

China Customs & Trade News

New Development of Import VAT Exemption Policy

May 2009



I. Recap of changes to import VAT exemption policy

As part of VAT reform, MOF¹, GAC² and SAT³ issued a joint announcement - Announcement 43/2008 - in December 2008 to refine the import VAT exemption policy. Subsequently, the GAC issued Announcement 103/2008 to provide further guidance in relation to the enforcement of the new policy.

To recap, the new VAT policy will affect companies in the below projects and industries:

1. Encouraged domestic investment / foreign investment projects
2. Projects financed by loans from foreign governments or International Finance Corporations
3. Processing Trade enterprises which use consigned equipment provided by foreign principals on a free-of-charge basis
4. Foreign investment projects which fall within the Advantageous Industries of Middle and Western China
5. Technology innovation with self-owned funded projects by foreign invested enterprises and the research and development centres of foreign investment enterprises as per Shushui 791/1999
6. Software manufacturers and circuit manufacturers
7. City railway projects
8. Other companies and projects which refer to Guofa [1997] No.37

¹ MOF: Ministry of Finance.

² GAC: General Administration of Customs

³ SAT: State Administration of Taxation

Generally speaking, for new projects (i.e. projects approved on or after 10 November 2008 and equipment handbook registered on or after 1 January 2009), import VAT will be imposed on the imports after 1 January 2009. For old projects, a transition period is allowed which ends on 30 June 2009.

Note, ideally, the import VAT imposed is supposed to be creditable against the output VAT and thus would not bring additional cost to importer (except a time money issue for cash flow). However, for certain types of enterprises, which do not have sufficient output VAT to be credited against, such as those mainly dealing in toll manufacturing or research and development, this new policy could lead to additional VAT. We understand that the authorities are still evaluating potential solutions for these types of enterprises.

II. Good News Comes?

In the past four months, the GAC has received series of inquiries on the implementation of the new policy. In an internal Notice, the GAC provided further clarification on some of the salient inquiries.

1. Import VAT exemption policy continues for Customs special zones

The internal Notice gives a positive answer that import VAT exemption policy will continue to apply. This is good news for manufacturers within Free Trade Zones, Export Processing Zones and Bonded Port Areas, and other operators within the special bonded zones.

2. Import VAT exemption may still apply in equipment bonded transfer

The internal Notice sheds light on the possibility of import VAT exemption during the bonded transfer of bonded equipment (including capital equipment and consigned equipment), which are imported on or before 30 June 2009 and which are exempted from VAT upon importation. One of the pre-conditions is the receiving entity should be eligible for import VAT exemption under the old import VAT policy before 30 June 2009. This would be relevant and potentially good news for companies contemplating a merger, acquisition, rationalisation, or a plan to convert a toll manufacturing factory into a wholly owned foreign enterprise.

III. Tighten control upon equipment importation?

The internal Notice has urged port Customs to pay high attention to the declared value for imported equipment. Companies which have declared “nominal prices” for capital / consigned equipment should be alerted to a potential review of this pricing practice and prepare supporting documents to justify the declared price.

IV. PwC Observations

The new Import VAT Policy has been in place for a few months and it is still in a transition period. There will be some challenges in implementation. Companies are advised to study the policy thoroughly to protect benefits and minimise risks, and to consult with the in-charge authorities where appropriate.

Companies which are eligible to enjoy the preference within the transition period should seize the last chance and file declarations before the deadline.

The same principle applies for companies that are contemplating the bonded transfer of capital or consigned equipment, mergers or acquisitions.

Last but not the least, since imported capital equipment will now be assessed import VAT Customs will more closely scrutinize the declared value. Use of a “nominal price” may no longer be an acceptable practice for Customs. Companies should ensure that capital equipment is valued per the principles set out in GAC Order 148-2006 (The Valuation Measures).

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