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From Source-oriented to Residence-oriented: China's International Tax Law Reshaped by BRI?

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Serie Política de la Competencia y Regulación

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Contenido

Abstract

The Belt and Road Initiative (BRI), as one of the most remarkable events of international economic cooperation nowadays, has noticeable implications for many areas of study. This article is to explore how BRI, an initiative proposed and championed by China, has influenced China's international tax system. To answer the question, the article sets two poles for depicting a country's position of international taxation, namely, the source-oriented tax system and residence-oriented tax system. Based on that, this article puts forward the proposition that there is a trend that China's international tax system is transforming from source-oriented to residence-oriented. To verify the proposition, this article uses a conceptual and factual approach to analyze the rule-based changes driven by BRI. And those changes are from two aspects, the domestic tax law and the bilateral tax treaty of China. In addition to them, the top design of BRI with particular reference to international tax policy will be discussed beforehand. In the end, the article is concluded by rendering the proposition as tenable.

A. Introduction

The Belt and Road Initiative[1] is a regional and transnational cooperative economic framework launched by China, which aims to revive its ancient economic ties with Eurasian countries.[2] Although announced by President Xi Jinping only in 2013, the geographic coverage and economic data that BRI has achieved are eye-catching. Up to April 2019, China has signed BRI 'Cooperation Agreements' with 131 countries[3], which has shown the parties' political commitment to further cooperating under the initiative. In the first 5 years (2013-2018) of BRI, the flow of foreign direct investment (FDI) from China to BRI countries had surpassed USD 90 billion, and the newly signed engineering project contracts valued more than USD 600 billion, with an annual increase rate of 11.9%.[4]

For China, BRI has been the strategic focus of the government since its launch. The Party and the central government ministries have been enacting guiding documents frequently to reform and regulate, but ultimately to facilitate the construction of BRI. Their efforts have covered considerable fields, including but not limited to infrastructure, technology, energy, environment, economy and so forth. Among those areas of rules, taxation has also been viewed as having a key role to play in advancing BRI.

The purpose of this article is to question the implications of BRI for the development of China's international tax system as a whole. And it presupposes that there exists a mode of transformation that could be used to capture the evolution of an international tax system. According to that, this article proposes the claim that under the influences of BRI, there is a trend that the international tax system of China ('ITSC'), is transforming from source-oriented to residence-oriented. To start the verification process of the claim, the Part B lays down some background information about BRI and the ITSC. Part C will elucidate the research claim and the verifying approach. Part D then turns to explore the top design

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1 The 'Belt' is for 'Silk Road Economic Belt', and 'Road' is for '21st-Century Maritime Silk Road'. In 2015, several ministries of China published the official English translation for BRI. Before that, the 'Belt and Road' was also mostly known as 'OBOR' for 'One Belt and One Road' or 'One Belt, One Road'. See for example, Zheng Yawen, The Establishment of a Multilateral Investment Treaty for the 'One Belt, One Road' Initiative, (2018) Special Issue Cambridge Law Review.

2 However, as shown in Chart 5, BRI reaches out further than Eurasia, which has embraced Africa, Oceania, North and South America into its map.

3 See 'List of Countries that Have Signed 'Belt and Road' Cooperation Document with China' https://www.yidaiyilu.gov.cn/gbjg/gbgk/77073.htm, accessed 30 April 2019.

4 See 'The Regular Press Conference of the Ministry of Commerce (MOFCOM) (18 April 2019)' http://www.mofcom.gov.cn/xwfbh/20190418.shtml, accessed 30 April 2019.

of BRI with a special reference to tax policies. Part E and Part F will identify and analyze the BRI-driven changes of the two components of the international tax system, respectively the domestic tax laws and the double tax agreements. For domestic part, the discussions will cover the foreign tax credit system and the controlled foreign corporation (CFC) regime. For tax treaty part, this article will inspect the changes from breadth and depth. For breadth, the analysis looks into the general picture of China's bilateral treaty network, while the depth part will discuss the content changes of sparing credit, the withholding tax liability, and the most-favored-nation clause. Based on all these discussions, this article is concluded by Part G revisiting the claim and rendering the result of the verification.

B. The International Tax Law of China

1. BRI and International Taxation

Being a transnational framework, the key starting point of BRI is to `connect the markets of China and its partners in the BRI. Yet comparing the level of development of China and most of BRI countries, the export of investment from China outweighs China's import from BRI countries. As a result, such 'inter-connection' implicitly advocates more for the removal of barriers to the Chinese outbound investment at both the China side and BRI countries. The other way round, facilitating the inbound investment into China, however, only gains normative weight in the framework of BRI.

