

# Highlights of fiscal and taxation reform in 2016 as announced by Premier Li

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## In brief

On 5 March 2016, Premier Li Keqiang made a speech on the government work report for the new year (the “Work Report”) at the fourth session of the 12th National People’s Congress (NPC). The Work Report announced the main objectives and major initiatives for 13th Five-Year Plan period as well as the key tasks deployed for 2016. In this issue of our China Tax and Business News Flash, we will introduce the tax related measures and policies in the Work Report and analyse their impact on enterprises.

## In detail

### **Reducing the tax burden of enterprises generally**

Premier Li Keqiang firstly put forth policies to stabilize and improve the economy, in particular, he pointed out the need to further alleviate the burden of enterprises by reducing taxes and fees which is in line with the supply-side structural reform and is an important measure in promoting economic growth and invigorating the market.

In respect of tax reduction, since 2012, China has committed to pushing ahead the pilot programme for the transformation of Business Tax (BT) to Value Added Tax (VAT) (the “B2V Reform”) in the last four years, in order to mitigate the multiple taxation issue and improve the input VAT credit chain. Premier Li indicated in the Work Report that “Starting from 1 May, the B2V Reform will be expanded to cover all the remaining sectors, i.e. construction, real estate, financial services and consumer

services sectors and the input VAT incurred by all enterprises on newly acquired immovable properties will be allowed to be credited to ensure that the tax burden of all sectors will be reduced with the completion of the B2V Reform.” With this clear objective, we believe that all levels of government and especially the fiscal and tax departments will spare no efforts to facilitate the last stage of B2V Reform in the next couple of months.

In respect of fees reduction, since 2015, China has taken a series of measures to cancel, cease collecting or integrate part of the government funds. The Work Report also provided a combination approach to deal with government-managed funds and administrative charges, including suspending the collection of contributions to and consolidating certain government-managed funds, expanding the exemption scope for contributions to water conservancy construction funds and other government-managed funds, and expanding the exemption scope of 18 administrative charges which currently only applies to small and thin profit enterprises to all enterprises and individuals. We hope these measures will be

implemented within this year to further alleviate the financial burden of enterprises.

### **Accelerating fiscal and taxation reform**

The fiscal and taxation reform is always a pivotal part in China’s economic reform, and continues to play an important role in monitoring macro-control, upgrading industrial structure and adjusting income distribution. The 12th Five-Year Plan released in 2011 had launched a new round of fiscal and taxation reform, in which one of the most crucial parts is the tax system reform including VAT, consumption tax, resource tax, environmental protection tax, property tax and individual income tax, etc. Most of reforms of these taxes have achieved significant progress in the past five years. 2016 is the first year of 13th Five-Year Plan, the 13<sup>th</sup> Five-Year Plan mentions that the government will continue to speed up the fiscal and taxation reform.

The fiscal and taxation reform will inevitably involve the allocation of tax revenue between the central and local government. In particular, as BT which is a main source of tax revenue for the local government will become part of

the history, it is a big question on how to fill up for this local government's revenue gap? The Work Report pointed out the major reform direction, including reasonable allocation of VAT revenue between the central and local government, moving the tax revenue of certain tax categories to the local government and appropriately delegating the administrative power of certain tax policies to the local authorities. We believe such reform direction will be applied in the implementation of fiscal and taxation reform.

Additionally, the Plan on Deepening the Reform of Tax Collection and Administration System of State Tax Bureau (STB) and Local Tax Bureau (LTB) ("the Reform Plan") jointly released by the General Offices of the Central Committee of the Communist Party of China and the State Council is another key document which taxpayers have to pay attention to. In particular, the change of tax collection and administration methodologies mentioned in the Reform Plan will directly impact many taxpayers.

Furthermore, the Work Report also addressed pushing ahead with the resources tax reform of changing the tax to an ad valorem tax and implements the administration according to the law. Implementing according to the law has been under the focus of government, industries and academia in the last two years. Only if tax collection and administration is implemented according to law, can the right of the taxpayers be protected and the sound operation of the tax system be secured. *The Tax Collection and Administration Law (TCAL)* is still in the amendment process, we believe the revised TCAL will achieve breakthrough in strengthening the protection of taxpayers' right. In January 2015, the Legislative Affairs Office of the State Council released the Discussion Draft of TCAL to solicit public comments and the Discussion Draft is currently still under review. We also see that the implementation of the revised TCAL and the drafting of the detailed implementation rule of the CAL are on the agenda of the State Administration of Taxation (SAT)'s 2016 work plan. Therefore, it is anticipated that the relevant fiscal and tax departments will push for the release and implementation of new TCAL with all their efforts.

