

Notices of the Ministry of Finance and the State Administration of Taxation regarding Adjusting Value-added Tax Rates and Standardized Criteria for Small-scale VAT Taxpayers

China Business Solution Office
RMB Internationalization Business Promotion Office

On April 4, 2018, the Ministry of Finance (MOF) and the State Administration of Taxation issued the Circular of the Ministry of Finance and the State Administration of Taxation on Adjusting Value-added Tax Rates (MOF No.32 [2018], hereinafter “Circular 32”) and the Circular of the Ministry of Finance and the State Administration of Taxation on Unifying the Standard for Qualifying as Small-scale VAT Taxpayers (MOF No.33 [2018], hereinafter “Circular 33”). Both notices took effect on May 1, 2018.

1. Background of the policies

In recent years, China has announced tax policies to help the economy grow by providing financial support, such as a reform to replace business tax with VAT and corporate tax incentives for small businesses. In particular, the VAT reform has helped reduce the tax burden by approximately RMB2Tn over the past five years, according to the announcement made by the National Taxation Work Conference in January 2018. On March 28, 2018, the Standing Committee of the State Council decided to take actions to further implement VAT reforms to improve tax policies. Specifically, VAT rates will be reduced for some businesses, the criteria for small-scale VAT taxpayers will be standardized, and taxes incurred on purchased goods and services (but not deducted yet) will be refunded in a lump sum for specific industries. Circulars 32 and 33 stipulate the reduction of VAT rates and the standardized criteria for small-scale VAT payers.

2. Details of the policies

Circular 32 stipulates the adjustment of VAT rates for some goods and businesses and the adjustment of refund rates. Important points from Circular 32 are noted below.

(1) Reduction of VAT rates

According to Circular 32, VAT rates will be adjusted to the three levels of 16%, 10% and 6%.

[Figure 1] Reduction of VAT rates

Taxable activities	Applicable VAT rates	
	Before	After
Freight, processing and repair services, leasing services and sales of tangible and moveable assets, import of general goods ¹	17%	16%
Transportation services, postal services, basic telecom services, construction, leasing services and sales of real estate, transfer of land use rights, sale and import of agricultural products and other goods ²	11%	10%

¹ Goods refer to those other than the ones listed in Note 2

² Goods specified in provisional regulations of the People's Republic of China on VAT, revised on November 19, 2017: food and other agricultural products, edible vegetable oil, edible salt, tap water, heating gas, air conditioning gas, hot water, coal gas, liquefied petroleum gas, natural gas, dimethyl ether, methane, coal products for residential use, publications, newspapers, magazines, audio and visual products, electronic publications, feed, chemical fertilizer, agricultural machinery, pesticides, agricultural film, and other goods specified by the State Council.

(2) Reduction of input VAT calculation rates for agricultural products

The deduction rates for agricultural products will also be changed.

[Figure 2] Reduction of deduction rates for agricultural products

Taxable activities	Applicable rates	
	Before	After
Purchase of agricultural products	11%	10%
Purchase of agricultural products for producing, selling or processing into goods to be sold at the 16% VAT rate	13%	12%

(3) Reduction of export VAT refund rates

Export VAT refund rates will be adjusted in line with the reduction of VAT rates.

[Figure 3] Reduction of export VAT refund rates

Taxable activities	Applicable VAT rates	
	Before	After
Exports of goods	VAT rates: 17%, export VAT refunds rates: 17%	16%
Exports of goods, cross-border taxable activities	VAT rates: 11%, export VAT refunds rates: 11%	10%

Depending on corporate type, different transitional rules will apply to exports of goods and cross-border taxable activities until July 31, 2018. The export date shall be the date noted on the export customs declaration form for exports of goods, and the export invoice date for cross-border taxable activities.

[Figure 4] Export VAT refund rates applicable during the transitional period

Corporate type	Export VAT refund rates
Trading company	The export VAT refund rate before adjustment will apply if the goods were subject to 17% or 11% VAT when they were purchased by the trading company.
	The export VAT refund rate after adjustment will apply if the goods were subject to the 16% or 10% VAT when they were purchased by the trading company.
Manufacturing company	The 17% or 11% export VAT refund rate (before adjustment) will apply.

Circular 33 standardizes the criteria for small-scale VAT payers and specifies the conditions for changing taxpayer status from general to small-scale. Important points in Circular 33 are noted below.

(1) Standardized annual taxable sales criteria for small-scale VAT payers

Criteria for small-scale VAT taxpayers have differed for manufacturing companies, trading companies, and companies under the VAT pilot program. Circular 33 standardizes those criteria.

[Figure 5] Adjustment of criteria for small-scale VAT taxpayers

Corporate type	Before	After
Manufacturing companies	Annual taxable sales ≤ RMB 500,000	Annual taxable sales ≤ RMB 5 million
Trading companies	Annual taxable sales ≤ RMB 800,000	
Companies under the VAT pilot program	Annual taxable sales ≤ RMB 5 million	

(2) Any business (company, organization or privately-managed business) that is registered as a general VAT taxpayer may change its status to small-scale VAT taxpayer by a specified deadline. Any business (company, organization or privately-managed business) that reached the threshold for general VAT taxpayer prior to the announcement of Circular 33 and registered as such may change its status to small-scale VAT taxpayer by December 31, 2018. Taxes incurred on purchased goods and services (not deducted yet) shall be booked as “VAT payable (input tax)” or “VAT payable (transfer out input tax)”.

3. Impact on enterprises

A portion of VAT rates will be adjusted with the promulgation of Circular 32. Reducing tax rates will alleviate the financial burden on corporations. Circular 32 took effect on May 1, 2018, but it is not clear when the new VAT rates will start to apply. If it is when tax obligation arises, the new rates will apply to any taxable activities that occur on May 1 or after. When tax obligation arises might be interpreted as the day when sales proceeds are received, when the goods are shipped, or when the advance is received. Companies need to correctly understand the tax rate applicable to each activity and reflect it in operations.

According to Circular 33, a general VAT taxpayer with annual taxable sales of RMB5Mn or less may change its status to small-scale VAT taxpayer. Changing to a small-scale VAT taxpayer will reduce tax management costs. However, if you have business with a general VAT taxpayer, the customer will be no longer allowed to deduct taxes incurred on purchased goods and services due to your status of small-scale VAT taxpayer, and so may cease to do business with you. Therefore, a thorough understanding of the advantages and risks and careful decision-making is necessary. If changing to a small-scale VAT taxpayer, ensure that taxes incurred on purchased goods and services are deducted. We will continue to follow up on relevant information and share it as appropriate.

Disclaimer

This document does not constitute any entrustment or any other contractual obligations. MUFG: Bank (China) (the Bank) shall not be responsible for any legal consequences hereof. Although this document is based on reliable data, the Bank does not guarantee its accuracy or completeness.

The contents herein are limited to our current understanding. The Bank shall not be responsible for any losses or damages related to this document. Please consult your lawyers, tax consultants, accountants or other specialists for their professional advices, as appropriate.

This document is the copyright of the Bank and is protected by the law. No partial or entire part of this document may be quoted, duplicated, or forwarded without the Bank's permission.

Copyright 2018 Bank of Tokyo-Mitsubishi UFJ (China), Ltd. All rights reserved.