Analysis and Research on the New Policy of Value Added Tax in China in 2020

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Abstract: In view of problems in the actual operation, at the end of 2019, the State Taxation Administration issued the Announcement on Value-added Tax Collection and Management Issues, Including Canceling the Time Restriction in the Certification of Value-added Tax Credit Document. The regulation makes clear provisions on canceling the time restriction of VAT credit document, confirming the overseas income of the construction industry under special circumstances, and stipulates whether fiscal subsidy income should be included in taxable income, and how to determine the tax payment credit grade when applying for tax refund. This article studies these provisions in-depth.

1. Introduction

At the end of 2019, the State Taxation Administration issued the *Announcement on Value-added Tax Collection and Management Issues, Including Canceling the Time Restriction in the Certification of Value-added Tax Credit Document* (Announcement No. 45 of the State Taxation Administration in 2019, hereinafter referred to as Announcement No. 45), which clarified several major VAT collection and management issues. Except for the provisions on the credit document which has implemented since March 1, 2020, other provisions have implemented since January 1, 2020. According to relevant provisions of the Announcement No. 45, this paper makes an in-depth analysis and research on provisions canceling the time restriction of VAT credit document certification, confirming the overseas income of the construction industry under special circumstances, whether fiscal subsidy income should be included in taxable income, and how to determine the tax payment credit grade when applying for tax refund. This article studies these provisions in-depth.

2. Cancel the Time Restriction of Vat Credit Document

According to Announcement No. 45, for special VAT invoices, the special import VAT payment certificates, the unified motor vehicle sales invoices and common electronic VAT invoices of toll obtained by general VAT taxpayers after January 1, 2017, the time restrictions for certification, confirmation, audit and declaration in tax deduction are canceled. In VAT declaration, the taxpayer shall confirm the purpose of above tax deduction vouchers through the VAT invoice comprehensive service platform of the province (the autonomous region, the municipality directly under the central government or the city specifically listed in the plan). For general VAT taxpayers who have obtained VAT special invoices, custom import VAT special payment certificates and unified invoices for motor vehicle sales before December 31, 2016, if they exceed the time limit of certification, audit and declaration in deduction, but can meet the specified conditions, they can still follow the *Announcement of the State Taxation Administration on the Deduction of Overdue VAT Deduction Voucher* (No. 50 Document in 2011, revised by the No. 36 Document in 2017 and No. 31 Document in 2018 of the State Taxation Administration) and the *Announcement of the State Taxation Administration on Cases Failing to Declare VAT Deduction Voucher in Time* (No. 78 Announcement of the State Taxation Administration in 2011, revised by No. 31 Announcement of the State Taxation Administration in 2018). The input tax can be deducted.

Before that, after general VAT taxpayers obtain VAT special invoices, custom import VAT special payment certificates and other tax deduction vouchers, they should verify (compare) within

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360 days from the date of issuing the vouchers, and deduct relevant input tax within the declaration period of the next month (i.e. before the 15th of the next month) after the certification (comparison). If they do not certify and deduct on time due to objective reasons, the tax can only be deducted after applying to the provincial tax authorities for approval. [1] In that situation, the tax can only be deducted for specified objective reasons.

In the real operation, many taxpayers have suffered losses because they have not been certified and deducted in the prescribed time. For example, after a company purchases some equipment, it did not deduct it in next month after passing the certification due to the error of the financial staff. The tax authorities do not allow the taxpayer to deduct the tax. Compared with previous regulations, Announcement No. 45 canceled the time restriction on the certification of VAT deduction vouchers, and eliminated a major risk of taxpayers. If the taxpayer certificate after 360 days after the date of invoice issuing, or fails to make deduction in next month after certification, it can continue the certification and deduction without applying to tax authorities.

From the perspective of taxpayers, it is a right of them to deduct the input tax according to the tax law. Since it is a right, taxpayers can choose their own time to exercise it. It is not in line with legal principles to set the time boundaries for certification and deduction in order to facilitate the collection and management of tax authorities. The provisions of Announcement No. 45, taking into account the special circumstances in real life, are more suitable for the actual operation. Of course, after the Announcement No. 45, although tax authorities will no longer prescribe the deduction and certification period, in order to ensure the taxpayer's own interests, it is recommended that the financial personnel should verify the invoice and deduct tax as soon as possible after obtaining the invoice, so that the authenticity of the invoice can be identified in time. (If the certification is passed, it means that the invoice obtained has no problem. If it can't pass the certification, the voice should be reissued as soon as possible to avoid the loss of tax benefits). In this way, the company can enjoy benefits of tax deduction in advance, such as early certification, early deduction and less tax payment. Of course, in accordance with the provisions of Announcement No. 45, for tax deduction vouchers such as VAT special invoices issued on or before December 31, 2016, the former provisions should be follow. However, from the perspective of the tax authorities, the original “certification period” was proposed by the State Taxation Administration in response to the continuous occurrence of big false invoices cases, as well as inappropriate behaviors such as malicious regulation and control of the balance of VAT negative rate to avoid tax management and inspection, and arbitrary adjustment of the current tax payable to maximize the benefits of tax policies. After the Announcement No. 45, how to prevent tax authorities from maliciously obtaining false invoices, how to avoid evasion from tax management by adjusting tax burden and extra value-added tax preference seeking by adjusting the current tax payable, and how to balance the tax collection and management and the interests of taxpayers, need to be further studied and solved.

