

Research on Preferential Tax System in Shaanxi Free Trade Area*

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Abstract—Based on the relevant theories and functions of the preferential tax system in the Free Trade Zone, this paper introduces the basic situation of the preferential tax system in Shaanxi Free Trade Zone. By drawing on the successful experience of the preferential tax system in the regional free trade zone, the paper proposes to improve the preferential tax system in Shaanxi Free Trade, so as to better serve the local economic construction, promote the rapid development of Shaanxi's economy, and promote the development strategies of the Silk Road in "the Belt and Road". At the same time, it provides feasible ideas for exploring a normative, rational and effective development path of tax preference in China's free trade zones.

Keywords—free trade zone; taxation; tax preference

I. INTRODUCTION

On October 24, 2018, General Secretary Xi made important instructions on the construction of free trade pilot zone, which is a strategic measure for the Party Central Committee to promote reform and opening up in the new era, and is a milestone in China's reform and opening up process. The General Secretary stressed that facing the future, on the basis of in-depth summary and evaluation, we should continue to emancipate our minds and actively explore, strengthen overall planning and reform, continuously improve the development level of free trade pilot zones, form more institutional innovations that can be replicated and promoted, build free trade pilot zones into new highlands for reform and opening up in the new era, and struggle for the realization of the "two centenary goals" and contribute more to the realization of the Chinese dream of the nation's great rejuvenation.

Since the establishment of Shaanxi Pilot Free Trade Zone for more than a year, it has actively explored around the strategic positioning, boldly tried, boldly progressed and independently reformed, made some positive explorations in the reform of "streamlining administration, delegating power, strengthening regulation and optimizing services", facilitation reform of investment and trade, financial service innovation and economic cooperation and humanities exchanges with the countries along "the Belt and Road", and achieved staged results. In the next step, the construction of Shaanxi Pilot Free

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Trade Zone will focus on institutional innovation, rely on the advantages of the starting point of the Silk Road in "Belt and Road" and the Great Western Development Strategy, strengthen the ability of duplicating and promoting, give full play to the "test field" of reform and opening up, accelerate the formation of an international and convenient business environment ruled by law, and a fair, open, unified and efficient market environment, accelerate the construction of the "five centers" on "the Belt and Road", namely transportation and trade logistics center, international capacity cooperation center, science and technology innovation center, international tourism center and regional financial center, strive to build Shaanxi into a new highland that comprehensively deepens reform and opening up, and form a new pattern of higher-level reform and opening up.

Looking around the developed free trade zones in the world, "convenient port environment, attractive taxation policies, developed infrastructure and complete management system" are important factors supporting the successful operation of the free trade zones. The same is true for the establishment of Shaanxi Pilot Free Trade Zone, in which the "tax preference" will undoubtedly play an active role in promoting the economic development, institutional reform, and management transformation of Shaanxi Pilot Free Trade Zone. On the basis of expounding the theoretical basis and function of the preferential tax system in the free trade zone, this paper comprehensively introduces the basic situation of the preferential tax system of Shaanxi Pilot Free Trade Zone, and proposes suggestions for the improvement of the preferential tax system of Shaanxi Pilot Free Trade Zone by learning from the successful experience of the preferential tax systems of the regional free trade zones abroad, and provides a feasible way to explore a normative, rational and effective development path of tax preference of China's free trade zones.

II. OVERVIEW OF THE THEORY OF TAX PREFERENCE OF FREE TRADE ZONES

A. Definition of Related Concepts

1) *Free Trade Zone*: As one of the main forms of regional economic integration, Free Trade Zones are very common in the world, but their manifestations are different. Free trade zones are sometimes called as foreign trade zones or tax-free trade zones. A free trade zone is a special customs zone

within the territorial part of a country that is legally considered to be outside the customs boundary and implements special customs control measures that goods can be stored without restriction in this zone, including trading, manufacturing, processing and assembly operations. A free trade zone has definitions in a broad sense and a narrow sense. Free trade zone in a broad sense refers to a free trade zone built between countries, and the resulting investment and trade agreement is a regional trade agreement. Since this level of free trade zone construction is not limited to trading fields, it also covers many other aspects of investment. Therefore, the internationally accurate reference to this is "closer economic partnership arrangement". For example, the North American Free Trade Zone, the European Union, etc. are free trade zones in a broad sense; free trade zone in a narrow sense refers to free trade zones within a country, which is also known as "free trade park", namely a special area in its territory that implements free trade policies. For example, the Panama Cologne Free Trade Zone and the Singapore Free Trade Zone are free trade zones in a narrow sense. Shaanxi Pilot Free Trade Zone is a free trade zone in a narrow sense.

