Asia Market Intelligence

Mainland China

Presence

HSBC Bank (China) Company Limited started operations in Shanghai in April 2007 as a wholly-foreign owned bank, solely owned by The Hongkong and Shanghai Banking Corporation Limited. As HSBC China, the Bank incorporates the previous mainland China offices of The Hongkong and Shanghai Banking Corporation Limited.

The Hongkong and Shanghai Banking Corporation Limited has been present in mainland China for 144 years. It is one of the largest investors among foreign banks in mainland China, having invested over USD5 billion in select mainland financial services entities and in the growth of its own operations. These include a 19.0% stake in Bank of Communications, a 16.8% stake in Ping An Insurance, and an 8.0% stake in Bank of Shanghai. There is also a branch in Shanghai, which conducts a foreign currency wholesale banking business.

HSBC China has one of the largest service networks among foreign banks in mainland China. Our current network comprises 82 outlets, including 19 branches in Beijing, Changsha, Chengdu, Chongqing, Dalian, Dongguan, Guangzhou, Hangzhou, Ningbo, Qingdao, Shanghai, Shenyang, Shenzhen, Suzhou, Tianjin, Wuhan, Xiamen, Xi'an and Zhengzhou and 63 sub-branches in Beijing, Chengdu, Chongqing, Dalian, Guangzhou, Hangzhou, Qingdao, Shenzhen, Shanghai, Shenyang, Suzhou, Tianjin, Wuhan, Ximan and Xi'an. As a locally incorporated bank, HSBC China provides foreign currency and renminbi (RMB) services to local enterprises, foreign invested enterprises and other individual customers. With the full opening of the China market, HSBC China will further expand its network and service range to provide a comprehensive range of banking services and products to our customers.

Population:
1.33 billion

Total Area:
9.60 million sq km

Currency:
Renminbi (RMB)

Capital:
Beijing

Gross Domestic Product:
6,991.0bn total (2007 est.); 11.4% real growth rate (2007 est.); 5,292 per capita (2007 est.)

Major Language(s):
Putonghua (Mandarin)

Time zone:
GMT +8 hrs

Central Bank:
The People's Bank of China

Inflation rate (consumer prices):
4.8% (2007 est.)

HSBC

The world's local bank

Clearing Systems and Payment Instruments

- The China National Advanced Payment System (CNAPS) comprises a high-value payment system (HVPS) and bulk electronic payment system (BEPS):
  - HVPS: This is a real-time gross settlement system that has covered all cities in China since June 2005. Payments made via HVPS between banks with direct membership can take a few seconds or minutes, regardless of their geographic locations. CNAPS HVPS has become the most popular collection channel for cross-city settlements. CNAPS allows up to 60 Chinese characters of information to be carried with the payment.
  - BEPS: This is a low-value clearing system (similar to an automated clearing house or general interbank recurring order) that has been implemented throughout China. It uses the CNAPS architecture and caters to ordinary credit and debit transactions as well as bulk payments and collection processing, such as monthly salary payments or utility charge collections. As with HVPS, BEPS caters to both in-city and cross-city transactions. In some cities, such as Shenzhen, where BEPS has been implemented, it has replaced local in-city paper clearing for transactions less than RMB 20,000.

Time period	Paper-based clearing	Instrument	Clearing channels	Availability of funds
Prior to June 2005	In-city payments	Cash	Bilateral	Immediate
		Cashier's orders	Local in-city clearing house	Immediate
		Company cheques	Local in-city clearing house	24-48 hours
		Funds transfers via paper-based vouchers	Local in-city clearing house	24 hours
	Cross-city payments	Bank drafts	Local bank in-house clearing network plus local in-city clearing house	24 hours
		Commercial/bank-accepted drafts	Correspondent banks	Anywhere from five to 35 days
		Funds transfers via local banks	Local banks in-house clearing network	24-48 hours
		Funds transfers via CNAPS (HVPS) [1]	Limited nationwide CNAPS coverage	Real-time
June 2005 to date	In-city/Cross-city payments	Funds transfers via CNAPS (HVPS)	Nationwide CNAPS architecture	Real-time
		Funds transfers via CNAPS (BEPS)[2]	Nationwide CNAPS architecture	Batch processing/Same-day credit

1. Dependent on bank membership and connectivity to CNAPS architecture. Sending and receiving banks with direct membership in and connectivity to CNAPS will be able to process and receive inward collections in a real-time and straight-through process.
2. For transactions of less than RMB20,000.

