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Relevant industries: All
Relevant companies: All
Relevant taxes: All

Potential impacts on businesses:

- Operational costs reduced

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China tax reform - Next steps

Mr. Xiao Jie, the Chinese Minister of Finance, published an article entitled "Speeding up the Establishment of the Modern Fiscal System" in the People's Daily newspaper on 20 December 2017. The article highlighted further tax reform steps that China will take.

Improve direct tax system	• Set up a new individual income tax (IIT) system under which there will be "comprehensive and classified tax levying" of IIT. Under the "comprehensive and classified tax levying" system, individual income such as salaries and wages, and independent service income, will be consolidated for the tax calculation, and filings made on an annual basis (this would be a change from separate IIT calculation and levying for each of these income streams, on a monthly basis, as at present). At the same time, other income types such as dividends and interest, would continue to be taxed separately, at income-specific IIT rates (as at present). • The government will also optimize the IIT rate structure, improve IIT deductions, revise the IIT tax base and enhance IIT collection. In particular: ➢ IIT will be collected on a withholding and self-filing basis; ➢ Improve IIT collection measures and establish a comprehensive national system for collecting information on personal income and property holdings (see KPMG *China Tax Weekly Update (Issue 22, June 2017)* for more information about the system). • Enhance the corporate income tax (CIT) system to adapt to economic globalization and the requirements of the "Belt and Road Initiative". The changes will aim to enhance international tax coherence and the competitiveness of China's tax system. • Push forward the legislation and implementation of real estate tax (RET). RET will be levied based on assessed value for real estate property owned by industrial and commercial businesses and residential housing owned by individuals. The tax burdens currently imposed at the construction and trading stage would be commensurately reduced.

Improve indirect tax system	• Enhance the VAT reform according to tax neutrality principle, including: ➢ Improving the VAT creditable chain; ➢ Simplifying VAT rate structure; ➢ Improving VAT policies, such as VAT export refund rules; ➢ Put the VAT on a statutory basis (i.e., replacing the State Council-issued VAT regulation by statutory law). • Adjust the application of consumption tax (CT). • Adjust the tax revenue distribution between central and local government.
Push forward local taxation system reform	• Expand the scope of local taxes (currently, the existing local taxes include urban and township land use tax (UTLUT), RET, vehicle and vessel tax (VVT), arable land occupation tax (A LOT), deed tax (DT), tobacco tax (TT) and land appreciation tax (LAT)). • Expand water resource tax reform pilot areas (at present, this is being piloted in Hebei, Beijing, Tianjin, Shanxi, Inner Mongolia, Shandong, Henan, Sichuan, Shaanxi and Ningxia). • Improve urban maintenance and construction tax (UMCT). • Grant more power to local government (mainly at provincial level) to administer local taxes. • Put non-tax fiscal impositions (such as administrative fees, penalties, charges etc.) on a statutory basis, as taxes in place of fees. • Delegate administrative authority to local government to collect certain non-tax revenues.
Implement tax statutory principle	• All new taxes will be put on a statutory basis. • Replace the existing State Council-issued rules by statutory law issued by the National People’s Congress. • Strive to complete all the legislation processes by 2019 • By 2020, complete the “implementation of tax statutory principle” (i.e., all taxes will by 2020 be governed by statutory laws).

Reference: MOFCOM Announcement [2017] No. 86
Issuance date: 20 December 2017
Effective date: 1 January 2018

Relevant industries: All
Relevant companies: Enterprises under the CEPA
Relevant taxes: N/A

Potential impacts on businesses:

- Compliance costs reduced

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Recordal for investments made by Hong Kong/Macao investors

On 20 December 2017, the Ministry of Commerce (MOFCOM) issued Announcement [2017] No. 86 ("Announcement 86"). This sets out the recordal filing requirements for investments made in Mainland China enterprises by Hong Kong/Macao investors. This follows the implementation of the Investment Agreement under the framework of the Mainland and Hong Kong/Macao Closer Economic Partnership Arrangements ("CEPAs").

Mainland China entered into separate Investment Agreements with Hong Kong and Macao on 28 June 2017 and 18 December 2017, respectively. Both Investment Agreements will come into force from 1 January 2018 (see KPMG *China Tax Weekly Update (Issue 26, July 2017)* for more information about Mainland-Hong Kong Investment Agreement).