2) *Tax preference*: Taxation is the most important form and source of income for public finances. It is a special income relationship formed by the state's mandatory increase in fiscal revenues as permitted by law. In the whole process of taxation, the state enjoys the taxation rights granted by the law on the one hand, and provides public services to the public on the other hand. Tax preference refers to the preferential policy that the state or government takes measures such as lowering tax rates and extending tax time for specific enterprises or investors to promote investment growth and industrial agglomeration to a certain extent. With the development of the economy and the deepening of theoretical research, people gradually realize that the tax preference essentially means that the state does not levy the part of the tax that should be levied. Therefore, tax preference is also called "tax expenditure". The difference between tax expenditure and fiscal expenditure is that the fiscal expenditure means that the state distributes the funds it owns to the social subjects, while tax expenditure means that the government does not levy the part of the tax that should belong to the government, and such expenditure method is sometimes more conducive to solving the problems faced by social subjects than general fiscal expenditures.

B. Functions of Tax Preference

The first is to promote knowledge spillover and technology transfer. No matter it is based on social public goals or based on the needs of economic development; tax preference will reflect the tilt to high-tech industries to varying degrees. Tax preference of free trade zones, as a prerequisite for the successful development of any free trade zone, will also promote technological innovation.

The second is to drive economic development. There is no doubt that the direct purpose for the establishment of free trade zone is to promote the economic development of ports or surrounding areas. The taxation policy of free trade zones will

promote the development of investment, trade, service industry and processing industry in the region to a large extent, and the objects of tax preference are not specific to the economic entities that meet the relevant conditions, which provide opportunities for equal participation in market competition by various enterprises. Under the incentive of preferential tax system, funds, technology, talents, services and other resources will continue to flow into the free trade zones under the guidance of market profit opportunities, so that the resources in the free trade zone will form a huge cluster effect, thereby driving the economic development of the free trade zone. In addition, due to the radiation effect of the free trade zone, the economic outlook of the surrounding areas will also be completely new.

The third is to attract foreign investment. Since Shaanxi Pilot Free Trade Zone implements "pre-establishment national treatment", foreign investors will enjoy the same tax preference offered by Shaanxi Pilot Free Trade Zone as domestic investors, which will attract more foreign investors to invest.

III. STATUS QUO OF PREFERENTIAL TAX SYSTEM IN SHAANXI PILOT FREE TRADE ZONE

A. Formation of Preferential Tax System in the Free Trade Zone

The preferential tax system in the free trade zone consists of two parts: the preferential tax policy determined by the Overall Plan and the specific tax preference issued by the relevant ministries. The Overall Plan is based on the premise of "maintaining the existing fair, unified and standard tax system" and guided by the "cultivation function", and has determined a number of preferential tax policies, including the promotion of foreign investment and foreign trade by the enterprises in the free trade zone. Taxes mainly involve corporate income tax, personal income tax, value-added tax and customs duties, etc. On the basis of the Overall Plan, the Ministry of Finance and the State Administration of Taxation have issued specific rules on relevant tax preference, thus forming a preferential tax system in the free trade zone.

1) *Promoting the composition of investment preferential tax system*: Enterprises or individual shareholders registered in Shaanxi Pilot Free Trade Zone may pay the taxes on the portion of proceeds from non-monetary asset investment and asset restructuring within 5 years. In order to implement this policy, the Ministry of Finance and the State Administration of Taxation have jointly issued the Notice on the Taxation on Proceeds from Non-Monetary Assets of Enterprises in Shaanxi Pilot Free Trade Zone, and the Notice on Corporate Income Tax Policies for Foreign Investment with Non-monetary Assets and Other Asset Restructuring Behaviors of Enterprises in China (Shaanxi) Pilot Free Trade Zone (Cai Shui [2013] No. 91) (hereinafter referred to as Cai Shui No. 91 file), which stipulate that "if enterprises or individuals registered in the pilot zone achieve assets assessment appreciation from foreign investment with non-monetary assets and other asset restructuring behaviors, the proceeds

from the transfer of non-monetary assets thereof can be evenly included in the taxable income of the corresponding year within a period of not more than five years, and the corporate income tax will be calculated and paid according to the regulations". This policy extends the tax period for enterprise or individuals to earn proceeds from non-monetary asset investments, and avoids the reduction of working capital of enterprises or individuals.

