



China Tax Newsletter

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1. Goods Exported by Comprehensive Service Enterprises for Foreign Trade that Meet Certain Criteria Are Eligible for Tax Refund (Exemption)

For goods exported by export enterprises on self-run basis with both the purchase contract and the export agency contract signed ("export agency under the cover of self-run declaration") were not eligible for tax refund, as previously stated by the State Administration of Taxation ("SAT"). However, the Announcement of the State Administration of Taxation [2014] No.13 repeals the abovementioned regulation. A comprehensive service enterprise for foreign trade may file tax refund (exemption) pursuant to the provisions on self-run exports for its goods that meet the following criteria:

- (1) The goods to be exported are goods produced by the manufacturing enterprise itself;
- (2) The manufacturing enterprise has sold the goods to be exported to the comprehensive service enterprise for foreign trade;
- (3) The manufacturing enterprise has concluded an export contract with an overseas entity or individual, agreeing upon that the goods would be exported by the comprehensive service enterprise for foreign trade to the overseas entity or individual and the payment for the goods would be made by the overseas entity or individual to the comprehensive service enterprise for foreign trade; and
- (4) Goods are exported on self-run basis by the comprehensive service enterprise for foreign trade.

Tips from BDO China

- (1) For the purpose of this Announcement, comprehensive service enterprises for foreign trade refer to foreign trade enterprises providing domestic small and medium-sized manufacturing enterprises with logistics, customs clearance, credit insurance, financing, receipt of proceeds, tax refund and other services for export.
- (2) Announcement #13 not only endows the comprehensive service enterprises for foreign trade with the qualification for filling tax refund (exemption), but also defines the legal responsibilities of these enterprises. In the event that a comprehensive service enterprise for foreign trade commits tax-related irregularities such as falsely issuing VAT invoices, it shall be punished as the subject of liability pursuant to relevant regulations. Therefore, comprehensive service enterprises for foreign trade shall strengthen risk control and strictly review the business conditions and production capacity of the manufacturing enterprises concerned to ensure the authenticity of the domestic purchases and exports of goods for which the tax refund (exemption) is declared.

2. Large Hydropower Enterprises Are Entitled to the Policy of VAT Refund upon Collection

Hydroelectric power stations (including pumped storage power stations) with installed capacity of over 1 million kw are entitled to the policy of value-added tax ("VAT") refund upon collection for their selling of self-produced electric products. Detailed provisions are as below:

- (1) Starting from 1 January 2013 to 31 December 2015, hydropower enterprises are eligible for the VAT refund upon collection for the portion of VAT actually paid which exceeds 8%;
- (2) Starting from 1 January 2016 to 31 December 2017, hydropower enterprises are eligible for the VAT refund upon collection for the portion of VAT actually paid which exceeds 12%.

Tips from BDO China

Installed capacity refers to the total rated installed capacities of all generator sets in a station. The rated installed capacity includes both the total installed capacity (including capacities for various stages and the added generator sets) of the hydroelectric power station examined and approved (approved) by the project examining and approving (approving) authorities according to jurisdiction and the approved additional installed capacity due to technology transformation and upgrade, etc.

3. Tax Treaty and Protocol for the Avoidance of Double Taxation between China and Ecuador Come into Force

The tax treaty and protocol between China and Ecuador come into force as of 6 March 2014 and are applicable to income derived on 1 January 2015 and thereafter.

Tips from BDO China

(1) Activities in connection with construction projects constitute permanent establishments ("PEs") only if the activities last more than 12 months;

(2) Services such as consultation constitute PEs only if the service activities continue within a Contracting State for a period or periods aggregating more than 183 days in the fiscal year concerned;

(3) If the beneficiary owner of the dividends is the resident of the other Contracting State, the withholding income tax rate applicable is 5%. Tax rates for dividends, interest, and royalties paid by Ecuador to China are reduced to 3%, 8%, and 8% respectively.

4. Approval from the SAT Is Not Required for Pre-tax Deduction of Asset Losses Caused by the Decisions of the State Council

In the Announcement of the State Administration of Taxation [2014] No. 25, it is stated that for asset losses caused by the decisions of the State Council, the enterprise shall submit relevant materials to the SAT, which will, upon reviewing the relevant information, inform the tax authority concerned of the losses.

Recently, the SAT released a new circular, stating that approval from the SAT is not required for pre-tax deduction of asset losses caused by the decisions of the State Council. Instead, enterprises shall make a special declaration of the pre-tax deduction of asset losses with the competent tax authorities.

5. The SAT Simplifies the Procedures for Obtaining and Using VAT Invoices

Starting from May 1st, the simplified procedures for obtaining and using the VAT invoices will come into force, featuring the following aspects:

(1) A simplified procedure for obtaining VAT invoices

Currently, before obtaining VAT invoices, taxpayers need to provide the VAT invoice issuing list and the stub copy of the last issued VAT invoice for old invoice verification and new invoice application (i.e. "manual verification of old VAT invoices"). The new circular repeals this manual verification of old VAT invoices and requires the tax authorities to complete the verification of old VAT invoices using data in the tax control system.

