

1. The evolution of EU-China trade partnership and tax-related issues

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1.1. Introduction

The People's Republic of China ("China") nowadays is a strategic partner of the European Union ("EU"), as well as a strategic rival, proposing alternative models of governance in certain fields and being a leading technological power.

The EU-China trade relationship started officially in 1975. Since then, the soaring globalised economy and the intensification of digitalization broadened the connections between the two parties, and so the interactions of the tax systems who lead to an increase of the risk of tax-related barriers and distortions on the one hand, and on the other hand the exploitation of mismatches between different tax regimes by businesses operating internationally. International trade and taxation are strictly related.

Even if sometimes it is alleged the lack of transparency and of level playing field on the Chinese side, it is undeniable that the EU and China are still open to cooperation and that the EU is showing its intention to found a balance in trade and tax matters, insisting on reciprocity, to minimize the mentioned risks.

1.2. Evolution of relationships from the 1978 Trade Agreement to the CAI and the BEPS Action Plan: bridging the links

Ten years after the creation of the EU Customs Union, a first agreement marked the beginning of trade relationships between the EU and China, despite the different nature of the interests of the two contracting parties underlying the signature – primarily economic for the first and political for the second². On 3rd April 1978, the official signing ceremony took place in Brussels – it was the first occasion on which the institutions of the European Economic Community ("EEC") received a member of the Chinese government³– and on 1st June 1978 the *Trade Agreement between the European Economic Community and the People's Republic of China* entered into force⁴ ("1978 Trade Agreement").

As far as tariffs are concerned, the two parties agreed to apply the most-favoured-nation ("MFN") clause⁵. So, any favourable provisions as regards customs duties and any taxes and charges in connection with importation and exportation of goods and services under other treaties with other contracting parties shall be accorded in the exchanges between the nine EEC countries⁶ and China – exception made for customs unions, free trade areas, advantages to neighbouring countries and obligations undertaken under international commodity agreements. One of the main clauses of the General Agreement on Tariffs

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2 ECC was interested in signing a trade agreement with China for "economic gains", while the reasons encouraging China to these negotiations were mainly political, see XIAOTONG, Z. "Linkage Power. How the EU and China managed their economic and trade relationship", in TELÓ, M., CHUN, D. and XIAOTONG, Z. (2018) (eds.), *Deepening the EU-China Partnership. Bridging Institutional and Ideational Differences in an Unstable World*, Routledge, Oxon and New York, 2018, p. 155-156.

3 See European Communities – The Council, *Signing of the trade agreement between the EEC and the People's Republic of China. Speech by K.B. Andersen, President in Office of the Council, Minister for Foreign Affairs of the Kingdom of Denmark*, Brussels, 3 April 1978.

4 COUNCIL REGULATION (EEC) No 946/78 of 2 May 1978 concerning the conclusion of the Trade Agreement between the European Economic Community and the People's Republic of China.

5 Art. 2 of the 1978 Trade Agreement.

6 Belgium, Denmark, France, Germany, Ireland, Italy, Luxembourg, Netherlands and United Kingdom.

and Trade (“GATT”)⁷ were therefore included in this first agreement, even if China was not yet a member of the GATT/WTO (*see below*).

Moreover, China undertook to consider Community imports in a favourable light and the ECC of nine, for its part, committed itself to endeavour to increasingly liberalize imports of Chinese origin, extending the list of liberalized products and augment the amounts of quotas⁸. To boost the cooperation, they also agreed to create a Joint Committee.

Considering the satisfactory application of the 1978 Trade Agreement⁹, the EEC and China decided to enter into a new trade agreement –the *Agreement on Trade and Economic Cooperation between the European Economic Community and the People’s Republic of China* (“1985 Trade Agreement”)– which was signed on 21st May 1985 and entered into force on 1st October 1985. As regards tariffs, the terms of the 1985 Trade Agreement were the same as those of the 1978 Trade Agreement: the MFN was reiterated. As it is evoked by the official title, the novelty aspect with respect to the previous treaty relates to the new provisions about the *economic cooperation*, including the promotion of investments and the enhancement of a propitious framework for the latter¹⁰. In any case, the EEC Members States were still allowed to undertake bilateral activities and conclude agreements relating to economic cooperation¹¹.

The mentioned two agreement are a manifestation of the trend reversal of the Beijing glance towards the outside world, opening the doors to foreign investment¹².

This change is also perceived in the purely (international) fiscal sector. It is during the Eighties that the first double tax treaties, including those with some of the EEC countries¹³, were negotiated and signed. Moreover, starting from the 1979, several acts concerning the taxation of foreign investments were enacted to attract the latter and expand economic cooperation: on 1 July 1979 the Act of the People’s Republic of China on Joint Ventures Using Chinese and Foreign Investment, on 10 September 1980 the Income Tax Act of the People’s Republic of China Concerning Joint Ventures with Chinese and Foreign Investment, on 13 December 1981 the Income Tax Act of the People’s Republic of China for Foreign Enterprises (the two latter then replaced in 1991 by the Income Tax Act of the People’s Republic of China for Enterprises with Foreign Investment and Foreign Enterprises)¹⁴.

In the period at hand, the financial flow was mainly unidirectional: from the EEC companies to China and it is also confirmed by article 13 of the 1985 Trade Agreement which drawn attention on the different levels of development of the two contracting parties¹⁵. However, this was about to change.

China was determined to pursue the path undertaken as increasingly market-driven economy and therefore to participate in the multilateral trading system. In 1986, China requested the resumption¹⁶ of its status as a GATT contracting party. An early accession of China to the GATT was supported by the

7 Art. 1 of the GATT.

8 Art. 4 of the 1978 Trade Agreement.

9 Preamble of the Agreement on Trade and Economic Cooperation between the European Economic Community and the People’s Republic of China.