Based on the above, inspecting how China adjusts itself to the demand and reality of BRI may provide valuable insights to understanding China's strategy and foreseeing its future actions as well. This article, limits that inspection to the area of taxation, and more specifically, to the international aspects of corporate taxation.

2. China's International Tax System

The international tax system of China, or technically, China's foreign-related tax law has two components[5], the domestic tax law and the double tax agreements (DTA) signed with other tax jurisdictions. And that composition generally reflects the basic norm of international taxation. The following only lays down some background information for the purpose of later and deeper discussions.

The current international tax model has been commonly accredited to the contributions made in the 1920s by the League of Nations.[6] To this day, if we compare the international tax law of China to the common international tax model, the former is still an 'infant' to the latter, which is going to celebrate its 100th anniversary. The ITSC was born in the 1980s, for the facts that either its first DTA was signed in 1983[7], or that the first foreign-related enterprise income tax law was enacted in 1980 as well[8]. However, in modern times, China's international tax system is closer to maturity, after going through its 'adolescent' restlessness. That maturity can be partly explained by the so-called 'latecomer advantage', in that Chinese international tax system grows out of the modern international tax institutions.[9]

For one thing, the ITSC is consistent with the *residence-source* model of international tax model. China taxes the worldwide income of residents while providing foreign tax credit to eliminate double taxation. For non-residents, the Chinese tax liability is limited to the income derived within China. As a result, to be well-functioning, the residence-source international tax model is in turn dependent on the delineation of

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5 This relates to the nature of international tax law, see for example, Brian J. Arnold, Canada's International Tax System: Historical Review, Problems and Outlook for the Future, Canada in International Law at 150 and Beyond Paper No. 8, pp. 1-2.

6 de Wilde, Maarten Floris, 'Sharing the Pie'; Taxing Multinationals in a Global Market (January 15, 2015), available at SSRN: https://ssrn.com/abstract=2564181, p. 12.

7 SAT, 'List of Double Taxation Agreements Signed by China', see http://www.chinatax.gov.cn/n810341/n810770/index.html, accessed 1 May, 2019.

8 Income Tax Law of China Concerning Chinese-Foreign Equity Joint Ventures.

9 Jinyan Li, International Taxation in China: A Contextualized Analysis, IBFD, para. 1.3.2.2.

residence and source concepts. For the concept of residence, China uses the test of place of incorporation and place of effective management[10], which is further supplemented by provisions of its DTAs (usually article 4). The identification of source is generally aligned with the categorization of incomes, of which the foundational division is between positive(business) incomes and passive(investment) incomes.

For another, China now has one of the largest tax treaty networks in the world. By the end of April 2019, China has concluded DTAs with 107[11] countries, even though the network has been 'weaved' only from 1983. The technical design of its DTAs follows either the OECD model or UN model so that all these tax treaties are basically the same in structure, and the divergence of content is limited. It is expected that China's bilateral tax treaty network will further expand. As for the interplay of DTA with the domestic tax law of China, where there are conflicts the treaty provisions shall prevail.

C. Research Claim and Verifying Approach

This article, with a focus on the implications of BRI for the international tax law of China, proposes that under the influences of BRI, there is an evolving trend that the ITSC is shifting from *source-oriented* to *residence-oriented*. This pair of terms, the source-oriented tax (SOT) system and residence-oriented tax (ROT) system, will be refined in the following.

To validate the above claim, a comprehensive approach to inspecting and evaluating the implications of BRI for China's international tax system must be designed. For that purpose, this article uses a two-fold approach, which consists of a conceptual approach as core to identifying an international tax system as SOT or ROT, and a factual approach to systematically unfolding the concrete rule changes brought by BRI. The two sub-approaches work together to test the claim.

1. Conceptual Approach – Catching the Trend

The division of SOT and ROT is the conceptualization of and in line with a country's relative stance on the so-called 'inbound' taxation and 'outbound' taxation.

In the case of China, the inbound taxation is the taxation of non-residents, on their incomes sourced from China, manifested as taxable *outflow* of income from China; while the outbound taxation is the taxation of Chinese residents, on their worldwide especially foreign-source incomes, manifested as taxable *inflow* of income to China. As inbound taxation arises from the country being the source of taxable income outflow, it can be entitled 'source-based' taxation (SBT). In the same vein, the outbound taxation can be named as 'residence-based' taxation (RBT). In this article, SBT and RBT refer to the two integral modules of the international tax system of a country.

