

Export sales vs Domestic sales

Q: My factory in China is considering of transforming part of our businesses from export sales to domestic sales. Yet we are not familiar with the taxes related to domestic sales. I would like know if there are any changes in tax rates (e.g. VAT, import-related tax, etc) involved in domestic sales compared with export sales, and does China have preferential tax policy for domestic sales? Thank you for your assistance.

A: [1] It all depends on the trading mode for your existing operations. That is, whether you already set up a wholly foreign owned enterprise (WFOE) to do the export processing, or you just signed a processing agreement with a party in China who undertakes to do the processing job for you for a processing fee. The use of WFOE is called “export processing with purchased materials” (進料加工 jin liao jia gong). The use of a Chinese party for export processing is called “export processing with supplied materials” (來料加工 lai liao jia gong). A WFOE has both the export and domestic trading right on its own. The WFOE is not required to apply for approval to do domestic sales if it imports the goods for which customs duty and VAT has been paid at the time of importation. Where you carry on the business of export processing with supplied materials (來料加工), then you have to convert it into a WFOE. 來料加工 is not a legal entity in China. It has got no domestic trading rights and accordingly it cannot issue tax invoices. Extensive information about the conversion is available on power points in the seminars we held on 31st July 2008 and 18th December 2008 respectively. Please visit the following website address for details <http://www.china-tax.net/about/seminar.html>.

[2] For domestic transactions, one needs to acquire information about the following issues: (i) the law and practices on tax invoices and VAT special invoices in China. (ii) the VAT rules on domestic transactions. Specifically the following articles will give details on the issues that you raised.

<http://www.china-tax.net/pub/TaxCompliancePlanning4TradingBizPRC-BNA.pdf>

<http://www.china-tax.net/pub/Admin-Pract-Tax-Invoices.pdf>