the mainland.

Management/consultancy: Most companies can set up wholly-owned enterprises.

Medical and dental: Hong Kong doctors can work on the mainland for up to three years. Hong Kong medical workers can sit exams to work on the mainland.

Securities: Hong Kong Exchanges and Clearing can set up a representative office in Beijing.

Storage/warehousing: Hong Kong companies can operate wholly-owned operations.

Telecommunications: Hong Kong companies can set up JV enterprises on the mainland. No geographic restriction for JV enterprises formed by Hong Kong service suppliers and the mainland to provide value-added services.

Tourism: Hong Kong companies can run hotels/restaurants on a wholly-owned basis.

Transport: Hong Kong companies can operate on a wholly-owned basis.

For more detail, check www.tid.gov.hk/english/cepa

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