2) *Preferential tax policy for promoting trade*

a) *Preferential tax policy for financial leasing companies*: The financial leasing companies registered in the free trade zone or project subsidiaries established by the financial leasing companies in the free trade zone are included in the pilot scope of financial leasing export tax rebate. In China's current tax rebate policy, financial leasing companies are different from general enterprises in exporting goods. Before "replacing business tax with value-added tax", financial leasing companies are the payer of business tax and cannot enjoy the VAT export tax rebate. After "replacing business tax with value-added tax", according to the Notice of the Ministry of Finance and the State Administration of Taxation on Carrying out Pilot Taxation Policies for Replacing Business Tax with Value-added Tax in the Transportation Industry and Some Modern Service Industries Nationwide (Cai Shui [2013] No. 37), "leasing services of tangible assets for the subject matter used outside the territory shall be exempted from VAT unless otherwise stipulated by the Ministry of Finance and the State Administration of Taxation". Unlike the zero-tariff policy of VAT, tangible movable property purchased by leasing companies does not include VAT tax, which means that the financial leasing companies after "replacing business tax with value-added tax" still cannot enjoy the export tax rebate policy, resulting in higher tax of financial leasing companies on exporting leases than the tax burden of the goods of the manufacturer, which will weaken the competitiveness of China's financial leasing companies in providing transnational services. Based on this, the Overall Plan will include the financial leasing companies in free trade zones into the scope of export tax rebate pilot, which is of great significance for encouraging the development of Shaanxi financial leasing industry.

b) *Selective tax policy*: For the goods produced and processed in Shaanxi Pilot Free Trade Zone and sold in the mainland, enterprises may decide to pay the consumption tax and value-added tax in the import link according to the "the nature of the imported materials in the finished product" or the "the actual sales status of the goods". According to the Customs Law, the Regulations on Import and Export Tariffs of the People's Republic of China and the Rules on Import and Export Tariffs of the People's Republic of China, customs duty-paid prices must be determined according to the nature of the materials, and the management is relatively complicated. The levying methods can be roughly divided into two types: one is to levy according to the imported materials contained in the finished products, and the other is to levy according to the actual state at the time of domestic sales. Different tax calculation methods will affect the

customs duty-paid price and tariff rate, and affect the import value-added tax and consumption tax in turn. The implementation of "selective tax policy" means that enterprises registered in free trade zones can choose the basis for customs declaration and tax paying of domestic goods: enterprises can either pay taxes according to the state of the goods imported, or according to the actual customs declaration status of the goods. Enterprises have the right to choose independently to pay taxes in the way with lower tax rate according to the above two situations. The introduction of the "selective tax policy" clarifies the choice of enterprises on the one hand, and reduces the tax burden of enterprises on the other hand.

IV. REFERENCES TO THE PREFERENTIAL TAX SYSTEM IN FREE TRADE ZONES ABROAD

A. *Hamburg Free Trade Zone*

As a pioneer in the development of free trade zones in the world, Europe's free trade zones use their unique port location and developed transportation network to develop entrepot trade, and Europe's free trade zone have gradually become the world's cargo gathering and divergence centers. Hamburg Free Trade Zone used to be the largest free trade zone in Europe, and its biggest feature lies in its management of tax preference. Since Hamburg, Germany has its own independent parliament and government, forming a preferential tax management pattern in which Hamburg government formulates an overall plan for issues related to the free trade zone, specific labor and economic departments implement, and enterprises operate freely in the free trade zone. In addition, according to Article 166 of the European Commission's Articles, "there is almost no need for any customs formalities within Hamburg Free Trade Zone, Germany, thus providing maximum freedom for the exchange of international goods". The German Federal Law also stipulates that the status of the "the free trade zone" is like a third country's territory, the customs grants maximum freedom to the goods entering and leaving the free port, the goods can be arbitrarily circulated in the Free Trade Zone without the need to pay customs duties, and the customs formalities and related tariffs are required only when the goods enter the EU market." Such special management model reduces the daily workload of the government while enhancing the liquidity of goods, and improves the independent competitiveness of enterprises. The original intention of convenient customs supervision in Hamburg Free Trade Zone is not to increase the taxation of the free trade zone, but to allow the free circulation of goods in the free port through the convenient and free trading environment in the free port to the utmost extent through the convenient and free trade environment in the free port, promote the development of trade and logistics in the free port, and drive the economic development of the entire region, the country and even Europe.

