

PHASE III OF CEPA

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An agreement for the third phase of CEPA (so-called CEPA III) was signed between the Central People's Government and the Government of the Hong Kong Special Administrative Region on 18 October 2005 concerning the further liberalization measures for CEPA. Effective from 1 January 2006, CEPA III provides duty-free access for all Hong Kong-origin products and grants liberalisation measures in 10 service areas on top of the provisions granted in earlier phases.



The Financial Secretary of Hong Kong, Mr. Henry Tang and the Vice Minister of Commerce of the Mainland China, Mr. Liao Xiaoqi, shake hands after the signing ceremony.

Trade in Goods

Under phases I and II of CEPA, the Mainland agreed to apply zero tariff to 1,087 Hong Kong products (374 from CEPA I and 713 from CEPA II) of local manufacturers if they can meet with the CEPA rules of origin ("ROO"). CEPA III further stipulates that all products of Hong Kong origin, except for prohibited articles and articles that are subject to special requirements, will become tariff free with effect from 1 January 2006.

In determining the ROO, Hong Kong and the Mainland have already reached agreement on the rules for 1,369 products. For those products that have no agreed ROO, Hong Kong will initiate discussions with the Mainland within six months upon application by manufacturers.

It is welcomed that the Mainland has agreed to relax the ROO of watches by waiving the 30% value adding requirement for watches of Hong Kong brand names, which may include brands originating from Hong Kong or foreign brands wholly acquired by registered companies in Hong Kong. Accordingly CEPA qualified watches will only need to undergo design, assembly, testing and quality control in Hong Kong.

Details of the tariff codes, product descriptions, origins criteria and procedures for claiming zero tariff can be downloaded from Annex I of the Supplement II to CEPA posted at the website of Trade & Industry Department ("TID") <http://www.tid.gov.hk/english/cepa/legaltext/cepa3.html>.

Trade in Services

On top of the liberalization measures covered in phases I and II of CEPA, there are 23 additional liberalization measures in CEPA III to further relax the market access conditions for qualified Hong Kong service suppliers in 10 service sectors. Broadly speaking, these liberalization measures permit earlier access for Hong Kong service suppliers to the Mainland market, ahead of China's committed timetable to World Trade Organization ("WTO"). Full details of these measures can be found on Annex II of the Supplement II to CEPA.

Some of the major trade and investment facilitation measures to qualified service suppliers are summarized as follows:

Sector	Access for Hong Kong under CEPA III
1. Legal	<ul style="list-style-type: none"> • A Hong Kong law firm having a representative office in the Mainland is permitted to operate in association with one Mainland law firm in different cities of the same province.
2. Accounting	<ul style="list-style-type: none"> • The validity of Temporary Business Permit is extended to 2 years.
3. Construction	<ul style="list-style-type: none"> • The qualification requirements of construction and engineering design enterprises and urban planning service enterprises set up by Hong Kong service suppliers are relaxed. • Hong Kong construction professional service firms can operate wholly owned foreign enterprises (“WOFE”) in the Mainland. • The application procedures for setting up a construction and engineering design WOFE are simplified.
4. Audiovisual	<ul style="list-style-type: none"> • Hong Kong companies can establish WOFE, each of which may construct or renovate more than one cinema theatre at more than one location for the operation of film screening business. • Cantonese version of films co-produced by Hong Kong and the Mainland can be distributed and screened in Guangdong Province upon approval. • Hong Kong-produced Chinese language films are free from the annual import quota.
5. Tourism	<ul style="list-style-type: none"> • Hong Kong tourist companies can now set up WOFE in the Mainland (i.e. 2 years ahead of competitors from other nations). • The entry requirements for Hong Kong travel agencies in the Mainland are lowered.
6. Banking	<ul style="list-style-type: none"> • The level of operating funds required of Mainland branches of a Hong Kong bank for offering Renminbi and foreign currency businesses to local customers will be assessed on the basis of all Mainland branches of the bank concerned, rather than each branch individually.
7. Securities	<ul style="list-style-type: none"> • Qualified Mainland securities companies belonging to the pilot innovation type can set up subsidiaries in Hong Kong in accordance with the relevant requirements. • Qualified Mainland futures companies are allowed to operate futures business in Hong Kong, including the setting up of subsidiaries.
8. Distribution	<ul style="list-style-type: none"> • Hong Kong companies can operate commission agent services in respect of chemical fertilizers, processed oil and crude oil, and wholesale and retail services in respect of chemical fertilizers. • Hong Kong service supplier, which opens more than 30 stores accumulatively in the Mainland, can be the controlling shareholder, with the proportion of capital contribution not exceeding 51% (except for processed oil).
9. Transport	<ul style="list-style-type: none"> • Hong Kong service suppliers are allowed to set up WOFE to provide tug services between Hong Kong and Mainland ports, ship maintenance and repair services, international ocean container leasing, buying and selling as well as trading of container parts, and ship survey services for ships registered in Hong Kong. • Hong Kong companies can form joint ventures to provide air transport sales agency services. • The registered capital for setting up air transport sales agency will be the same as that for the Mainland enterprises.
10. Individually Owned Stores	<ul style="list-style-type: none"> • The scope of business allowed to Hong Kong permanent residents' individually owned stores is expanded to cover the following: <ul style="list-style-type: none"> – import and export of goods and technologies – photography and photographic processing services – washing, cleaning and dyeing services – repair and maintenance of motor vehicles and motorcycles

Conclusion

The elimination of import tariff and relaxation in the application of origin for watches will help to attract more investment and production targeting goods with higher-value added contents to Hong Kong. Although the origin of certain products are not yet clearly defined, the bi-yearly discussions between Hong Kong and the Mainland will provide further flexibility to potential investors planning to manufacture products that are not currently produced in Hong Kong.

For qualified service suppliers, CEPA offers earlier access to the Mainland ahead of China's WTO timetable. For instance, CEPA III offers concessions to audiovisual, transport and distribution industries of Hong Kong service suppliers that go beyond the WTO commitments. Meanwhile, the Mainland's initiative to allow its securities and futures firms to set up subsidiaries in Hong Kong will help broaden the intermediary base of Hong Kong, strengthening Hong Kong's role as an international financial centre.

Regarding individually owned stores, the further liberalization measures will expand the scope and flexibility of Hong Kong residents doing business in the Mainland and hence further stimulating the entrepreneurship of Hong Kong residents.

As our Financial Secretary Mr. Henry Tang said, these additional measures in CEPA III would offer new business opportunities to Hong Kong enterprises and professionals in the Mainland. We also believe that these measures will effectively help to sustain Hong Kong's broad-based economic recovery and enhance Hong Kong's attractiveness to overseas investors. We believe our clients can make use of the opportunity being offered by CEPA to successfully expand their businesses in China. **PKF**