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Conference Addresses Key Tax Issues In China.

Summary by taxanalysts

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====== HIGHLIGHT ======

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The two substantive speakers, Anna Han, professor of law at Santa Clara University School of Law in Santa Clara, California, and Joyce Peck of Price Waterhouse's China Business Center in New York City, discussed tax issues affecting both the present and future of China.

Speaker handouts covered some of the mechanical aspects of Chinese taxes, but the theme of the presentation was more about what to expect in the future. Han described what she perceived as the emerging issues in China's tax system, voicing her opinion that as China's tax system became more sophisticated, China would rely increasingly on domestic tax administration and revenue rather than merely foreign receipts. She also opined that the trend in favor of parity between foreign and domestic taxpayers in China would become greater.

====== FULL TEXT ======

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Han described current issues of interest under the Chinese personal income tax law, and then turned to the more popular topic of tax issues arising with respect to foreign investment. In contrast to the old rules in which the manner of investment was highly relevant to tax consequences, she elaborated on the recent trend in favor of parity between different types of business entities.

A considerable colloquy with the audience occurred when issues concerning tax-free zones, tax holidays, and negotiated deals with local officials arose. Both Han and Peck had views about how best to nail down exactly what kind of tax relief was available, and precisely who had the authority to grant it. The consensus was that obtaining commitments in writing, and obtaining written assurance as to the authority of the writing officials to grant the abatement or waiver, were critical. Audience participation on this point made it clear that many foreign companies have had trouble with ostensible commitments on which their reliance turns out to be misplaced. On many past occasions, foreign investors have been understandably upset when promised relief turns out not to be available.

Han also addressed China's VAT, which underwent fundamental reform in 1994, its business tax, and even its land appreciation tax enacted in 1993. With the current panoply of taxes, China's tax system is fairly complete. Han suggested that China would now focus on its domestic tax system, which seems likely to become significantly more important as more companies privatize.

Peck largely endorsed Han's views about the outlook for the future of China's tax system, but she also made several other significant observations about China's tax system. Peck commented that automation was definitely coming to the Chinese system. She also voiced the opinion that as parity between Chinese domestic and foreign taxpayers comes to fruition, there will be major disadvantages to that parity for foreign companies. For example, she noted that the recent imposition of VAT and customs duties on capital imports of foreign investment enterprises is highly negative to foreign companies because the VAT is not a creditable tax, but must be capitalized and amortized over the life of the asset.

Peck also noted that the nature of foreign investors had changed in China. Although some years ago the only visible type of foreign investor in China was a large public company, now consumer goods, fast food, U.S. beer, and a variety of other ventures proliferate. She noted that even technology companies are now heavily involved in China despite previously voiced concerns about the protection of their intellectual property.

The topic of tax holidays and negotiated reduced tax rates arose once again before the close of the session, and again there was considerable audience interest. Peck took the view that most such accommodations would eventually disappear. While she thought reduced tax rates might continue in specific locations or for targeted projects, she felt that most special arrangements would eventually go by the wayside. On the topic of negotiated tax rate reductions, the internal Chinese allocation between the federal government and the local government as to collected tax revenue was discussed, inasmuch as it bore on the incentives that both local and national officials had in entering into -- or at least promising -- special deals.

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