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Relevant companies: All
Relevant taxes: VAT

Potential impacts on businesses:

- Operational costs reduced

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Further development on China's VAT system in 2017

As highlighted in KPMG *China Tax Weekly Update (Issue 10, March 2017)*, Premier Li Keqiang delivered the *2017 Report on the Work of the Government,* at the opening of the 5th session of 12th National People's Congress (NPC) on 5 March 2017. In this he noted that China will build further upon the progress made with the 2016 VAT reforms, and simplify the VAT rate structure with a reduction in the four current VAT brackets to three in 2017.

On 12 March 2017, Mr. Wang Jun, Director of the State Administration of Taxation (SAT), further clarified the future VAT reform plans at a press conference on the sidelines of the 5th session of China's 12th NPC. He confirmed the reduction in the number of VAT brackets – tax commentators anticipate that the 13% rate bracket, which applies to some food products and water, may be consolidated into the 11% rate bracket, though this remains to be confirmed.

With respect to transitional rules on the usage of input VAT credits where transactions straddle the commencement of the May 2016 VAT reforms, Mr. Wang made a number of clarifications. Pursuant to Cai Shui [2016] No. 36, where real estate is purchased on or after 1 May 2016, where the purchaser is registered as a general VAT taxpayer, and where the supply was subject to the 11% VAT rate, then purchaser may claim an input VAT credit in its VAT return. However, a special rule 'spreads' the input VAT credit over a 2 year period following the purchase, with 60% of the input VAT credit claimable in year 1, and the remaining 40% claimable in year 2. Mr. Wang clarified that the remaining 40% claimable input VAT incurred by new real estate purchased in 2016, can be carried forwarded to 2017 and claimed.

Mr. Wang also indicated that a preferred transitional VAT treatment for certain real estate projects, underway at the time of the 2016 VAT reform, might be extended to cover further projects. Under the preferred transitional VAT treatment 'old' real estate projects (i.e. those commenced prior to the May 2016 VAT reform rollout) can benefit from a 5% simplified VAT rate, as compared with 'new' real estate projects, which are subject to an 11% VAT rate. The 5% VAT rate is intended to mirror the 5% Business Tax rate which applied, pre-May 2016 VAT reform. As time passes, ever more projects will be subject to the 11% VAT rate. As this increase in rate can lead to challenges for transitioning businesses, the SAT are apparently, per Mr. Wang's remarks, considering further regulations that may be helpful to affected taxpayers.

Per a supplemental official news posting on 13 March 2017, Mr. Wang Jun also indicated that the SAT will promote greater use of the tax credit rating system. Under this taxpayers are given a certain rating by the SAT – for example, A, B, C etc. The rating is determined by a taxpayer's history of compliance with their tax obligations. Tax and other incentives (such as rapid administrative approvals) are being made contingent on taxpayers having better ratings.

Ratings systems for taxpayers are already applied in a number countries around the world and have generally been very successful. They tend to have a dual effect in that: (i) they encourage tax authorities to focus their limited resources in terms of audits and investigations on taxpayers who have a higher risk of non-compliance, whilst recognising that taxpayers with a good rating will generally voluntarily be compliant; and (ii) they incentivise taxpayers to attain a good rating because this lowers their administrative compliance costs (e.g. they need less approvals), and therefore enables them to carry on business more efficiently. Increasing the tax authorities' use of such a rating system should be warmly welcomed by all businesses because it provides a clear return to those who do comply and invest in proactively managing their tax risks in China.

It appears that the SAT is targeting to introduce these measures during 2017, but the precise dates are not stated. We will monitor these matter and will keep you posted on any development.

* With regard to the relevant VAT reform policies, please see KPMG *China Tax Weekly Update* *(Issue 16, May 2016)*, *(Issue 49, December 2016)* for details.

** In the summer of 2016, 29 Chinese regulatory authorities jointly signed a cooperation memorandum under which they committed to grant more incentives to taxpayers with class-A tax credit rating. Many such incentives have been set out in the meantime. You may access KPMG *China Tax Weekly Update (Issue 27, July 2016)* for details. Regarding the administrative measures to classify and grade taxpayers, you may access KPMG *China Tax Weekly Update (Issue 33, August 2016)* for details.

*** VAT invoices obtained by general VAT taxpayers with class-A/B/C tax credit rating are now no longer required to be scanned for authentication. Please see KPMG *China Tax Weekly Update* *(Issue 6, February 2016)*, *(Issue 15, April 2016)* and *(Issue 45, December 2016)* for details.

