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Relevant industries: Private equity industries
Relevant companies: Private equity enterprises
Relevant taxes: N/A

Potential impacts on businesses:

- Compliance risks due to regulatory uncertainties reduced

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China to tighten regulation of private investment funds

On 30 August 2017, the legislative affairs office of the State Council issued the draft *Interim Regulations for the Administration of Private Investment Funds* (the "Draft") to solicit the public comments by 30 September 2017. The Draft clarifies the following:

General rules	• Private investment funds, a term encompassing both private equity funds and private securities funds managed by designated fund managers, are defined as investment funds established in China with capital raised from qualified investors, sourced otherwise than through public capital markets. The term 'private fund' is used in the Draft. • Under the existing 2014-issued *Interim Measures for Oversight of Private Funds* (CSRC Order No. 105), qualified investors in private funds mean organisations and individuals that possess the requisite risk identification ability and capacity for risk assumption, whose investment in a single private fund is not less than RMB1 million, and that meet the following standards: 1) organisations whose net assets are not less than RMB10 million; 2) individuals whose financial assets (such as deposits, shares, bonds) are not less than RMB3 million or whose average income for the past three years is not less than RMB500,000. • Private funds may be used for (i) investment in securities and derivatives; (ii) acquiring equity in limited liability companies; and (iii) other investments stipulated by China Securities Regulatory Commission (CSRC). The investments may be Chinese or foreign. • CSRC and its branches will oversee private fund activities, applying both the Securities Investment Law and the Draft.

Private fund managers	• Private fund managers must take the form of companies or partnerships. • Circumstances are set out under which (i) companies or partnerships are not allowed to act as private fund managers or major shareholders/partners in the private fund managers; (ii) persons are not allowed to assume roles as directors, supervisors, senior executives, managing partners and delegates of a private fund manager. • Private fund managers must not concurrently engage in (i) other businesses that are not relevant to the private fund management services; or (ii) other businesses that involve a potential conflict of interest with the private fund. • Private fund managers must complete the registration formalities with the Asset Management Association of China (AMAC) when the initial fund raising occurs.
Fund raising	• Private funds must be raised from specific qualified investors and interests in the funds can only be sold/transferred to such qualified investors. Intentional bypassing of qualified investor criteria is prohibited, such as by splitting/transferring fund units or rights to earnings in the private fund. • Private fund managers or private fund promoters/ sellers must not raise funds from non-qualified investors, exaggerate potential fund performance or make promises to investors concerning minimum income or no losses. • Private fund managers must make a recordal filing with AMAC within 20 working days of the completion of fund raising.

The Draft also sets out obligations for private fund custodians, rules for investment operation, provision of information, supervision and administration of private funds, and special provisions for venture capital investment funds.

* Asset manager VAT treatments was recently clarified in circulars Cai Shui [2016] No.140 (Circular 140) and Cai Shui [2017] No. 56 (Circular 56), issued by the Ministry of Finance (MOF) and State Administration of Taxation (SAT) in December 2016 and June 2017. These provide that private fund managers, which are classified as providers of asset management products, are the VAT taxpayers for private fund businesses and subject to the 3% simplified VAT method. However, a VAT exemption is provided for returns from holdings of non-principal protected financial products until maturity. For detail analysis of Circular 140 and Circular 56 as well as their impact on businesses, please refer to the following KPMG China Tax Alerts:

- ❑ *China Tax Alert: New VAT rules applicable to Asset Management Products (Issue 22, July 2017)*
- ❑ *China Tax Alert: Significant retrospective changes introduced to clarify VAT reform policies (Issue 38, December 2016)*

Reference: Yin Jian Fa [2017] No. 47
Issuance date: 25 August 2017
Effective date: 1 September 2017

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

Potential impacts on businesses:
- Compliance risks due to regulatory uncertainties reduced

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China commences trust registration

On 25 August 2017, the China Banking Regulatory Commission ("CBRC") issued *Administrative Measures on Trust Registration* (the "2017 Measures"). The 2017 Measures come into effect from 1 September 2017 and require trust companies as well as other institutions authorized by the banking regulatory authorities of the State Council to register trust products which they have created and issued. This is built on the 2014 CBRC measures (Yin Jian Ban Fa [2014] No. 99) and clarifies that:

