



CHINA (SHANGHAI) FREE TRADE ZONE

Preliminary report prepared by New Zealand Trade & Enterprise
and the New Zealand Consulate General (Shanghai)



Background

The establishment of the China (Shanghai) Pilot Free Trade Zone, more commonly known as the SFTZ, as the first free trade zone in China marks a milestone for China's economic reforms and the strategy of opening up the domestic market. SFTZ will pilot a new model that will not only open up the local economy, but also reform trade and investment administration systems.

SFTZ will promote the development of new business and trade options available to offshore companies, for example international trade settlement; international bulk commodities transactions; financial leasing; bonded delivery of futures; cross-border e-commerce; and a regional shipping hub.

Over the next three years the Chinese government will keep refining the policies and measures implemented in the SFTZ and, by the end of the third year, the model could be replicated and rolled out to the other parts of the country.

An overall Framework Plan was released by the Chinese Government in September containing some general measures, with more implementation details being released in the first quarter of 2014, and full implementation scheduled to be carried out later in the year.

Timelines

The SFTZ is the first zone of its kind in China. Given the trial nature of SFTZ and the implementation of an innovative management system, it was not possible to finalise all of the details before the Framework Plan was released. The government will take a "step by step" approach and release various policies over time, to ensure that all administrative mechanisms are constantly being refined while all the risks are well understood and managed.

Geographical Coverage



Geographically, SFTZ covers around 28 square kilometres, including four customs supervisory zones: the Shanghai Waigaoqiao Bonded Zone; Shanghai Waigaoqiao Bonded Logistics Park; Yangshan Bonded Port; and Shanghai Pudong Airport Comprehensive Bonded Zone.

The free trade zone is about 25km from Shanghai CBD and it takes 45-60 minutes to drive to the Waigaoqiao zone and Pudong Airport zone depending on the traffic, and 1.5 hours to drive to Yangshan.

Before the establishment of SFTZ, Shanghai had already opened a number of customs supervisory zones with some characteristics of a free trade zone. SFTZ is different because it is NOT about preferential policies offered to companies operating inside the zone, but about creating an innovative mechanism that will improve administrative processes, change the government's functionality (particularly in the administrative approval system), and ease the market entry of foreign investments. Although SFTZ is only 28 square kilometres, it will have significant influence on Shanghai's economy (as well as other parts of the country) through the comprehensive interaction of the companies inside and outside SFTZ.

The policies of SFTZ are approved by the State Council and the implementation is administrated and managed by the Shanghai Municipal Government.

Highlights of Key Policies Released

Foreign Investment Management

- **Pre-establishment of National Treatment**

A pre-establishment of National Treatment will be introduced for foreign investment in SFTZ on a pilot basis. It provides equal treatment for foreign investors during the stages of establishment, acquisition and expansion.

- **Change of Law**

Foreign investments into China, including office set-up, operational and financial obligations, are currently governed by the Foreign Investment Law, which in many ways has made it difficult for foreign companies to do business in China. Soon after the Administrative Measures of SFTZ were released, it was announced that the implementation of the Foreign Investment Law was to be suspended in SFTZ from 1 Oct 2013. SFTZ is governed by an Administrative Measure and five documents, including registration rules for the establishment of foreign firms, foreign-funded projects, and the management rules for investment and entry by foreign investors.

- **Negative List Management Mode**

SFTZ will implement a "Negative List" approach towards foreign investment management. Only those business areas covered under the Negative List are prohibited or restricted from foreign investment. Any business areas not covered under the Negative List need only go through record-filing procedures, with no permission or approval required. It is understood that an updated Negative List will be released in 2014 and annually thereafter. The list will be shortened over time as zone liberalisation gains steam and risks are better understood. The details of the Negative List is attached as Appendix 1.

- **Business Licence**

A new simplified registration and processing system have been applied, which will help corporations get business licences within a week – down from 29 days. Companies in SFTZ may commence production and operation after obtaining the business license. Companies engaged in businesses which require administrative approval may file an application with the relevant authorities after obtaining the business license.

The timeframe for setting up a foreign entity will be significantly shortened, from four to five months to a few weeks.

