China Tax & Investment Express

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Tax circulars

- **Notice regarding certain issues related to Corporate Income Tax (CIT) on gains derived from indirect transfers of assets by non-residents (SAT Announcement [2015] No. 7)**

**Synopsis**

Pursuant to Guoshuihan [2009] No. 698 (“Circular 698”, i.e., Notice regarding the CIT administration of share transfers by non-residents), on 3 February 2015, the State Administration of Taxation (SAT) released SAT Announcement [2015] No. 7 (“Announcement 7”) to provide further clarification in various areas, such as the definition of reasonable business purpose, safe harbor rules for group restructuring, and certain administrative procedures. Announcement 7 also expands the applicable scope of indirect transfer taxation and introduces new measures and requirements on filing and tax administration. (Please refer to China Tax & Investment News (CTIN) Issues No. 2009011, 2010003, 2011004, 2013001 and 2013002 for details of Circular 698.)

Key points of Announcement 7 include:

- Applicable scope
- Business purpose test
- Safe harbor rules
- Reporting and documentation requirements
- PRC tax implications
- Withholding obligation on buyers
- Administrations
- Penalty for noncompliance
- Interaction with Administrative Measures for General Anti-avoidance Rules
Notice regarding Value-Added Tax (VAT) policies related to the subsequent free use of newly developed medicines (Caishui [2015] No. 4)

Synopsis

To encourage research and development as well as the adoption of newly developed medicines after clinical trial, on 26 January 2015, the Ministry of Finance (MOF) and SAT jointly released Caishui [2015] No. 4 (“Circular 4”) which announced relevant VAT policies in this regard.

Turnover of pharmaceutical manufacturing enterprises includes all sales consideration and any additional income received from customers. However, the subsequent free supply of newly developed medicines to patients for clinical trial purposes shall not be considered as deemed sales for VAT. “Newly developed medicines” means active pharmaceutical ingredients and preparations registered and approved by the China Food and Drug Administration as prescribed in Circular 4.

Circular 4 also sets out the documents that pharmaceutical manufacturers should maintain for the aforementioned free of charge supplies in case of tax inspections.

Circular 4 became effective on 1 January 2015 and applies to any open tax matter.

You can click this link to access the full content of Circular 4:
http://szs.mof.gov.cn/zhengwuxinxi/zhengcefabu/201502/t20150204_1188417.html

Notice regarding certain issues related to the collection and administration of Consumption Tax (CT) on battery and paint (SAT Announcement [2015] No. 5)

Notice regarding the collection of import-level CT on battery and paint (GAC Announcement [2015] No. 4)

Synopsis

Pursuant to Caishui [2015] No. 16 (“Circular 16”, i.e., Notice regarding CT collection on battery and paint), on 30 January 2015, the SAT released SAT Announcement [2015] No. 5 (“Announcement 5”) to specify the following issues related to CT filing on battery and paints (please refer to CTIE2015004 for details of Circular 16):

CT registration and filing

- Taxpayers engaged in manufacturing, entrusted processing and importation of batteries and paint (hereinafter referred to as the “CT taxable products”) as prescribed in Article 1 of Circular 16 are required to complete CT registration with their local tax offices. A detailed CT registration process and timeline will be determined by state tax bureaus at the provincial level.

- The aforementioned taxpayers should complete CT returns for batteries (Attachment II of Announcement 5) or CT returns for paint (Attachment III of Announcement 5) for CT filing purposes.
Entrusted processing

Where taxpayers obtain CT taxable products through entrusted processing and resell the products at a price higher than the taxable price adopted by the consignees, the taxpayers are subject to CT according to the prevailing CT policies and the CT withheld by the consignees can be credited.

Documentation maintenance

Tax payment vouchers for withholding purposes (《税收缴款书 (代扣代收专用)》) supporting the credited CT amounts are required to be maintained by taxpayers on a monthly basis. Also, taxpayers are required to establish written ledgers recording the creditable CT amount on CT taxable products (Attachment I of Announcement 5).

Documentation requirements for tax exemption

For manufacturing or entrusted processing of products eligible for CT preferential policies as prescribed in Article 2 of Circular 16 (i.e., mercury-free non-rechargeable batteries, metal hydride nickel rechargeable batteries, lithium non-rechargeable batteries, lithium-ion rechargeable batteries, solar batteries, fuel cells, vanadium redox batteries and paint with emissions of volatile organic compounds during application not exceeding 420g/L, as well as lead rechargeable batteries1), taxpayers are required to submit inspection reports issued by qualifying product testing institutions as prescribed in Announcement 5 to their local tax bureaus.

On the same day, i.e., 30 January 2015, the General Administration of Customs (GAC) also released GAC Announcement [2015] No. 4 ("Announcement 4") to specify the collection issues of import-level CT on CT taxable products as prescribed in Circular 16 from an import-level CT perspective and announce the HS codes for the relevant CT taxable products.