- Trust registration includes pre-registration, initial registration and registrations for alteration/rectification of previously registered matters. Trust companies are required to record their trust products and beneficial owners of the products with the state-owned China Trust Registration Co., Ltd (China TRC). This was established in 2016 on approval of the State Council and CBRC.
- Set-up and administration of beneficial owners' accounts will be dealt with by China TRC. CBRC and other government authorities will be in a position to access these records. However the records will not be open to the public. It might be noted that there is a global trend towards establishing obligations for the registration/recordal of the beneficial ownership of trusts with public authorities, with the EU and OECD both developing rules and frameworks in this space. As such, China's new rules in line with the global trend, and should prove of use to efforts against tax evasion. It might be noted though that the proposals in some EU countries look to establish public registers of trust ownership – the Chinese trust register does not yet go this far.
- An unique code will be granted to the registered trust product by China TRC. This will facilitate regulatory authorities to oversee the whole business chain of the trust product.
- Basic information on trust plans involving pooled funds (funds from two or more investors) must be publicized by China TRC on their website.

A three-month transitional period is set out in the 2017 Measures. Where a new trust product is released in the course of the 1 September to 30 November 2017 period, both the 2017 Measures and the 2014 Measures (Yin Jian Ban Fa [2014] No. 99) may be applied. For an existing trust product, which is still in existence by 1 July 2018, the trust registration is also required.

Reference: N/A
Issuance date: 6 September 2017
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Relevant industries: Tobacco industry
Relevant companies: Tobacco enterprises
Relevant taxes: Tobacco Tax

Potential impacts on businesses:
- Compliance risks due to regulatory uncertainties reduced

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Draft Tobacco Tax Law in development

The Standing Committee of the National People's Congress (NPC) on 6 September 2017 reviewed the *Draft Tobacco Tax Law* (the "draft bill") and released the draft bill to solicit public comments by 5 October 2017. Placing existing Chinese taxes on a statutory basis is part of a wider Chinese government effort to reinforce the 'rule of law'. Taxes such as arable land occupation tax and VAT are also undergoing a similar transition.

Tobacco tax is currently based on 2006 State Council-issued rules and these will be replaced by statutory law issued by the NPC. Under the current rules, when taxpayers purchase tobacco leaves from tobacco growers, tobacco tax is triggered and is levied at 20% of the tobacco leaves purchase price. It should be noted that, an input VAT credit may be treated as arising from the purchase of tobacco leaves, and can be offset against the output VAT on onward sale of these tobacco leaves, or supplies made out of them, by the taxpayers. This is despite the fact that no VAT will have been levied on the supply from the tobacco growers to the initial purchaser of the tobacco leaves. The input VAT credit calculated by multiplying 13% by the purchase price plus the tobacco tax.

The framework of the existing tobacco tax, and its tax burden, will remain basically unchanged, but certain clarifications are made:

Taxpayers and taxable items	• Under the draft bill, the designated taxpayers subject to tobacco tax are the same as under the existing rules, i.e., an entity that engages in the purchase of tobacco leaves, shall be payer of tobacco tax. The draft bill gives further definition to "entity", i.e., entity refers to a tobacco company that has right to buy the tobacco leaves or an enterprise that is entrusted by the tobacco company to buy the tobacco leaves. • Under the draft bill, the taxable items are the same as those prescribed in the existing rules, i.e., the tobacco, including baked tobacco and aired tobacco, shall be subject to tobacco tax.
Tax basis	• The tobacco tax shall be computed based on the total sum that is actually paid by the taxpayer for the purchase of tobacco. The scope and standard for such total sum to be clarified by the State Council.
Tax rate	• In the draft bill, provisions on the tax rate remain unchanged, i.e., tobacco tax shall be levied at 20%.

In addition, the draft bill also clarifies the timing of tax liabilities, filing deadlines and location for tax filing and payment.

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