- **Registration Capital**

There is no minimum cap on registration capital required (except for some industries such as banks, insurance, etc), and it will be up to the stakeholders of the company to decide on the amount of registration capital and the timeframe to inject the capital. Foreign companies are not required to seek approval for repatriating profit to an overseas' head office. Filing is only required once tax obligations are fulfilled and audits completed. Annual examination of financial accounts will also be replaced by annual filing.

- **Office Set-up**

You can set up a legal entity with a physical office in SFTZ and a branch office outside of SFTZ. Certain funds can be transferred between the two offices through dedicated accounts in a managed way. The details on how to do this are still being worked on.

One option is to set up a virtual office in SFTZ as the legal entity with an annual cost of RMB20,000, however this could change over the time, so it is suggested that companies consult with the local authority or business advisors in China before they set up a virtual office.

As of November 22, a total of 1,434 companies have registered in SFTZ. Of this, 38 are foreign-funded with an average registered capital of US\$15 million, and 1,396 are domestically funded with an average registered capital of RMB25 million (about US\$4.07 million).

Finance and Foreign Exchange Administration

People's Bank of China issued a guideline on 2 Dec 2013 regarding supporting the SFTZ in the financial sector with the aim of promoting RMB convertibility under the capital account and expanding cross-border usage of the currency. The guideline included 30 detailed instructions. For more details, please [click here](#) for the information on SFTZ's website, or [click here](#) for the English version on Deloitte's website.

Four Main Aspects Covered by the Guidelines:

1. Exploring ways to facilitate investment and financing remittance, and promoting the convertibility of capital account;
2. Promoting the cross-border use of RMB to allow enterprises and individuals in the Shanghai FTZ to use RMB to carry out cross-border trade in a more flexible way;
3. Pushing forward the market-oriented reform of interest rate; and
4. Deepening foreign exchange reform and further streamlining administrative examination and approval, so as to gradually establish a suitable foreign exchange control system.

Highlights of the Guidelines:

- Allowing residents of the Shanghai FTZ to set up "resident free trade accounts" in both domestic and foreign currencies, and allowing RMB to be fully convertible under those accounts "when conditions are ripe";
- Allowing non-residents of the Shanghai FTZ to open the "free-trade accounts for non-residents" and to enjoy financial services according to the pre-establishment national treatment principles;
- Allowing foreign banks and other enterprises registered in the Shanghai FTZ to invest in Shanghai's securities market;
- Allowing foreign companies with subsidiaries in the Shanghai FTZ to issue RMB-denominated bonds;
- Allowing qualified individual investors to conduct various foreign investment, including trading overseas securities;
- Allowing enterprises in the Shanghai FTZ to borrow RMB funds from overseas lenders;

- Allowing enterprises in the Shanghai FTZ to directly invest overseas without going through pre-approval procedures;
- Allowing financial institutions in Shanghai to provide RMB clearing services to cross-border e-commerce business;
- Allowing financial institutions in Shanghai to handle the cross-border RMB transactions related to current account and FDI transactions;
- Allowing certain qualified institutions to issue negotiable certificates of deposit; and
- Removing the interest rate ceiling on small amount of foreign currency deposits at an appropriate time.

(Source: [China Briefing, 5th Dec, China Issues Financial Reform Guidelines to Boost Shanghai Free Trade Zone](#))

Relaxed Customs Supervision

Once goods arrive in the SFTZ Customs territories, they can be transferred to a bonded warehouse before completing Customs formalities. Goods can be cleared in batches when needed rather than the whole shipment having to be cleared at one time.

The zone will implement a “one declaration, one inspection and one approval” mode. This means that for the majority of products, Customs and local CIQ inspection (if applicable) will be conducted at one time, and at the same time as approval. Companies can decide when to apply for inspection. This is another way of fast tracking the clearing process. However, it is still not clear exactly what type of products CIQ will require a separate inspection on. This will be clarified by local CIQ soon.

Further Opening up Investment Industries

Six service sectors: financial services; shipping services; professional services; commercial and trading services; cultural services; and social services are further opened up to foreign investment. Measures include: suspending or cancelling qualification requirements for investors; cancelling restrictions on shareholding ratios; cancelling restrictions on business scope; etc. See Appendix 2 for a summary.

