



# Tax Newsflash

China

Deloitte Tohmatsu Tax Co.

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## Additional Guidance Issued on VAT Zero-Rated Services

China's State Administration of Taxation (SAT) announced new guidance (Bulletin 88<sup>1</sup>) on 21 December 2015 that supplements the Administrative Measures for VAT Refunds (Exemption) of Zero-Rated Services, which was originally issued via Bulletin [2014] No. 11<sup>2</sup>. Circular 118<sup>3</sup>, issued jointly by the Ministry of Finance and the SAT in October 2015, expanded the scope of zero-rated services. Bulletin 88 provides additional guidance relating to the services added to the list of zero-rated items by Circular 118 and clarifies several issues. Bulletin 88 applies retroactively from 1 December 2015, the same date that Circular 118 became effective.

### (1) Highlights of Bulletin 88

#### 1) Documentation requirements

In addition to the typical documents (e.g. service agreements, invoices, remittance receipts, etc.) that must be submitted with a request for a VAT refund for zero-rated services, Bulletin 88 introduces specific documentation requirements that must be met to receive a refund relating to the newly added services:

Services	Documents required
Software services, circuit design and testing services, information system services, business process management services and offshore outsourcing services provided to overseas companies	Certificate that proves that the service agreement has been recorded in the "Information System for Managing Service Outsourcing and Software Exports" and approved by the Ministry of Commerce
Production and distribution of radio, film and television programs (works) provided to overseas companies	Certificate that proves that the service agreement has been recorded in the "Management System for Trading of Culture-Related Items" and approved by the Ministry of Commerce, as well as film/television production and/or distribution permits and copyright certificates
Technology transfer services provided to overseas companies	Registration Certificate for Technology Export Contracts and the related data form

1 See [SAT Bulletin \[2015\] No. 88](#) (Chinese version)

2 See [SAT Bulletin \[2014\] No. 11](#) (Chinese version)

3 See "[VAT Zero-rated Services: Scope Expanded](#)" of [Tax Newsflash dated on 3 November 2015](#)

## 2) Documentation review

When tax officials are reviewing a taxpayer's documentation submitted to support a VAT refund claim for zero-rated services, Bulletin 11 required the reviewer to determine whether the foreign contracting party to the service agreement was the same party that paid the service charge to the service provider. Any discrepancy in the identity of the parties could result in a denial of the refund request. Bulletin 88 relaxes this requirement in the situation where the service fee is collected from the foreign recipient of the services by a domestic entity affiliated with the Chinese service provider and on its behalf under a group-centralized treasury arrangement. However, the service provider will have to submit supporting documentation to the tax authorities to demonstrate that the group/entity with which it is affiliated has obtained approval from the State Administration of Foreign Exchange or the People's Bank of China in respect of the arrangement.

Bulletin 11 requires the reviewer to ascertain whether the zero-rated income reported in the filing documents equals to or is lower than the amount agreed in the service contract. Bulletin 88 clarifies that, if the reported income is higher than the agreed service amount shown in the contract, the taxpayer will have to explain the disparity. The bulletin implies that zero-rated treatment and a VAT refund still may be granted on the excess amount if there is a reasonable explanation for the higher amount.

## 3) Late filings

According to Bulletin 11, the VAT refund request must be made by 30 April of the year following the year in which the relevant income was recognized for financial accounting purposes. Failure to file a timely claim will result in denial of zero-rated treatment and VAT will be charged.

Bulletin 88 introduces more flexible procedure that allows a taxpayer to apply for VAT-exempt treatment for the relevant supplies if the refund request was not made in a timely manner. With a VAT exemption filing, no VAT will be charged, but the taxpayer will not be able to recover the relevant input VAT.

## **(2) Deloitte's comments and recommendations**

The issuance of Bulletin 88 is welcome as it provides timely guidance for taxpayers to apply for the VAT refunds for services that now are entitled to zero-rated treatment. For certain items (e.g. offshore service outsourcing) that were moved from VAT-exempt to zero-rated treatment on 1 December 2015, the documentation required for a VAT refund under the zero-rated treatment generally are the same as the documentation previously required for VAT-exempt treatment.

Affected taxpayers should consider taking the following actions:

- Review current business operations and quantify the potential tax impact and compliance costs in order to assess the pros and cons of applying for VAT zero-rated treatment;
- If a decision is made to apply for zero-rated treatment, prepare the relevant documents and file the necessary refund claims in a timely manner;
- Consider any service projects that commenced before 1 December 2015 but were completed after that date because different VAT treatment may apply to the same project;
- Maintain communication with the relevant tax authorities with respect to the application of zero-rated treatment, request clarification of uncertain issues in a timely manner and seek professional assistance where needed.

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