



China Tax Newsletter

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1. Announcement on Value-added Tax Policies for Finance, Real Estate Development, Education Ancillary Service and Other Services

Cai Shui [2016] No.140 clarifies related value-added tax (VAT) policies for finance, real estate development, education ancillary service and other services. Considering the close connection between Cai Shui [2016] No. 140 and Announcement of the State Administration of Taxation on VAT Levy and Administration Related Issues Including the Time for Deducting Land Price (Announcement of the State Administration of Taxation [2016] No. 86), main contents of both circular are hereby announced as follows:

(1) Non-capital guaranteed proceeds such as gain, remunerations, charge for capital occupation and compensation obtaining from financial products during the holding period (including the mature date) do not fall into the scope of interest or income of interest nature and are not subject to VAT.

(2) Holding of funds, trusts, financial products and other asset management products from purchase to maturity do not fall into the scope of transfer of financial commodities.

(3) After institutions operating financial and insurance business extend loans, they shall pay VAT according to the prevailing provisions on the interest that is receivable but is not received within 90 days from the expiration date, while VAT is temporarily not required on the interest that is receivable but is not received after 90 days from the expiration date, instead, the VAT shall be paid upon the actual receipt of the interest.

(4) The manager of the asset management products shall pay VAT for his/her VAT taxable activities during the operation of the asset management products.

(5) A negative difference as a result of the transfer of financial products by taxpayers between January and April of 2016 can be carried forward to next taxable period and offsets the sales income arising from the transfer of financial products during May to December of 2016.

(6) Pilot taxpayers engaged in finance leasing business mentioned in Cai Shui [2016] No.36 include the pilot taxpayers approved by related authorities as well as those who have finished the record filling with related authorities.

(7) Where VAT general taxpayers among real estate developers sell real estate development projects they have developed (excluding the old real estate projects to which the simplified tax calculation method is applied), the sales amount shall be the balance of the total price and other charges gained after deduction of the land price paid to the government departments at the time of acceptance of the transferred land. The land price paid to the government department includes compensation for land acquisition and demolition paid by the land assignee to the government departments, the preliminary development expenses and land transfer proceeds, etc.

Where VAT general taxpayers among real estate developers sell real estate development projects they have developed (excluding the old real estate projects to which the simplified tax calculation method is applied), the compensation for demolition paid to other units or individuals upon land acquisition is also allowed to be deducted for the purpose of calculating the sales amount. When taxpayers deduct the compensation for demolition in accordance with the above provisions, the demolition agreement, certificates of payment and receipt of demolition compensation of both parties and other documents which can prove the authenticity of the compensation for demolition shall be provided.

Announcement of the State Administration of Taxation [2016] No.86 further clarifies the time for deducting land price. The land price paid to the government department or the compensation for demolition paid to other units or individuals upon land acquisition by

real estate developers allowed to be deducted but haven't been deducted can be tax-deductible according to the above provision from December 2016 (taxation period) on.

(8) After real estate development enterprises (including a consortium formed by a number of real estate developers) take the land, pay the land price to the government departments and establish a project company to develop the land, if all of the following conditions are met, the project company may deduct the land price that has been paid by the real estate developers to the government departments.

a. Real estate developers, the project company, and the government departments have signed an alteration agreement or supplementary contract, changing the land assignee to the project company;

b. Under the circumstance that the purpose, planning and other conditions for the government departments to transfer the land remain unchanged, the total land price does not change when an alteration agreement or supplementary contract is signed.

c. The total equity of the project company is owned by the real estate developers taking the land.

Announcement of the State Administration of Taxation [2016] No.86 further clarifies the time for deducting land price. The land price paid to the government department allowed to be deducted but haven't been deducted can be tax-deductible according to the above provision from December 2016 (taxation period) on.

(9) Where taxpayers engaged in catering business sell takeaway food, VAT shall be paid under the "catering service".

(10) Hotels, taverns, resthouses, resorts and other commercial accommodations shall pay VAT under the "conference and exhibition services" for their provision of conference facilities and ancillary services.

(11) Taxpayers are required to pay VAT under the "culture and sports services" for their income obtained from the operation of cableways, ferry pushes, battery carts, cruise ships and others.

(12) With respect to the education ancillary services provided by VAT general taxpayers, VAT can be calculated and paid at a tax rate of 3% under the simplified tax calculation method.

(13) Where taxpayers provide armed guard and escort services, they shall pay VAT for the provision of "security services".

(14) A property services business shall pay VAT under "construction services" for the decoration services provided for owners.

(15) Where taxpayers lease their construction equipment equipped with operators to others, they shall pay VAT under "construction services".

The Circular takes effect as of May 1st, 2016.

