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Relevant industries: E-commerce industry
 Relevant companies: Companies carrying out e-commerce activities
 Relevant taxes: N/A

Potential impacts on businesses:

- Compliance risks due to regulatory uncertainties reduced
- Compliance costs increased

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Draft E-commerce Law in development

According to an item of news on the National People's Congress (NPC) official website, the *E-commerce Law of the People's Republic of China (Draft)* ("the Draft") was submitted to the NPC Standing Committee for a first review on 19 December 2016, though the document has not yet been published.

Explaining the Draft to lawmakers, Lv Zushan, deputy director with the NPC's Financial and Economic Affairs Committee, said booming e-commerce in recent years had served to reveal loopholes in China's legal system and commercial rules. The draft law will facilitate e-commerce growth, help maintain market order and protect consumer rights. Operators must also ensure personal information security for consumers. Those that fail will face fines up to RMB500,000 and could have their business certificates revoked.

An interpretation of the Draft has been released on the NPC website, and it describes how the Draft regulates a range of matters pertinent to e-commerce transactions and services, including particular issues for cross-border e-commerce, security issues, overall governmental supervision and management of e-commerce, and the legal responsibilities of e-commerce enterprises.

Activities within the scope of the law	<ul style="list-style-type: none"> • The definition of e-commerce is "business activities involving goods or service transactions conducted through the internet or other information network". Definitions of the scope of the above terms, for the purposes of the law, are provided. • <i>The Draft</i> explicitly excludes, from the scope of its provisions, provision of financial products and services, or content services such as audio and video programs via internet and network publishing.
E-commerce operators, their rights and responsibilities	<ul style="list-style-type: none"> • E-commerce operators subject to the law include third-party e-commerce platforms and e-commerce business dealers. • Third-party e-commerce platforms refer to those enterprises or bodies who provide web space, virtual business premises, information exchange services, or information publishing etc. to facilitate e-commerce activities.

E-commerce operators, their rights and responsibilities	<ul style="list-style-type: none"> • <i>The Draft</i> requires third-party e-commerce platforms to: <ul style="list-style-type: none"> ❖ Conduct formal examinations of business dealers which do transactions through the platform and provide stable and safe services; ❖ Develop transacting rules of the platform openly and transparently; ❖ Follow the requirements on publicizing important information and keeping transaction records; and ❖ Follow the requirements on business dealers' exit.
Cross-border e-commerce	<ul style="list-style-type: none"> • China encourages the development of cross-border e-commerce. • It will promote the establishment of a specialized administrative system that adapts to cross-border e-commerce activities, and improve the efficiency of customs clearance, safeguard trade security and promote trade facilitation. • It will also promote the online conduct of customs clearance, tax collection and inspection and quarantine procedures for cross-border e-commerce activities. • China will promote communication and cooperation between various countries on the regulation of cross-border e-commerce businesses.

Reference: N/A
 Issuance date: N/A
 Effective date: N/A

Relevant industries: N/A
 Relevant companies: Apple
 Relevant taxes: N/A

Potential impacts on businesses:

- Apple is challenged by EU for abuse of tax benefits and shall be subject to unpaid tax
- Uncertainties of international tax between the U.S. and Europe increased
- Risks of being challenged due to cross-border tax anti-avoidance arrangements of MNEs increased

You may click [here](#) to access full content of the case.

EU Commission decision on Apple State Aid tax case

As mentioned in KPMG [China Tax Weekly Update \(Issue 34, September 2016\)](#), the EU Commission had concluded that Ireland granted illegal state aid, in the amount of USD14.5 billion, to the US MNE Apple Inc. This was on the asserted basis that several Irish incorporated Apple subsidiaries benefitted from tax treatment preferential to that which would apply to other businesses in comparable circumstances, under the general provisions of Irish tax law. The consequent selective advantage was considered to distort competition in the EU, to be illegal state aid, and Ireland is required to recover this amount.

On 19 December 2016, the EU released their long-awaited legal reasoning. The [decision](#) is 130 pages in total and focuses on two rulings given to Apple by the Irish tax authorities. The Irish incorporated entities were considered, under Irish tax law, to be not tax resident in Ireland (i.e. to be "stateless entities") but to possess Irish branches. The legal reasoning examines whether the profit attribution to the Irish branches was at arm's-length. The EU Commission, in particular, disputes the position of Apple/the Irish government that the income associated with the IP of the Irish incorporated entities can be attributed to their head offices (which existed solely on paper and are 'stateless') rather than to their Irish branches.

