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CHINA

# Master Tax Guide 2009/10



**7TH EDITION**

The Professional's First Choice



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# **Master Tax Guide**

# **2009/10**

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Deloitte's experience in China is extensive and the firm continues to play a significant role in developing the accounting and tax professions in China by assisting the PRC Government in formulating tax policies and accounting standards. With the establishment of Deloitte Tax Research Foundation, the firm promotes education, research and innovation in the field of taxation by supporting an array of national and local program, including Deloitte Tax Championship as a key initiative for developing future talents in taxation in China.

In its seventh edition, the *China Master Tax Guide 2009/10* is updated by Deloitte's tax professionals. The publication is intended to provide an overview of the current China tax system, helping companies to gain an understanding of how the system has developed to date. While every effort is made to ensure that the information contained in the Guide is up-to-date, readers are advised to seek professional advice when special projects are being undertaken. The first edition published in 2003, was written by CCH Tax Editors and was reviewed by Deloitte's tax professionals.

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## Foreword

In its seventh edition, the *China Master Tax Guide 2009/10* provides comprehensive and up-to-date information on the concepts governing taxation of companies, businesses, individuals, etc, in China.

The Guide examines various taxes imposed in China. The full spectrum of taxation issues is explored, including procedural matters such as assessments and payments. Legislation, Tax Bureau Interpretation and Circulars are also examined. Main contents include an overview of China taxes, individual and enterprise income taxes, turnover taxes, consumption tax, transaction and property-related taxes, applicable tax rates, exemptions and preferential tax treatments, withholding tax, tax registration, administration and collection, disputes and penalties, double tax relief and more.

To enable quick and easy access to information, a comprehensive subject Index and Legislation Finding List are provided.

The legislation covered in this Guide is available in full text in CCH's three-volume loose-leaf publication *China Laws for Foreign Business — Taxation & Customs*.

**CCH Tax Editors**  
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# TABLE OF CONTENTS

Page

## PART I — INTRODUCTION

Legal and Administrative Framework of China Tax .....	3
Introduction to China Taxes .....	11

## PART II — INDIVIDUAL AND ENTERPRISE INCOME TAXES

Individuals and Enterprises Liable to Income Tax .....	43
Taxable Income and Exemptions .....	65
Deductions .....	121
Depreciation of Fixed Assets .....	143
Withholding Tax .....	157
Tax Rates and Computations .....	173
Tax Administration and Collection .....	209
Investigations, Disputes and Penalties .....	243
Double Tax Relief .....	257
Preferential Tax Treatment .....	341

## PART III — TURNOVER, CONSUMPTION AND OTHER TAXES

Value-added Tax .....	379
Consumption Tax .....	455
Business Tax .....	487
Transaction and Property-Related Taxes .....	513

## FINDING AIDS

Abbreviations .....	559
Legislation Finding List .....	563
Index .....	595

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# **PART I: INTRODUCTION**

	<b>Page</b>
Legal and administrative framework of China tax .....	<b>3</b>
Introduction to China taxes .....	<b>11</b>



# Chapter 1

## LEGAL AND ADMINISTRATIVE FRAMEWORK OF CHINA TAX

Tax reform background .....	¶1-010
Sources of law .....	¶1-020
Types of laws and regulations .....	¶1-030
Language and interpretation of laws .....	¶1-040
Tax policy and administration .....	¶1-050
Tax laws .....	¶1-060
Useful contacts .....	¶1-070

### ¶1-010 Tax reform background

China's current tax system is relatively new, having been developed only since the 1980s. Prior to that, China's tax system was concerned primarily with the taxation of domestic enterprises. With the introduction of "open door" economic policies, the tax system was reformed and developed in order to levy tax on foreigners, foreign enterprises and foreign investment enterprises.

To attract foreigners and foreign enterprises to make investment in China, China issued a separate income tax law in 1991 to tax on foreigners, foreign enterprises and foreign investment enterprises, which provided tax incentives and various favourable tax treatments, whereas domestic enterprises were governed under another tax code with less beneficial treatments, thus resulting in unbalanced taxation and unfair competition over the years. In addition, due to the existence of the two different tax regimes, there were ambiguity and inefficiency reported in tax levy and administration.