B. *New York Free Trade Zone*

The free trade zones in the United States are generally located in convenient locations such as port or airport. There is no tax on goods shipped abroad in this special area, and customs clearance and customs duties are not required for

goods entering the area; goods subject to customs clearance entering other free trade zones are regarded as goods exporting. The biggest feature of New York Free Trade Zone is that the US Foreign Trade Zones Act identifies 21 clear and specific provisions on tax preference. As one of the largest free trade zones in the United States, the New York Harbor Free Trade Zone plays a role in free trade and cargo transfer based on the

main business of import and export goods. In order to further stimulate the development of manufacturing industry in the Free Trade Zone, New York Free Trade Zone has given 21 tax reduction policies, including 9 preferential tax measures such as delaying the payment of import tariffs, independent choice of tariff rates, tariff-free exports, and international returns. (See “Table I”).

TABLE I. PREFERENTIAL TAX MEASURES OF NEW YORK FREE TRADE ZONE

Type of preferential tax	Specific preferential tax measure
Delay in paying import tariffs	No import tariff is required for goods shipped into the Free Trade Zone immediately. The tariff is required only when the goods are shipped into the United States through customs, which is beneficial to companies' cash management.
Independent choice of tariff rate	By setting up a factory in the Free Trade Zone, companies can independently choose the tax rate of the raw materials or the finished products, so that they can choose to pay with the lower tax rate.
Tariff-free export	Enterprises in the Free Trade Zone can set up factories to export without the need to pay any import and export tariffs.
Save tariff paid for scrap	If the enterprise has not set up a factory in the Free Trade Zone, no import tariff is required for the scraps in the imported raw materials and the raw materials wasted in the production process.
International return	If the products of the Free Trade Zone exported overseas are returned, no import tariff is required for the returned goods.
Imported spare parts	Enterprises can store unneeded imported spare parts in the Free Trade Zone's warehouse, and if they do not need the spare part at last, they can return or destroy them without tariff.
Save cargo handling fees	Goods in the Free Trade Zone can pass through the customs 24 hours a day without restrictions. Enterprises only need to declare the customs clearance record once a week and pay the cargo handling fees. The weekly processing fee for each enterprise is up to US\$485.
Port maintenance fee	Enterprises in the Free Trade Zone pay quarterly maintenance fees based on the quantity of goods shipped into the Free Trade Zone, without the need to pay for each import.
Inventory tax	Most state and local tax authorities in the United States exempt the inventory tax on all goods in the Free Trade Zone.

C. Singapore Free Trade Zone

The biggest feature of the early stage of Asian economic development is the "labor-intensive industry", which takes advantage of the relatively low labor cost and develops a large number of export-oriented trades on the basis of attracting foreign investment and technology. In the later period, with the rapid rise of the economy and the accumulation of technology, the Asian free trade zones gradually developed from single manufacturing and processing business to comprehensive business with higher technology content, among which the development of the Singapore Free Trade Zone attracted people's attention. The biggest feature of the Singapore Free Trade Zone is that the tax preference in the Free Trade Zone has unified laws as support.

In 1969, Singapore established its first free trade zone in Jurong Terminal in Jurong Industrial Zone. With the continuous development of the world economy and international trade, Jurong Free Trade Zone has gradually developed into a highly open trade free port. In the construction of laws for the Singapore Free Trade Zone, the Singapore Government has enacted three laws: Management Measures of Singapore for Import and Export Commodities, the Customs Law of Singapore and the Singapore Free Trade Zone Act. Under the support of these free trade zone acts, the Singapore Government has successfully built the Free Trade Zone into a duty-free zone and a cargo distribution center with international standards, which facilitates the enterprises to store goods in the Free Trade Zone and re-evaluates, processes, packages these goods, and finally re-exports or transits. These policies attract goods from Asia Pacific and even around the

world to transit in Singapore. Today, Singapore Free Trade Zone has become one of the freest regions in global trade, with foreign direct investment accounting for 70% of total manufacturing investment.

