

Tax Newsflash

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Cross-border equity transfers: new rules issued concerning special reorganisation tax treatment



On 12 December 2013, the Chinese State Administration of Taxation ("SAT") issued Bulletin of the SAT [2013] No. 72 ("Bulletin 72"). Bulletin 72 concerns two of the cross border equity transfers which qualify for special reorganisation treatment, namely:

- **"Foreign-to-foreign" transfer (Circular 59, Article 7(1))**: the transfer of a resident enterprise ("PRC Co") shares by a non-resident enterprise ("Foreign Co1") to its 100% owned non-resident enterprise ("Foreign Co2")
- **"Foreign-to-domestic" transfer (Circular 59, Article 7(2))**: the transfer of resident enterprise ("PRC Co1") shares by a non-resident enterprise to its 100% owned resident enterprise ("PRC Co2")

Bulletin 72 takes effect from the issuance date; however, it also applies in respect of prior transactions, the tax treatment of which is yet to be finalised.

Highlights

- **Split or merger of foreign enterprises**: Bulletin 72 clarifies that the transfer of a Chinese resident enterprise's equity as the result of the split or merger of a foreign enterprise is covered by Circular 59, Article 7(1).
- **Cross border transfers to be reported to responsible tax authorities**: Cross border transfers in respect of which special reorganisation tax treatment is sought, must be reported to the responsible tax authority, being the responsible tax authority of the transferred enterprise in the case of a "foreign-to-foreign" transfer (Circular 59, Article 7(1)), and the responsible tax authority of the transferee enterprise in the case of a "foreign-to-domestic" transfer (Circular 59, Article 7(2)); otherwise, the transfer will be not qualify for special reorganisation tax treatment. Such reports are to be made within 30 days of the effective date of

the relevant contract or agreement or the completion of required PRC business registration change of the PRC enterprise, whichever is the later.

- **Undistributed profits at time of "foreign to foreign" transfers, on subsequent distribution, not eligible for more favourable dividend withholding tax treaty rate, if any:** In a "foreign-to-foreign" transfer (Circular 59, Article 7(1)) in which the transferor and transferee enterprises are tax residents of different jurisdictions and special reorganisation treatment is applied, the preferential dividend withholding tax rate, if any, provided for in the tax treaty between the jurisdiction of the transferee enterprise and the PRC is not to be applied in respect of subsequent distributions of the undistributed profits, at the time of the transfer, of the transferred enterprise.
- **Circular 698, Article 9, requiring provincial tax authority "approval" ("核准") of special tax reorganisation tax treatment abolished, but tax authorities required to internally report on eligibility for such tax treatment:** Specific approval of special reorganisation tax treatment in respect of the transfer by provincial tax authorities is abolished; however, Bulletin 72 requires responsible tax authorities to review all transfers in respect of which filing is made by relevant parties, and report on their eligibility for special reorganisation tax treatment to responsible provincial tax authorities, generally within 30 business days of the completion of required filing by relevant parties. In the case of a "foreign-to-domestic" transfer (Circular 59, Article 7(2)), the responsible provincial tax authority of the transferee enterprise is required to report on the eligibility of that transfer for special reorganisation tax treatment to responsible provincial tax authority of the transferred enterprise, within 30 days of receiving the report thereon of the responsible tax authority of the transferee enterprise. Internal annual reporting to the SAT is also mandated.

We understand that in issuing Bulletin 72, the SAT intends to clarify and internally streamline the review procedure in respect of transfers for which special reorganisation tax treatment is elected. This action on the part of the SAT is welcome; however, for taxpayers who seek confirmation that responsible tax authorities agree that the transfers qualify for special reorganisation tax treatment before undertaking transfers, Bulletin 72 is expected, practically, to have little impact other than in relation to the provision of the particular information and documents now specifically stipulated as required on filing. Cases "in progress" are expected immediately to be further delayed, as the responsible authorities consider the specific requirements of Bulletin 72.

For taxpayers who proposing to undertake, or have undertaken transfers without filing,

are now required to file; otherwise the relevant transfers will not be eligible for special reorganisation tax treatment.

If you have any questions please contact:

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