Announcements 4 and 5 both became effective on 1 February 2015.

1 According to Circular 16, the aforesaid products shall be exempt from CT except for lead rechargeable batteries. CT collection on lead batteries shall be postponed until 2016, when CT shall be collected at 4% of its VAT-exclusive sales amount from 1 January 2016.

Notice regarding certain CT filing issues related to refined oil (SAT Announcement [2015] No. 3)

Synopsis

Pursuant to Caishui [2015] No. 11 ("Circular 11", i.e., Notice regarding further increase in per unit rates of CT on refined oil), on 29 January 2015, the SAT released SAT Announcement [2015] No. 3 ("Announcement 3") to specify the following CT filing requirements (please refer to CTIE2015003 for details of Circular 11):

Starting from January 2015, taxpayers should complete and file updated CT returns for refined oil (i.e., Attachment I of Announcement 3), which add columns with applicable unit rates for refined oil in the lead sheet and CT withholding sheet.

Taxpayers are required to complete stock reports for refined oil for the period from 13 December 2014 to 12 January 2015 manually (i.e., Attachment II of Announcement 3) and file same to the tax bureaus in charge as supporting documents for the CT filing for January 2015.

Announcement 3 became effective on its promulgation date, i.e., 29 January 2015.
Notice regarding further regulating tax collection and administration and improving the quality of tax revenue (Shuizonghan [2015] No. 79)

Synopsis

On 5 February 2015, the SAT released Shuizonghan [2015] No. 79 (“Circular 79”) to urge tax authorities at all levels to further regulate tax collection and administration and improve the quality of tax revenue.

Circular 79 calls for the establishment of statutory principles of taxation, proper implementation of tax preferential policies, reinforcing quality control on tax collection as well as strengthening the supervision of performances of subordinated tax bureaus.

Circular 79 reiterates the requirement to regulate and implement tax preferential policies properly, which was echoed the State Council’s message on the same through Guofa [2014] No. 62 (“Circular 62”, i.e., Notice regarding cleaning up and regulating various taxes and other preferential policies). Both regulations provide that Tax exemption/reduction granted to taxpayers without proper delegation shall be strictly prohibited.

Business circular

Notice regarding the pilot run of cross-border foreign exchange payments by payment institutions (Huifa [2015] No. 7)

Synopsis

To facilitate e-commerce transactions via the internet by domestic institutions and individuals, regulate cross-border foreign exchange payments by payment institutions and prevent risks of cross-border fund flows via the internet, on 20 January 2015, the State Administration of Foreign Exchange (SAFE) announced the Guiding Opinions on the Pilot Run of Cross-border Foreign Exchange Payments by Payment Institutions through Huifa [2015] No. 7 (“Circular 7”). Circular 7 came into effect on its promulgation date and superseded Huizongfa [2013] No. 5 (“Circular 5”, i.e., Notice regarding the pilot run of foreign exchange payments for cross-border e-commerce by payment institutions.)

Key points of Circular 7 are as follows:

Definition of cross-border foreign exchange payments by payment institutions

Cross-border foreign exchange payments by payment institutions refers to the arrangement that payment institutions provide through banks centralized foreign exchange collection/payments and relevant exchange settlement/sales services to both parties of e-commerce (commodity trade or service trade) transactions involved in cross-border internet payments.
Registration under the directory of companies engaging in foreign exchange collection and payments for trade purposes (hereinafter referred to as “Directory”)

Payment institutions meeting the following conditions can conduct cross-border foreign exchange payment business on a pilot basis upon completion of the registration under the Directory. No separate registration is required for payment institutions that have started the aforesaid business before the enforcement of Circular 7.

- Must have obtained payment business licenses issued by the People's Bank of China (PBOC); the approved business scope covers internet payments
- Must not have significantly violated RMB and foreign exchange administration rules in the most recent two years
- Must have full-fledged organization structures, business process rules and risk management systems
- Must meet technical conditions for collecting and retaining transaction information and data; must be able to ensure the authenticity and safety of transactions

Circular 7 also sets out the documentation requirements and application procedures for registration under the Directory.

Business management

- Payment institutions should strictly review the authenticity of identity information of their clients participating in cross-border foreign exchange payment business and retain relevant information for five years for future review.
- Cross-border foreign exchange payment business should be conducted for authentic and legitimate commodity and service trade transactions.
- The amount of a single cross-border transaction shall not exceed the equivalent of USD50,000, unless otherwise prescribed.
- When providing cross-border foreign exchange payment services, payment institutions shall allow their clients to use RMB or self-owned foreign exchange for payments.

Account management

- Payment institutions must open accounts for foreign exchange reserves (外汇备付金账户) with banks by presenting the Directory documents issued by the foreign exchange authorities they have registered with. Payment institutions should conduct exchange settlement/sales and cross-border foreign exchange collection/payments for their clients through the aforesaid accounts.
- Accounts for foreign exchange reserves shall not be used for cash withdrawal and deposits. Advance collection and advance deposits without commercial substance are also not allowed.
- Payment institutions must choose commercial banks qualifying for custody of clients’ reserves to open accounts for foreign exchange reserves. Payment institutions can choose foreign exchange reserves cooperative banks according to their business needs at their sole discretion.

