

China Business Advisory

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Withholding Tax Deferral for Direct Reinvestment of Profit in China

In August 2017, the State Council (“SC”) released Guofa [2017] No.39 which brings forward 22 measures to

further widen market access and improve business environment for foreign investments and foreign talents. One of these measures is the tax incentive to allow the deferral of Withholding Tax (“WHT”) for profit directly reinvested in eligible industries (See “China Business Advisory 2017 Issue 9”).

In order to give detailed implementation guidance, the Ministry of Finance (“MOF”), State Administration of Taxation (“SAT”), National Development and Reform Commission (“NDRC”), and Ministry of Commerce (“MOC”) jointly issued Caishui [2017] No.88 (“Notice 88”) on 21st December 2017 to provide specific definitions, requirements, criteria and some other relevant information with a pertinent list of Q&As on the website of MOF for interpretations. The highlights of Notice 88 include:

- Applicable conditions of the WHT deferral treatment (should fulfill all of the followings)
 - Distributed profits of foreign investors should be used for equity investment in the form of

capital increase, capital injection and share acquisition. However, using distributed profits to increase paid-in capital or capital reserves of publicly listed companies or to acquire shares in publicly listed companies, unless qualified strategic investment, are excluded from the policy;

- The profits distributed to foreign investors should be dividends, profit distributions and other returns on equity investments, arising from the distribution of realized retained earnings by resident enterprises in China;
 - Regardless of whether the profits distribution is in the form of cash or non-cash, it must be directly transferred to the invested enterprises or equity transferees, rather than through a third party;
 - The reinvestment should fall into either programs under the encouraged section of the “Catalogue of Foreign Investment Industry Guidance” or “Catalogue of Preferential Industry for Foreign Investments in Central and Western Regions”, both of which were updated in 2017.
- Procedures to enjoy the preferential tax policy
 - Foreign investors that meet the deferral conditions should file with tax authority in accordance with relevant tax collection and administration requirements and provide necessary documents to the profit-distributing enterprise in China;
 - The profit-distributing company would handle the procedures on behalf of the foreign investor for recording in competent tax authority without any WHT for the time being if all the conditions are satisfied during their adequate review;

- If the tax authority identifies ineligibility of the recorded transactions during subsequent administrative review, late fees could be levied in addition to WHT.
- Effective date and retroactive effect
 - Notice 88 clarifies that the policy would come into force and has a retroactive effect on 1st January 2017. For dividends, profits and other equity investment income distributed to foreign investors, on or after the effective date, which are eligible for WHT deferral, a refund for the tax already paid could be applied.
 - Moreover, any eligible foreign investors who have not enjoyed this preferential tax treatment can apply for the tax treatment retrospectively and claim the tax refunds within 3 years from the payment date.

The release of WHT deferral for reinvestment of distributed profit in China would have a significant impact on the investment strategy of foreign investors, especially to multinational corporations. There is no doubt that overseas investors will increasingly consider expanding their investment to China in the foreseeable future.

Revision of Customs Law

On 4th November 2017, the Standing Committee of the National People's Congress (“NPC”) has completed the revision of the Customs Law of China, which is the fifth amendment since its first release in 1987. The update to the Customs Law is mainly based on Announcement 45 (“Announcement 45”) which was jointly issued by the MOC and the General Administration of Customs (“GAC”) in August 2016. Announcement 45 formally abolished the examination and approval procedures of processing trade operations (See “China Business Advisory 2016 Issue 9”).

The key changes to the Customs Law are highlighted as follows:

- **Modified requirements of processing trade enterprises (“PTEs”) for customs filing**

There is no longer a need for PTEs to apply for approval of the commercial authority. They are however required to go through the formalities for filing in accordance with the requirements of the GAC.

- **Removal of procedures for domestic sales of bonded processing materials and finished goods**

As Announcement 45 has cancelled the approval procedures of the commercial authority for domestic sale of bonded processing materials and finished goods, this update is conforming to the actual need of PTEs and would relieve the examination and approval stress of the Customs accordingly.

With effect from 5th November 2017, the revision of the Customs Law would simplify the Customs administrative procedures and improve enterprises’ efficiency. Meanwhile, enterprises should also pay attention to the local implementation of relevant updates.

Implementation of the Investment Agreement under CEPA with Hong Kong and Macau

Approved by the SC, China signed two investment agreements under Closer Economic Partnership Arrangement (“CEPA”) with Hong Kong and Macau on 28th June 2017 and 18th December 2017 respectively. Both came into effect on 1st January 2018. CEPA is a free trade agreement concluded

by Mainland China and Hong Kong/Macau, which covers all parts of economic and trade exchanges and greatly promotes development and corporation in all parties. As new sub-agreements under CEPA, the investment agreements cover fully the areas of market access, investment treatment, settlement of dispute and investment promotion.

In order to facilitate the implementation of the Investment Agreements, MOC Announcement [2017] No.86 was issued by MOC on 20th December 2017. The key contents of the announcement are as follows:

- Hong Kong and Macau investors who intend to invest in Mainland based on the investment agreement shall follow the establishment and alternation record filing procedures and regulations stated in “Provisional Regulations on Record Filings for the Establishment and Alteration of Foreign Investment Enterprise” (“Provisional Regulations”);
- Hong Kong and Macau investors where Appendix 1 of the investment agreement is applicable to must only access fields opened to Hong Kong and Macau investors respectively. In addition to the documents required by the Provisional Regulations, these investors should also submit the relevant identity proof documents online according to the investment agreement.

The investment agreements are of great significance to protect the rights and interests of investors and promote the gradual realization of investment liberalization and greater cooperation between China, Hong Kong and Macau.

Service Highlight

The Chinese government has been incurring continuous effort to improve domestic regulations and simplify the administrative processes in order to enhance the business environment for foreign investors. More positive changes in policies and regulations are expected to follow. Sino-Bridge is always well prepared and pleased to help investors to realize their full potentials. Our Marketing Executive, Ms. Kimme Chan, would like to hear from you at (852) 3579 8745 or kimmechan@sinobridge-consulting.com to learn of how we can assist you with your business plan.

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