- Before June 2005, it was difficult for companies to collect funds efficiently because of the existing clearing systems and payment instruments. Although CNAPS had been nominated by the central bank as the new nationwide clearing system, the system was still in its infancy, so companies were not able to use it on a nationwide basis to speed up collections. By June 2005, CNAPS (high-value payment system) was finally established throughout China – a milestone enabling companies to realise the efficiency of a nationwide clearing mechanism that can cater to in-city and cross-city payments. The nationwide implementation of CNAPS (bulk electronic payment system) in 2006 resulted in even greater use of CNAPS for payments, compared with traditional methods of paper-based clearing. CNAPS enables companies to ensure that receipts in bank accounts are processed quickly and efficiently. While paper-based clearing instruments are still in use, increased usage of CNAPS is expected.

- In China, there are numerous instruments that can be used for in-city and cross-city payments, as well as underlying clearing mechanisms that will determine how quickly and efficiently funds will be credited to recipients' bank accounts.

Banking System and Bank Accounts

- The People's Bank of China (PBOC) is the central bank of China. Its main aim is to formulate and implement monetary policy and to safeguard financial stability. The PBOC also regulates the interbank lending and bond markets.
- The banking sector is dominated by the "Big Four" state-owned banks: Industrial and Commercial Bank of China, China Construction Bank, Bank of China and Agricultural Bank of China. By the end of the five-year transitional period since China's entry to the World Trade Organization, many of the barriers to foreign bank operations in China have been removed. Foreign global banks that have made significant direct investments in China include HSBC, Citigroup, Standard Chartered Bank and Deutsche Bank.
- A resident company is allowed to open one basic RMB account and general RMB accounts. General accounts cannot be used for cash withdrawal.
- The following types of bank account are currently available:

Account type	Local basic[1]	Local general	Foreign
Resident	Yes	Yes	Yes[2]
Non-resident	No	No	Yes

1. Cash can only be withdrawn from the basic account; salary payments can only be effected from the basic account; only one basic account can be opened by each company, irrespective of how many banks are used. Multiple general accounts can be opened.
2. There are various regulatory requirements applicable to the opening and operation of foreign currency (FCY) accounts. Different types of FCY accounts are opened for different purposes, and the operation of these accounts is subject to regulatory restrictions in relation to these specific purposes.

- All account types in China earn interest. Details of RMB and FCY accounts are as follows:
  - RMB deposits: The upper limits of interest rates on these two account types are set and controlled by the central bank.
  - Resident FCY accounts in US dollar, yen, euro or Hong Kong dollar: If the deposit amount is below USD3m equivalent and the term deposit tenor is less than one year (inclusive), the upper limits of deposits interest rates are regulated by the central bank. Otherwise, favourable interest rates may be negotiated between the customer and the bank. For non-resident FCY accounts, the interest rates applied are not regulated by the central bank.

Foreign account types	Inflows	Outflows	Comments
Capital account	To receive capital injections and capital increases	Payments for current items and approved capital items	In principal, only one account can be opened with a bank located in the same region as the company
Settlement account	Collections for FCY current items (i.e. trade- and service-related items)	Current items and items approved by SAFE	–
Foreign debt special account	To receive loan proceeds from overseas	As specified in the loan agreement, but cannot be used to repay RMB loans	Foreign debt registration and State Administration for Foreign Exchange (SAFE) approval for account opening required
Foreign debt special loan repayment account	Transferred from other FCY accounts, or exchanged from RMB	Repayment of the FCY loan principal and interest	Not necessary, as foreign debt can be repaid through a foreign debt special account
FCY loan account (including loan account and repayment account)	To receive the loan proceeds from onshore FCY loans by banks or through entrusted loans	To repay the principal and interest of onshore FCY loans from banks or though entrusted loans	Exchange to RMB not allowed with a few exceptions
Foreign investment special account (applicable to foreign companies)	To temporarily receive funds related to direct China investment	Payment of expenses associated with direct investment in China. SAFE's approval is required for each payment and conversion	One account only. SAFE's approval is required for account opening