Support of Outbound Investment

Over the last few years any significant outbound investment was primarily made by large SOEs, while private firms were constrained by various regulations and administrative approvals. One of the major problems has been to get approval from the relevant authorities and remit the money offshore. SFTZ should remove these barriers and make it possible and easier for private firms to make outbound investments.

Insurance

SFTZ will be used as an offshore insurance market test zone, which will mainly develop the areas of shipping insurance; high-end health insurance; liability insurance; and credit insurance, and will also explore the construction of an insurance market (exchange).

For more details, please refer to [China Briefing's Plan for the Future Development of the Shanghai Free trade zone](#).

Tax

No major tax incentives have been released other than a few installment plans for income taxes. Companies in SFTZ will still enjoy existing preferential tax policies given by the four bonded areas. It is understood that a supporting tax regime is being discussed. Given that all trial results at SFTZ have been tasked as being “replicable”, there is little room for further tax cuts.

E-commerce

In order to meet the demands of domestic customers for mid- to high-end products such as luxury handbags, milk powder, branded cosmetics, and the wish to clean up the untidy cross-border e-commerce market, China's National Development and Reform Commission (NDRC) has delegated the General Administration of Customs (GAC) to pilot a cross border e-commerce service in five cities including Shanghai. (Source: *Shanghai FTZ Launches Cross-Border E-Commerce Platform* Posted on October 11, 2013 by China Briefing)

SFTZ launched a pilot cross-border e-commerce platform – buyeasi.com – in November, constructed by Orient Electronic Payment Co, a Shanghai-based company that owns the Easipay electronic payment platform. Shanghai Customs will be in charge of the Customs declaration system connected to the website and vendors listed on the platform (either foreign suppliers or their local agents) must file records with the Customs authorities. Both product price and duty amount will be listed under each product.

Once an order is confirmed online, the supplier's information will be displayed and any after-sales issues will be handled directly by suppliers. Buyeasi.com prefers to deal with foreign suppliers who have local agents in China. All products listed require Chinese labels, particularly food products, which will be inspected by the local CIQ.

The products offered on Buyeasi.com are imported through bonded warehouses, which will significantly decrease logistic costs, so the price could be much lower (30% to 40%) than the price of the same products selling in other parts of the country.

Again because the platform has just been launched on a trial basis, many areas remain to be clarified eg will products be sent through the postal service as personal items; and how will CIQ carry out inspection on those products?

For more information on trading through Buyeasi contact:

Customer service hotline: +86 400 921 8899

Email: kuajingtong@easipay.net

Wine Trade Exhibition Centre

A Wine Trade Exhibition Centre has been set up in SFTZ where customers can buy wine at near wholesale prices, although they are subject to normal Chinese duty and taxes, currently set at 48% if taken outside SFTZ. Wine will be freely traded within the zone, but purchases are not subject to tax until removal from the bonded warehouse.

Significance of SFTZ to Shanghai and other regions

Shanghai's role in trade, finance, investment and shipping, together with an increasingly open service sector, improved regulatory environment, and focus on institutional innovation will eventually lead to domestic market reform and drive China's integration into new trade agreements.

Opportunities of SFTZ for New Zealand Firms

In the absence of detailed implementation rules in many key areas, it is difficult to draw early conclusions on the significance of SFTZ to New Zealand firms. We can make some observations:

- For those companies engaged in the goods trade and seeking to set up a physical presence in Shanghai, they may consider setting up a Wholly Foreign Owned Enterprise in SFTZ to take the advantage of a basket of relaxed policies offered by the zone, such as the low cost of company set up; ease of repatriating profits back to head office offshore; fast track of customs/CIQ procedures;

improved logistic arrangement; and liberalised RMB conversion and settlement.

- For those engaged in the services trade, such as professional training, healthcare services, etc, they may wish to set up a virtual office in SFTZ while having the actual operation outside the zone. This will allow companies to enjoy the preferential policies given by SFTZ and at the same time extending services outside SFTZ.
- On the investment side, with relaxed control on the transfer of funds offshore, more Chinese firms, in particular Chinese private firms, will be able to invest their capital overseas, including New Zealand.
- The SFTZ also provides good opportunities for New Zealand companies who are seeking project financing from investors in China, as the zone offers more lax legislations regarding investments which Chinese private investment firms and venture capitalists can take advantage of.

