

General Communication with Tax Authorities in friendly or unfriendly ways

Tax Commission – of course...!

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National Report of (P.R. China)

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1. Introduction

Tax authorities – surely each one of us had the pleasure to deal with one: as taxpayer at least with the tax authority of the country you are resident of, as a lawyer helping others in tax matters you might have had the chance to deal with the tax authorities of other countries as well. If the latter is the case you might have seen some differences in the behaviour of the different tax authorities. You might have realized that the tax authorities in some or even the majority of the countries do treat the taxpayers not as their customers or clients but rather as subordinates. In such cases the communications tends to be rather hierarchical and often results in administrative proceedings against the tax authorities with more or less success.

Other countries have realized that treating the taxpayer in ways like we know from the tale of Robin Hood and the Sheriff of Nottingham only results in the tax payers trying to circumvent their tax obligations. Some countries, thus, have not only reduced the taxes in their countries. They also made their tax authorities treat the taxpayers as their clients e.g. in offering the taxpayers the possibilities for tax rulings and trying to take a more tailored approach towards their taxpayers .

These – sometimes very significant – differences are what we are focusing on in this year's tax report: We want to show that there are big distinctions in the behaviour of and the dealing with the tax authorities in different countries both in the stage of an advance agreement on a tax position as well as in an objection or litigation phase. For this reason AIJA members from several countries around the globe were so kind to volunteer as national reporters for this report which is crucial for such a comparative topic.

The General Reporters would like to thank you all in advance for your contributions and are already very interested in the results of this year's annual congress session of the AIJA Tax Commission.

2. Questionnaire

Note: General assumption is discussions with the tax authorities regarding (corporate) income tax or indirect taxes. If a difference would apply in the treatment between either of these, please indicate in your report. Also, if there are different levels of tax authorities for different taxes or issues, please mark that in your report.

2.1 Communication general

How does the General Communication with the Tax Authorities take place?

- a. Is a direct contact in between the tax payer and the Tax Authorities possible/common/advisable?

Yes. Usually each tax payer (enterprise) has a special tax collector in the competent tax authority. The tax payer can communicate with the tax collector on most general tax issues.

- b. If not, does the communication only take place via tax counsels?

N/A

- c. How can the communication regarding special matters be described?

The process is the same. Always starts with direct communication with the tax officer

- d. Does it take place only in a written form or are meetings possible?

A meeting is possible but the written form is a must.

- e. Can the behaviour of the Tax Authorities in your country be described as all dominant, cooperative, customer-oriented or otherwise?

It is hard to describe the behavior of the tax authorities in whole China. In general, "customer-oriented" does not apply to most of the tax authorities. Dominant would be more commonplace.

2.2 Agreements between tax payers and tax authority

- a. Is there the possibility of a tax ruling and, if so, which costs can be expected?

Tax rulings are not common in China. In practice, enterprises as tax payers may consult with their specific tax officers for an informal opinion regarding

the applicable tax and tax rates, however, this seldom results in a formal tax ruling.

Under PRC tax law, an advance pricing arrangement (APA) is possible for certain enterprises which satisfy stipulated conditions, where tax payers and tax authority enter into an arrangement specifying the pricing method that is applicable to its related party transactions. This helps taxpayers voluntarily resolve actual or potential transfer pricing disputes in a proactive, cooperative manner, as an alternative to the traditional examination process.

- b. What is the average time frame to get a tax ruling done?

For APA, a number of steps would be involve – preparatory talks, formal application, review and assessment, negotiation and signing. Although the required time limits for some steps are stipulated in related laws and regulations, it is hard to predict the overall time required until the arrangement is reached and signed as these will vary greatly between tax offices.

- c. Are these consultations binding and, if so, which possible remedies do exist?

As mentioned, the informal consultation normally would not be binding on the tax authority.

For APA, as long as the enterprise abides by all the clauses and requirements as mentioned in the arrangement, it is binding on the tax authority and the tax authority would normally implement it. If the enterprise and tax authority have a dispute in relation to the implementation of APA, the parties would negotiate first and if the dispute cannot be resolved, such dispute shall be submitted to the superior tax authority (or State Administration of Tax if it is a bilateral or multilateral arrangement) for coordination. The subordinate tax authority shall follow the superior authority's decision and if the enterprise cannot accept such decision, the implementation of the arrangement shall be terminated.

- d. Once a tax ruling between all the parties concerned has been achieved, can one rely on it?

See answers above.

- e. What is the exact legal status of a tax ruling?

See answers above.

- f. Is it common in order to get a tax ruling that the tax payer has to give up certain rights or explicitly agree to e.g. information exchange?

In the process of reaching APA, it is inevitable that bargaining will happen during the negotiation. The enterprise needs to submit related documents (e.g. group structure, accounting statements, financial information, etc.) for the tax authority's review. In light of this, the enterprise's information is to some extent disclosed to the tax authority (as a general rule the tax bureau would keep all the information obtained during the process confidential).

