



## China Cuts VAT Tax Rebates to Curb Exports

In June 2007, the Chinese government announced that it would cut tax rebates on more than 2,800 export items starting July 1. Manufacturers importing products from China should familiarize themselves with the changes and how they are impacting costs for their Chinese vendors.

In China, suppliers pay a VAT of 17% on most products. Like most countries with a VAT tax structure, China rebates a portion of the VAT back to producers when goods are exported from the country. Until July 1<sup>st</sup> of this year, the VAT rebate was 8% to 17% on most exported items. After July 1, China is reducing the rebate to 0% to 11% on affected products. These include certain metal products, textiles, shoes, and other manufactured goods (see attached Ministry of Finance Circular). In total, the goods affected amount to about 37% of China's exports.

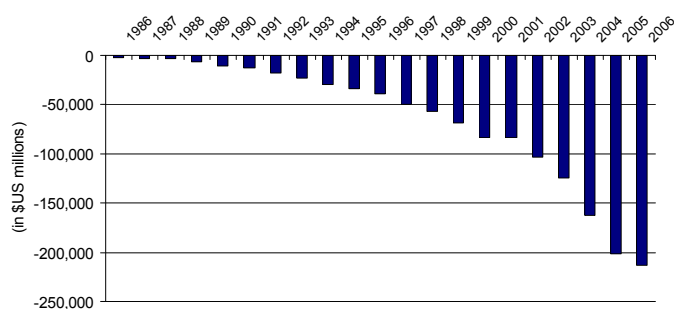
### VAT Explained

VAT or Value Added Tax is a tax paid by each firm in the supply-chain based on the value they add to a given product. For example, if a firm sold an item for \$1,000 and paid \$750 for the materials that went into the product, the firm would pay VAT as a percentage of \$250. Most developed countries use the indirect VAT system to collect taxes on goods and services. The United States is somewhat unusual in using a sales tax paid directly by the consumer at time of purchase.

### Why China is enacting a VAT reduction

In the 12 months through May 2007, China's trade surplus with the US alone equaled \$217 billion. Due to mounting pressure from the U.S. and European Union, the Chinese want to control the growth of this surplus by effectively raising taxes on items described as "easy to trigger trade friction". Also, the Chinese government says they want to restrict industries that use high amounts of energy, consume too many natural resources, or are highly polluting.

### U.S. TRADE BALANCE WITH CHINA



Note - 2006 = January thru November

Source: U.S. Census Bureau

### Effect of rebate reductions and a stronger Yuan on pricing

For affected Chinese suppliers, the impact of the VAT reductions is a cost increase of 2% to 8%. At the same time, the US dollar has been weakening steadily at about 4% a year against the RMB since September, 2005. The combined effect of these measures is likely to be price increases of 6% to 12% on affected products. Since Chinese suppliers frequently operate on thin margins, North American importers can expect attempts by their Chinese suppliers to pass these costs along.

#### VAT Rebates on Select Categories

	Old Rate	New Rate
Plastic products	13%	5%
Stampings	13%	5%
Wood door parts	11%	5%
Capital equipments	11%	9%

### Next steps

We recommend determining the cost impact of these tax changes on your suppliers prior to price renegotiations. The attached circular is the most comprehensive information published by the Chinese government in English. On the China Customs web page ([www.customs.gov.cn](http://www.customs.gov.cn)), users can input the specific HTS code of their items and confirm the new rebate. Unfortunately, this tool is only available on the Mandarin language version of the page. Please contact us if you would like our China team to do this for you. If your items are affected, now may be the right time to reconsider domestic sources or suppliers in other lower-cost countries such as Vietnam, Thailand, India, Malaysia, or Indonesia.

