

Tax

Issue P406/2025 – 14 August 2025

Tax Analysis

Draft VAT law implementation regulations released for public consultation

To ensure a smooth implementation of the new VAT law, which is effective as from 1 January 2026, China's Ministry of Finance (MOF) and State Taxation Administration (STA) released draft implementation regulations on 11 August 2025. The draft regulations are open for public consultation until 10 September 2025.

The draft regulations would largely maintain continuity with the current VAT system by incorporating most existing policies. However, they also introduce key refinements, such as certain compliance requirements for allocating input VAT between projects with different VAT treatments and anti-avoidance rules. These proposed changes address practical operational needs and align with evolving priorities of tax administration.

Highlights of draft regulations

1. Cross-border transactions

Determination of "consumed in China"

The VAT law establishes a general principle that a service is deemed supplied within China if it is "consumed in China." The draft regulations would provide further clarification by defining this term to include the following situations:

Authors:

Candy Tang

Partner

Tel: +86 21 6141 1081

Email:

catang@deloittecn.com.cn

Charles Gong

Partner

Tel: +86 10 8520 7527

Email:

charlesgong@deloittecn.com.cn

Alex Guo

Senior Manager

Tel: +86 21 6141 1646

Email: aleguo@deloittecn.com.cn

Maggie Ding

Senior Manager

Tel: +86 21 2316 6620

Email: mding@deloittecn.com.cn

Sophie Lu

Manager

Tel: +86 10 8512 5531

Email: sophilu@deloittecn.com.cn

- Services supplied to a domestic entity or individual, unless the services are *consumed entirely overseas*;
- Services supplied by a foreign entity or individual, and the services are *directly related to goods, real estate, or natural resources in China*; and
- Other circumstances as stipulated by the MOF/STA.

To refine the rules for determining the place of consumption, the draft regulations would introduce new concepts, including "consumed entirely overseas" and "directly related to goods, real estate, or natural resources in China." Nevertheless, the interpretation and practical application of these concepts would likely present challenges, indicating that further guidance from the authorities may be necessary.

Withholding agents

The draft regulations stipulate that a foreign taxpayer leasing immovable property in China to an individual would be required to appoint a domestic agent to handle VAT filing and payment obligations.

However, the draft regulations do not specify whether this requirement would extend to other scenarios, such as when a foreign taxpayer provides other taxable services or intangible assets to domestic individuals. In the absence of a formal mechanism for appointing a domestic agent in these cases, it is left to be clarified by the government authorities whether the individual purchasers would act as VAT withholding agents.

2. "Deemed sales"

The VAT law has removed the free-of-charge services from the scope of transactions considered taxable under the "deemed sales" provisions. The draft regulations would not amend these rules further.

Consequently, there have been discussions about whether taxpayers would no longer be subject to the deemed sales rules in several common scenarios, such as provision of interest-free loans between related parties or rent-free leases. However, it remains uncertain whether some gratuitous service arrangements might still be challenged by tax authorities, for instance, whether they would question the truly "free" nature of a transaction and seek to recharacterize certain arrangements by applying the anti-avoidance rules.

For more information, please contact:

Indirect Tax National Leader

Lily Li

Partner

Tel: +86 21 6141 1099

Email: lilyxcli@deloittecn.com.cn

Northern/Western China

Marilyn Lu

Partner

Tel: +86 10 8520 7668

Email:

marilynlu@deloittecn.com.cn

Eastern China

Candy Tang

Partner

Tel: +86 21 6141 1081

Email:

catang@deloittecn.com.cn

Southern China

Janet Zhang

Partner

Tel: +86 20 2831 1212

Email:

jazhang@deloittecn.com.cn

3. Input VAT

Input VAT attributable to non-VATable transactions

The draft regulations introduce a new provision that would restrict the credit for input VAT attributable to non-VATable transactions, with exceptions only for the specific scenarios outlined in article 6 of the VAT law.

This proposed rule indicates that taxpayers may face stricter requirements to demonstrate a direct link between input VAT incurred and VATable supplies to claim credits.

Input VAT allocation

- *New annual reconciliation requirement:* For general VAT taxpayers, the VAT law requires the allocation of input VAT on goods (excluding long-term assets) and services used for both VATable transactions (subject to the general taxing method) and other transactions (including those subject to the simplified taxing method or that are VAT exempt). Input VAT allocated to other transactions is non-creditable.

Currently, the allocation is performed monthly or quarterly (depending on a taxpayer's VAT assessment period) based on input VAT and sales data of the respective period. In addition to that, the draft regulations would introduce an annual reconciliation. While taxpayers would continue to use the existing monthly or quarterly method for their periodic VAT filings, they would also be required to perform an annual adjustment in January of the following year based on full-year data. This proposed process is expected to increase the tax compliance costs for businesses.