(2) A simplified procedure for approving the maximum invoicing amount of the special VAT invoice

Currently, competent tax authorities need to perform onsite inspections on taxpayers who apply for raising the maximum invoicing amount of the special VAT invoice. The new circular, however, states that onsite inspections are not required when the maximum invoicing amount of the special VAT invoice applied by the taxpayer does not exceed RMB100, 000.

(3) A simplified procedure for handling lost special VAT invoices

Currently, if the invoice copy and the deduction copy of an issued special VAT invoice are missing, the buyer needs to get the approval from its competent tax authorities before using the photocopy of the bookkeeping copy of the lost special VAT invoice and the Certificate of Tax Declaration for the Lost Special Value-added Tax Invoice sent by the seller as the deduction vouchers for input VAT. The new circular eliminates the procedure of getting approval from the competent tax authorities of the buyer, that is, the buyer can directly use the preceding documents as the deduction vouchers for input VAT.

Currently, if the deduction copy of an issued special VAT invoice is missing and has not been authenticated, the buyer shall submit the invoice copy of the special VAT invoice to the competent tax authorities for authentication. The new circular repeals this procedure, that is, the buyer can authenticate the invoice copy via the online authentication system.

(4) A simplified procedure for handling the special red-letter VAT invoice

Currently, if sales returns or sales allowances occur, taxpayers need to submit photocopies of the vouchers for the transaction to the competent tax authorities for filing after special red-letter VAT invoices are issued accordingly pursuant to relevant provisions. In the new circular, this filing procedure is repealed.

Tips from BDO China

(1) VAT general taxpayers under counseling period shall apply to the original provision of special VAT invoice management on a limited quantity and quota basis and shall not apply to regulations in this new circular.

(2) When the output VAT entered into the Anti-forgery Tax Control System by a seller is negative, a special red-letter VAT invoice will be issued. After a VAT general taxpayer has obtained the special VAT invoices, where there is a return of goods sold or discovery of an invoicing error but which do not satisfy the conditions for invoice voiding, or where there is a return of part of goods sold or sales allowances, the VAT general taxpayer needs to obtain the Advice Note concerning the Issuance of Special Red-letter VAT Invoices from competent tax authorities before issuing the special red-letter VAT invoice.

6. Range of Small and Low-profit Enterprises Eligible for EIT Reduction by Half Enlarges

Starting from 1 January 2014, the range of small and low-profit enterprises eligible for enterprise income tax ("EIT") reduction by half is enlarged to include those whose annual taxable income is less than RMB100,000 (including RMB100,000) which is RMB60,000 (including RMB60,000) originally. This policy terminates on 31 December 2016.

Tips from BDO China

(1) Small and low-profit enterprises are enterprises engaged in industries not restricted or prohibited by the state which meet the following criteria:

a. Industrial enterprises whose annual taxable income is RMB300,000 at most and the number of employees is 100 at most, with the total assets not exceeding RMB30,000,000;

and

b. Other types of enterprises whose annual taxable income is RMB300,000 at most and the number of employees is 80 at most, with the total assets not exceeding RMB10,000,000.

(2) Foreign-invested enterprises satisfying the preceding criteria are also eligible for this tax preference.

7. China and Germany Signed the New Tax Treaty for the Avoidance of Double Taxation

On 28 March 2014, China and Germany signed the new tax treaty for the avoidance of double taxation. Currently, this new tax treaty has not come into force.

Tips from BDO China

Compared to the tax treaty currently in force, the new tax treaty features the following changes:

(1) Dividends: The withholding tax rate for dividends is 5% if the beneficial owner is a company (other than a partnership) which holds directly at least 25% of the capital of the company paying the dividends.

(2) Royalties: The minimum withholding tax rate for royalties is reduced to 6%.

(3) Capital gains: Gains from the alienation of ships or aircraft operated in international traffic, or movable property pertaining to the operation of such ships or aircraft, shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated, rather than the Contracting State in which the place of head office of the enterprise is situated pursuant to the old tax treaty. Gains from the alienation of shares shall be taxable according to different conditions, rather than in only one Contracting State as stated in the old tax treaty. An example under the new tax treaty would be: Assume that a German company alienates shares of a Chinese company, it is taxable in China if it has owned, directly or indirectly, at least 25% of the shares of the Chinese company at any time during the 12 month period preceding the alienation; it is not taxable in China if the shares it has owned are less than 25%. However, if the annual trading volume of shares traded in stock exchanges does not exceed 3% of the quoted shares, these shares are not taxable in China.

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Jesse Wang

Tel: +86-755-82900993

E-mail: jesse.wang@bdo.com.cn jesse.wang@bdo.com.cn

Anne Raschick

E-mail: araschick@bdo.com

Jinsong Hu

Tel: +86-755-82966512

E-mail: jason.hu@bdo.com.cn tax@bdo.com.cn

Robert Pedersen

Partner, International Tax Services

+1 212-885-8398

E-mail: RPedersen@bdo.com

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