Tax Newsflash

China

Deloitte Tohmatsu Tax Co.

May 15, 2015

SAT Issues Tax Audit Plans for 2015

Following a meeting held in March 2015, China's State Administration of Taxation (SAT) issued the nationwide tax audit plans for 2015. The plans set out the main sectors/industries that will be subject to an audit during calendar year 2015, as well as the timetable for local tax bureaus to provide reports to the SAT.

(1) Audit targets

Audit targets are divided into two categories: mandatory and "instructive" (the latter being sectors/industries where the SAT recommends that audits be conducted). In addition, the local tax bureaus have discretion to carry out tax audits on taxpayers in other sectors/industries.

1) Mandatory targets

The local tax bureaus must select taxpayers from each of the following categories:

- Enterprises engaged in the export business that enjoy VAT/consumption tax exemptions or refunds;
- Enterprises conducting transactions in the gold sector (e.g. sales and purchase of gold); and
- Taxpayers conducting capital-related transactions (e.g. share transfers).

2) Instructive targets

The local tax bureaus have discretion to select taxpayers from one or more of the following categories:

- Taxpayers engaged in the real estate/construction business;
- High-income individuals (for individual income tax audits); and
- Enterprises engaged in the education/training business for profit.

3) Discretionary targets

The local tax bureaus often expand or refine the scope of audit targets. For example, in addition to the six categories in the national plan, the Shanghai tax bureau has added following industries/taxpayers:

- E-business;
- Oil trading;
- General wholesale and retailing;
- Auto maintenance and repair;
- "Key taxpayers," i.e. enterprises that are considered to contribute a comparatively larger share of government tax revenue (a first batch of key taxpayers (that includes 100 Shanghai companies) was selected for audit in mid-February and a second batch is

expected after June); and

- Senior management in the financial and real estate industries or state-owned enterprises and lawyers.

Some other local tax bureaus also list key taxpayers and large businesses as their audit targets while the detailed actions and focus may vary from location to location.

(2) Schedule of audit

The nationwide tax audit is divided into three stages:

- Planning (March) - Provincial tax bureaus submit their plans to the SAT Tax Audit Bureau (TAB) by 31 March 2015.
- Implementation (April - November) - A mid-term report must be submitted to the TAB by 30 June 2015.
- Conclusion (November - December) - A final report must be submitted to the TAB by 31 November 2015.

(3) Observations

Given the intensified scrutiny by China's tax authorities on service fee and royalties payments made overseas, these payments likely will be one of the most relevant items in tax audits. Some common issues relating to outbound payments include the following:

- Whether and when a payment made overseas is deductible for enterprise income tax purposes;
- Whether and when the domestic payer should withhold income tax and/or indirect tax on behalf of the overseas party; and
- How the penalty and/or late payment surcharges should be applied for any under-withheld taxes.

(4) Recommendations

Companies falling within the scope of the tax audit plan should closely monitor the progress and may wish to conduct self-reviews to ensure that risk areas are addressed and that appropriate supporting documentation is available. Professional assistance may be required for controversial issues where guidance is limited.

If a tax audit has been initiated, the company should cooperate with the audit officials and respond to any queries in an open, consistent and coordinated manner, and attention must be paid to areas where there are signs of possible disagreements with the officials on the company's positions. Instead of waiting for issues to be incorporated in the tax audit report, companies should communicate and explain their tax positions as early as possible to seek consensus from the audit officials.

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