- *Input VAT on long-term assets:* Under the current rules, input VAT on long-term assets (i.e. fixed assets, intangible assets and real estate) used for both VATable transactions (subject to the general taxing method) and other purposes (e.g., those subject to the simplified taxing method, VAT-exempt supplies, staff welfare, and private consumption) is fully creditable for general VAT taxpayers, with no allocation required.

The draft regulations, however, would introduce a significant change: an allocation requirement would apply to single long-term assets with an original value exceeding RMB 5 million. Although taxpayers may claim a full input VAT credit upon acquisition, they would be required to perform an annual reconciliation, reversing credits based on the asset's usage in different activities according to its depreciation or amortization schedule.

The draft regulations stipulate that further operational details would be issued by the MOF and STA. Key terms including the definition of "single long-term assets" await clarification in subsequent guidance. This new requirement could undoubtedly increase the compliance burden and demand greater sophistication in taxpayers' tax accounting systems.

Input VAT on interest

While the VAT law does not explicitly list input VAT on loan interest as non-creditable, the draft regulations would retain the current restrictive position. They would explicitly disallow the recovery of input VAT incurred on loan services and other costs directly related to loan arrangements, such as investment advisory or financing consultancy fees.

4. Mixed sales

A mixed sale is a single VAT transaction that is comprised of two or more elements that would be subject to different VAT rates if supplied separately. According to the VAT law, the VAT rate applicable to the principal element must be applied to the entire revenue derived from such a mixed sale.

The draft regulations would further clarify that the principal element should reflect the substance and purpose of the transaction, while any additional elements would serve as necessary supplements and arise only in conjunction with the principal element.

Mixed sales remain one of the most challenging areas in VAT practice, particularly regarding the disputes over whether a transaction should be treated as a single supply or multiple separate supplies, and how to identify the principal element. Although the general principles provided by the VAT law and draft regulations are a welcome development, taxpayers would benefit from additional guidance from the tax authorities (e.g., published cases, rulings, or detailed explanations) to facilitate a clearer understanding of how these rules should be applied in complex scenarios.

5. General anti-avoidance rule

Mirroring the approach in income tax laws, the draft regulations would introduce a general anti-avoidance rule. This provision would grant the tax authorities the power to attack arrangements that lack a genuine commercial purpose. As a result, taxpayers may need to evaluate potential tax risks and consider how to effectively demonstrate that their transactions are motivated by bona fide business reasons.

6. Miscellaneous

Business transfer

Neither the VAT law nor the draft regulations clarify whether the transfer of a business (or a part thereof) as a going concern would remain non-VATable. Furthermore, they provide no guidance on how to determine the input VAT attributable to such a transfer, should it be deemed non-VATable. It is generally expected that these matters may be addressed in the subsequent regulations to be issued by the tax authorities.

Preferential VAT treatment

To qualify for preferential VAT treatment on eligible projects, the draft regulations mandate that taxpayers would be required to maintain separate accounting not only for the revenue generated but also for the input VAT attributable to those projects. This proposed requirement further underscores the increasing compliance burden associated with input VAT management.

Exports of goods/services

Most exports of goods are exempt from VAT or qualify for zero-rating (under which relevant input VAT may be refunded). The draft regulations stipulate that exporters would be required to file for a VAT exemption or refund within 36 months from the date of customs declaration to secure such treatment. Failure to do so would result in the exports being treated as domestic taxable supplies. The draft regulations also would introduce a similar 36-month filing rule for exports of services that are eligible for a VAT exemption or zero-rating.

VAT refunds under the simplified taxing method

For taxpayers applying the simplified taxing method, current rules permit sales discounts, allowances, and returns (collectively referred to as deductible items) to be deducted from sales revenue when calculating VAT payable. However, if the total deductible items exceed the sales revenue, resulting in a net overpayment of VAT, the existing rules do not specify whether such overpayment may be refunded or must be carried forward to offset future VAT liabilities.

The draft regulations now clarify that taxpayers would be eligible to apply for a refund of the overpaid VAT amount, although detailed procedures for the refund process have yet to be established and published. This proposed clarification is expected to help alleviate cash flow pressures for certain taxpayers.

Comments

As the draft regulations are currently open for public consultation, businesses are encouraged to submit feedback to the relevant government authorities. It is also advisable for companies to evaluate the potential impact of the proposed provisions on their tax compliance obligations and business models, taking into account their specific industries and actual practices. Furthermore, enterprises should closely monitor the progress of the draft regulations and make adequate preparations to respond proactively to any forthcoming changes.

