

VAT in PRC

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Value Added Tax

Part One

VAT regulations and rules

- PRC VAT Tentative Regulations, State Council
- Detailed Rules on PRC VAT Tentative Regulations, MOF
- Rules, SAT singly or jointly with MOF/ Other Ministries

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Scope of VAT

1. Sale of goods
2. Importation of goods
3. Provision of services relating to processing, repairing, and replacement

within the Chinese territories

Exceptions:

- Export Processing Zones
- FTZ, BLP

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Scope between VAT and Business Tax (BT)

- Sale of goods: VAT, except for the sale of immovable properties
- Provision of taxable services: BT, except for that relating to processing, repairing, and replacement

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Parties to VAT

| | | | |
|------------------|---------------|----------------------|---|
| | Sale of goods | Importation of goods | Providing proc, repair, & replacement services. |
| Who bears? | Buyer | Consignee | Service user |
| Who collects it? | Seller | Customs | Service provider |

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Sale of goods (1)

Definition of goods?

Goods include the following:

Movable objects, gas, central heating, water, and electricity

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Sales of goods (2)

What does "sales" mean?

➤ Transfer the ownership of goods for a consideration, which includes:

1. Receipt of money
2. Goods
3. Other economic benefits

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Sales of goods (3)

Economic benefit?

➤ Exchange of goods for a consideration, which includes:

1. Discharging one's liability,
2. Shares in a company

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Deemed sales (1)

Transactions without change of ownership:

1. Delivery of goods from the principle to the agent for on-sale to customers
2. Sales of goods by the agent on behalf of the principle
3. Transfer of goods from the head office to the branch located at other cities

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Deemed sales (2)

Other circumstances

1. Turning inventory into non-taxable items (i.e. goods used in construction of own asset)
2. Using non-cash asset for external investment
3. Distributing goods to investors
4. Inventory (goods) used for staff benefits

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Computation of VAT payable

(1) General computation

VAT payable = output VAT – input VAT

(2) Simplified computation

VAT payable = Sale amount * levy rate

Scope : Small taxpayer; and Ordinary taxpayer selling certain specified goods

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How to compute VAT payable for imported goods?

For the sale of imported goods:

VAT payable = Output VAT – Input VAT

VAT input = (Dutiable value + customs duty + (consumption tax if any)) * tax rate

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Illustration

| | | |
|----------|-----------|------|
| Sale | 300 X 17% | = 51 |
| Purchase | 100 X 17% | = 17 |

200 X 17% = 34

Where : 51 is output VAT

17 is input VAT

34 is VAT payable amount

300 is the VAT sales amount

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How is VAT tax base determined?

VAT output amount
= VAT sales amount * tax rate

VAT sale amount = tax base

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Special rules on VAT sale amount (1)

When happen?

1. Price is exceptionally low without justification
2. The transaction is a deemed sale

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Special rules on VAT sale amount (2)

In the following order:

1. The average selling price for the same type of goods in the month
2. The average selling price for the same type of goods in recent period
3. Composite selling price = cost * (1 + 10% deemed profit rate)

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Examples of VAT-exempt goods

1. Own-grown agricultural produce **
 2. Old and used books
 3. Contraceptives medicine and devise
 4. Imported equipment used in the manufacture of export goods under processing agreements
 5. Items as specified by the State Council
- ** Notional input credits available for buyers who are general taxpayer

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How is VAT sales amount determined?

VAT sales amount = (1)+(2)+(3)-(4)

- (1) sales revenue recognized under accounting rules
- + (2) deemed sales amount
- + (3) charges additional to selling price
- (4) VAT exempt sales

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What are additional charges ?

Example: late payment interest, installation charge, testing fee, packing fee, loading and unloading charges, training and consulting fee, etc

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Extended scope of VAT - Summary

- Basic provisions: import; supply of goods & taxable services
- Deemed sales: transaction without change in ownership; change in use; gift
- Mixed sales: same transaction involving supply of goods and non-taxable service; paying one type of taxes

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Mixed vs. Sideline sale

- Mixed sale: Same transaction involving the supply of goods and non-taxable services to the same buyer; pay one type of tax.
- Sideline sale: Different transaction with different buyers; pay 2 or more types of taxes.

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Mixed vs. Sideline sale

Mixed sale:

- If taxpayer is engaged in production, wholesale and retail activities; and
- If > 50% of annual revenue is earned from sales and provision of taxable services,
- Then taxpayer should pay VAT.

