LEHMAN, LEE & XU

雷曼律师事务所

PRESS RELEASE

How does VAT work in China

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A value added tax (VAT) is a form of consumption tax. It is a tax on the estimated market value added to a product or material at each stage of its manufacture or distribution, ultimately passed on to the consumer. It differs from a sales tax, which is levied only at the point of purchase. but businesses are able to recover VAT (input tax) on the products and services that they buy in order to produce further goods or services that will be sold to yet another business in the supply chain or directly to a final consumer. In this way, the total tax levied at each stage in the economic chain of supply is a constant fraction of the value added by a business to its products, and most of the cost of collecting the tax is borne by business, rather than by the state. VAT was invented because very high sales taxes and tariffs encourage cheating and smuggling. Critics point out that it disproportionately raises taxes on middle- and low-income homes.

Edward E. Lehman, Managing Director of Lehman, Lee & Xu commented that, VAT is the major source of fiscal revenue for the Government of China, particularly the central government. In 2002, the revenue from VAT is 814.1 billion yuan, accounting for 47.61% of the state total tax revenue of the year, which is the first biggest tax in China. For making an equitable market environment and stimulating the investment, the government of China prepares to make a reform of VAT, which will change the type of China's VAT from the GNP type to the consumption type. On July 1, 2004, the state selected several north-east provinces as experimental area to implement the VAT of consumption type. In these provinces, the tax payers of VAT in eight selected industries can deduct the input tax of equipment used for production. With the development of Chinese economy and the increase of reform experiences, the central government will implement the VAT reform in all industries and provinces of China. What’s more, for setting up a uniform and equitable turnover tax system, some industries subjected to Business Tax would be levied on VAT at an opportune time.

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