The EU Commission's decision is being formally appealed and is expected to spend many years before the European courts. The case is very notable for many reasons including, (i) the very large tax amount at stake, (ii) the assertion by the EU Commission that an arm's length requirement is embedded in EU treaties, quite separate (and possibly different) from the arm's length standard in the OECD's TP Guidelines, (iii) the potential for EU-US tension resulting from the case, and consequent implications for global multilateral tax initiatives through the G20/OECD, (iv) legacy tax implications for other EU structures used by MNEs to manage their tax affairs, (v) stimulus to US corporate tax reform and (vi) the impact, going forward, on MNE preferences for other hub jurisdictions (e.g. Singapore) over EU hub jurisdictions.

Reference: Cai Shui[2016]

No. 140

Issuance date: 21 December 2016

Effective date: 1 May 2016

Relevant industries: All

Relevant companies: All

Relevant taxes: VAT

Potential impacts on businesses:

- Compliance risks due to regulatory uncertainties reduced

You may click [here](#) to access full content of the circular.

Further VAT implementation rules

On 21 December 2016, the Ministry of Finance (MOF) and State Administration of Taxation (SAT) jointly issued Cai Shui [2016] No. 140 ("Circular 140") which sets out new Value Added Tax (VAT) rules applicable to those sectors which recently transitioned from Business Tax (BT) to VAT, being financial services, real estate and construction services, and lifestyle services.

Circular 140 is retroactive to 1 May 2016 and provides that if a taxpayer has overpaid VAT in a prior period, it will be able to use the overpaid VAT to offset against VAT payable in the future.

- According to [Measures for Implementation of the Pilot Program of VAT Reform \(Cai Shui \[2016\] No. 36, "Circular 36"\)](#), issued in May 2016, the income derived from holding financial products, in the form of "a return on principal protected products, remuneration, fees for the use of funds, or other forms of compensation", is subject to VAT at the rate of 6 percent as loan service remuneration.
- Circular 140 now effectively creates a distinction between returns on principal protected products (subject to VAT at 6%), and returns from holding non-principal protected products (not subject to VAT).

"Returns on principal protected products, remuneration, fees for the use of funds, and other forms of compensation" is the term used in the VAT rules for the investment income which is explicitly stated in the contract, where the principal will be fully recovered upon maturity.

Circular 140 seeks to clarify the difference between returns on debt, and returns on non-debt instruments.

[If a taxpayer holds asset management products (such as funds, trusts, wealth management products) until maturity, the relevant income does not fall within the scope of financial products trading. (Such income would be subject to VAT at the rate of 6 percent as loan services if it is principal protected, or not subject to VAT if it is considered as non-principal protected.)]

- According to Circular 36, where a period of 90 days or more has expired from when interest was receivable but not received, the lender is not required to continue accounting for output VAT unless and until such time as the interest is actually paid. However, the output VAT applicable to interest which is receivable but not received during the initial 90 day period, cannot be reversed. The only taxpayers eligible under Circular 36 to apply a limited form of bad debt relief is "financial enterprises", which are defined as banks (including State-owned, collective, shareholding structure, equity joint venture, foreign-funded banks and banks with other ownership structures), urban credit cooperatives, rural credit cooperatives, trust investment companies and finance companies.

Circular 140 now extends this scope of eligible taxpayers beyond those covered by Circular 36 so as to include securities companies, insurance companies, financial leasing companies, securities funds management companies, securities investment funds and also other entities which are established with approval either by the People's Bank of China (PBOC), China Securities Regulatory Commission (CSRC) or China Insurance Regulatory Commission (CIRC) to engage in finance and insurance business.

Rules in relation to finance and insurance sectors

Rules in relation to finance and insurance sectors (Cont'd)	<ul style="list-style-type: none"> The asset manager shall be the VAT taxpayer in respect of all of the taxable activities occurring during the operating period of the asset management products. Losses from trading in financial products incurred in the period from January to April 2016 are allowed to be carried forward to the next filing period. This means the accrued losses incurred under the BT regime can be used, for output VAT calculation purposes, to offset any gains from trading in financial products derived under the new VAT regime for the period from May to December 2016.
Rules in relation to real estate industry	<ul style="list-style-type: none"> Circular 36 provides that when developers sell real estate, they are eligible to deduct from the sale proceeds the purchase price of land use rights from the local government authority in calculating their VAT liability. However, this does not apply where the simplified VAT method has been used. Circular 140 expands the scope of the deduction for "the purchase price of land use rights". The expanded scope includes: <ul style="list-style-type: none"> Land acquisition costs paid to the government; Resettlement compensation paid to the government, other individuals or entities when purchasing the land use rights; Initial land development costs paid to the government; and The purchase price of land use rights paid to the government. In practice, after a real estate developer obtains the land use rights, it will typically set up a separate project company to develop the land. Circular 140 clarifies that if all of conditions specified in Circular 140 are satisfied, the purchase price of the land use rights which is settled by the developer can be deducted by the project company.

