

Learning from cases and exploring innovation – PwC assists in achieving Fujian Province's first advance tax ruling case on cross-border issues

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In brief

In recent years, the exploration in advance tax rulings is accelerated, with practices becoming increasingly mature. Tax authorities in various regions, including Beijing, Shanghai, Nansha District of Guangzhou, Maoming City of Guangdong, Dongfang City of Hainan, Ding'an County of Hainan, and Qitaihe City of Heilongjiang, have issued administrative measures for advance tax rulings. Recently, Shanghai disclosed the completion of several cases in advance tax rulings. For enterprises, the implementation of advance tax rulings can reduce potential tax risks and improve tax compliance; for tax authorities, it can reduce tax disputes and lower tax administration costs, thereby improving the investment and business environment. For more details of local efforts made in advance tax rulings, please refer to *China Tax/Business News Flash* Issue 11 of 2024, Issue 1 of 2024, Issue 20 of 2022¹.

Meanwhile, PwC has assisted some enterprises in applying advance tax rulings. Recently, PwC assisted an enterprise in achieving the advance tax ruling opinion regarding tax treaty benefits, marking the successful conclusion of Fujian Province's first tax advance ruling case on cross-border issues.

In this issue of *China Tax/Business News Flash*, we will share the background of the case and the process of promoting the advance tax ruling, as well as our experience and observations in this process.

In detail

Background

The enterprise we assisted with the advance tax ruling is a foreign-invested enterprise in Fuzhou, Fujian Province (hereinafter referred to as "the enterprise"). In 2024, the enterprise planned to distribute dividends to its Dutch parent company and apply the preferential tax treatment for dividends stipulated by the tax treaty between China and the Netherlands, i.e., a 5% withholding income tax rate if the beneficial owner is a company (excluding partnerships) which holds directly at least 25% capital of the company paying the dividends.

According to the tax treaty and the *Public Notice of the STA Regarding the "Beneficial Ownership" under Tax Treaty* (STA Public Notice [2018] No. 9, hereinafter referred to as "PN9")², non-residents who would like to

enjoy the preferential treatment for dividends must qualify as the "beneficial owner." Whether the investment holding management activities carried out by a parent company as a holding company constitute "substantive" business activities is subject to different interpretations and practices in various regions, resulting in uncertainty.

Given the large amount of dividends involved, the enterprise, as a precaution, hoped that PwC would assist in communicating with the tax authorities to follow up the subsequent administration of the dividend distribution and obtain their opinion on the beneficial owner determination, to ensure tax compliance.

Process

At the beginning, Fuzhou had not yet established an advance tax ruling mechanism. However, the "TaxExpress - Maritime Silk Road · Devotion of Taxation" service brand created by the Fuzhou Municipal Tax Service requests actively promoting tax advance rulings on cross-border transactions. "TaxExpress" is a cross-border taxpayer service brand launched by the STA in recent years at the 10th anniversary of the "Belt and Road" initiative, aiming to better serve high-level opening-up. After studying the processes and positive impacts of advance tax rulings in other regions, the International Taxation Division of Fuzhou fully understood and supported the enterprise's need for tax certainty and took the lead in formulating internal administrative measures for tax advance rulings on cross-border issues in Fuzhou. In view of this, we assisted the enterprise in applying for advance tax ruling on the proposed preferential tax treatment for dividend distribution to the in-charge tax authority. After several rounds of on-site meetings and supplementary materials submitted, the tax authority recognized the "beneficial owner" status of the enterprise's Dutch parent company and ruled that it was eligible for the preferential tax treatment for dividend distribution under the tax treaty. The tax authority formed a written opinion on the ruling and issued a stamped *Advance Tax Ruling Opinion* to the enterprise.

Observations

This attempt for exploring advance tax rulings is an innovative move of the tax authorities in Fujian Province. In assisting the first case in Fujian Province, as well as, one of the few international tax advance ruling cases nationwide, we also had a deeper understanding of handling advance tax rulings.