Cash management products and services at a glance*

INVESTMENT PRODUCT	TRANSACTION MANAGEMENT		LIQUIDITY MANAGEMENT
	PAYMENTS	COLLECTIONS	
Due to local regulation limitations, a few investment alternatives can be offered: • Local currency contract saving • Local currency/foreign currency call deposits • Local currency/foreign currency time deposits • Other treasury products, such as structured deposits	Payment solutions deliver a full suite of accounts payable management services that meet customers' domestic and international payment needs. Our solution includes: • In-city/cross-city local currency payments via local clearing house, CNAPS and alliance banks • Domestic/cross-border foreign currency payments via local clearing house, alliance banks and overseas currency clearing centre • Automated beneficiary advising via email/fax/SMS • Company cheque outsourcing. • Electronic payroll solution	Receivables solutions that help customers shorten their receivables collection cycles (Day Sales Outstanding — DSO), and provide information for reconciliation. This solution set also allows customers to outsource their accounts receivable reconciliation and management to the bank. Customer can enjoy: • In-city/cross-city local currency collection via local clearing house, CNAPS and alliance banks • Domestic/cross-border foreign currency collection via local clearing house, alliance banks and overseas currency clearing centre • HSBC*net* Receivables Management System (RMS) • Virtual Account (VA)	Local currency cash concentration under the entrusted loan framework is available in China, which allows customers to optimise the efficiency of their idle cash balances among group entities. Due to current foreign exchange regulations and other business restrictions, corporates have few liquidity management options in China; nevertheless, HSBC has developed some innovative solutions on a case-by-case basis. We offer: • Bilateral entrusted loans • Group entrusted loans Group liquidity solutions (so-called cash concentration)

* Cash management services are delivered via HSBC*net*, HSBC's global Internet banking platform, and HSBC Connect, HSBC's host-to-host electronic banking system.

Alliance Network

Alliance banks and the scope of their cooperation with HSBC China are as follows:

Industrial and Commercial Bank of China (ICBC)

- Broadest geographic network in China with 16,997 domestic institutions
- Host-to-host connection supporting nationwide 3rd party bank reporting and payments
- Supports various cash services and RMB agent clearing

Bank of China (BOC)

- 11,300 domestic operations across China
- RMB cross-city clearing and cash collection services

China Construction Bank (CCB)

- 14,250 branches and sub-branches in China
- HSBC branches with CCB terminals rely on CCB for a portion of their payment processing

Agricultural Bank of China (ABC)

- The largest branch network in the country with 31,000 outlets
- A key partner in cash deposit over-the-counter service since May 2007
- Host-to-host connection supporting payment instruction delivery and intra-day account information transmission

Bank of Communications (BoCom)

- More than 2,600 outlets in 148 cities across mainland China
- Third party bank reporting and payment cooperation began in 2003. Host-to-host connectivity will be launched in the first half of 2009.
- Cash over-the-counter deposit agreement for both in-city and cross-city service

Bank of Shanghai (BOS)

- 208 branches and offices in Shanghai with equity investment from HSBC
- A major currency/small money supplier for the Shanghai market