For detail analysis of Circular 140 and its impacts on businesses, please refer to the following KPMG China Tax Alert:

[China Tax Alert: Significant retrospective changes introduced to clarify VAT reform policies \(Issue 38, December 2016\)](#)

Reference: Guo Fa [2016]

No.71

Issuance date: 11 December 2016

Effective date: 1 January 2016

Relevant industries: All

Relevant companies: All

Relevant taxes: VAT

Potential impacts on businesses:

- Compliance risks due to regulatory uncertainties reduced

You may click [here](#) to access full content of the circular.

State Council to adjust VAT rebates method

As mentioned in KPMG [China Tax Weekly Update \(Issue 46, December 2016\)](#), Premier Li Keqiang, at a State Council Committee meeting held on 29 November 2016, approved an allocation of VAT revenues to local governments to ensure their financial sustainability.

To carry out the decision above, the State Council issued Guo Fa [2016] No. 71 ("Circular 71") on 11 December 2016, to adjust the VAT revenue redistribution method. According to Circular 71, the current VAT rebating method, set since 1994, will be replaced by a method that the allocation of VAT revenues between local and central government levels will be carried out on a fixed basis, referring to the 2015 rates.

It will no longer add or deduct the amount of rebates to regions that see an increase or decrease in VAT revenue. The specific rebate amounts will be assessed and decided by the Ministry of Finance.

Reference: Guo Fa [2016]

No. 72

Issuance date: 20 December 2016

Effective date: 20 December 2016

Relevant industries: All

Relevant companies: All

Relevant taxes: N/A

Potential impacts on businesses:

- Compliance risks due to regulatory uncertainties reduced

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China releases 2016 Catalogue of Investment Projects

As mentioned in KPMG [China Tax Weekly Update \(Issue 48, December 2016\)](#), on 14 December 2016, the State Council issued regulations on approving and recordal filing in relation to physical asset investment projects in China. The investment projects affected by the new regulations are those in fixed asset investments made in China. It was noted at that time that the scope of projects requiring conferral with the approval authorities would be set out in the Catalogue of Investment Projects Subject to Governmental Approval. The new Catalogue would follow the so-called "negative list" approach.

On 20 December 2016, the State Council issued Guo Fa [2016] No. 72 ("Circular 72") and published the Catalogue of Investment Projects Subject to Governmental Approval (2016) ("the new Catalogue"), effective from the date of issuance. The investment projects included in the new Catalogue should go through the approval process, while others only need to do recordal filings.

Compared with the [Catalogue of Investment Projects Subject to Governmental Approval \(2014\)](#), the new Catalogue cancels or delegates approval authority for 17 items; of which, approval requirement for 2 items has been changed to recordal filing, and the approval authority for 15 items has been delegated to the local government (as opposed to needing central government approval).

Cancel pre-approval and change to recordal filing

- Cross-province (district or city) projects invested by China Railway Corporation and trunk projects in the national rail network
- Non cross-border independent road/railway bridges and tunnels projects mainly invested by China Railway Corporation

**Delegate
approval
authority to
local
government**

- New refinery, cross-province (district or city) local railway, national highway, independent road, bridges and tunnels, coal, ore and oil berths, container terminals, inland waterways, avionics hub, development for rare earth mine, coal to olefins, coal to methanol, smelting and separation of rare earth, newly-built cars (excluding pure electric passenger cars), motor vehicles, urban roads and bridges, tunnels, large theme parks etc.
- Restricted projects (excluding real estate) in the *Catalogue of Industries for Guiding Foreign Investment** with total investment (including capital increase) of USD 100 million (included) to USD 300 million. (Currently, restricted real estate projects and other restricted projects with total investment (including capital increase) below USD 100 million are being approved at provincial level)

