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CHINA TAX ALERT

ISSUE 20 | September 2013

State Council approves the establishment of China (Shanghai) Pilot Free Trade Zone

In the context of the overall drive towards global economic integration, the recent fall in market demand from overseas trade partners and the resultant increase in trade protectionism have posed a severe challenge to China's economic development. Furthermore, growth in domestic demand has been slow due to the reform bottleneck. As a result, a plan to establish China (Shanghai) Pilot Free Trade Zone and expand the scope of China's opening-up has been added to the national agenda in order to alleviate the difficulties faced by relevant industries and to infuse new energy into the economy by curbing the power of bureaucrats.

The establishment of the China (Shanghai) Pilot Free Trade Zone will initiate the launch of a restructured Chinese economy, prepare the ground for a new round of nationwide reforms, and reconstruct global rules for trade and investment, all of which will herald the arrival of a new epoch in China. We suggest that companies pay close attention to the publication of relevant policies and take full advantage of the enhanced economic structure, regardless of whether they have established a presence within the free trade zone.

Background

On 3 July 2013, the State Council passed the *Overall Plan for China (Shanghai) Pilot Free Trade Zone.* In August 2013, the establishment of the zone was formally approved.

China (Shanghai) Pilot Free Trade Zone will cover a total area of 28.78km^2 and will include Shanghai Waigaoqiao Free Trade Zone, Waigaoqiao Bonded Logistics Park, Yangshan Bonded Port and Shanghai Pudong Airport Comprehensive Bonded Zone.

Highlights

The main innovations put forward by the *Overall Plan for China (Shanghai) Pilot Free Trade Zone* include the following:

- deeper reforms
- accelerated transformation of government functions
- enhanced innovation in the investment management model

- further opening up of service industries
- accelerated transformation of the trade development model
- greater opening up and innovation in the field of finance
- establishment of an institutional environment adapted to the pilot zone.

The plan is expected to be implemented in the finance, trade and shipping fields, and will involve innovations in administration, taxation and legislation, including the convertibility of the RMB capital account, the construction of an offshore financial centre, the introduction of tax preferences, and new models of trade supervision.

Furthermore, in order to propel the establishment of China (Shanghai) Pilot Free Trade Zone, speed up the transformation of government functions, scrutinise the management of the foreign investment negative list and update the 'opening-up' model, the Standing Committee of the National People's Congress has approved a number of adjustments in the enforcement of certain legal administrative approvals and items within the pilot zone.

KPMG's observations

The establishment of China (Shanghai) Pilot Free Trade Zone will lead the way for innovation in China's trade supervision model. In the free trade zone, supervision of the state border will focus mainly on passengers, while goods will be subject to centralised, categorised and electronic supervision and will be able to flow efficiently and swiftly within the zone. These reforms will effectively enhance the development of modern service industries in the free trade zone, such as trade and shipping, leading to the formation of an attractive and competitive international logistics centre.

The impact of the establishment of the pilot free trade zone on the financial field will be no less significant than that on trade. The pilot content of the zone will gradually extend to free exchange of the RMB and the liberalisation of interest rates, which will promote the capital turnover of enterprises located in the free trade zone and bring about the formation of a new northeast Asian, or even Asia-Pacific level, offshore financial centre.

The *Overall Plan for China (Shanghai) Pilot Free Trade Zone* will be officially released once legal procedures are completed. We hope you will carefully consult our in-depth study of the plan once the finalised version is publicly available.

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