10 Art. 12 of the 1985 Trade Agreement.

11 Art. 14 of the 1985 Trade Agreement.

12 AUYEUNG, P. K. (2003). “Taxation Trends and Issues in the People’s Republic of China: 1984 to 2006”, in *Bulletin for International Taxation*, IBFD, Amsterdam, June 2008, p. 249.

13 E.g. with France in 1984, Italy in 1986, Netherlands in 1987, United Kingdom in 1984. See www.oecd.org.

14 WTO, *Accession of the People’s Republic of China. Decision of 10 November 2001*, 23 November 2001, WT/L/432, pp. 75-76, available at www.wto.org; AUYEUNG, P. K. (2003).; *op. cit.*, pp. 249-251; BAO, L. “China’s Tax Policy toward Enterprises with Foreign Investment: A Comprehensive Appraisal”, in *Intertax*, Kluwer Law International, 2003, Vol. 31, Issue 2, pp. 66 *et seq.*

15 “In view of the difference in the two Contracting Parties’ levels of development, the European Economic Community is prepared, within the context of its development aid activities, within the means at its disposal, and in accordance with its rules, to continue its development activities in the People’s Republic of China. / It confirms its willingness to examine the possibility of stepping up and diversifying these activities.”

16 China was a signatory of the GATT in 1948, but –after the revolution in 1949– the Taiwan government announced the withdrawal from the GATT. The Beijing government never acknowledged the latter withdrawal; however, it notified the resume of the membership in 1986. See WTO Press Release, “WTO successfully concludes negotiations on China’s entry”, 17 September 2001, Press/243, available at www.wto.org.

EEC with which Beijing carried out bilateral negotiations¹⁷; but due to historical, economic and political reasons it was delayed until 2001, when China acceded to the Marrakech Agreement Establishing the World Trade Organization (“WTO Agreement”) and thereby became a member of the World Trade Organization (“WTO”). One of the interests of the EEC, then –since 1993– the European Community (“EC”), was to improve “the climate for European investment in China”¹⁸ and so also to significantly whittle Chinese import tariffs on industrial and agricultural goods as well as to ameliorate the establishment and trade conditions in China for foreign companies¹⁹. This goal was attained quite successfully. From a tax perspective, a series of important commitments were undertaken by China, *inter alia*²⁰:

1. The foreign individuals and enterprises will be accorded treatment no less favourable than that accorded to those in China (even as regards border tax adjustments);
2. The elimination of subsidy programs falling within the scope of article 3 of the Agreement on Subsidies and Countervailing Measures (“SCM Agreement”);
3. China will ensure the compliance of customs fees, internal taxes and charges with the GATT;
4. The elimination of all taxes and charges on exports, except for those specifically provided in the Protocol or applied in conformity with Article 6 of the GATT;
5. The notification of subsidies pursuant to Article 25 of the SCM Agreement;
6. China bound tariffs for imported goods, it committed to decrease the average bound tariff level for agricultural and industrial products and it will eliminate several tariffs and reduce others mostly by 2004 and in any case no later than 2010.

Simultaneously, in 1997 the EC Council authorised the EC Commission to negotiate a customs cooperation agreement on behalf of the EC and in 2004 it approved the *Agreement between the European Community and the Government of the People’s Republic of China on cooperation and mutual administrative assistance in customs matters* (“CCMAA”). Taking also into account that “operations in breach of customs legislation including infringements of intellectual property rights are prejudicial to the economic, fiscal and commercial interests of both Contracting Parties”²¹, China and the EC decided to enhance the cooperation between competent administrative authorities in ensuring the accurate assessment of customs duties and other taxes. Customs cooperation covers all matters relating to the application of customs legislation²², including exchange of information and expertise on customs techniques and procedures, exchange of personnel and training, seeking a coordinate position in the context of international organisations as well as the assistance in ensuring the proper application of customs duties (*i.e.* recovery of duties, taxes or fines, arrest or detention) and prevention and fight against fraud²³. Recently, to reiterate and increase the effectiveness of the mutual cooperation and assistance in the field of customs, the European Commissioner for Economic and Financial Affairs and the Minister of Customs of China has signed a *Strategic Framework for Customs Cooperation for the years 2018-2020*, which *inter alia* extends the collaboration to the e-commerce sector and supports the review of the CCMAA²⁴.

17 Commission of the EC, *Communication from the Commission. Building a Comprehensive Partnership with China*, 25 March 1998, COM(1998)181, p. 12.

18 *Ibidem*.

19 *Ib.*, pp. 12-16.

20 Protocol on the accession of China annexed to WTO, *Accession of the People’s Republic of China. Decision of 10 November 2001*, *op. cit.*; WTO Press Release, “WTO successfully concludes negotiations on China’s entry”, *op. cit.*

21 COUNCIL DECISION of 16 November 2004 on the conclusion of an Agreement between the European Community and the Government of the People’s Republic of China on cooperation and mutual administrative assistance in customs matters, 2004/889/EC.

22 Art. 6 CCMAA.

23 Art. 6-10 CCMAA.

24 The mentioned Framework follows the *Strategic Framework for Cooperation* for the period 2010-2012 and that for the period 2014-2017. See the note to delegation of the Council of the European Union, *Enhancing EU-China Trade Security and Facilitation: Strategic Framework for Customs Cooperation 2018-2020 between the European Union and the Government of the People’s Republic of China*, 22 May 2017, 9548/17.