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Mixed vs. Sideline sale

Sideline sale:

- Either taxpayer is supplying goods and non-taxable services (pay different taxes),
- OR taxpayer is supplying goods and taxable services (pay same tax at different rates).
- Taxpayer should separately account for different types of activities respectively.
- Otherwise, taxpayer pays VAT.

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Taxpayer and VAT invoice

Taxpayer and tax invoices (1)

Comparison: General taxpayer and Small-scale taxpayer

Annual sales revenue of general taxpayer

1. >1 million if engaged in manufacturing activities;
>1.8 million if engaged in wholesale or retail distribution activities
2. Satisfy the requirement for VAT record keeping

Taxpayer and tax invoices (2)

Comparison: General taxpayer and Small-scale taxpayer

3. Can claim input credit
4. Can apply for VAT export rebates
5. Can apply for VAT incentives

Taxpayer and tax invoices (3)

Comparison

| | General taxpayer | Small-scale taxpayer |
|----------------------|------------------|----------------------|
| VAT special invoices | Yes | No(1) |
| Ordinary invoices | Yes | Yes |

- The small-scale taxpayer may request the tax office to issue VAT special invoice on its behalf. The small-scale taxpayer pays a 6% or 4% VAT at the tax office.

Taxpayer and tax invoices (4)

When ordinary tax invoices are used?

1. Small scale taxpayer supplying goods or taxable services
2. The sales of VAT-exempt goods
3. For the retailer:
 - Sale of goods to final consumer (or user)
 - Sale to general taxpayer, use VAT invoice (4%)

Taxpayer and tax invoices (5)

Tax invoices vs. VAT liability

- Using ordinary invoices in retail business \leq the general taxpayer is not liable to output VAT
- The 2 issues are independent with each other
- Taxpayer shall compute output VAT as follows:
 - Sale amount = 100
 - Output VAT = $100 / 117 * 17$
 - Output VAT = 14.53

Input credit

Input credits (1)

The following input VAT are not creditable against output VAT:

1. VAT paid for buying fixed assets
2. VAT special invoices bearing issue date over 90 days
3. VAT special invoices not matched by genuine transactions
4. VAT invoices not yet certified by tax authority

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Input credits (2)

The following input VAT are not creditable against output VAT:

5. Purchased goods used for personal use for welfare
6. Purchased goods used in the construction of fixed asset
7. Amount represented by excess of VAT rate over export refund rate

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Input credit : special deduction rules for VAT general taxpayer

1. Purchase of VAT-exempt agricultural produce (10%)
2. Delivery charge with Invoice issued by company in transportation business (7%)
3. Purchase from company in the business of collecting 2nd hand articles and waste items (10%)

Note : Ordinary tax invoices can not be used to claim input credit in general

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Time to claim input credit

1. Manufacturing business: VAT invoice and purchase appearing in store (inventory) ledger
2. Commercial business: VAT invoice and after payment of purchase
3. Taxpayer with computerized certification system: within 90 days obtaining the certification
4. Provision of services: VAT invoice issued upon completion of services

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Determination of input VAT amount

Input VAT = (1) + (2) – (3)

- = (1) VAT on purchase as ascertained under accounting rule
+ (2) Special deductions (notional credit, transport charges) against output VAT
- (3) Input VAT not creditable against output VAT

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House keeping for the good faith buyer (1)

1. Obtaining information on seller's business license, tax registration, invoice purchase book
2. VAT invoices must be purchased from tax office in the city / county where the seller resides
3. VAT invoices are properly stamped.

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House keeping for the good faith buyer (2)

4. Information of seller's name, payee printed in VAT invoice must be matched with seller.
5. Particulars in VAT invoices must be matched against actual transactions
6. Authentication by confirmation with the tax offices at seller's place if in doubt

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VAT liability and ordinary invoices

Use of ordinary tax invoices (1)

1. General taxpayer selling goods to final consumer
2. Sale of VAT-exempt goods
3. Small-scale taxpayer supplying taxable services and goods
4. The sale of certain specified goods (i.e. food, cosmetics, vehicles)

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Use of ordinary tax invoice (2)

➢ When the selling prices are quoted including VAT, the quotes is converted into sales as below:

Selling price = quote amount / (1 + tax rate)