### About Transpac Access

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## **June 19, 2007 Circular of Ministry of Finance and State Administration of Taxation on Adjusting Export Rebate Rate of Some Commodities**

Authorized by the State Council, here are adjusted export rebate rates of some commodities. Related issues are announced as follows:

### **I. Dismantle export rebate rate of following commodities**

1. animals and plants on the verge of extinction as well as related products;
2. mineral products such as salt, solvent oil, cement, liquefied propane, liquefied butane and liquefied petroleum gas;
3. fertilizer (carbamide and ammonium phosphate whose rebated are dismantled already are excluded );
4. chemical product such as chlorine and coloring matters (fine chemical product is excluded);
5. metal carbide and active carbon products;
6. leather;
7. a part of wood block and disposable wooden products;
8. plain carbon welded tubes products (petroleum double-pipe is excluded);
9. simple non-ferrous metal products such as non-alloy aluminum bars;
10. vessel section and non-mechanized vessel.
11. Please refer to appendix 1 for commodity name and tariff code.

### **II. Deduct export rebate rate of the following commodities**

1. deducting the export rebate rate of plant oil to 5 percent;
2. deducting the export rebate rate of a part of chemical products to 9 percent or 5 percent;
3. deducting the export rebate rate of plastics, rubber and their products to 5 percent;
4. deducting the export rebate rate of box and bags to 11 percent, the leather products to 5 percent;
5. deducting the export rebate rate of paper products to 5 percent;
6. deducting the export rebate rate of wearing apparel to 11 percent;
7. deducting the export rebate rate of shoes and hat, umbrella and feather products to 11 percent;
8. deducting the export rebate rate of some stone materials, pottery, glass, pearl, gem, noble metal and its products to 5 percent;
9. deducting the export rebate rate of a part of steel and products (excluding petroleum double pipe) to 5 percent. The export rebate rate of the marine engineering construction of domestic trade stipulated in Circular of Ministry of Finance and General Administration of Customs on Rebate of VAT of Marine Engineering Construction (announcement No.46, 2003) shall stay unchanged;
10. deducting the export rebate rate of other base metals as well as their products (excluding commodities with their export rebates already dismantled and aluminum foil, aluminum pipe and aluminum construction) to 5 percent;
11. deducting the export rebate rate of planer, slotting machine, cutting machine and broaching machine to 11 percent, diesel engine, pump, fan, drain tap and its parts, revolving furnace, coke oven, Sartorius, stapler, snowmobile, motorcycle, bike, trailer, riser and its parts, tap and brazing machine to 9 percent;
12. deducting the export rebate rate of furniture to 11 percent or 9 percent;
13. deducting the export rebate rate of timekeeper, toy and other miscellaneous products to 11 percent;
14. deducting the export rebate rate of a part of wooden products to 5 percent;
15. deducting the export rebate rate of viscose fiber to 5 percent.

Please refer to appendix 2 for commodity name and tariff code.

III. The following commodities shall be exempted from tax peanut, canvas, carved board, stamp, and fiscal stamp. Please refer to appendix 3 for commodity name and tariff code.

IV. Time for implementation - The export rebate rate adjustment of above commodity shall take effect as from Jul 1, 2007. The specific time shall subject to the date of export on Declaration Form of Export Commodity (only for export rebate).

Export enterprises, which sign export contract involving export rebate cancellation before Jul 1, 2007 and would take the export contract (both original and copy are required) to tax authorities in charge of export rebate to register before Jul 20, 2007, shall be permitted to follow the original export rebate rate. Those failing to register before Jul 20, 2007 shall have the export rebate cancelled.

The equipment and building materials, involved in the long term foreign contracted project won or long term contract of foreign contracted project signed before Jul 1, 2007 by export enterprises with foreign contacted project qualification, shall be permitted to follow the original export rebate rate when the related export enterprises take effective certification of bid winning (both original and copy are required) or contract of long term foreign contracted project (both original and copy are required) and budgetary estimate bill of the project to tax authorities in charge of export rebate to register before Jul 20, 2007. Those failing to register before Jul 20, 2007 shall follow the adjusted export rebate rate.

Ministry of Finance  
State Administration of Taxation  
Date: Jun 19, 2007