

BEPS Actions implementation by country

China

On 5 October 2015, the G20/OECD published 13 final reports and an explanatory statement outlining consensus actions under the base erosion and profit shifting (BEPS) project. The output under each of the BEPS actions is intended to form a complete and cohesive approach covering domestic law recommendations and international principles under the OECD model tax treaty and transfer pricing guidelines. The G20/OECD output broadly falls into the following categories:

OECD categorisation	Definition
Minimum standard	All G20/OECD members are committed to consistent implementation
Revision of existing standard	
Common approach	Common approaches to facilitate convergence of national practices
Best practice	Guidance drawing on best practices

It is now for governments to digest and introduce the necessary legislation. The table below sets out a summary of the expected local country implementation and timing in China.



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Action	OECD categorisation	Notes on local country implementation	Expected timing
VAT on business to customers digital services (Action 1)	Common approach	No action currently is expected in relation to Action 1, but the tax authorities (SAT) and other government agencies are studying ways to tax the digital economy.	N/A
Hybrids (Action 2)	Common approach	The tax treatment of hybrids is being reviewed by the SAT. China's provisional list of reservations and notifications at the time it signed the multilateral instrument (MLI) on 7 June 2017 indicates that China has reserved the right not to apply article 3 of the MLI, which deals with hybrid mismatches, to all China's tax treaties.	N/A
CFCs (Action 3)	Best practice	China already has CFC rules, which are being reviewed as part of planned changes to existing guidance (i.e. Circular 2).	Expected during 2017
Interest deductions (Action 4)	Common approach	China uses thin capitalisation and transfer pricing rules to limit interest deductions, although these rules only cover interest paid between related parties. The Enterprise Income Tax (EIT) law uses a debt-to-equity ratio, rather than an interest expense-based ratio, as the relevant criteria.	N/A
Harmful tax practices (Action 5)	Minimum standard	The government is reviewing relevant regimes to ascertain whether they are affected by the Action 5 conclusions. The reduced EIT rate for high and new technology enterprises has been reviewed by the OECD and is not regarded as harmful, so no change is expected in the short term.	Ongoing

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Prevent treaty abuse (Action 6)	Minimum standard	<p>The recommendations in the Action 6 report are broadly in line with long-standing practices of the SAT.</p> <p>China's provisional list of reservations and notifications at the time it signed the MLI on 7 June 2017 indicates that it intends to include a PPT in its covered tax agreements. The SAT is also studying the "equivalent beneficiary" concept.</p>	Immediate (for existing practices)
Permanent establishment (PE) status (Action 7)	Revision of existing standard	<p>The PE discussion continues to be an area of focus in relation to agency PEs, e-commerce and the cross-border provision of services. The SAT considers that its current position regarding PE issues (contained in Circular 75) already reflect the Action 7 recommendations regarding the "agency PE" and the "preparatory or auxiliary" condition in relation to the article 5(4) exceptions and has therefore reserved the right not to apply the PE provisions in the MLI.</p> <p>Compliance with respect to PEs is expected to be enhanced, and the long-standing practice of attributing profits on a "deemed profit basis" is under review.</p>	Immediate (for existing practices)
Transfer pricing (Actions 8-10)	Revision of existing standard	<p>The recommendations in the Actions 8-10 reports are in line with long-standing practices of the SAT.</p> <p>The draft changes to Circular 2 would incorporate the recommendations, adapted as appropriate for China.</p> <p>Relevant provisions in Circular 2 are expected to be revised in a new circular(s).</p>	Not yet known
Disclosure of aggressive tax planning (Action 12)	Best practice	<p>The SAT is considering introducing mandatory disclosure rules into domestic law by revising the Tax Collection and Administration Law and its implementation rules.</p>	Subject to the reform of the relevant law, which is unlikely in 2017

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Transfer pricing documentation (Action 13)	Common approach	On 29 June 2016, the SAT issued a new regulation (Bulletin 42), which replaced the relevant requirement in Circular 2 relating to transfer pricing compliance (disclosure and documentation). It includes a three-tier contemporaneous documentation framework that includes the master file, local file and a special issue file. In particular, the local file requires a quantitative and qualitative value chain analysis.	As from the 2016 income tax year that commenced on 1 January 2016
CbC reporting (Action 13)	Minimum standard	Bulletin 42 introduced CbC reporting for qualified groups. The parent or designated entity is required to file a CbC form, along with the entity's annual EIT return. China is one of the countries that signed a multilateral competent authority agreement for the automatic exchange of CbC reports.	As from the 2016 income tax year that commenced on 1 January 2016

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Dispute resolution (Action 14)	Minimum standard Complemented by best practice	Action 14 conclusions present challenges for the Chinese tax system, which contains some ambiguous rules, such as the rules on tax suspension and the relationship between administrative remedies (e.g. the relationship between the mutual agreement procedure (MAP) and administrative review), etc. The SAT plans to take three actions in relation to Action 14: <ul style="list-style-type: none">• Strengthen the relevant legislation;• Improve accuracy and uniformity in local practice; and• Join the MAP forum to enhance cooperation with other countries.	Bulletin 64 applies from the 2016 income tax year, which commenced on 1 December 2016
		The SAT issued new regulations on advance pricing arrangements in October 2016.	Effective from 1 December 2016
Multilateral Instrument (Action 15)	Applicable across all four categories	China is one of the 68 countries that signed the MLI on 7 June 2017.	Not yet known

Unilateral BEPS Actions

Payments made offshore for service fees and royalties are under scrutiny based on Bulletin 6, and the tax authorities will monitor the profit level from related party transactions.

As mentioned above Bulletin 64 clarifies the relevant requirements on APA matters, such as the threshold of application, procedures for concluding APAs and application materials, etc., which also represent the proactive attitude of the SAT towards APAs.

The government has indicated that it will intensify its focus on offshore indirect transfers and will use all sources of information at its disposal to identify significant unreported transfers.

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The SAT appears to be looking more closely at potential cases of "disguised dividends," in particular, Chinese subsidiaries with large retained earnings that have not paid dividends for some years and that have large amounts of receivables owed by the offshore parent and/or affiliates.

The SAT is reviewing two situations relating to Action 2 (Hybrids):

- Hybrid instruments that are treated as debt in China but equity in the jurisdiction of a related party recipient; and
- Income derived by certain offshore branch structures of a Chinese enterprise.

Other Tax Developments

None.



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