

China Tax Weekly Update

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Reference: SAT
Announcement [2017] No. 37
Issuance date: 17 October
2017
Effective date: 1 December
2017

Relevant industries: All
Relevant companies: Non-
resident enterprises
Relevant taxes: CIT

Potential impacts on
businesses:

- Operational costs reduced

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full content of the circular.

New China withholding tax administrative guidance

On 17 October 2017, the State Administration of Taxation (SAT) issued new guidance on withholding tax (WHT) administration in SAT Announcement [2017] No. 37 (Announcement 37).

Announcement 37 replaces, with effect from 1 December 2017, the principal existing WHT administrative guidance in Circular Guo Shui Fa [2009] No. 3 (Circular 3). It also replaces the remaining provisions of Circular Guo Shui Han [2009] No. 698 (Circular 698) on the calculation of disposal gains. The indirect transfer rules in Circular 698 had already been replaced by SAT Announcement [2015] No. 7 (Announcement 7). The new guidance makes the following key changes:

Reduced tax compliance burden for WHT agents

- Announcement 37 reduces the compliance burden on WHT agents by abolishing the Circular 3 requirements for WHT agents to:
 - register business contracts, involving non-resident payees, with the tax authorities, within 30 days of contract conclusion.
 - conduct final clearance and settlement procedures for contracts with multiple instalment payments. Tax authority clearance was previously required at least 15 days before the final instalment payment was due to be paid.
- Under Circular 3, where a non-resident enterprise derives income from several locations in China, it may select a tax authority in one of these locations to perform the tax filing. Announcement 37 continues this provision, and it also clarifies how it interacts with the relevant provisions in Announcement 7.

Tax calculation clarified

- Announcement 37 provides clarification on the calculation of equity transfer gains, previously set out in Circular 698. The guidance also observes that the base cost of equity, referred to as its 'net value', must be adjusted for any asset value write downs/increments previously recognized for tax purposes. Detailed calculation examples are provided in the official interpretative guidance to Announcement 37.
- Announcement 37 also clarifies that foreign exchange (forex) changes are factored into equity transfer gain calculations.

<p>Timing of WHT payment obligations</p>	<ul style="list-style-type: none"> • Under Announcement 37, a WHT obligation on dividend distributions paid offshore arise on the actual dividend payment date. Previously, under Circular 3, the WHT obligation arose on the date in which the board decision was made to allocate profits to dividends. • This provides better cash flow management for companies as the tax payment is effectively deferred until actual dividend payment date. • For transfers involving multiple instalment payments, the obligation to pay tax would not arise until all instalments were made. However, Announcement 37 does not provide a clear definition on what qualifies as multiple instalment payments. • Where an asset transfer consideration is to be paid in instalments, the tax law will treat the investment cost as first being recovered, followed by the crystallization of disposal gains. This will consequently defer the time that a WHT obligation arises, relative to the Circular 3 guidance.
<p>More reasonable tax settlement timeframes for foreign payees</p>	<ul style="list-style-type: none"> • Announcement 37 abolishes the Circular 3 requirement for the foreign payee to settle WHT within a predefined period, where the WHT agent fails to pay (a WHT agent has a 7 day period to file and pay). • Previously, Circular 3 required the foreign payee to file and pay the underpaid tax within 7 days of the original WHT obligation arising (e.g. within 7 days of an equity disposal in the case of capital gains WHT). • Announcement 37 states that the tax authorities will now prescribe a timeframe for sellers to pay tax, where the withholding agent fails to do so, and that payment within this period would be recognised by the Chinese tax authorities as being “on-time settlement”. There is a degree of uncertainty as to whether the late interest portion would be imposed on the seller if the tax was paid to the China tax authorities within the prescribed timeframe (as set by the authorities under Announcement 37), but after the June due date, as stipulated under Announcement 7.
<p>Clarified responsibilities for WHT agents and foreign payees</p>	<ul style="list-style-type: none"> • Announcement 37 now states that, if the withholding agent does not withhold for and on behalf of the seller, then the seller has the obligation to pay tax in the location where the Chinese being transferred is located. • Announcement 37 draws a distinction between (i) situations in which tax can be regarded as having been withheld by the WHT agent but not remitted to the tax authorities, and (ii) situations in which tax was not withheld at all. It appears that in the former case the WHT agent is to be pursued for recovery of tax, while in the latter case, the China tax authorities could either pursue the WHT agent or the foreign payee.