V. MEASURES OF PREFERENTIAL TAX SYSTEM IN SHAANXI PILOT FREE TRADE ZONE

A. Unified Legislative Power on Tax Preference

According to the Notice of the State Council on Clearing and Regulating Taxes and Other Preferential Policies issued by the State Council on November 27, 2014, "under the guidance of the statutory principle of taxation, from November 27, 2014, the State Council is the only administrative department that has the authority to establish preferential tax laws and regulations, and other regional or administrative departments may not formulate preferential tax laws and regulations, unless in accordance with the Law on Regional National Autonomy and the special tax laws or the approval of the State Council". The Notice excludes the legitimacy of local and regional formulation of tax preference, and limits the prerequisites for legality to special tax laws and regulations and the authorization of national regional autonomy legislation, in which the "laws and regulations" obviously mean the "administrative laws and regulations", which means that the legality of tax preference includes administrative laws and regulations. The tax preference in the Pilot Free Trade Zone is introduced by the State Council, and then the Ministry of Finance, the General Administration of Customs, the State Administration of Taxation and other relevant departments are responsible for the implementation rules of the collectives,

which is not in line with China's current basic tax laws and regulations. Under the guidance of the statutory principle of taxation, the National People's Congress or its Standing Committee shall formulate a tax preferential law for regional free trade zones and provide a unified and universally applicable basic rule for regulating the tax preference of Shaanxi Pilot Free Trade Zone. At the same time, according to the authorization of the National People's Congress in 1985 and the needs of practical development, the State Council may formulate administrative regulations on the establishment of operational tax preference in specific free trade zones.

B. Strengthening Supervision of Tax Preference

First of all, it is necessary to establish a tax preference budget management system, and estimate the tax losses of finance and the incentive effects on market entities brought by various tax preference measures in advance before the implementation of tax preference. Through comparative analysis, with the support of relevant statistical data, a special tax preference budget report is made and included in the budget approval process.

Second is to establish a regular assessment and exit mechanism for tax preference. As far as tax preference assessment is concerned, the Ministry of Finance can be responsible for formulating a comprehensive tax preference assessment method and assessment system. The specific assessment of Shaanxi Pilot Free Trade Zone's tax preference law can be implemented jointly by Shaanxi Provincial Government and the Management Committee of Shaanxi Pilot Free Trade Zone. For tax preference measures that have already been implemented, effectiveness of their implementation and the necessity and feasibility of continuing implementation in the future should be assessed. Measures that are clearly not necessary and feasible should be stopped through standardized procedures; for those tax preference measures that have been recently issued but not yet implemented, the necessity and feasibility of their implementation and possible results of future implementation should be assessed in advance. Through assessment, the tax preference measures that are not necessary to be implemented should be abolished; the tax preference measures that do not meet the current economic development situation but are likely to achieve good results in the future should be actively adjusted.

C. Establishing Disclosure and Accountability System for Tax Preference Information

The basis for strengthening tax preference management is the statistics of tax preference data. Without accurate statistics, it is impossible to make reasonable assessment and management. Based on this, the Management Committee of Shaanxi Pilot Free Trade Zone should establish a directory listing system for the tax preference laws of Shaanxi Pilot Free Trade Zone. The list of tax preference in Shaanxi Pilot Free Trade Zone should focus on tax rates, tax types, tax paying time, tax preference cost, tax preference budget, performance evaluations and other data. Unless it involves national trade secrets or national security, all tax-related information such as the formulation, implementation, adjustment and abolition of

the tax preferential laws of Shaanxi Pilot Free Trade Zone shall be announced to the public in a timely and comprehensive manner in the form of a directory list and accept social supervision. The financial department, discipline inspection department and procuratorial department shall be responsible according to division of labor, promptly investigate and punish various violations of the tax preference laws and regulations, and severely punish those responsible persons.

VI. CONCLUSION

Establishing preferential tax measures in Shaanxi Pilot Free Trade Zone is an important measure to promote China's economic development and promote a new round of reform and opening up. Due to the short development time of Shaanxi Pilot Free Trade Zone, there are many defects in establishment basis, content composition and supervision mechanism of tax preference. Based on the advanced experience of foreign free trade zone construction, combined with China's national conditions, this paper puts forward some constructive opinions for tax preference system reform. The tax preference system of Shaanxi Pilot Free Trade Zone should unify the legislative powers of tax preference, establish an evaluation and exit mechanism, and establish an information disclosure and accountability system. It is hoped that Shaanxi Pilot Free Trade Zone will be able to better serve local economic construction by establishing a tax preference system, promote the rapid development of Shaanxi's economy, promote the development strategy of the Silk Road in "the Belt and Road", and provides feasible ideas for exploring a normative, rational and effective development path of tax preference in China's free trade zones at the same time.

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