According to Announcement of the State Administration of Taxation [2016] No.86, below measures shall be adopted when dealing with the issue related to the application of the suitable tax categories with respect to the above provisions (9), (10), (11), (13), (14) and (15):

a. It is no need to adjust the filing of VAT returns if the tax rates haven't been changed for the services.

b. Where the original applicable tax rates of the services are higher than the tax rates mentioned above, the overpaid output VAT shall be deducted from output VAT of future taxable periods.

c. Where the original applicable tax rates of the services are lower than the tax rates mentioned above, it is no need to adjust the filing of VAT returns and taxpayers shall follow the provisions above from December 2016 (taxation period) on.

Taxpayers who already issued special VAT invoices to the purchasers for the services mentioned above should collect the special VAT invoices back and issue new invoices with suitable tax rate, while it is not allowed to make adjustment if the invoices cannot be collect back.

According to Article 5 of Announcement of the State Administration of Taxation [2016] No. 86, “the gross floor area of a real estate project sold for the current period” and “the saleable floor area of a real estate project” mentioned in Article 5 of Announcement of the State Administration of Taxation [2016] No. 18 refer to the ground floor area counted in plot ratio but excluding the floor area of underground parking spaces.

Article 6 in Announcement of the State Administration of Taxation [2016] No. 86 stipulates that when handling formalities for the exemption of VAT levied on real estates gratuitously given or acquired, taxpayers shall be in accordance with the provisions mentioned in Announcement of the State Administration of Taxation [2015] No. 75 except for the subitem 2 of item 4 of Article 1 that “the original and copy of the notarized certificate of legal right to inheritance or bequest” which is modified as “the original and copy of certificate of legal right to inheritance or bequest”.

In accordance with Article 7 of Announcement of the State Administration of Taxation [2016] No. 86, free rental provision in leasing contract of real estate leasing does not fall into the scope of deemed sales of services as stipulated by Article 14 of Cai Shui [2016] No. 36.

Announcement of the State Administration of Taxation [2016] No. 86 shall become effective from December 24, 2016.

Tips from BDO China

Both Cai Shui [2016] No.36 and Announcement of the State Administration of Taxation [2016] No. 18 stipulate that where VAT general taxpayers among real estate developers sell real estate development projects they have developed (excluding the old real estate projects to which the simplified tax calculation method is applied), the sales amount shall be the balance of the total price and other charges gained after deduction of the land price paid to the government departments at the time of acceptance of the transferred land. In addition, the range of direct receivers of the payment for land acquisition is strictly limited to the government, land management department or organizations authorized by the government. Moreover, the tax-deductible certificates of payment are strictly limited to fiscal receipts printed under the supervision of (or printed by) the finance authorities of provincial level and above. However, according to Cai Shui [2016] No. 140, the tax-deductible range has been extended to compensation for land acquisition and demolition paid by the land assignee to the government departments, the preliminary development expenses, land transfer proceeds as well as the compensation for demolition paid to other units or individuals upon land acquisition. Accordingly, the range of tax-deductible certificates has also been extended to the demolition agreement, certificates of payment and receipt of demolition compensation of both parties and other documents which can prove the authenticity of the compensation for demolition.

Item (8) of the above provisions states that a project company may deduct the land price that has been paid by the real estate developer(s) to the government departments, which solves some of the frequently-occurred practical problems. For instance, a real estate developer developing land elsewhere by “auction first, registration later” method results in the receipt of land price being issued to the parent company (i.e. real estate developer) and hence the land price cannot be deducted after the project company is established.

Meanwhile, the provision states that the project company shall be 100% wholly-owned by the real estate developer(s) taking the land before and after changing the land assignee, which is rather strict.

2. Announcement of the State Administration of Taxation on Matters Related to the Enterprise Income Tax Refund Involved in the Settlement of Land Appreciation Tax by Real Estate Developers

According to the Announcement of the State Administration of Taxation on Dealing with Issues Concerning Enterprise Income Tax before the De-registration of Real Estate Developers (Announcement of the State Administration of Taxation [2010] No. 29), real estate developers could apply for the refunds of enterprise income tax overpaid as a result of losses identified after land appreciation tax (LAT) final settlement before making the taxation cancellation application. Normally, real estate developers could not be cancelled in a short time after finishing the sales of the developed commodities, which results in the failure of the refunds of overpaid enterprise income tax. Hence, Announcement of the State Administration of Taxation [2016] No. 81 improves the tax refunds policy and the main contents are hereby announced as follows:

(1) When to apply for tax refunds

Application for tax refunds begins after the LAT settlement of all developed projects. More specific, where a developer settles the LAT on a developed project according to regulations and a loss occurs in the settlement and payment of its enterprise income tax for the current year while there is no other follow-up development project, the developer could apply for tax refunds. The follow-up development projects refer to the projects in development and the projects for which a developer wins tenders.