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Relevant taxes: N/A

Potential impacts on businesses:
- Operational costs reduced

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China to move on business system reform

As highlighted in KPMG *China Tax Weekly Update (Issue 19, May 2016)*, at an executive meeting of the State Council held on 18 May 2016, several measures to push forward business system reform were identified. These included, in particular, the "five licenses into one, one license one code" reforms. To complement this, on 5 July 2016, the State Council issued Guo Ban Fa [2016] No. 53, inter alia, to: (i). officially launch the "five licenses into one, one license one code" reform from 1 October 2016 on a nationwide basis; (ii). set up a broader and deeper information sharing and collaboration mechanism between the local administrations of industry and commerce (AICs) and other government authorities (see KPMG *China Tax Weekly Update (Issue 26, July 2017)* for details).

On 10 March 2017, Mr. Zhang Mao, head of the State Administration for Industry and Commerce (SAIC), provided further relevant clarifications at a press conference held on the side lines of the 5th session of the 12th NPC. Mr. Zhang indicated that China will:

- Simplify market entry: It is planned to finalize the combination of multiple government registrations, licenses and permits into a single registration by 1 October 2017.
- Digitalize business licenses: Start issuing electronic business licenses by the end of 2017. Conventional paper business licenses will still be printed for those companies requiring them.
- Process for naming an enterprise: In the past, before a new Chinese enterprise could be established, it needed to go through a cumbersome name pre-approval process with the SAIC. The SAIC has since simplified and digitized the enterprise name registration process. Enterprises may search a desired name online through the enterprise name database platform - where the desired name is not already in use and is not prohibited it can be selected through the platform. Please refer to KPMG *China Tax Weekly Update (Issue 41, November 2016)*. AICs at county level were empowered to deal with name approval matters from 2016 onwards. Under the latest step, the national and provincial registration authorities shall open their name databases in 2017.
- Facilitate the use of simplified de-registration processes on a nationwide basis in 2017. These simplified processes should in particular be open to those enterprises that have not started their businesses, and those without heavy debt. (please refer to KPMG *China Tax Weekly Update (Issue 1, January 2017)* for more information about the simplified de-registration process reform).

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Relevant industries: Live streaming platforms
Relevant companies: Live streaming platforms
Relevant taxes: IIT

Potential impacts on businesses:
- Compliance risks increased

Taxing live streaming services

China's live-streaming sites have become a very popular form of entertainment in recent years. Individual 'hosts' chat and interact with viewers and these 'fans' can make voluntary cash gifts to the hosts, through the live streaming platform. The platforms take a cut of these gifts, with the remainder being cashed out by the hosts from the platform. The same holds for other sources of income of the hosts, including advertising income and remuneration from offline performances. Regulatory control of these sites has recently tightened with regard to content and now the tax authorities have tightened their scrutiny.

Recently more than RMB60 million (US$8.7 million) individual income tax (IIT) has been reported as being recovered by Beijing Chaoyang Local Tax Bureau from a live streaming platform. The latter had failed to withhold the IIT for its live streaming hosts in 2016. The tax authorities used "big data" analysis of several large live streaming platforms, covering their operational and tax payment data, to identify suspected non-compliance.

We would note several matters of note from this case of relevance to the future taxation of these and other digital business platforms:

- Chinese tax rules are unclear in relation to the taxation of live streaming, and the novel way in which these activities are monetized (e.g. voluntary gifts). In practice, some platforms regard host income to fall under the IIT category of "remuneration for personal services", and withhold IIT on this basis. By contrast, some of platforms treat this to fall under the IIT category of "incidental income", and apply withholding on a different basis. The tax treatment of newly emerging digital industries, with novel approaches to monetization, needs clarification.

- The draft E-commerce Law was submitted to the NPC Standing Committee for a first review on 19 December 2016. It regulates a range of matters pertinent to e-commerce third-party platforms, including the registration of the identities of parties using online platforms to sell goods or provide services. Approvals can be necessary, and ongoing monitoring is mandated. (see KPMG *China Tax Weekly Update (Issue 49, December 2016)* for details or click here to access full content of the draft E-commerce Law).

- In the draft Tax Administration and Collection Law (TACL), released in early 2015, provisions on internet e-commerce had been set out:

  (i). A taxpayer engaging online trading shall disclose information in respect of its tax registration certificate or a link to its tax registration certificate in a prominent position on it website homepage;

  (ii). Online trading platforms shall provide the registration information of e-commerce traders to the tax authorities; and

  (iii). Tax authorities are entitled to inspect online trading platforms and online payment service providers, when determining tax amount, conducting tax audits, and other administration matters.

  It might be noted that the State Council, in their 2017 legislation work plan released on 20 March 2017, identified the TACL as an urgent item for completion as soon as is practicable.

- All of the above show that the government, including the tax authorities, is determined to enhance the surveillance of emerging digital economy businesses, and a steady stream of additional guidance is anticipated going forward.

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