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China relaxes foreign exchange procedures on outbound payments for trade in services

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China's State Administration of Taxation (SAT) and the State Administration of Foreign Exchange (SAFE) jointly issued a bulletin in July 2013 (SAT/SAFE [2013] No. 40, (Bulletin 40)) that will ease the administrative procedures for making certain foreign exchange transactions.

The new rules, which will apply as from 1 September 2013, abolish the tax clearance certificate requirement for outbound payments exceeding USD 30,000 (or its equivalent) made with respect to trade in services and other items. Instead, domestic organizations and individuals (Applicants) that make such payments exceeding USD 50,000 (or its equivalent) will be required to submit a "Tax Filing Form" and relevant transaction documents to the competent state tax authorities. A copy of the Tax Filing Form will have to be provided to the bank before an offshore payment can be made.

In conjunction with Bulletin 40, the SAFE issued a circular (Huifa [2013] No. 30 (Circular 30)) that simplifies the administrative procedures for making payments offshore for the services trade and other items, and eliminates the requirement to present a tax clearance certificate to a bank when making a payment offshore for trade in services.

Background

Under existing rules (e.g. Huifa [2008] No. 64 and other circulars), an Applicant wishing to make a payment offshore for trade in services and other items exceeding USD 30,000 is required to obtain a tax clearance certificate from the competent state and local tax authorities before the payment is made. The tax certificate must be provided to the relevant bank to make the payment.

Obtaining a tax clearance certificate is not always a straightforward process, particularly if the Applicant and the competent state and local tax authorities are unable to reach an agreement on the relevant tax treatment of the payment. Consequently, cash can become "trapped" in China due to the inability to make such payments offshore timely.

The issuance of Bulletin 40 and Circular 30 eliminate the need for an advance "review" by the tax authorities before a payment exceeding USD 30,000 is to be made offshore for trade in services and other items, and the introduction of the tax reporting requirement (which also increases the monetary threshold to USD 50,000 (or its equivalent)) simplifies the administrative procedures.

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Highlights of Bulletin 40

1. Types of payments that require tax reporting – The types of payments that must be reported under the new rules generally are consistent with the current rules regulating payments that require a tax clearance certificate (see Appendix 1). Similarly, payments that will not be subject to the tax reporting requirement generally are the same as those not requiring a tax certificate under current rules.

2. Competent tax authorities – The new rules will require an Applicant to report only to the competent state tax authorities (rather than both state and local tax authorities). The competent state tax authorities will stamp the Tax Filing Form and return one stamped copy to the Applicant and deliver another copy to the competent local tax authorities. After the tax reporting procedure is completed, the Applicant must provide the stamped Tax Filing Form to the bank in order to make a payment offshore.

3. Documents – An applicant will be required to provide three copies of the Tax Filing Form and copies of relevant transaction documents (e.g. contracts with an official seal, etc.) to the state tax authorities. Transaction documents also have to be submitted under current rules.

4. Multiple payments – If multiple payments are required for the same contract, the Applicant must submit a Tax Filing Form for each payment. However, the relevant transaction documents only have to be submitted with the first tax reporting. Under current rules, a tax clearance certificate is required for each payment exceeding USD 30,000.

5. Review timeline – The state (and/or) local tax authorities will be required to review the tax treatment of the relevant payment within 15 working days after the Tax Filing Form and accompanying transaction documents are submitted. If necessary, the authorities can request additional information from the Applicant. The review will focus on the following areas:

   - Whether the information reported is consistent with the actual outbound payment;
   - Whether relevant taxes have been paid in accordance with Chinese law; and
   - Whether any tax reductions or exemptions applied are in accordance with relevant tax laws and applicable tax treaty.

   The rule seems to suggest that competent state or local tax authority is not required to render their decision on the tax treatment on the payment within 15 working days.

6. Effective date – Bulletin 40 and Circular 30 will apply as from 1 September 2013.

Although the tax certificate will no longer be required, Applicants will not be relieved from any of their normal tax obligations, such as tax registration, tax reporting, tax withholding and document reporting (if any) as required under relevant tax laws and regulations. Failure to comply with these rules could result in the tax authorities recovering any unpaid tax and imposing penalties.

Bulletin 40 is mainly a change in administrative emphasis to enable domestic entities to make outbound payments in a timely manner. It does not exempt the taxpayer or the withholding agent from their tax obligations. It also encourages the competent tax authorities to focus on a review of the tax-related matters after a tax reporting is made by an Applicant.

Appendix 1

The types of outbound payments that are subject to tax reporting under Bulletin 40 include most payments relating to income (other than those relating to trade in goods) derived by foreign organizations and individuals from China, such as the following:

- Income from services
  - transportation;
  - tourism;
  - communication;
  - construction, installation and contracted labor services;
  - insurance services;
  - financial services;
  - computer and information services;
  - licensing of patents, know-how, copyrights, etc., and franchising;
  - culture, sport and entertainment services;
  - other commercial services; and
  - government services.
- Salaries and wages;
- Dividends and profits;
- Direct debt interest;
- Guarantee fees;
- Rent paid under finance leases;
- Income from real estate transfers; and
- Income from equity transfers.

Where a foreign investor reinvests legitimate income obtained through a direct investment in China and the amount of a single reinvestment exceeds USD 50,000 (or its equivalent), a similar tax reporting obligation arises, as stipulated in Bulletin 40, even though no outbound payment is being made.

Note: Contents discussed in this Tax Analysis pertains to Deloitte International Tax Services

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