- g. Is a tax ruling a public document or will it be treated confidentially by the tax authority? Does the taxpayer have an obligation to keep it confidential?

Normally, the detailed contents of APA is treated confidentially and not publicized.

2.3 Remedies against decisions of the Tax Authorities

- a. Is it common that one has to litigate if a decision has been made by the Tax Authorities and which remedies do exist?

No, it is not common.

- b. Is there the possibility of addressing a court or is this an administrative procedure?

There is an administrative procedure first and addressing a court is possible after completing the administrative procedure.

- c. Which costs are to be expected in such a case?

Litigation costs, consultant or lawyer costs, etc.

- d. Is it compulsory to have a lawyer in case of any remedy?

No.

- e. What timeframe can be expected in case of a remedy/litigation?

The tax reconsideration would be given within max. 90 working days. It may take longer if a tax administrative litigation is put forward.

- f. Is it possible to postpone the payment of the tax debt as assessed by the tax authority until the end of a pending litigation with the tax authority? Will the tax authorities require guarantees for the postponement (Bank guarantees, mortgages etc.)?

Normally it cannot be postponed. The payment of the tax debt or a guarantee would normally need to be made before the remedies.

- g. Is it possible that the tax authorities submit a report to the public prosecutor to investigate on possible criminal tax offences and under what circumstances?

Yes. If they have reasonable suspicion that a tax crime has been committed they may make such report.

- h. Is it possible to include a clause in an agreement to automatically amend this agreement in accordance with the outcome of a discussion or litigation with the tax authority (e.g. if an “at arms length payment” is not accepted as such by the tax authority or if interests are held to be dividends or a loan is seen to be a gift)?

It is possible to include a clause in an agreement that the amount/nature of the tax will be based on the final opinion of tax authority, provided that it does not violate mandatory laws and regulations. It is also possible to make stipulations in a contract which are contingent upon a decision of a tax authority, as long as said stipulations do not contradict any mandatory laws regulations.

2.4 Sanctions

- a. What is the statute of limitations for tax related matters?

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Generally, according to the PRC Law on Administration of Tax Collection, (i) if the tax payer/withholding agent does not pay or pays less tax due to the reason of the tax authority, the tax authority is entitled to ask the tax payer/withholding agent to pay to make up the deficiency within 3 years without surcharge for overdue payment; (ii) if the tax payer/withholding agent does not pay or pays less tax due to its own calculation errors, the tax authority is entitled to retrieve the tax payable and surcharge for overdue payment within 3 years and in special cases, this can be extended to 5 years; (iii) in case of tax evasion, tax revolt or tax fraud, the afore-mentioned limitations will not be applicable.

- b. What is the typical sanction/amount of fines in your jurisdiction? Is there a different fine level for direct or indirect taxes?

Normally, if the tax payer/withholding agent does not pay the tax within the stipulated period, the tax bureau will usually surcharge for overdue payment at a rate of 0.05% per day (commencing from overdue date). This rate is normally applicable for overdue payment of both direct and indirect taxes.

The amount of additional fine imposed by the tax bureau varies on case-by-case basis.

- c. Is it possible for a taxpayer to prevent tax penalties to be imposed should he/she be able to prove her good faith or reasonable interpretation of the law?

In practice, the answer is generally no.

- d. Is it possible to regularize your tax situation with reduced or no fines/sanctions?

Yes.

- e. May tax advisors/tax lawyers be held responsible by the tax authority for their advice to taxpayers?

If the registered tax advisors failed to abide by the tax laws and regulations, there is a risk that a fine/revocation of license, etc. might be imposed.

2.5 Tax information exchange

- a. Does a tax information exchange on the EU level or OECD level happen and how does it take place?

China is neither a part of EU nor a member country of OECD so this question would not be relevant to China.

- b. Does your country enter into tax treaties that obligate to exchange information spontaneously, automatically and/or upon request?

Yes. The types of information exchange include all three types (exchange upon request, automatic exchange, spontaneous exchange). The information exchange is implemented in accordance with the stipulations as agreed in the tax treaty signed with that specific country.

- c. Is the tax payer notified in case information is exchanged with foreign tax authorities?

The tax authority has discretion as to whether it informs the related tax payers, withholding agents or other concerned parties about the purpose of information gathering and the source and contents of information, etc. Notwithstanding the foregoing, without the approval of SAT, the tax authority shall not do so if (a) the tax payers, withholding agents or other concerned parties are suspected of committing serious tax offences, and such notification would influence the investigation of the case; or (b) the contracting treaty country declares that the source and contents of the

information should not be disclosed to the tax payers, withholding agents or other concerned parties.

d. Can the tax payer object against an exchange of information?

If the tax payer is notified he/she may register his/her objection, however, it is unclear what weight this kind of objection would have.