3. Recognition of Overseas Income of the Construction Industry

According to Announcement No. 45, for units and individuals within the territory of the People's Republic of China (hereinafter referred to as “domestic”) who provide construction services for projects which the construction site is overseas as subcontractors, the income of subcontracting obtained from the main contractor of the project within the territory of China, belongs to “income deemed to be obtained from overseas” in Article 6 of the *Announcement the State Taxation Administration on Value Added Tax Exemption Provisions in Cross Border Taxable Activities after Replacing Business Tax with VAT (Trial)* (No. 29 Document of 2016, revised by the Announcement No. 31 of 2018 of the State Taxation Administration, hereinafter referred to as Announcement No. 29). It can be exempted from value-added tax.

According to Announcement No. 29, the construction service provided by the project subcontractor for the abroad project (the construction site is overseas) belongs to construction services for projects abroad. In the operation model composed of a main contractor and several subcontractors, the main contractor may first obtain total project funds from abroad, and then pays subcontractors. The settlement method does not change the nature of the income source of domestic

subcontractors. Therefore, Announcement No. 45 clearly states that, for domestic units and individuals who provide construction services for the project which the construction site is overseas as subcontractors, the income of subcontracting obtained from the main contractor of China belongs to “income deemed to be obtained from abroad”, which can be applied to current VAT exemption policies for cross-border services.

The issue of Announcement No. 45 is conducive to the settlement of disputes after the issue of Announcement No. 29. That is, the main contractor is a domestic enterprise and the subcontractor is a domestic enterprise, but the construction site is overseas; the subcontractor is paid by the domestic main contractor. Can the payment by included in the overseas income and exempted from VAT? Are the construction services provided by the main contractor and the subcontractor for abroad projects belong to construction services for projects abroad?

According to Article 2 of Announcement No. 29, the construction service provided for abroad project is exempt from value-added tax. The judgment standard of “abroad” is that the construction site is abroad, and there is no provision that the subcontractor must be connected with a main contractor from abroad. In principle, the above situation should be in line with the provisions. However, Article 6 of Announcement No. 29 also stipulates that if a taxpayer sells services or intangible assets to an overseas entity and is exempted from value-added tax according to the regulations, the total income from the sale of such services or intangible assets shall be obtained from overseas, otherwise it shall not be exempted from value-added tax. Article 6 does not specify whether “obtained from overseas” refers to income obtained from abroad projects or income paid from overseas; the dispute rises. For domestic subcontractors who provide services for overseas projects but get income from the domestic main contractor, can the income be exempted from value-added tax? Announcement No. 45 made clear this issue and resolved the above dispute. That is, for both the main contractor and the subcontractor of construction services, as long as the construction site is overseas, the service they provide belongs to overseas construction services.

4. Whether the Financial Subsidy Income Should Be Included in Taxable Income

According to Announcement No. 45, if the income from financial subsidies obtained by taxpayers is directly related to the revenue or quantity of the sale of goods, services, intangible assets and real estate, VAT shall be calculated and paid in accordance with provisions. The revenue from financial subsidies obtained by taxpayers under other circumstances shall not belong to the taxable income and shall not be subject to value-added tax. According to Announcement No. 45, if the income from financial subsidies obtained by taxpayers is directly related to the revenue or quantity of goods, services, intangible assets and real estate, it belongs to taxable income, and shall be calculated and paid value-added tax; if it is not directly related, it does not belong to the taxable income and shall not be subject to value-added tax.

In addition, it should be noted that the “income directly related to the revenue or quantity” mentioned in Announcement No. 45 not refers to all subsidy income calculated according to the income and quantity. Only subsidies closely relate to the sales activities of taxpayers, and constitute the subsidy income of the consideration of sales behavior, can be included in the sales scope of VAT. For example, enterprise A is a transportation company, which is subsidized by the government. The subsidies include car purchase subsidies at the provincial and municipal levels, new energy subsidies at the ministerial level, operation subsidies come from the municipal government, and park subsidies at the municipal level. Among the above subsidies, the municipal government's operation subsidies are calculated according to the transportation workload of enterprise A. They are closely related to the sales activities of the enterprise, and are subsidies for its service income. The subsidies should be directly related to the income and quantity of enterprise A's sales of transportation services, and should be calculated according to the value-added tax sales. Other government subsidies, which do not meet above conditions, do not constitute value-added tax sales.