### ***Encouraging innovation and implement tax incentives***

Since 2015, China has released a series of tax incentives aiming to support start-up and innovation, including improving the super deduction policy for Research and Development (R&D) expenses<sup>1</sup>, refining the administrative measures for the assessment of High and New Technology Enterprises (HNTEs)<sup>2</sup>, and extending certain income tax policies in the National Innovation Demonstration Zones (NIDZs) nationwide (i.e. tax preferential treatment for income derived from technology transfer, tax preferential treatment on equity awards plan, etc.)<sup>3</sup>.

We are glad to see that further implementation of the above tax incentives were addressed in the Work Report. It reflects the Chinese government's determination in supporting start-up and innovation and fostering the growth of innovative enterprises, which provide a direction for adjusting the industrial structure and enhance competitiveness through technology and innovation.

### ***Lowering the tax on consumer goods to stimulate domestic demand***

Since the start of the 12th Five-year Plan, expanding domestic demand has been a long-term strategy in China's economic development. To echo this strategy, China has released a series of tax incentives including reducing tariffs on consumer goods in batches, promoting measures to support cross-border e-commerce, permitting the opening of duty-free shops, etc., to enhance the domestic consumption level and support the development of retail and e-commerce business. It was also indicated in the Work Report that further tax incentives such as reducing tariffs on consumer goods and increasing duty-free shops will be released in 2016 to open up more development opportunities and match supply with demand. We look forward to the implementation of these policies which will bring along benefits and convenience to consumers.

Apart from the above, the Work Report also touched upon other tax related measures to complement the economic development work of the 13th Five-year Plan, including refining tax policies to support reasonable housing consumption, improving the implementation of financial and tax supporting policies, optimizing export tax refund, etc.

### ***Key tasks of individual income tax reform***

Although the individual income tax (IIT) reform has not been addressed in the Work Report, the Minister of the Ministry of Finance (MOF), Mr. Lou Jiwei provided his views on important development of the IIT reform in the Q&A session of a press conference held on 7 March.

Firstly, Minister Lou indicated that the IIT reform is imperative. Back in 2015, the MOF and SAT has submitted a draft of the IIT reform scheme which covers the reform difficulties and key points to the State Council. In 2016, a discussion draft of new IIT law comprising of a combination of comprehensive and category taxation will be submitted to NPC for review. In addition, he also indicated that the premise of IIT reform is the building up a complete record system of individual income and property information, which echoed the proposition of constructing a tax administration system of natural persons in the Reform Plan at the end of 2015. Minister Lou further pointed out that the IIT reform will be implemented in stages, certain simple part will be addressed first and other parts will be gradually refined as the information technology for tax collection improves and the individual taxpayers form the habits in paying tax. It can be seen that the government is already well prepared for the IIT reform. IIT reform has an important mission, not only for enhancing government's tax revenue, but also undertaking the social responsibility of adjusting the allocation of people's income and wealth. The IIT reform is relevant to each individual taxpayer and worth everyone's attention.

### ***Take away***

Fiscal and taxation reform is an important task in the 13th Five-year Plan for continuing the deepening of the reform of the whole country system. If it can be said that the 12th Five-year Plan has completed the top-level design stage of the fiscal and taxation reform, then the fiscal and taxation reform in 13th Five-year Plan period, will be the main event stage. Minister Lou has touched upon certain related plans regarding the 13th Five-year reform in the Q&A session of the press conference. These plans including: B2V Reform will be fully completed in 2016, property tax is already under the legislative stage, IIT reform scheme has been submitted,

and other local taxes are under reform in varying degrees. For the next five years, the Chinese government will continue with the reform and focus on critical issues such as resolving the allocation of roles and responsibilities between the central and local government that matches the central and local expenditures, improving the local tax system, increasing the developing capability of local areas, reducing financial burdens for enterprises. The objective of the reform is to establish a modern fiscal and taxation system by 2020.

We believe that the reform plan for each tax category will gradually be released as the fiscal and taxation reform deepens. These reforms will impact enterprises and individuals. We suggest taxpayers to pay close attention to the development of the reform, and consider in advance whether they should adjust or improve their business models to adapt to the impact brought by the reform. We will continue to focus on the progress of China's fiscal and taxation reform and the detailed measures of the policies and timely share our observation and interpretation.

### **Endnote**

1. For the details of new R&D super deduction policy, please refer to our *China Tax and Business News Flash 2015 Issue 43*.
2. For the details of new HITE policy, please refer to our *China Tax and Business News Flash 2016 Issue 4*.
3. For the details of tax incentives released by the State Council to drive up start-up and innovation, please refer to our *China Tax and Business News Flash 2015 Issue 47*.

### **Let's talk**

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