(2) Method of calculation of enterprise income tax overpaid

Similar to the provision of Announcement of the State Administration of Taxation [2010] No. 29, the total amount of LAT paid for a project by a real estate developer shall be apportioned to each year of project development according to the percentage of the project sales revenue generated each year in the project development to the total sales revenue of the whole project and the developer shall calculate the yearly and accumulative amounts of tax refunds.

(3) Documents for application

In the process of applying for tax refunds, a developer shall provide written materials to the competent tax authorities to account for the calculation process of the refundable enterprise income tax, including the total LAT paid for the project, the total project sales revenue, the annual project sales revenue, LAT apportioned to each year, LAT that has been pre-tax deducted, the applicable tax rate for each year, and whether there are follow-up development projects.

This Announcement shall come into force as of the date of December 15th, 2016.

3. Announcement of the State Administration of Taxation on Relevant Issues Concerning the Determination and Handling of Special VAT Invoices Issued by Evading (Unreachable) Enterprises

According to Announcement of the State Administration of Taxation [2016] No. 76, evading (unreachable) enterprises refer to enterprises which do not fulfill the tax obligations and escape from the regulation of tax authority. Main contents of the circular are as follows:

(1) Abnormal proofs for offsetting against VAT (hereinafter referred to the "abnormal proofs") of evading (unreachable) enterprises

Where an evading (unreachable) enterprise falls under any of the following circumstances during the period of existence and operation, special VAT invoices issued during the corresponding period shall be treated as abnormal proofs:

a. For a commercial and trading enterprise, the names of goods purchased and sold are seriously inconsistent; for a manufacturing enterprise, it does not have manufacturing and processing capabilities and has not consigned processing, or its manufacturing consumption cannot match with its sales, or the goods purchased by the enterprise cannot be used directly to manufacture the goods it sells and it has not consigned processing.

b. An enterprise evades or disappears directly and does not file a tax return, or files a tax return with false information.

(2) Handling of abnormal proofs obtained by a VAT general taxpayer

Where a VAT general taxpayer receives an abnormal proof and has not yet declared for VAT credits or for export tax rebate, it is not allowed to use the proof to offset against VAT or apply for tax rebate temporarily; where the taxpayer has already declared for tax credits, the input VAT shall be transferred out with no exception; where the taxpayer has completed procedures for export tax rebate, the tax authority may suspend the handling of export tax rebate for other approved refundable taxes of the enterprise based on the amount of tax rebate involved in the abnormal proof.

This Announcement shall come into force as of the date of December 1, 2016.

4. Announcement of the State Administration of Taxation on Relevant Issues Concerning the Deduction of Certain Items for VAT Levied on the Transfer of Real Property by Taxpayers

Announcement of the State Administration of Taxation [2016] No. 73 clarifies related issues related to the deduction of certain items for VAT levied on the transfer of real property by taxpayers. Main contents of the circular are as follows:

(1) For taxpayers involved in the transfer of real property who cannot provide invoices obtained during the acquisition of the real property, they can provide other documents such as tax payment certificates that can prove the basis of calculation of deed tax for deduction purpose.

(2) Taxpayers using the calculation basis of deed tax for calculating the differential amount shall follow the formula below to calculate the VAT payable:

a. Deed tax payment on and before April 30, 2016

VAT payable = [total transaction price (including VAT) - calculation basis of deed tax (including business tax)] / (1+5%) × 5%

b. Deed tax payment on and after May 1, 2016

VAT payable = [total transaction price (including VAT) / (1+5%) - calculation basis of deed tax (not including VAT)] × 5%

(3) For taxpayers who preserve both invoices relating to obtaining of the real property and other documents such as tax payment certificates that can prove the basis of calculation of deed tax, they shall calculate the difference amount based on the invoices.

This Announcement shall come into force as of the date of November 24, 2016.

5. Policies on Matters Related to Pre-tax Deduction of Personal Accident Insurance Premiums and Determination of Sales Income from Disposal of Enterprise Assets

Announcement of the State Administration of Taxation [2016] No. 80 promulgates the following policies on the matters related to pre-tax deduction of personal accident insurance premiums and determination of sales income from disposal of enterprise assets:

Enterprises are permitted to deduct the personal accident insurance premiums incurred by enterprise employees who travel on business trips from taxable income.

