One Belt One Road—Tax Issues for Chinese Going-out Companies

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ABSTRACT

The One Belt One Road initiative is regarded as the most ambitious foreign policy proposed by Xi Jinping, which involves billions of dollars of infrastructure investment along the routes. It is a great chance for Chinese multinational corporations to enter international market, but tax issues derived from this complicated economic environment need to be aware. Different taxation systems, double taxation on the same source of income and specific regulation on profit shifting relates to transfer price are threatening going-out companies. Based on the analyses of these risks, this paper discusses the countermeasures from national level and enterprise level. China has already taken actions like enhancing tax cooperation mechanism and establishing comprehensive taxation database, going-out companies also should be well-prepared before getting into the world market.¹

INTRODUCTION

One Belt One Road initiative is one of the most burning issues in China which was first raised by Chinese President Xi Jinping. In 2015, the Chinese government drafted and published the Vision and Actions on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road [1]. Unlike the ancient Silk Road which merely focused on trading between Asia and Europe, the One Belt One Road emphasizes on both boosting trades and the development of the economy.

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Along the One Belt One Road, China’s investment in cooperative countries of this initiative has hit $33 billion. More and more companies are actively responding to the initiative and investing their resources through mergers and acquisitions in the oversight areas. However, when state-owned companies are operating overseas, it is unavoidable to face some accompanying problems, such as troubles of adapting to the investment climate, the political environment or the monetary policy in other countries. As mentioned by Lu Hui [2], the countries along the One Belt One Road are world’s major high-risk countries, representing that they are different from China in economic systems, cultural characteristics etc. This leads to different regulation and law system, which means the risk of trade between these countries increases.

According to Angel Gurria[3], the secretary-General of Organization of Economic Cooperation and Development, better tax policies will help promote global trade cooperation and encourage innovation and promote inclusive growth in all countries. While making transnational investments, enterprises should be aware of those inconsistencies in tax practice and tax law systems among countries and are able to make reasonable tax avoidance without breaching the relative provisions in the operating country. PwC has suggested that those ‘going abroad’ enterprises pay high attention to the relevant tax policies, study the relevant tax laws, comprehensively consider the possible tax risks associated with the projects and plan for the appropriate action [4].

TAX-RELATED RISKS FOR GOING-OUT CORPORATIONS UNDER THE BACKGROUND OF ONE BELT ONE ROAD

For multinational corporations, there are three main risks relating to tax revenues. Firstly, the multinational corporations are often faced with the risk of failing to comply with the taxation law in different countries. Those countries have diversified tax culture that is suitable for their national situation. Obviously, it can be a big challenge for companies to comply with the regional tax legislation when they have transactions in the countries along One Belt One Road.

Secondly, the double taxation problem in One Belt One Road refers to the income taxes paid in different countries on the same source of earned income when international trade occurs. It violates the principle of tax equity and neutrality [5], for those companies’ concern, double taxation is an inevitable risk that affecting their return on the overseas investments. Basically, the shareholders will suffer a huge loss because of this problem and will be demotivated to operate firms in these countries. Besides, the international exchange of talent and technology will also be negatively influenced.

Thirdly, from the Chinese tax department’s point of view, it is a problem that multinational enterprises take advantage of different tax rates and policies among different areas to lower their own tax burden. For example, the cross-border companies might tend to provide subsidiaries with intangible assets, such as patents...
and technology, to get free of charge. In this case, profits from related party transactions have not been correctly reflected in accounting records. On the other hand, setting a reasonable transfer price to avoid being investigated by local tax office because of suspected tax evasion would also be a challenge for firms in related-party transactions. Some countries have specific regulation on profit shifting between parent firms and subsidiaries. However, it is hard to say what is a fair transfer price, especially for services and intangible assets. Investigation on Counter-tax from local government can be a serious problem for those corporations, which may lead to penalties.

NECESSARY STRATEGIES MADE BY CHINESE GOVERNMENT

China has already taken actions to manage tax risks in overseas enterprise operation. To eliminate tax barriers, international tax harmonization is the most effective method [6]. That is, majority of countries along the Belt and Road have signed Bilateral tax treaty with China. This tax cooperation mechanism includes harmonized tariff, coordination of commodity tax and income tax, etc. It also protects their legitimate rights from damaging when entering the global market. To alleviate the problem of double taxation, China signed comprehensive double taxation avoidance agreement with many countries, which provides companies preferential tax rate under different tax treaty. Chinese government put forward that profit should be taxed where the economic activities happen and create value. In those tax treaty, multinational corporations are entitled to obtain tax credit by showing tax payment receipts from other countries during tax return filing process.

Besides, under the background of this era of globalization and informatization, it is a significant step to make full use of big data platform, through which collecting and analyzing information, and giving feedback to companies offers them huge advantages to participate in the global market. To be more specific, State Administration of Taxation introduced a tax information website to build a comprehensive taxation guidance database that covers all One Belt One Road countries, which helps eliminate mismatches between regional law enforcement and improve transparency of various tax policies.

What’s more, there is no doubt that Chinese government is supposed to improve the ability of resolving disputation about tax among countries. Once a conflict occurred, “Going-out” companies that lack protection from tax policy may find difficulty in reasonable defense with local tax bureau.

As a result, State Administration of Taxation shows that tax burden of Chinese companies decreased by 270 million yuan because of the tax agreement signed in 2015. In 2016, tax deductions and exemptions were 28 billion yuan for overseas taxpayer due to reciprocity of bilateral agreement [7]. Apparently, China has made nations along the Silk Road better merge into international tax rules and gave material benefit to enterprise abroad.
COUNTERMEASURES FOR GOING-OUT COMPANIES

Based on the discussion above, to better implement “Going-out” strategy, firstly, Chinese companies need to learn more about legislation and understand regional tax ruling where trade will occur. In the long term, risks will be minimized only if companies get more and more familiar with local system and convention. Furthermore, it is indispensable to figure out tax revenue preferential policy in a region and gain an insight into tax system environment before investment. According to the collected information, company should develop tax management strategy that is consistent with company’s investment in overseas.

Secondly, companies should establish accounting teams equipped with professional tax knowledge to deal with cross-border trades and acquisitions. Involving local people in the team or having accounting firms to deal with tax issue can be helpful for the going-out companies to quickly adapt to the regional legal environment. China has joined the action plan of Base Erosion and Profit Shifting, which means multinational corporations should be cautious of tax avoidance and evasion [8].

Thirdly, companies should be aware of the importance of tax treaty and improve the ability of protecting themselves by reasonably making use of it. For the companies that are new to the foreign market, they should actively seek for help from Chinese government and tax authority when enterprises have problem managing tax. To safeguard the legal rights and interests in an international tax disputes, company can apply to State Administration of Taxation for Mutual Agreement Procedure.

REFERENCES