

## Client Alert

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### China Issues Environmental Protection Tax Law

#### Recent development

Just days before the 2017 new year, the Standing Committee of China's National People's Congress passed China's first Environmental Protection Tax Law (the 'Law'). The Law is poised to replace the existing pollutant discharge fee system with a pollution tax as the main economic tool regulating environmental pollution by businesses in China. This historic development is expected to have sweeping impacts on enterprises' compliance with China's environmental regulations. The Law will come into effect on 1 January 2018.

#### What it means for pollutant-discharging enterprises

With the replacement of the existing discharge fee system with the environmental tax system, China's regulation of environmental pollution by businesses is expected to be more efficacious. The loopholes that have been exploited by local authorities and enterprises will disappear. Accordingly, the enterprises that directly discharge the taxable pollutants in China will be liable for the new tax payments under the Law. In response to the unprecedented system, enterprises are advised to plan ahead before the Law comes into effect, ascertain the standard and amount of the tax payable in their location, and make changes as necessary.

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#### What the Law says

The highlights of the Environmental Protection Tax Law are:

- The Law only targets the enterprises and other entities that directly emit a taxable pollutant. It does not tax those indirectly discharging pollutants.
- The Law also specifies what pollutants are taxable. The taxable pollutants, as listed on the Table of Taxable Items and Amount of Environmental Protection Tax appended to the Law, include air and water pollutants, solid waste, and noise. While common pollutants like sulphur dioxide and chemical oxygen demand (CDO) are among the taxable air pollutants, carbon dioxide (CO<sub>2</sub>) is excluded.
- The implementation of the Law requires coordination between the tax authority, who is in charge of administering the collection of environmental protection tax, and the environmental protection authority, who will monitor pollutants. Local governments are tasked with establishing mechanisms for the government agencies' coordination.
- The violators of the Law will be held liable under the Law on the Administration of Tax Collection and the Law on Environmental Protection.
- Enterprises that emit taxable pollutants into legitimate, centralised sewage and domestic waste treatment facilities, or store or dispose of solid wastes in facilities that meet relevant standards, are exempted from paying tax on such indirect emissions.





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- The Law grants local governments the discretion to determine and adjust the applicable tax amount on air and water pollutants within a specified range. In making such determinations and adjustments, governments at the levels of province, autonomous region, or municipality may take account of their specific environmental capacity; status quo of pollutant emissions; and economic, social, and ecological goals. The local adjustment is subject to approval by the Standing Committee of the National People's Congress.
- Five types of taxable pollutants are temporarily exempt from the tax: 1) those emitted from agricultural production (with scale-intensive farming excluded); 2) those emitted by motor vehicles, locomotives, ships, aircraft and other mobile sources; 3) those emitted from lawfully established, centralised urban sewage and domestic waste treatment facilities so long as the amount of emitted pollutants does not exceed the national or local standard; 4) solid waste comprehensively utilised by the taxpayer in compliance with the national or local standard; and 5) any other pollutants specifically exempted by the State Council.
- Environmental protection tax is calculated monthly and declared and paid quarterly.

Detailed regulations for implementing the Law are expected to be issued this year.

## Actions to consider

At the current stage, enterprises in China are advised to:

- Identify if they are liable for the new tax as an entity directly discharging the taxable pollutants specified in the Law.
- Ascertain if their discharges may be temporarily exempt from the tax under one of the five specified circumstances.
- Confirm the applicable tax rate in their location, which may be adjusted by the local government at its discretion.
- Keep an eye out for implementing regulations and measures put in place by local environmental and tax authorities for monitoring emissions and paying the tax.
- Consider ways in which to reduce emissions and the related tax liability.
- Seek advice from tax and environmental specialists where needed.

## Conclusion

The Law will likely result in substantial changes to the monitoring of environmental emissions and could have significant fiscal impacts on many enterprises in China. Chinese lawmakers have given companies and local governments one year to make the necessary preparations. Enterprises should take advantage of this time to understand the Law's implications for their business and make plans and relevant changes accordingly.

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