

SOUNDINGS

Chinese Tax Issues

The imposition of tax on shipping operations into/out of Chinese ports pursuant to the recent Enterprise Income Tax regulations

The China State Administration of Taxation (CSAT) recently issued a notice clarifying its entitlement to tax companies not resident or domiciled in China, but engaged in commercial transportation within Chinese territory (Notice on Provisional Measures on the Collection of Tax on Non-Resident Taxpayers Engaged in International Transportation Business 2014 No. 37 Notice).

Local tax authorities are entitled to tax non-resident firms by imposing an Enterprise Income Tax (EIT) and Business Tax (BT) on income derived from international transportation into/out of Chinese ports, either through withholding part of the remittances from Chinese bank accounts of Chinese companies, or by non-resident firm's self-declaration.

However, these powers have historically been unevenly applied, and there has been some uncertainty over the manner in which these taxes operated. EIT and BT has, when imposed, tended to be between 4.45% - 10% of remittances.

The recent Notice confirms that EIT attaches to income derived from "international transportation" which includes non-resident shipowners and charterers and defines the mechanisms for collection of this tax.

There are a number of unresolved elements in the application of EIT, together with BT, and further clarification from CSAT is awaited. In the interim, the following observations can be made in respect of shipping and chartering activities of non-resident firms trading with Chinese companies:-

continued overleaf

The EIS tax applies to non-China resident taxpayer “engaged in international transportation”, which enjoys a wide scope.

Who is liable for taxation?

The EIS tax applies to non-China resident taxpayers “engaged in international transportation”, which enjoys a wide scope. It includes non-resident firms engaged in:-

- Voyage chartering or time chartering (but not bareboat chartering) to Chinese firms;
- Importing goods into, or exporting goods from, China;
- Cargo-handling operations within China;
- The transportation of passengers into/out of China;

How is the tax collected?

Given the practical difficulties in gathering remittances from non-resident firms, the CSAT has created two mechanisms for the collection of EIT by either (i) registration for tax of the non-resident firm within China; or (ii) a deduction of tax by a “withholding agent”.

i) tax registration

In the event a non-resident firm elects to register in China for tax, their accounts are available to the tax authorities for inspection and assessment. EIT will, generally, be taxed at 20% of the total taxable income, as calculated by deducting allowable expenses from the actual revenue received. A firm should register within 30 days of concluding a charterparty or relevant international transportation services agreement. BT will be taxed at 3% of revenue.

ii) withholding agent

Many non-resident firms may choose not to register for tax in China, especially if they do not regularly trade to that jurisdiction.

In such cases, Chinese firms who have contracted with non-resident firms are required to collect EIT tax from any taxable income (such as hire or freight) for remittance to the local tax authority. Withholding agents face significant fines for failing properly to garnish the appropriate tax.

It is understood that the withholding agent will also apply a 3% BT revenue tax.

Are double-taxation treaties available?

China has concluded a number of double-taxation treaties and specific agreements with countries (such as Greece, Cyprus & Singapore) for the special treatment of taxable income derived from shipping operations. The recent Notice recognises treaty benefits, available to non-resident firms that have registered for tax in China. However the application of any relief is dependent upon the terms of any specific treaty.

The Notice reflects a consolidation of taxation legislation currently underway in China. The new regulations are acknowledged as “Interim Measures” and further clarification is awaited. In the interim, Members should seek to ensure that any new charterparties provide for the payment of freight or hire net of any tax that may be imposed upon owners or charterers.

The Managers will report further as additional information emerges.

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