* China has been in the process of revising its inbound investment rules. Following various pilot programs in certain localities, a new nationwide system for the administration of foreign investment approvals is being rolled out. Whereas previously, all foreign investment into China needed pre-approval by the Ministry of Commerce (MOFCOM), the new system generally allows for simple recordals to be made for investments in industries where foreign investment is encouraged/permited, with pre-approvals limited to industries where investment is restricted. This is the so-called "Negative List" system (under the "special administrative measures for foreign investment access") and it is effective from 1 October 2016. The Negative List is to set out the sectors which are prohibited/restricted, or for which pre-approvals may otherwise be needed (e.g. investments in the previous encouraged industrial sectors for which foreign investors are limited in terms of the percentage of equity they can hold in the Chinese investment entity, or in terms of a requirement for certain senior executives to be Chinese citizens). To complement this, the [Catalogue of Industries for Guiding Foreign Investment](#) ("the Catalogue"), which sets out the encouraged, restricted and prohibited industrial sectors, and which was last updated in 2015, is also evolving (permitted industries are those not listed). On 7 December 2016, the National Development and Reform Commission (NDRC) and MOFCOM issued a notice to solicit public opinions on a revised version of the Catalogue. For details, you may click KPMG [China Tax Weekly Update \(Issue 47, November 2016\)](#) for more.

Circular 72 also emphasized that industries plagued by serious overcapacity issues such as steel and iron, cement, boats and ships, and traditional fuel automotive projects are not allowed to apply for new production capacity projects, in an effort to better resolve the issue of excess capacity.

Reference: Shang Zi Han [2016] No.954

Issuance date: 13 December 2016

Effective date: N/A

Relevant industries: All

Relevant companies: FIEs

Relevant taxes: N/A

Potential impacts on businesses:

- Compliance risks due to regulatory uncertainties reduced
- Compliance costs increased

You may click [here](#) to access full content of the circular.

MOFCOM clarifies FIE establishment and alteration rules

As mentioned in [KPMG China Tax Weekly Update \(Issue 35, September 2016\)](#), from 1 October 2016, on a nationwide basis, establishment and alteration Foreign-invested enterprises (FIEs) that are not included in the “Negative List” shall solely be subject to recordal filing rather than to pre-approval. Further to this change, on 8 October 2016, the Ministry of Commerce (MOFCOM) issued *Interim Measures for Filing Administration of Establishment & Change of FIEs*, which shall take effect from the date of issuance ([KPMG China Tax Weekly Update \(Issue 39, October 2016\)](#)).

On 13 December 2016, MOFCOM further released Shang Zi Han [2016] No. 954. This is to clarify supervision and inspection measures on the establishment and alteration of FIEs.

- Local departments of commerce shall carry out inspections with choice of cases based primarily on random selection. An annual random inspection plan is to be prepared and the frequency of inspections shall be no less than twice a year for an enterprise.
- During the course of supervision and inspection, where the local department of commerce discovers that an inspection target may have committed illegal activities or a legal violation which does not fall under the administrative duties of the commerce authorities, the commerce authorities shall notify the relevant authorities (SAT, General Administration of Customs (GAC), State Administration for Industry and Commerce (SAIC), State Administration for Foreign Exchange (SAFE), etc.) promptly. The Commerce authorities shall share above information through Foreign Investment Integrity Files System with other relevant authorities.



Roll-type ordinary VAT invoice to be introduced

On 13 December 2016, the SAT issued Announcement [2016] No. 82 to clarify that the ordinary VAT invoice (roll type) will be introduced from 1 January 2017. The roll-type ordinary VAT invoice is optional for the taxpayers and will be promoted and applied primarily in the life service areas.

You may click [here](#) to access the full content of the circular.

Vehicle purchase tax on passenger cars clarified

On 13 December 2016, the MOF and the SAT jointly issued Cai Shui [2016] No. 136 ("Circular 136") to clarify that, between 1 January 2017 and 31 December 2017, vehicle purchase tax on passenger cars with 1.6L or lower displacement will be levied by the tax rate of 7.5%. Beginning from 1 January 2018, the 10% statutory tax rate of vehicle purchase tax will be resumed. For vehicle purchase tax policy of new energy vehicles, [Announcement on Exemption of Vehicle Purchase Tax on New Energy Vehicles \(MOF, SAT, and Ministry of Industry and Information Technology Announcement \[2014\] No. 53, Announcement 53\)](#) is still applied to. Announcement 53 stipulates that new energy vehicles purchased will be exempt from vehicle purchase tax from 1 September 2014 to 31 December 2017.

You may click [here](#) to access the full content of the circular.

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