News Flash
China Tax and Business Advisory

A Glance at the tax implications of the Shenzhen – Hong Kong Stock Connect

December 2016
Issue 39

In brief

The Shenzhen – Hong Kong Stock Connect (SZ–HK Stock Connect) has been launched on 5 December 2016. It is modelled after the Shanghai – Hong Kong Stock Connect (SH-HK Stock Connect) and offers more opportunities for investors to invest in the China stock markets. The Ministry of Finance ("MOF"), the State Administration of Taxation ("SAT") and China Securities Regulatory Commission ("CSRC") jointly released Caishui[2016]No.127 on 2 December 2016 to clarify the China tax policies in relation to the SZ–HK Stock Connect. These China tax policies are similar to those for the SH–HK Stock Connect. We hereby summarise the major China tax and Hong Kong tax issues which investors of both sides should be aware of when making investment via this new investment channel.

In detail

Shortly after the SH–HK Stock Connect was officially launched on 17 November 2014, the MOF, SAT and CSRC jointly released Caishui [2014] No.81 setting the China tax policies in relation to Hong Kong and Mainland investors which invest the shares listed in the other stock market via the SH–HK Stock Connect. [1]

The SZ-HK Stock Connect was launched after two years ofsmooth implementation of the SH–HK Stock Connect. The China tax policies (including corporate income tax (CIT), individual income tax (IIT), turnover tax and stamp duty) in Caishui [2016] No.127 for investors of both sides are similar to those in Caishui [2014] No.81. Meanwhile, Caishui [2016] No.127 also clarifies that the borrowing and repayment of shares under covered short selling transactions carried out by Hong Kong/foreign investors under the north bound trading link (for both the SZ–HK Stock Connect and SH – HK Stock Connect) will be temporarily exempt from stamp duty in China.

The major China tax and Hong Kong tax implications for the SZ–HK Stock Connect are summarised in the attached Appendix.

The takeaway

After two years of successful trial run of the SH–HK Stock Connect, the launch of the SZ–HK Stock Connect earmarks further connection of the financial markets of Mainland China and Hong Kong. Meanwhile, it also constructively supports China's national strategies, including the opening up of its capital market, economic transformation and upgrade, strengthening the role of Hong Kong as an international financial centre and the internationalization of RMB. The consistent tax policies for both the SZ–HK Stock Connect and the SH –HK Stock Connect and the clarification of the stamp duty treatment for covered short selling transactions will further facilitate investors from both sides to make the relevant investments.

Endnote

1. *Please refer to our News Flash [2014] Issue 27 for more details of Caishui [2014] No. 81.*

Appendix

Income	Investor	China tax implications	Hong Kong tax implications
Southbound Trading Link			
Gains from the transfer of eligible shares listed in HK	**Mainland China corporate investors**	• Subject to CIT • Will be taxed or exempted in accordance with the current value added tax (VAT) regulations	• Disposal gains derived by Mainland investors will not be subject to Hong Kong profit tax provided that they are not regarded as a trading receipt of the Mainland investors or not from trade or business carried out by them in Hong Kong. This usually will be the case as the Mainland investors will place their purchase/sales orders through a stock broker in China and no activity is required to be performed by them in Hong Kong. Furthermore under the Hong Kong/Mainland double tax arrangement, the taxing right of gains derived from disposal of shares of Hong Kong resident companies listed in Hong Kong is granted solely to the Chinese tax authorities and the Hong Kong tax authority cannot impose tax on these gains. • Stamp duty is applicable on the transfer of Hong Kong stocks and it is currently at the rate of 0.1%, payable by each of the transferor and transferee, of the consideration or the fair market value of the stocks transferred, whichever is higher.
	Mainland China individual investors	• Temporarily exempted from IIT for the period from 5 December 2016 to 4 December 2019 • Temporarily exempted from VAT in accordance with the current regulations	• Disposal gains derived by Mainland individual investors in shares are not subject to Hong Kong salaries tax or are being regarded as non-trading receipts. • Stamp duty is applicable on the transfer of Hong Kong stocks and it is currently at the rate of 0.1%, payable by each of the transferor and transferee, of the consideration or the fair market value of the stocks transferred, whichever is higher.
Dividend income from eligible shares listed in HK	**Mainland China corporate investors**	• Generally subject to CIT, except for dividends from H shares which the Mainland China corporate investors held for no less than 12 months which will be exempted from CIT • Mainland China corporate investors should make self-declaration and settle the tax payable	Dividends paid out from a company chargeable to Hong Kong profits tax are specifically exempt from tax and there is no withholding tax on the dividends.
	Mainland China individual investors	• Dividends will be subject to IIT of 20%. H share company has to withhold IIT in regards to its dividend distribution, whereas the China Securities Depository and Clearing Corporation has to withhold IIT for dividends distributed from non-H shares	Same as above

Income	Investor	China tax implications	Hong Kong tax implications
		• Dividends paid to Mainland securities investment fund shall follow the same IIT treatment as above	
Northbound Trading Link			
Gains from the transfer of eligible A shares	**Both Hong Kong / foreign corporate investors and individual investors**	• Temporarily exempt from IIT / CIT • Temporarily exempted from VAT • Stamp Duty on the seller with the rate of 0.1%	Disposal gain and dividend income derived by Hong Kong or overseas individual / institutional investors from securities listed in the Mainland will generally not be subject to tax in Hong Kong as the income is either outside the charging scope of Hong Kong salaries tax or being regarded as non-trading receipts (for individual investors) or qualifies as non-trading or non-Hong Kong sourced income for Hong Kong profits tax purposes (for institutional investors)
Dividend income from eligible A shares		• Dividends will be subject to 10% withholding tax and the listed company distributing the dividends has the withholding obligation. • If the recipient is entitled to a lower treaty rate, it can apply to the in-charge tax bureau of the payer for a refund	

Let's talk

For a deeper discussion of how this issue might affect your business, please contact a member of **PwC's China Tax and Business Service** :

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In the context of this News Flash, China, Mainland China or the PRC refers to the People's Republic of China but excludes Hong Kong Special Administrative Region, Macao Special Administrative Region and Taiwan Region.

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