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Consulting Group

China Business Advisory

2017 Issue 8 August 2017

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Further Value-Added Tax Policy for Construction and Other Services

The Ministry of Finance ("MOF") and State Administration of Taxation ("SAT") issued Caishui [2017] No. 58 ("Circular 58") on "Relevant Issues concerning Value-Added Tax ("VAT") for Construction and Other Services" as an improvement derived from the practice of the VAT reform pilot programme. The key points include:

1. Tax treatments related to construction services

Instead of the previous discretion to choose between the normal tax rate of 11% with VAT input and a simplified tax rate of 3% without VAT input, general contractors will only be subject to VAT at the reduced rate of 3% without VAT input for services related to building foundation and main structure with purchases of all or part of the steel, concrete, masonry materials and prefabricated parts.

When a taxpayer receives advance payment for construction services, advance VAT should be paid at the following rates based on the amount of the advance payment net of amounts paid to subcontractors:

- 2% where a normal VAT calculation method is applied;
- 3% where a simplified VAT calculation method is applied.

2. Agricultural business

VAT exemption is granted to taxpayers who subcontract, lease, swap, transfer, or invest as equity with the land-use right to farmers for agricultural production.

3. Tax treatments related to finance services

From 1st January 2018, financial institutions will pay VAT on interest income over their holding period with regard to discounting and re-discounting businesses.

These new rules which took effect on 1st July 2017 (except that being stated otherwise) may bring the following impacts to businesses:

- Reduced VAT rate of 3% without VAT input could benefit general contractors since it is usually hard for them to obtain required documents to claim VAT input under the current situation of the industry;

- The reduced rate of 3% also means VAT advance payment could be less for services with advance payments and this in turn improves taxpayer's cash situation;

- Agricultural production would be better supported through the clarification of VAT exemption on transactions relating to the land-use right.

Revision of Policy regarding FIE Establishment and Alteration

On 30th July 2017, the Ministry of Commerce ("MOC") released MOC Order [2017] No. 2 ("Order 2") to revise the original "Provisional Regulations on Record Filings for the Establishment and Alteration of Foreign Investment Enterprise ("FIE")" published as MOC Order [2016] No. 3. The revised version became effective on the promulgation date.

According to Order 2, the following establishments/alterations will fall into the scope of record filings management system in lieu of the previous administrative examination and approval system if they are not within the Negative List and not related-party transactions:

- When a non-FIE is converted into a FIE due to merger and acquisition ("M&A") with a foreign investor
- When a foreign investor is to make strategic investments in a listed non-FIE
- When a new foreign investor is to invest in a listed FIE

On the same day of the promulgation of Order 2, the MOC also released Public Notice [2017] No. 37 ("Public Notice 37") to deal with the transitional issues related to the launch of Order 2, including the negative list applicable in Pilot Free Trade Zones ("FTZs") and that applicable to other areas as well as specific definition of M&A and strategic investments in Order 2.

In summary, in the case of M&A of domestic enterprises and strategic investments to listed companies by foreign investors, the establishments or alterations of FIEs should be subject to the record filing management system, except for those covered by the negative lists or being a related-party transaction. It will facilitate foreign direct investments entering into China market.

Expansion of the Customs Clearance System Integration Reform

On 28th June 2017, the General Administration of Customs ("GAC") issued the Announcement of the General Administration of Customs on the Implementation of National Customs Clearance Integration Reform (Announcement No.25), announcing that the Customs Clearance Integration Reform will be expanded to the whole nation from 1st July 2017 after the one-year try-out in Shanghai.

As the first pilot area of the Customs Clearance Integration Reform, Shanghai has been implementing the Customs Clearance Integration Reform from 1st June 2016 onward. GAC subsequently released Announcement [2016] No.62 on 29th October 2016 to shift the pre-goods release review to post-goods release review. The trial experience made a good base for this nationwide reform, enabling the customs to standardize nationally its law enforcement and enhance customs clearance efficiency.

Under Customs Clearance System Integration, two centers have been established: National Customs Risk Prevention and Control Center and Duty Collection and Administration Center. The former provides high-level oversight and management for customs risk prevention and control while the latter verifies the accuracy of customs duty and tax filings for goods imported through all Chinese ports.

In addition, the following three systems will be implemented nationwide,

- "One declaration with review in stages" – Enterprises can handle issues arising from customs declaration in one go where goods would be allowed to be released if the risks are considered low by customs. Customs will deal with the tax relevant matters afterward;

- "Reform of tax collection and administration procedure" – The enterprise has the obligations to perform the declaration truthfully and pay the taxes properly. Customs will perform random checks instead of verifying each shipment;

- "Cooperative supervision" – Port customs will mainly focus on on-site supervision of customs clearance while territorial customs will mainly focus on enterprise inspection and credit management.

This reform allows enterprises to choose any port that is most convenient to them, which can be different from the importation port, to fulfil customs declaration. The procedures will be simpler and quicker and it is expected to bring lower costs and speedier logistics for companies.

China to Enhance its Appeal to Foreign Investment

A decision was made on 28th July 2017 at a State Council executive meeting for China to enhance its appeal to foreign investments and foreign talents by widening market access and improving business environment. The key points are:

- The "Negative List" approach which has been successfully implemented in FTZs and should be applied nationwide;
- No Withholding Tax ("WHT") will be levied when foreign investors reinvest in eligible industries in China with distributed profits from FIEs;
- The Corporate Income Tax incentives for advanced technology service enterprises in pilot cities will be expanded nationwide;
- Actions will be taken to cancel or liberalize the proportion of foreign investment in manufacturing and service industry through encouraging local government to promote the establishment of multinational enterprise regional headquarters in China and strengthening the protection of foreign investment in intellectual property rights;
- National high-tech development zones will be further developed with the facilitation of land grants to foreign invested projects and provision of financial support to technology and green projects in western and northeast China;
- Work permit system for foreigners working in China will be improved to attract foreign talents.

Service Highlight

The Chinese government continues to put strenuous efforts to improve the investment environment in China through reforms in many key areas including business registration, tax and customs administration. To this end, many new policies and regulations have been released while old ones have been revised. More changes in policies and regulations are expected to follow. We are more than pleased to discuss with you how to leverage these positive measures to enhance your business success. Sino-Bridge is always well prepared and pleased to help investors to realize their full potential. Our Marketing Executive, Ms. Kimme Chan, looks forward to hearing from you at (852) 3579 8745 or kimmechan@sinobridge-consulting.com for any assistance and support we could provide you with.

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