- From the perspective of the **ruling issues**, this case focuses on the preferential tax treatment for dividend distribution under the tax treaty. Based on our practical experience, the application of tax treaty provisions is a high-frequency issue that leads to tax disputes between enterprises and tax authorities, including the determination of the beneficial owner status of dividends, the determination of permanent establishments for non-resident enterprises, the distinction between royalties and service fees, and the application of provisions on capital gains in cross-border transactions. Due to the complexity of the treaty provisions, enterprises may encounter difficulties in interpreting and applying these provisions. Moreover, the tax treaty treatment is based on the mechanism of "self-assessment, claim for treaty benefits, documents preservation for reference", which leads to greater uncertainty for enterprises. If such matters could be subject to advance tax rulings, it would be a more efficient and reliable way to ensure that enterprises fully utilize tax treaty benefits and reduce tax costs and risks with tax compliance. Currently, there are only a handful of publicly disclosed cases of advance tax rulings on cross-border issues nationwide. To stabilize enterprises' business expectations and optimize the tax business environment, we look forward to more advance tax rulings on cross-border issues given by tax authorities.
- From the perspective of the **ruling mechanism and process**, although most regions do not have publicly issued administrative measures, the *Opinions on Further Deepening the Reform of Tax Collection and Administration* issued in 2021 stipulated "exploring the implementation of advance tax rulings for large enterprises and establishing and improving related systems." Thus internal documents of working mechanism may have been formed within many tax authorities, or they may have experience with completed ruling cases. For advance tax rulings, China adopts a case-based approach, with both tax authorities and enterprises accumulating experience through real cases. In our case, even though the local tax authority had not yet worked on advance tax rulings, they showed high initiative in exploring the ruling mechanism. Moreover, the tax authority attached great importance to it. The tax service team, communicated with the enterprise, is established by members from the provincial, municipal and district tax authorities, and issue the *Advance Tax Ruling Opinion* within only four months. In this regard, for issues with tax uncertainty, enterprises can proactively discuss the feasibility of applying for advance tax rulings with tax authorities, which may encourage more active cooperation between tax authorities and enterprises.

The takeaway

Based on our experience, if enterprises consider obtaining tax certainty through advance tax rulings, it is essential to conduct a feasibility analysis of the costs, benefits and business considerations in advance. The issues that enterprises need to prepare and analyze before applying include but are not limited to:

- Estimating the transaction information that may need to be disclosed to the tax authorities and its potential impact;
- Calculating the tax impact amount of uncertain issues;
- Conducting advance technical analysis and forming reports;
- Estimating the tax authorities and departments that need to be communicated with;
- Estimating the duration to complete the advance ruling process;
- Estimating the potential tax effects, etc.

A thorough understanding of tax rules, a comprehensive analysis of tax issues and practical experience in the application process for rulings can help promote advance tax rulings and reduce the communication cost for both tax authorities and enterprises. It is recommended that enterprises seek assistance from tax professionals when necessary to ensure that advance tax rulings are implemented smoothly and professionally.

Endnote

1. *China Tax/Business News Flash Issue 11 of 2024: Beijing piloting advance tax rulings to optimise the tax business environment*

<https://www.pwccn.com/en/china-tax-news/2024q2/chinatax-news-may2024-11.pdf>

China Tax/Business News Flash Issue 1 of 2024: Interpreting the taxation breakthrough in 2024: Shanghai piloting advance tax rulings to enhance tax certainty

<https://www.pwccn.com/en/china-tax-news/2024q1/chinatax-news-jan2024-1.pdf>

China Tax/Business News Flash Issue 20 of 2022: Exploring cross-regional tax advance rulings to better support the national strategy for coordinated regional development

<https://www.pwccn.com/zh/china-tax-news/2022q3/chinatax-news-aug2022-20.pdf>

2. *Public Notice of the STA Regarding the "Beneficial Ownership" under Tax Treaty*

<https://fgk.chinatax.gov.cn/zcfgk/c100012/c5194781/content.html>

Let's talk

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