Legal, Company and Regulatory

- The China Banking Regulatory Commission (CBRC) formulates supervisory rules and regulations governing the banking institutions, while the State Administration of Foreign Exchange (SAFE) is the government bureau in charge of China's balance of payments and foreign exchange positions.
- Establishing a foreign-invested enterprise (FIE) requires interacting with three key government departments: the National Development and Reform Commission (NDRC), the State Administration of Industry and Commerce (SAIC) and the Ministry of Commerce (MOFCOM). First, a Project Approval Report must be submitted to the NDRC, which outlines fundamental business operations such as scale of operations, products and technology as well as target markets and planned workforce. Next, MOFCOM will issue formal approval for the FIE; specific requirements will depend on the type of FIE established – common types include a wholly owned foreign enterprise or a joint venture. At the MOFCOM stage, it is critical to clearly define the correct business scope as it is burdensome to modify the business scope thereafter and firms cannot engage in revenue-generating activities outside their specified scope. Finally, the business licence will be issued by SAIC, thereby formally establishing the FIE. The actual commencement of operations, however, may depend on specific conditions such as the payment of registered capital or receiving industry specific permits.

- Increasing debt while decreasing equity capital in order to maximise tax deductions (thin capitalisation) is subject to restriction in China. According to Article 46 of the Corporate Income Tax Law of China, once the ratio of debt financing from related parties to equity financing exceeds the prescribed limit, any interest expenses incurred above the limit are not deductible.

Liquidity, Currency and Tax

- The RMB is not currently an internationally traded currency, but as market reforms continue apace in China, regulations governing foreign exchange are evolving. The practice of planning and managing working capital through RMB cash concentration techniques has been widely accepted. However, designing and constructing a feasible FCY cash concentration solution within the boundaries of current regulations remains a significant challenge, but is definitely possible.
- Local currency cash concentration is normally based on an entrusted loan framework for multiple entity structures. For local currency cash concentration, there is no requirement for the corporation to obtain the approval from the regulators as long as the facilitating bank has filed this product with regulators beforehand. However, for FCY cash concentration, case-by-case special approval should be obtained before implementation.
- SAFE is responsible for regulating both domestic and FCY cash concentration as well as cross-border cash concentration between China and another country. SAFE has multiple branch and sub-branch offices around China that will mostly act as the day-to-day contacts for banks. However, for FCY cash concentration, special approval from SAFE headquarters in Beijing should be obtained, irrespective of whether it is a regional or country-wide structure. In addition, for a FCY cash concentration, monthly and annual regulatory reports should be submitted to SAFE for review.
- Critical corporate tax rates include:

Tax	Comments
Corporate income tax	Generally 25% (SMEs 20%, high-tech firms 15%)
Value-added tax	Generally 13% or 17%, but small-scale taxpayers are charged 4% or 6%
Business tax	Varies by industry. Common rates include 3% (construction), 5% (banking) to 20% (entertainment)

- Key cash concentration tax considerations include:
  - Stamp duty: In a cash concentration agreement, the pool header company will set up a revolving credit facility for a bilateral entrusted loan relationship with each subsidiary. The borrower (the pool header company or subsidiaries) can borrow or lend as much as it wishes as long as the amount is within the revolving credit facility during the prescribed period of time. All participants including commercial banks should pay stamp duty according to the amount of the revolving credit facility at the time the cash concentration master agreement was signed. The current domestic stamp duty for such contracts stands at 0.005%.
  - Business tax: In cash concentration, there are typically deposits and withdrawals of the entrusted loans taking place every day between the pool header company and subsidiaries.
- Other tax considerations:
  - A Chinese resident company is liable for income tax on its worldwide income. Non-residents are liable for income tax on Chinese-sourced income.
  - Information on loans, interest and related expenses has to be disclosed and reported when filing annual tax returns.
  - Withholding income tax is imposed at 10% for non-resident companies, unless a double tax treaty offers a lower tax rate.

Market Watch

In August 2008, SAFE launched a new Export Fund Pending for Verification (EFPV) regulation that has implications for any company receiving foreign funds from exports. All firms receiving foreign funds from export operations must create an EFPV account where SAFE regulators may inspect all trade-related FCY activity. To ensure foreign funds are promptly credited to their operational accounts, all companies should formally notify their banks regarding the trade or non-trade nature of their inward transactions and provide relevant supporting documentation. In addition, all companies are strongly advised to require their trade partners to specify the nature of all FCY receivables in the payment narrative field of any payment instruction.

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