Announcement 86 clarifies the following recordal filing requirements for Hong Kong/Macao investors making investments in mainland enterprises after the implementation of the Investment Agreement:

- Where a Hong Kong (or Macao) investor makes an investment in a mainland enterprise, in accordance with the Hong Kong/Macao Investment Agreement, the recordal filing procedures for establishment or alteration (e.g. name changes, registered capital increases, and transfer of FIE equity interests between foreign investors) of the investee enterprise, shall be subject to the procedures and requirements set forth in the revised Interim Measures for Filing Administration of Establishment and Alteration of Foreign-invested Enterprises (FIEs) * (MOFCOM Order [2017] No. 2).
- The eligible Hong Kong/Macao investors are required to submit certificates evidencing that they are Hong Kong/Macao investors as well as the required documents set out in MOFCOM Order No. 2 (e.g. business license, equity structure chart of ultimate actual controlling party of the FIE).

* On 30 July 2017, MOFCOM issued MOFCOM Order [2017] No. 2 with the revised Interim Measures for Filing Administration of Establishment and Alteration of Foreign-invested Enterprises (FIEs) (the "July 2017 Interim Measures". The July 2017 Interim Measures came into force from the date of issuance and supercedes the Interim Measures for Filing Administration of Establishment & Alteration of FIEs ("October 2016 Interim Measures") issued by MOFCOM in October 2016.

The October 2016 Interim Measures had provided that the set up of new FIEs and alteration of FIEs would be subject to MOFCOM recordal filings rather than to MOFCOM pre-approval procedures, as was previously the case. This new measure applies nationwide and is extended to FIEs in sectors which were not on the national 'Negative List" (which sets out sectors which are restricted/prohibited to foreign investment and these sectors are specified in 2017 Catalogue of Industries for Guiding Foreign Investment). For FIEs in restricted sectors, the MOFCOM pre-approval process would still need to be followed (see KPMG *China Tax Weekly Update* *(Issue 26, July 2017)* and *(Issue 31, August 2017)* for more details).

Reference: Fa Gai Wai Zi [2017] No. 2050
Issuance date: 6 December 2017
Effective date: N/A

Relevant industries: All
Relevant companies: POEs embark on outbound investments
Relevant taxes: N/A

Potential impacts on businesses:
- Compliance requirements increased

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Private-Owned Enterprise (POE) outbound investment guidance

On 6 December 2017, the National Development and Reform Commission (NDRC) issued Fa Gai Wai Zi [2017] No. 2050, along with five other authorities including MOFCOM and People's Bank of China (PBOC). This sets out the guidance to regulate outbound investment activities made by private-owned enterprises (POEs). The notable guidance is as follows:

- The government supports POEs, which possess the necessary capabilities, to engage in outbound investment. Both POEs and state-owned enterprises (SOEs) will be treated on an equal basis, by the government, in relation to their conduct of outbound investments.
- POEs are encouraged, based on their capabilities, to make outbound investments, participate "Belt and Road" initiative and international industrial capacity cooperation projects, and promote the transformation and upgrade of Chinese economy.
- POEs which plan to engage in outbound investments are required to (i) set up an in-house department to administer their outbound investments; (ii) specify decision-making procedures for committing to outbound investments; (iii) establish a system to manage the set-up of overseas entities and improve their internal authorization system; and (iv) establish a system to control outbound investment risks.
- POE are required to (i) intensify supervision over their overseas entities in term of fund transfer, financing, equity (and other interest) transfer, reinvestment and guarantee; (ii) exercise prudence when making highly-leveraged overseas investments; and (iii) ensure that overseas derivatives investments are adequately monitored and managed.
- Where a POE's outbound investment is made in sensitive jurisdictions or industries (such as outbound investment in real estate, hotels, cinemas, entertainment, sports clubs and other specified restricted sectors), NDRC's pre-approval is required. Sensitive jurisdictions refer to those jurisdictions that: (i) have no diplomatic relationships with China; (ii) are at war (with China or a third country) or at civil war; and (iii) have agreed the restrictions in their bilateral/multilateral treaties or agreements concluded with China. Otherwise the recordal filing (without pre-approval) applies (i.e., NDRC will subsequently review whether the outbound investment project complies with relevant law and regulations, on the basis of the recordal).
- POEs are prohibited from engaging in foreign currency dealings, asset transfers, or money laundering, under the cover of simulated outbound investment transactions.

* The State Council on 18 August 2017 issued Guo Ban Fa [2017] No. 74 to further regulate outbound investment. The guidance was jointly issued by the NDRC, MOFCOM, PBOC and Ministry of Foreign Affairs (MFA), setting out the outbound investments that are encouraged, restricted and prohibited (see KPMG *China Tax Weekly Update (Issue 33, August 2017)* for more details).

Prior to that, MOF had issued Cai Zi [2017] No. 24, which seeks to upgrade the rigour with which Chinese SOEs evaluate their outbound investments and entered into force from 1 August 2017 (see KPMG *China Tax Weekly Update (Issue 31, August 2017)* for more details).

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