Reference: N/A
 Issuance date: 24 October 2017
 Effective date: N/A

Relevant industries: All
 Relevant companies: Enterprises with related party transaction
 Relevant taxes: N/A

Potential impacts on businesses:

- Risks of being challenged due to cross-border tax avoidance arrangements increased

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2016 China Advance Pricing Arrangement Annual Report

On 8 October 2017, China's SAT published its [2016 Advance Pricing Arrangement \(APA\) Annual Report](#). This is the eighth APA annual report released by SAT to describe the latest mechanisms, procedures, and implementation of the APA program in China. This report contains data pertaining to the period from 1 January 2005 to 31 December 2016.

In 2016, China signed 8 unilateral APAs and 6 bilateral APAs (cumulatively 139 APAs including 84 unilateral and 55 bilateral has been signed as of 31 December 2016). Three out of 6 bilateral APAs (BAPAs) were signed with European countries and 3 were signed with Asian countries. Most of the 2016-signed APAs still involve the manufacturing industry but we see a further diversification in the types of industries covered.

In prioritizing APA requests, the tax authority will typically consider the following factors:

- (i) Overall principle: first come, first served.
- (ii) The quality of the request submission.
- (iii) Whether the applicant is in a specific industry or located in a specific region that merits prioritized attention.
- (iv) For a BAPA request, whether the BAPA partner country (region) has the intention to accept the case, and pursue the BAPA, will also be an important factor for consideration.

To fulfill the minimum standard of BEPS Action 5, the unilateral APAs signed after 1 April 2016 will come under the compulsory spontaneous exchange of information framework.

With stricter anti-avoidance approaches being taken by tax administrations all over the world, the number of mutual agreement procedure cases is also expected to increase in coming years.

* In October 2016 SAT set out rules on enhancement of APA administration (SAT Announcement 64) and subsequently in March 2017, SAT also released its long-awaited Announcement on Special Tax Investigations, Adjustments and Mutual Agreement Procedures (SAT Announcement 6). Announcement 64 replaces the relevant regulations on APA administrations as prescribed under Guo Shui Fa [2009] No.2 and Announcement 6 regulates mutual agreement procedures in relation to APA. Please refer to the following KPMG publications for more details:

- ❑ [China Tax Alert: State Administration of Taxation Issued Announcement on the Enhancement of Administration of APA \(Issue 28, October 2016\)](#)
- ❑ [China Tax Alert: SAT Releases the Long-awaited Announcement on Special Tax Investigations, Adjustments and Mutual Agreement Procedures \(Issue 10, March 2017\)](#)

Reference: N/A
 Issuance date: 24 October 2017
 Effective date: N/A

Relevant industries: All
 Relevant companies:
 Enterprises engaged in cross-border B2C e-commerce business
 Relevant taxes: N/A

Potential impacts on businesses:

- Risks of being challenged due to cross-border tax avoidance arrangements increased

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OECD VAT/GST guidance for cross-border sales

On 24 October, the OECD released new implementation guidance to promote the effective collection of consumption taxes on cross-border sales. This guidance will support the consistent implementation of internationally agreed standards for the VAT treatment of cross-border trade given the rapid digitalisation of the economy.

The boom in e-commerce and its impact on the collection of VAT on business to consumer (B2C) supplies in the market jurisdiction was identified as a key tax challenge in the context of the OECD/G20 Project on Base Erosion and Profit Shifting (the BEPS project).

The new guidance [Mechanisms for the Effective Collection of VAT/GST Where the Supplier Is Not Located in the Jurisdiction of Taxation](#) (implementation guidance) focuses on the implementation of the recommended approaches included in the 2015 Final Report on Action 1 "Addressing the Tax Challenges of the Digital Economy" of the BEPS project ([BEPS Action 1 report](#)). These recommended approaches, which are also included in the [International VAT/GST Guidelines](#), have already been successfully implemented by a large number of countries.

The new implementation guidance will support enhanced compliance levels while limiting compliance costs for digital suppliers by promoting consistent and coherent implementation of these collection mechanisms across jurisdictions.

This new implementation guidance on collection mechanisms consists of the following components:

- A general description of basic policy questions and design issues concerning the collection of VAT/GST on supplies of services and intangibles by foreign suppliers;
- An overview of the key policy and design issues for tax authorities to consider when designing and implementing a registration-based collection regime. These considerations may be equally relevant for regimes with specific simplification measures and for registration-based regimes without simplifications; and
- More detailed guidance on the design and practical operation of a simplified registration and collection regime as recommended by [the Guidelines](#) and by [the BEPS Action 1 Report](#).

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