Information collection

Payment institutions must submit data and information of relevant businesses to foreign exchange authorities according to the requirements of Circular 7 and ensure the accuracy, completeness and consistency of the data. Banks should submit relevant information based on data provided by payment institutions according to the relevant rules.

Supervision and inspection

According to Circular 7 and relevant foreign exchange rules, local foreign exchange authorities should perform prudent supervision and administration of the aforesaid pilot businesses, and conduct off-site or field inspections of cross-border foreign exchange payment businesses of payment institutions within their jurisdictions. Payment institutions and banks are obliged to cooperate in the supervision and administration of foreign exchange authorities.
Our observations

In recent years, China has been rapidly developing e-commerce businesses. To support the development of cross-border e-commerce, to regulate cross-border internet payments by payment institutions and prevent risks of foreign exchange payments via internet, the SAFE released Circular 5 launching a pilot run of cross-border e-commerce foreign exchange payments in five areas including Shanghai, Beijing, Chongqing, Zhejiang and Shenzhen. Following the success of the pilot in the five regions, the SAFE released Circular 7 expanding the program nationwide.

Compared to Circular 5, Circular 7 further improves foreign exchange administration of cross-border foreign exchange payment businesses in the following respects:

- Increases the upper limit for a single cross-border transaction from USD10,000 to USD50,000 to facilitate online shopping.
- Relaxes restrictions on the number of accounts for foreign exchange reserves. Under Circular 5, a payment institution must choose a domestic RMB reserves custodian bank to open one account for foreign exchange reserves. In the meantime, a payment institution can choose no more than three domestic commercial banks as their reserves cooperative banks according to business needs; only one account for foreign exchange reserves can be opened with each reserves cooperative bank. Circular 7 removes the above restrictions.
- Regulates the procedures of the aforesaid pilot business. Payment institutions are required to apply to foreign exchange authorities for registration under the Directory in order to conduct a cross-border foreign exchange payment business.
- Tightens up risk management. Circular 7 requires payment institutions to exercise their responsibilities to perform an authenticity review on relevant transactions, retain relevant information for five years for future review and submit data and information in an accurate and timely manner. In addition, foreign exchange authorities shall perform off-site or field inspections and prudent supervision of the pilot business.

Circular 7 is good news for the cross-border e-commerce market. Relevant institutions having an interest in this area should study Circular 7 carefully to explore new business opportunities; while existing payment institutions should also become familiar with this circular to ensure full compliance with the law. If in doubt, please consult with a tax professional.

You can click this link to access the full content of Circular 7:

You can click this link to access the full content of Circular 5:

You can click this link to access the full content of Announcement 6:

2 Pursuant to PBOC Announcement [2013] No. 6 (“Announcement 6”, i.e., Measures for the Custody of Client’s Reserves of Payment Institutions), “reserve bank” means a domestic banking financial institution that has entered into agreements with payment institutions to provide custodian services for client’s reserves, which includes (i) a reserve custodian bank (providing inter-bank receipt and payment of client’s reserves for payment institutions) or (ii) a reserve cooperative bank (receiving clients’ reserves for a payment institution and paying with clients’ reserves deposited therein).
Other business and tax related circulars recently announced by the central government authorities:

- **Notice regarding certain issues related to the collection and administration of Vehicle Purchase Tax**  
  (SAT Announcement [2015] No. 4)  
  [http://www.chinatax.gov.cn/n810341/n810755/c1485828/content.html](http://www.chinatax.gov.cn/n810341/n810755/c1485828/content.html)

- **Notice regarding the "Administrative Measures for the Supervision of the Subordinate Tax Authorities (Trial)" (Shuizongfa [2015] No. 19)**  
  [http://www.chinatax.gov.cn/n810341/n810755/c1490524/content.html](http://www.chinatax.gov.cn/n810341/n810755/c1490524/content.html)

- **Notice regarding regulating and improving the administrative approval conducted by departments under the State Council (Guofa [2015] No. 6)**  
  [http://www.gov.cn/zhengce/content/2015-02/04/content_9454.htm](http://www.gov.cn/zhengce/content/2015-02/04/content_9454.htm)

- **Notice regarding certain issues related to the implementation of post-approval business registration of certified public accountant firms (Caikuai [2014] No. 30)**  
  [http://www.tjkj.gov.cn/platform/tjkj/contents.jsp?channelId=46&contentId=280283](http://www.tjkj.gov.cn/platform/tjkj/contents.jsp?channelId=46&contentId=280283)

- **Notice regarding the "Guidelines on the Auditing of Commercial Banks" (Kuaixie [2014] No. 77)**  
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