As China's economy continues to grow, efforts had been made to unify the income tax system such that foreign enterprises, foreign investment enterprises and domestic enterprises can be taxed under the same tax scheme. The new *Enterprise Income Tax Law* (EITL) was finally enacted in the Tenth National People's Congress on 16 March 2007. The new EITL, which unifies the income tax treatment of domestic enterprises and foreign enterprises, has come into effect on 1 January 2008.

The new EITL attempts to balance the sometimes competing goals of encouraging and attracting foreign and domestic investments, spurring economic development and innovation, enhancing tax administration and achieving tax justice. The new EITL not only responds to the appeal from domestic enterprises for balanced taxation and fair competition, but also

provides some transitional relief to foreign investment enterprises for the loss of certain incentives. The EITL balances the government's financial revenue needs with the goal of keeping China's tax environment internationally competitive.

## ¶1-020 Sources of law

China's legal system is a legislative (as opposed to common law) system. The regulation-making system is not strictly centralised in practice. Regulations are codified in statutory instruments which are derived from various sources at different levels of government (from national to local) and with a hierarchical basis of authority.

According to *The Constitution of the People's Republic of China* (Constitution), supreme legislative authority is vested in the National People's Congress (NPC) and its Standing Committee, which also have the final authority to make and interpret legislation. In practice, much of this power has been delegated to the State Council.

The State Council, headed by the Premier, is the chief executive organ of government at the central level. Administrative regulations made by the State Council rank immediately below those laws enacted by the NPC. These regulations are in turn supplemented by instructions, orders and rules issued by the appropriate subordinate ministries under the State Council. The major ministry responsible for tax matters is the State Administration of Taxation (SAT).

At a provincial level, People's Congresses are empowered to make local rules and regulations, provided they do not contravene the *Constitution* or the laws made by the NPC or the administrative regulations made by State Council. People's Congresses and their Standing Committees in provinces, autonomous regions, centrally administered municipalities and large cities are authorised to make local regulations. The large cities include cities where the People's Governments of provinces or autonomous regions are located, or where Special Economic Zones (SEZs) are located, and other cities approved by the State Council. People's Governments in these jurisdictions are also authorised to make provisions or measures.

## ¶1-030 Types of laws and regulations

### Laws promulgated by National People's Congress

Enactments promulgated by the NPC and its Standing Committee are broadly categorised as either:

- basic laws; or
- laws and amendments.



Before a new basic law is promulgated by the NPC, a bill must be introduced. New legislation proposed is usually vetted by the Legal Work Committee of NPC, which will examine and research the proposed bill, and recommend any changes that may be necessary.

The NPC commonly uses resolutions to make amendments to laws, or to enact supplementary provisions to laws and/or orders promulgating basic laws.

### **Administrative regulations issued by the State Council**

With effect from 1 January 2002 administrative regulations issued by the State Council are normally designated as “regulations”, “provisions” or “measures”. (Previously the State Council also issued administrative regulations designated as “articles”, “rules for observation”, “guiding principles”, “principles”, “rules” or “detailed rules for implementation”.)

Similar to enactments promulgated by the NPC, bills must be drafted and submitted to the legislative body of the State Council. Normally, draft versions are first prepared by the appropriate subordinate ministries or commissions and then submitted to the State Council for examination and approval.

All administrative regulations are published in the *Gazette* of the State Council and national newspapers. This is a requirement of the *Regulations on the Enactment of Administrative Regulations* (Art 28). Administrative regulations usually take effect 30 days after promulgation unless otherwise specified.

### **Other administrative documents**

In addition to NPC basic laws and resolutions, and State Council administrative regulations, various other administrative documents are issued to State agencies including decrees, directives, notices and circulars which give instructions or provide clarification regarding specific laws or legal provisions.

Many of these documents have been classified as “internal” and for these, foreigners must rely on the opinion of professional advisors, or on unofficial summaries of the documents provided by Chinese business partners, in order to understand how the documents affect and alter the published laws and regulations. Chinese legal officials have recognised that practices regarding “internal” law are unsatisfactory and have pledged to reduce the number of such documents.

### **Local regulations and rules**

There are three types of local regulations:

- regulations required to implement the laws of the central government in accordance with special local conditions;