The Next Step

New Zealand Trade & Enterprise will closely monitor the development of detailed implementation rules and provide an updated report in February or March when more details on the rules on tax, finance, foreign exchange, outbound investment, border-crossing inspections and e-commerce trading are released.

Contact Numbers for Official Departments in SFTZ:

General enquiries:

+86 21 5869 6822

Industrial and Commerce Bureau (for office set up)

+86 21 5869 8202

Customs

+86 21 5869 7065, +86 21 5869 7028

Foreign Exchange

+86 21 5869 7858

Other sources of reference materials used in the report:

- [Administrative Measures Released for Shanghai Free Trade Zone Asia Briefing by Dezan Shira, 16th Oct 2013](#)
- [Shanghai FTZ Launches Cross-Border E-Commerce Platform Posted on October 11, 2013 by China Briefing Dezan Shira](#)
- [Shanghai Pilot Free Trade Zone - China's new wave of economic, 8 Oct 2013, International Tax Alert, E&Y](#)
- [China Issues Financial Reform Guidelines to Boost Shanghai Free Trade Zone by China Briefing 5th Dec 2013-](#)
- [Deloitte's SFTZ webpage](#)

Appendix 1

Other key plans and measures issued:

Framework Plan for the China (Shanghai) Pilot Free Trade Zone
<http://en.SFTZ.gov.cn/FrameworkPlan.html>

Special Administrative Measures (Negative List) on Foreign Investment
<http://en.SFTZ.gov.cn/Special.html>

Administrative Measures for the China (Shanghai) Pilot Free Trade Zone
<http://en.SFTZ.gov.cn/Administrative%20Measures.html>

Filing Administrative Measures for Outbound Investment in Setting up Enterprises
<http://en.SFTZ.gov.cn/Investment.html>

Filing Administrative Measures for Outbound Investment Projects
<http://en.SFTZ.gov.cn/Enterprises.html>

Polices and Measures on Capital Market for Supporting and Promoting SFTZ
<http://en.SFTZ.gov.cn/Polices.html>

Circular of China Banking Regulatory Commission on Issues Concerning Banking Supervision in SFTZ
<http://en.SFTZ.gov.cn/Circular.html>

Appendix 2

Areas of Further Opening Up of Investment Industries

The Plan highlights further opening up of investment industries that cover six sectors including finance, shipping, commercial, professional, as well as cultural and social services.

- Financial services
 - Banking services – allow qualifying foreign financial institutions to set up foreign banks; allow qualified private capitals and foreign financial institutions to establish joint venture banks; allow qualified domestic banks to engage in offshore business.
 - Health and medical insurance – allow foreign investment of health and medical insurance institutions on a pilot basis.
 - Finance lease – Cancel the minimum threshold requirement of registration capital and expanding business scope.
- Shipping services
 - Ocean Shipping – Relax the restriction of the equity ratio between foreign funds and domestic funds for joint venture international marine business.
 - International ship management – to allow for Wholly Foreign Owned Enterprises (WFOE).
- Commercial services
 - Valued-added telecommunications – allow foreign investment enterprises to engage in certain value-added telecommunication services.
- Professional services
 - Law firms – new way of cooperation between foreign and domestic law firms
 - Credit investigation – Allow foreign investment
 - Travel agency – Expand the business scope of the Sino-Foreign Equity JV travel agency

Hunter service – Increase the limitation of foreign equity to 70%; allow it to be wholly owned by HK and Macau equity; reduce the minimum requirement of registered capital.

Investment management – Allow establishment of foreign invested holding companies limited by shares

Engineering design – relax application criteria.

- Cultural services
 - Artists' agency – Cancel restrictions on the equity ratio between foreign funds and domestic funds; allow WFOE to engage
 - Entertainment – Allow WFOE to engage
- Social services
 - Education and training, employment skills training – allow JV to engage
 - Medical services – allow WFOE medical institutions

(Source: E&Y Issue No 2013005 – A milestone for China's new wave of economic reform – Shanghai Pilot Free Trade Zone)

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