Where an enterprise falls under any of the circumstances stipulated in Article 2 of the Notice of the State Administration of Taxation on the Income Tax Issues Relating to Disposal of Assets by Enterprise (Guo Shui Han [2008] No. 828), the sales income shall be determined based on the fair value of the assets transferred unless otherwise stipulated.

This Announcement shall apply to the annual settlement and payment of enterprise income tax for the year 2016 and subsequent years.

Tips from BDO China

Article 2 of the Notice of the State Administration of Taxation on Income Tax Issues Relating to the Disposal of Assets by Enterprises (Guo Shui Han [2008] No. 828) states that:

Where an enterprise transfers assets to another party for any of the following purposes, such transfer should be treated as a sales act to determine income therefrom due to the fact that such transfer is not an internal disposal of assets as a result of the change in the ownership of the assets:

- (1) The purpose of marketing or sales;
- (2) The purpose of social communication and entertainment;
- (3) The purpose of the distribution of bonus or benefits to employees;
- (4) The purpose of the distribution of dividends;
- (5) The purpose of external donations;
- (6) Any other purpose which changes the ownership of the assets.

6. Circular on Promoting Preferential Enterprise Income Tax Policies for Advanced Technology Service Enterprises within Pilot Regions Carrying out Innovative Development of Trade in Services

Cai Shui [2016] No. 122 promotes the following preferential enterprise income tax policies for advanced technology service enterprises within pilot regions carrying out innovative development of trade in services:

- (1) Pilot regions carrying out innovative development of trade in services

Tianjin, Shanghai, Hainan, Shenzhen, Hangzhou, Wuhan, Guangzhou, Chengdu, Suzhou, Weihai and Harbing New Area, Jiangbei New Area, Liangjiang New Area, Gui'an New Area, Xixian New Area.

- (2) Preferential enterprise income tax policies for advanced technology service enterprises within pilot regions carrying out innovative development of trade in services

- a. With regard to a recognized advanced technology service enterprise, enterprise income tax is to be collected at the reduced tax rate of 15%; and

b. Spending on the vocational education of employees incurred by recognized advanced technology service enterprises which does not exceed 8% of its total salaries and wages is allowed to be deducted at the time of calculation of taxable income; and the part that exceeds 8% is allowed to be carried forward to subsequent tax years for deduction.

The execution period of the tax policies mentioned in the circular is from January 1, 2016 to December 31, 2017.

Tips from BDO China

Cai Shui [2014] No. 59 stipulates the requirements and accreditation administration of advanced technology service enterprises.

7. Notice on Promulgation of the Relevant Preferential Import Tax Policies on Further Supporting the Development of the New-type Display Device Industry

Cai Guan Shui [2016] No. 62 stipulates the preferential tax policies on import of materials by production enterprises in the new-type display device industry as well as the upper-stream enterprises producing raw materials, components and parts for the industry. Main contents are as follows:

(1) From January 1, 2016 to December 31, 2020, new-type display device production enterprises (including those producing thin-film-transistor liquid-crystal displays and organic light emitting diode display panels) shall be exempt from import tariffs for import of the self-use raw materials and consumables for production (including those for research and development) that cannot be produced domestically, and the import VAT thereon shall be levied as legally required; and the import of the supporting systems that have not yet been available in China currently (or that, in other words, cannot be produced domestically or the performance of domestic ones fail to meet requirements) as needed for the construction of clean rooms as well as the components and parts for the maintenance of production equipment by the aforementioned enterprises shall be exempted from import tariffs and import VAT.

(2) From January 1, 2016 to December 31, 2020, production enterprises of key raw materials and components and parts belonging to upper-stream of new-type display device industry, such as color filter film and polaroid, that conform to the domestic independent development planning of the industry in China can enjoy the preferential policies of import tariffs exemption for import of self-use raw materials and consumables for production that cannot be produced domestically.

8. Law of the People's Republic of China on Environmental Protection Tax

The Law of the People's Republic of China on Environmental Protection Tax (Order of the President of the People's Republic of China [2016] No. 61) is approved on December 25, 2016 at the 25th Session of the Standing Committee of the 12th National People's Congress of the People's Republic of China.

Enterprises, public institutions, other producers and operators that directly emit taxable pollutants into the environment within the territory and other sea areas under the jurisdiction of the People's Republic of China are taxpayers of environmental protection tax, who shall pay tax in accordance with this Law. For the purpose of this Law, taxable pollutants refer to air and water pollutants, solid waste and noise specified in the Table of Taxable Items and Amount of Environmental Protection Tax and the Table of Taxable Pollutants and Equivalent Values. From the day when this Law takes effect, environmental protection tax shall be collected as stipulated by this Law, and the pollutant emission fee shall no longer apply.

This Law shall become effective as of the date of January 1, 2018.

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