Tax Analysis is published for the clients and professionals of the Hong Kong and Chinese Mainland offices of Deloitte China. The contents are of a general nature only. Readers are advised to consult their tax advisors before acting on any information contained in this newsletter. For more information or advice on the above subject or analysis of other tax issues, please contact:

Country Leader of Tax and Business Advisory services, Deloitte China

Victor Li

Partner

Tel: +86 755 3353 8113

Fax: +86 755 8246 3222

Email: vicli@deloittecn.com.cn

Northern China

Xiaoli Huang

Partner

Tel: +86 10 8520 7707

Fax: +86 10 6508 8781

Email: xiaoli Huang@deloittecn.com.cn

Eastern China

Maria Liang

Partner

Tel: +86 21 6141 1059

Fax: +86 21 6335 0003

Email: mliang@deloittecn.com.cn

Southern China

Jennifer Zhang

Partner

Tel: +86 20 2885 8608

Fax: +86 20 3888 0115

Email: jenzhang@deloittecn.com.cn

Western China

Frank Tang

Partner

Tel: +86 23 8823 1208

Fax: +86 22 8312 6099

Email: ftang@deloittecn.com.cn

About the Deloitte China National Tax Technical Centre

The Deloitte China National Tax Technical Centre ("NTC") was established in 2006 to continuously improve the quality of Deloitte China's tax services and help Deloitte China's tax team better serve the clients. The Deloitte China NTC issues "Tax Analysis" which are commentaries on newly issued tax laws, regulations and circulars from technical perspectives. The Deloitte China NTC also conducts research and analysis and provides professional opinions on ambiguous and complex issues. For more information, please contact:

Northern/Western China

Tony Zhang

Partner

Tel: +86 28 6789 8008

Fax: +86 28 6317 3500

Email: tonzhang@deloittecn.com.cn

Eastern China

Kevin Zhu

Partner

Tel: +86 21 6141 1262

Fax: +86 21 6335 0003

Email: kzhu@deloittecn.com.cn

Southern China (Mainland)

Tony Yao

Partner

Tel: +86 755 3353 8103

Fax: +86 755 8246 3222

Email: heyao@deloittecn.com.cn

Southern China (Hong Kong)

Doris Chik

Partner

Tel: +852 2852 6608

Fax: +852 2543 4647

Email: dchik@deloitte.com.hk

If you prefer to receive future issues by soft copy or update us with your new correspondence details, please notify national marketing team of Deloitte China by email at cimchina@deloittecn.com.cn.

About Deloitte

Deloitte China provides integrated professional services, with our long-term commitment to be a leading contributor to China's reform, opening-up and economic development. We are a globally connected firm with deep roots locally, owned by our partners in China. With over 20,000 professionals across 31 Chinese cities, we provide our clients with a one-stop shop offering world-leading audit, tax and consulting services.

We serve with integrity, uphold quality and strive to innovate. With our professional excellence, insight across industries, and intelligent technology solutions, we help clients and partners from many sectors seize opportunities, tackle challenges and attain world-class, high-quality development goals.

The Deloitte brand originated in 1845, and its name in Chinese (德勤) denotes integrity, diligence and excellence. Deloitte's global professional network of member firms now spans more than 150 countries and territories. Through our mission to make an impact that matters, we help reinforce public trust in capital markets, enable clients to transform and thrive, empower talents to be future-ready, and lead the way toward a stronger economy, a more equitable society and a sustainable world.

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited ("DTTL"), its global network of member firms, and their related entities (collectively, the "Deloitte organization"). DTTL (also referred to as "Deloitte Global") and each of its member firms and related entities are legally separate and independent entities, which cannot obligate or bind each other in respect of third parties. DTTL and each DTTL member firm and related entity is liable only for its own acts and omissions, and not those of each other. DTTL does not provide services to clients. Please see www.deloitte.com/about to learn more.

Deloitte Asia Pacific Limited is a company limited by guarantee and a member firm of DTTL. Members of Deloitte Asia Pacific Limited and their related entities, each of which is a separate and independent legal entity, provide services from more than 100 cities across the region, including Auckland, Bangkok, Beijing, Bengaluru, Hanoi, Hong Kong, Jakarta, Kuala Lumpur, Manila, Melbourne, Mumbai, New Delhi, Osaka, Seoul, Shanghai, Singapore, Sydney, Taipei and Tokyo.

This communication contains general information only, and none of DTTL, its global network of member firms or their related entities is, by means of this communication, rendering professional advice or services. Before making any decision or taking any action that may affect your finances or your business, you should consult a qualified professional adviser.

No representations, warranties or undertakings (express or implied) are given as to the accuracy or completeness of the information in this communication, and none of DTTL, its member firms, related entities, employees or agents shall be liable or responsible for any loss or damage whatsoever arising directly or indirectly in connection with any person relying on this communication.

© 2025. For information, contact Deloitte China.