

China increases VAT Export Refund Rates

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On 21 October 2008, the Ministry of Finance ("MOF") and the State Administration of Taxation ("SAT") jointly issued Caishui [2008] No.138 ("Circular 138") to increase VAT export refund rates for a range of commodities. The commodities consist of labor intensive (i.e. textiles, garments, toys, etc), high-tech and high value-added commodities (i.e. anti-aids medicines). Circular 138 will become effective from 1 November 2008. The execution date refers to the export date specified in the Export Commodity Customs Declaration Form (Specially Used for Export Refund Purpose) by the PRC Customs.

1. Background

The decrease of VAT refund rates in year 2007, the appreciation of RMB and enforcement of new labor law caused pressure for export enterprises and affected the export growth rate in some export-oriented provinces. Some industries in China are in difficult position. For instance, according to the statistics published by Guangzhou Customs, the export trade of Guangdong for the first three quarters of 2008 reached USD301 billion with a growth rate decreasing by 10.7% in comparison with that of the first three quarters in 2007. Export trade is one of the major engines for China economy and hence it turns out to be an urgent matter for China to ease the operation pressure of export enterprises, enforce enterprises' export competitive power and keep the stable growth of economy especially under the current circumstances of global financial crisis and the bankruptcy of some China enterprises (i.e. the bankruptcy of the biggest toy manufacturer located in Dongguan city).

2. Increase in VAT Export Refund Rates for Certain Commodities

- VAT refund rates for certain textiles products, garment and toys raised to 14%;
- VAT refund rates for daily and artistic ceramics raised to 11%;
- VAT refund rates for certain plastic products raised to 9%;
- VAT refund rates for certain furniture raised to 11% and 13%;
- VAT refund rates for anti-aids medicines, sewing machines, electrical fans, certain books, and other commodities raised to 9%, 11% and 13% respectively.

The detailed list of the specific commodities and tariff codes is set out in the annex of Circular 138.

3. Our Suggestion

VAT refund is an export subsidy for enterprises. China government issued strict laws and regulations to administrate the claim of VAT refund. Tax Exemption, Credit and Refund system ("ECR system") has been implemented in export-oriented enterprises for years. In order to achieve the tax refund, enterprises are required to submit ECR tax returns, financial reports, breakdown, supporting documents such as export invoice, export customs declaration form, foreign exchange verification and cancellation form and other relevant documents to tax

authorities within specified period. Furthermore, it is important for investors to check local variations so as to safeguard their tax compliance status of their PRC operations. Any non-compliance on the documentation and tax filing might cause failure in achieving the VAT refund or even inspection by the state tax authorities and imposition of non-compliance penalties / late payment surcharges. For the management's rest assured, it is suggested to seek tax professional's advice and perform tax health check regularly.