China alert

Tax and regulatory developments

Issue 18, February 2009

TAX

Qualified Foreign Institutional Investors subject to withholding tax of 10 percent on PRC-sourced dividend and interest income

In Brief

- Circular 47 clarifies that according to the new Corporate Income Tax (CIT), Qualified Foreign Institutional Investors (QFIIs) will be subject to Withholding Tax (WHT) at a rate of 10 percent on their PRC-sourced dividend and interest income upon payment or upon accrual of interest by PRC resident enterprises.
- Circular 47 is silent on the CIT treatment of PRC-sourced gains derived by QFIIs from the disposal of A-shares or other investments.

Relevant regulation discussed in this issue:

Notice on Withholding Tax treatment for PRC-sourced dividend, profit distribution, interest income derived by Qualified Foreign Institutional Investor, Guoshuihan [2009] No. 47, issued by the State Administration of Taxation on 23 January 2009 (Circular 47)

Background

The old Foreign Enterprise Income Tax (FEIT) regime did not specifically address FEIT treatments for QFIIs. Caishui [2005] No. 155 exempts PRC Business Tax on QFIIs' gains derived from the disposal of A-shares or other investments. We understand that before 1 January 2008, in practice, QFIIs did not proactively pay any PRC tax.

According to new CIT Law and the Implementation Rules, a non-resident enterprise is subject to WHT at 10 percent on its PRC-sourced dividend and interest income that are not effectively connected with any establishment or place of business in the PRC.

Contents of Circular 47

Circular 47 clarifies that, according to the new CIT Law and the Implementation Rules, WHT shall be levied at a rate of 10 percent on QFIIs' PRC-sourced dividend and interest income upon payment or accrual of interest by PRC resident enterprises.

An eligible QFII may apply to the PRC tax authority for the relevant tax treaty relief. Upon approval from the PRC tax authority, QFIIs can enjoy the preferential treatment as provided in the relevant tax treaty, e.g. a WHT rate of lower than 10 percent, which may result in a tax refund.

www.kpmg.com.cn
www.kpmg.com.hk

Contact us

Beijing/Shenyang
Khoonming Ho
Tel. +86 (10) 8508 7082
khoonming.ho@kpmg.com.cn

Qingdao
Vincent Pang
Tel. +86 (532) 8907 1728
vincent.pang2@kpmg.com.cn

Shanghai
John Lee
Tel. +86 (21) 2212 3402
john.lee@kpmg.com.cn

Nanjing
Chris Ho
Tel. +86 (21) 2212 3406
chris.ho@kpmg.com.cn

Hangzhou
Martin Ng
Tel. +86 (571) 2803 8081
martin.ng@kpmg.com.cn

Chengdu
Anthony Chau
Tel. +86 (28) 8673 3916
anthony.chau@kpmg.com.cn

Guangzhou/Fuzhou
Bolivia Cheung
Tel. +86 (20) 3813 8710
bolivia.cheung@kpmg.com.cn

Shenzhen
Eileen Sun
Tel. + 86 (755) 2547 1188
eileen.gh.sun@kpmg.com.cn

Hong Kong
Peter Kung
Tel. +852 2826 8080
peter.kung@kpmg.com.hk

Noteworthy issues

Circular 47 does not stipulate an effective date. However, given that Circular 47 was issued to clarify the provisions of the new CIT Law and the Implementation Rules which were effective 1 January 2008, Circular 47 should technically also be effective from 1 January 2008.

Circular 47 does not address the CIT treatment of PRC-sourced gains that QFIIs derive from the disposal of A-shares or other investments.

By Lewis Lu, Partner and Flame Jin, Senior Manager

All issues of *China alert* are accessible on www.kpmg.com.cn or www.kpmg.com.hk