

Consultancy Services delivered in China

Q: We have closed a consultancy contract in China. Our Singapore office was told there will be a VAT for such service rendered in China, closed to 10% of the contract amount. Does a company registered in HKG subjected to such VAT as we are thinking of setting up a company in HKG to address China market, please advise us.

A: The provision of services will not attract VAT liability in China. Instead, it is subject to business tax at a rate of 5%. In addition, the provision of consulting services will attract income tax liability at 10%. The tax liabilities will depend on whether your company delivers the services inside China, outside China or both. The extent of tax liabilities is set out below:¹

I	Services wholly performed outside China	100% not taxable
II	Some of the services performed inside and some outside China	Where the information of time apportionment is not available, no less than 60% of the total income is deemed to have been derived from inside China.
III	Services all performed inside China	100% taxable

Assuming the consulting income is 100 (exchange rate ignored), the business tax (BT) rate is 5% and the income tax rate is 10%. The tax liabilities for different scenarios as mentioned above are give below:

I	100% services delivered outside China	BT = $100 \times 0\% \times 5\% = 0$ IT = $(100 - 5) \times 0\% \times 10\% = 0$
II	60% services delivered inside China, 40% outside China	BT = $100 \times 60\% \times 5\% = 3$ IT = $(100 - 5) \times 60\% \times 10\% = 5.7$
III	100% services delivered inside China	BT = $100 \times 100\% \times 5\% = 5$ IT = $(100 - 5) \times 100\% \times 10\% = 9.5$

Please note that where the presence of employees in China is over 183 days in a calendar year, the non-resident company that delivers the services is considered to have a permanent establishment in China. In that case, different tax rules shall apply to the non-resident company. The employees that have been assigned to work in China will have a liability to pay PRC individual income tax as well.

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¹ Please see document Guo Shui Fa (2000) 82, as issued by the State Administration of Taxation.