

Hwuason Alerts.

A summary of China tax developments for the fortnight ending 10 October 2009.



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NEW SINO-CZECH DTA SIGNED: CONFUSION ENDS.

On 29 August 2009 China and the Czech Republic finalized a new DTA replacing the DTA that have previously been entered into by China and the former Czechoslovak Socialist Republic in 1987. The new agreement was signed in Beijing by the Czech ambassador and the head of the SAT. On a side note, the absence of a specific DTA with the Czech Republic was often a source of confusion for practitioners who did not have a solid grasp of European history.

CLARIFICATION ON SAT PROCEDURE IN RESPECT OF "ROYALTIES" ARTICLE IN CHINA'S DTAs.

On 14 September 2009 the State Administration of Taxation ("SAT") issued circular Guoshuihan [2009] No. 507 entitled 'Questions about Implementation of the "Royalties" Article ("Circular 507") under Double Tax Agreements ("DTAs")' to provide guidance on how the SAT intends to implement this article in practice.

Circular 507 takes effect on 1 October 2009, and it is not the first time the tax authorities published relevant document addressing the implementation of certain article(s) under China DTAs. Circular 507 provides an indication as to what will be acceptable as a "royalty" for purpose of DTAs and what will not be.

A more detailed analysis of the circular will be provided in the October edition of *Hwuason Insights* – our detailed monthly analysis of China's tax laws

RISE IN CHINA'S FISCAL REVENUE.

Since the start of the financial crisis in 2008, and the ensuing decline in foreign direct investment, there has been a significant concern in government circles in China about a subsequent loss of fiscal revenue. This was a significant motivation behind an aggressive crack down by the SAT on tax avoidance by the SAT in the first half of this year. There were signs early in the year that the fiscal loss would not be as bad as was first feared. Recent months tend to support this. In August fiscal revenue rose by a whopping 31.6% on the same month last year.

It seems that this rise can be attributed to three things:

- The aggressive stance of the SAT in chasing tax owing
- A relatively low-level in August 2008; and
- An improved investment climate in China.

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Please feel free to contact us in respect of any China taxation issue at:

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IN FOCUS: BAD TAX RECORD PREVENTS ACCESS TO SHENZHEN'S NEW "SECOND" BOARD.

Early this year, the Shenzhen Stock Exchange launched a Nasdaq style "second" board for start ups. Applications for IPO on the board ended on 26 July 2009. As part of the application procedure, companies needed to obtain a taxation credit certificate from their provincial level taxation bureaus. It has recently become that apparent that many companies were unable to obtain such certificates because of recent violations of China's tax laws and related regulations. As such, these companies' applications for acceptance on the second board was rejected.

This is further proof of the advice that we regularly give to our clients – in China your taxation record may adversely affect other areas of your business. The SAT's credit information database on companies continues to expand and has been increasingly applied to service relevant government authorities (non-tax departments) in performing their supervisory functions. As such, violation of China's tax laws may not only result in the penalties prescribed in the tax laws and regulations, but in penalties that are not initially foreseen by the taxpayers.

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This reiterates the benefit to a company in maintaining a clean tax record. The growing complexity of China's tax laws makes that more difficult than it once was.

TRANSFER PRICING DOCUMENTATION REQUIREMENTS TARGETED BY SHANGDONG NATIONAL TAX BUREAU.

On 9 September 2009 the Shandong National Taxation Bureau issued a Notice on Administering Transfer Pricing Contemporaneous Documentation. The Notice covered the following matters:

- The scope of the enterprises who are required to prepare contemporaneous documentation for related party transactions;
- The requirements for preparation, maintenance and the submission schedule of the documents;
- The administration requirements for the documents.

Upon the request of the tax authorities, the enterprises that are required to prepare contemporaneous document for related party transactions occurring during 2008 will need to comply with a December 31 2009 deadline, which means the countdown has begun.

To understand more about how Hwuason can assist you in ensuring full compliance with China's transfer pricing requirements, contact us at china@hwuason.com