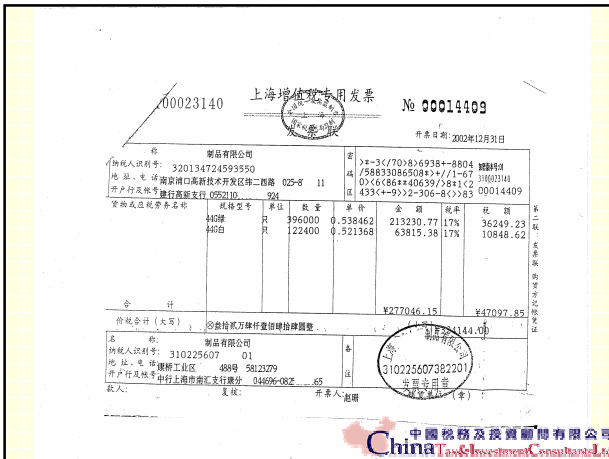
Selling price = 100 / (1 + 17%) = 85.47

VAT = 100 – 85.47 = 14.53

(or VAT = 85.47 * 17% = 14.53)

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| 机动车 专用发票 06473 | |
|----------------|--------------------|
| 开票日期 | 9月3日 |
| 开票人 | 刘玉玲 |
| 纳税人识别号/组织机构代码 | 70... |
| 开票类型 | 旅行车 |
| 开票号码 | 苏E5A918 |
| 开票地点 | 上海 |
| 开票金额 | 100.00 |
| 开票税率 | 17% |
| 开票税额 | 14.53 |
| 开票合计 | 114.53 |
| 开票单位 | 江苏天磊汽车服务有限公司 |
| 开票地址 | ... |
| 开票电话 | ... |
| 开票银行 | ... |
| 开票账号 | ... |
| 开票印章 | 江苏天磊汽车服务有限公司 发票专用章 |



Where the VAT is collected ?

1. At each stage of the VAT chain in domestic market
2. At the point of importation

Links in VAT chain:

- Manufacture processing
- Wholesale distribution
- Retail distribution

Where the VAT is collected ?

| | VAT | Consumption Tax |
|---------------|-----|---------------------|
| Manufacturing | Yes | Yes |
| Processing | Yes | Yes |
| Wholesaling | Yes | No |
| Retailing | Yes | No, with exceptions |
| Importation | Yes | Yes |

VAT rates

VAT rates (1)

| | |
|-----|--|
| 17% | Other than goods listed immediately below |
| 13% | Grain, vegetable oil, water, central heating, coal gas, LPG, books, newspaper, magazines, animal feeds, fertilizer, agrochemicals, agricultural machinery, agricultural film |
| 0% | for export of goods |
| 17% | for the supply of services relating to processing, repairing, and replacement |

Levy rates (2)

| | |
|----|---|
| 6% | Small scale taxpayer classified as manufacturing enterprise |
| 4% | Small scale taxpayer classified as commercial enterprise |
| 2% | General taxpayer or small taxpayer selling used articles at above original cost |

* Taxpayer paying VAT at levy rates cannot claim input credit

Tax rates (3)

A comparison

Tax exemption

- (1) Seller bears input VAT
- (2) Tax burden > 0

Zero-rated tax

- (1) Seller (exporter) does not bear input VAT
- (2) Tax burden = 0

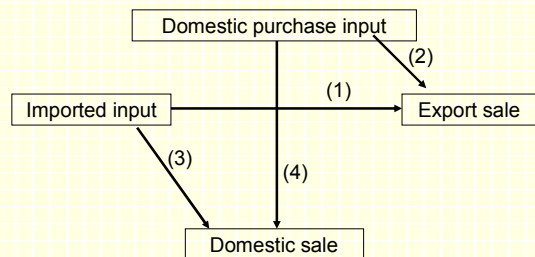
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VAT obligation - when it arises?

- Cash sales : receipt of sale money
- Credit sales : Pmt date by agreement
- Advance deposit : upon delivery
- Provision of taxable services : receipt of money
- Deemed sale: delivery of goods

Types of VAT liability

VAT implications for mfg operations



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Types of VAT liability

| | |
|--|---|
| 1. Export sales using imported inputs: | Exempted from VAT |
| 2. Export sales using domestically purchased inputs: | Entitled to export rebates (zero-rated) |
| 3. Domestic sales using imported inputs: | Taxable with input credits |
| 4. Domestic sales using domestically purchased inputs: | Taxable with input credits |

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Thank You

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