Prior to Announcement No. 45, the *Announcement of the State Taxation Administration on Issues Related to Value Added Tax Subsidized by Central Finance* (No. 3 Announcement in 2013,

invalid on January 1, 2020) stipulated that, “in accordance with the current value-added tax policy, the central financial subsidies obtained by taxpayers are not taxable income of VAT and are not subject to value-added tax”. According to the policy at that time, even if the central financial subsidy belongs to VAT sales, VAT will not be levied according to Announcement No. 3. Now Announcement No. 3 is invalid. After that, it is unnecessary to consider the influence of financial subsidy source on VAT. Generally speaking, compared with the original provisions, the provisions of Announcement No. 45 are more reasonable. First, Announcement No. 45 is applicable to the situation that enterprises obtain various subsidies, rather than provide special provisions for certain subsidies. Second, it is in line with basic provisions on VAT taxable sales. As long as the subsidy comes from taxable activities like the sales of goods and services, VAT should be levied.

5. How to Determine the Tax Payment Credit Grade When Applying for Tax Refund

The tax payment credit grade refers to the level assessed by the tax authority according to the taxpayer's performance on tax payment in a certain period. At present, the tax credit is divided into five levels: A, B, M, C and D. The credit grade of one year is rated in April of the next year. Before April, in the e-tax bureau, only the credit rating of the previous year can be queried. For example, when taxpayers apply for immediate levy and refund tax on the comprehensive utilization products in January 2020, they will find that there is a time difference in credit rating. The tax payment credit of the period in January 2020 can not be assessed before April. But the immediate levy and refund tax must be refunded, so it is necessary to clarify, how to determine the tax payment credit of the period in which the tax refund is applied?

There are two opinions on this problem. First is to calculate according to the credit level displayed in real time in the e-tax bureau corresponding to the period of tax refund. In above example, the real-time credit level of e-tax bureau shall be B in January 2020 (the evaluation year is 2018). Even if the year 2020 is rated as level C in 2021, there is no need to pursue the tax refunded immediately in January 2020. The second solution to calculate according to the credit level of the evaluation year corresponding to the period of tax refund. In the above example, the year 2020 shall be assessed in April 2021. If the year 2020 is assessed to be level C, the refunded tax collected and refunded in January 2020 shall be pursued.

In order to solve above disputes, Announcement No. 45 stipulates that taxpayers shall enjoy the policy of immediate collection and refund of value-added tax. If there are requirements for tax payment credit grade, the tax payment credit grade of the period in which the taxpayer applies for tax refund is adopted. In case of any changes in the tax payment credit grade within the period of applying for tax refund, we should adopt the tax payment credit grade after changing. There are new problems in the actual operation. Is the tax payment credit grade of the period in which the tax refund is applied the evaluation year corresponding to the period, or the credit level displayed in real time by the electronic tax bureau corresponding to the period?

For example, A company is a comprehensive resource utilization enterprise. Since its establishment, the company's tax payment credit has been A-level. Later, due to the violation of tax regulations, the tax payment credit grade was rated as level C in April 2019. The company corrected the error and the tax payment credit grade was restored to level B in July 2019. In September 2019, the company filed an application to the tax authority for refund of the tax for the period from January to August 2019 (previously the tax has been refunded according to the regulations). What period of time can the company enjoy the VAT immediate levy and refund policy?

According to Announcement No. 45, the company's tax payment credit grade for the period from January to March 2019 is level A, and the tax payment credit grade for the period from April to June 2019 is level C. After the tax payment credit grade is restored in July 2019, the tax payment credit grade for the period from July to August 2019 is level B. According to regulations, if the company meets other conditions of the immediate levy and refund policy, the tax authorities can refund the refundable tax of the resources comprehensive utilization project from January to March and from July to August 2019.

Generally speaking, the tax payment credit grade of the period in which the taxpayer applies for

tax refund refers to the credit level displayed by the corresponding e-tax bureau of the period in which the tax refund is applied, rather than the credit level corresponding to the assessment year. [2]

6. Conclusion

The *Announcement on Value-added Tax Collection and Management Issues, Including Canceling the Time Restriction in the Certification of Value-added Tax Credit Document* issued by the State Taxation Administration in 2020 solved actual problems in the collection and management of value added tax and settled relevant disputes. The new provisions are more considerate and in line with the principles of the tax law.

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