



CHINA AND KOREA SIGN BILATERAL ADVANCE PRICING AGREEMENT

China and South Korea have signed a third bilateral Advance Pricing Agreement (APA). The two countries have previously signed two APAs in November 2007. The APA was signed on 3 November 2009 by Xiao Jie from China's State Administration of Taxation and Yong-Ho Beak from South Korea's National Tax Office. The APA comes amidst campaigns to crack down on cross-border tax evasion by the tax authorities in both Korea and China. The APA should provide Chinese and Korean companies with more certainty in respect of cross-border business between the two countries

REMINDER: Transfer pricing Contemporaneous Documentation deadline ends 31 December 2009.

THE END OF OFF-SHORE SPVs IN CHINA?

On 4 November 2009 the State Administration for Taxation (SAT) issued a new notice (Guo Shui Han [2009] 601) (the "Notice") with respect to the interpretation of the term "beneficial ownership" in China's double taxation agreements (DTAs). This is just the most recent of a number of notices that the SAT have issued in the last few months in respect of the application of China's DTAs. It is a further indication that China's tax authorities intend to take a more aggressive approach to the review of cross-border transactions in the future.

Beneficial ownership is used in three articles of China DTAs – the dividends article (usually Article 10), the interest article (usually Article 11) and the royalties article (usually Article 12). The term operates in those article to establish the appropriate taxpayer entitled to access the benefits of the DTA. In China the concept of beneficial ownership does not have such an established meaning as it does in common law jurisdictions so the terms is capable of causing confusion. The Notice indicates that the critical factor in determining beneficial ownership is the right to own and dispose of the assets. The Notice expressly indicates that agent companies and companies which are set for transferring profits and conduct no business work are not qualified to be regarded as beneficial owners. This Notice suggests that the SAT will look-through interposed companies for determining who the appropriate beneficial owner is for the purpose of the relevant DTA. This may have a significant impact upon the use of off-shore Special Purpose Vehicles ("SPVs"). Traditionally the use of a Hong Kong SPV has been a very attractive model for structuring investments in China because any dividend, royalty or interest payments to Hong Kong resident companies attracts a lower tax rate under the Hong Kong-China DTA. This new Notice indicates that one of the attractive features of such an arrangement may no longer be available. This Notice is just the latest, and possibly most significant, step by the SAT to crack down on artificial arrangements that entered into for the purpose of reducing tax in China.

Circular 601 will be examined in greater detail in the November edition of *Hwuason Insights*, our detailed monthly analysis of China tax developments.

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IN FOCUS: TAX AND FOREX PAYMENTS

As most readers would be aware, China does not have a fully convertible currency. Under China's forex regulations when a domestic entity or resident individual make a non-trade forex payment (such as by way of telegraphic transfer) a tax certificate will be required to be supplied to the bank. A tax certificate will be required where the amount is above the specified threshold. The specified threshold from 1 January 2008 is USD30,000 for both entities and individuals (previously the threshold was USD1,000 for entities and USD500 for individuals). The taxation certificate is only required where the payment involves business tax or individual income tax (i.e. the payment is for a taxable service or the recipient is liable to individual income tax under Individual Income Tax Law). The administration of such tax certificates is handled by the relevant local tax bureau. The required tax certificate can come in 1 of 4 forms depending upon the circumstances; tax payment certificate, tax receipt, certificate of tax exemption or a certificate of non-taxable income. The tax certificate is not required where the transaction is entered into by an individual wholly for personal use (such as tuition fees). It is also not required for an entity where it relates to expenses incurred abroad (such as expenses for business trips).

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GOVERNMENT AUTHORITIES PLEDGE TO TARGET SALES OF SECOND-HAND CARS

Several Chinese government departments, including the SAT, have issued a joint notice in respect of better regulating the second-hand car market amidst concerns about current practices (the "Notice"). Concerns include the sale of stolen cars and the evasion of tax in such transactions. The Notice sets out the duties of each department in regulating the market and places significant emphasis on the importance of the second-hand car market to Chinese economy. The local taxation bureaus have instructed to take a progressive stance to ensure that tax is appropriately paid on such transactions.

VAT PAYABLE ON TRANSFER OF ASSETS TO SHAREHOLDER

The SAT has indicated that where a listed enterprise transfers assets to its controlling shareholder, they are required to pay VAT on the income of such a transfer. If the controlling shareholder subsequently transfers the assets to another company, VAT shall be additionally collected from the controlling shareholder.

DEED TAX ON PURCHASE OF LAND USE RIGHTS

The Beijing Local Tax Bureau has issued a clarification on the deed tax taxable price in respect of the purchase of land use rights. The clarification indicates that the taxable price will be all payments outlaid by the transferee in obtaining the relevant rights. The Deed Tax Law itself merely refers to the transactional price paid. This new clarification is presumably an attempt to crack down on anti-avoidance practices that seek to frame purchase prices as other types of payment.