SBT and RBT are inherently not overlapping or conflicting, for they are targeting different groups of taxpayers and incomes. And they do embody and reflect distinctive policy objectives and value orientations. The design of SBT rules aims to effectively tax the income of non-residents on one hand, on the other, they can play the role of attracting foreign investment. These two dimensions either echo the benefit principle that justifies the territorial taxation, or relate to the capital import neutrality (CIN) or the legal principle of non-discrimination. Correspondingly, besides effectively taxing the foreign income, the residence-based tax rules can be designed to facilitating outbound investment, by removing tax barriers or lowering tax burdens. Not free from controversies, the RBT is constructed upon ability-to-pay and capital export neutrality (CEN).

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10 Enterprise Income Tax Law of China, article 2.

11 SAT, 'List of Double Taxation Agreements Signed by China', see http://www.chinatax.gov.cn/n810341/n810770/index.html, accessed 1 May, 2019.

	SBT	RBT
Policy objectives	Effective taxation on non-resident	Effective taxation on resident's foreign income
	Attracting foreign investments	Facilitating outbound investment
Foundations	Benefit principle	Ability-to-pay
	CIN	CEN

Table 1

Even as said that SBT and RBT are equally being key to the integrality of an international tax system, different countries or a country in different stages may waver between the two**.** In other words, the relative weight of SBT and RBT is discrepant. For example, a developing economy that has barely any outbound investment is conceivable to have less sophisticated outbound or RBT rules, compared to that of a developed economy that relies much on foreign market and overseas investment. Or reversely, a traditional capital exporting country is expected to have less delicate inbound or SBT rules.

For the purpose of ongoing discussions, and based on the above comparison of SBT and RBT, this article further categorizes two modules of taxation, in delineation of a country's general orientation towards international taxation. That is what has been mentioned in the beginning, the *SOT* or *ROT,* which is determined by a country's inclination to or particular emphasis on SBT or RBT.

And being equally important in the purported claim, another focus falls on the 'trend'. That firstly means that the purported claim is not final or once for all, but is of the attribute of time, which is to catch the tendency of development within a certain period of time. In this article, it is for the period of BRI's construction. In other words, the claim and its validation are not to grab the 'destination', but the 'scenery' during the journey. The efforts throughout this article will not touch upon the model of ITSC *before* the BRI, or to demonstrate that the ITSC has *already* finished its transformation.

To catch the trend of SOT or ROT, the key challenge then is to measure the weight of SBT or RBT of an international tax system. It is unimaginable to accurately calculate their respective weight, either absolute or relative at an exact point of time. However, grasping the trend only entails inspecting the changes that are happening, and then distribute the changes to the weight of SBT or RBT to know the move.

In determining the trend of ITSC as source-oriented or residence-oriented, the *key* step is '*classification*', meaning that the process of grouping a certain tax rule into either SBT or RBT . For that purpose, the policy objectives pursued by a relevant set of tax rules are accessible indicators for its classification. In cases where the rule is already in place, the focus is then to delineate the changes of the rule. As a result, it is introduced the '*completeness*' as an index of the 'weight' of SBT or RBT. The completeness is in turn signified and materialized by the density or maturity of the rules in each camp, so factors like number, existence, robustness, or enforcement of rules are to be considered.

For illustration, let us suppose that a country introduces the CFC regime, being an anti-avoidance rule, of which the tenet is to safeguard the home taxing right on resident multinationals. The step classification will group the CFC regime into RBT, and it adds force to ROT. In comparison, if the country enhances the CFC regime to be more sophisticated, the classification step will be supplemented by the consideration of the completeness of RBT. And the CFC regime will be inspected in terms of its competency, practical implementation or other elements. All these improved elements increase the weight of RBT. If within a certain period of time many reforms of similar kind are adopted, a trend towards ROT can be established.

2. Factual Approach

The factual approach is a method to firstly 'find' the changes of tax rules, and then organize the changes in a systematic way. The factual approach provides the 'raw material' for the functioning of the conceptual

approach. However, the application of the conceptual approach is not as visible as the factual approach, for normally the former is imbedded into the later.

The factual approach proposes to explore the rule changes effected by or in service of BRI from three aspects. The first aspect is the top-level system design, which is not strictly the law. But in the context of law-making in China, usually it is the programmatic plan to guiding the future development of rules. The second aspect is the first element of a country's international tax system, the domestic tax laws of China. The third aspect is the second element of a country's international tax system, the bilateral DTAs of China. This aspect will research both the general picture of China's international tax treaty network, but also the material content of DTAs.

Beyond these three aspects, there are still two 'controllers' underlying the factual approach, one external controller and one internal controller of inspecting the above three objects. The external controller is the time range. That is to say that only the new moves since the launch of BRI in 2013 can be taken into account. Normally, this is not a long time for exciting things to happen in taxation. However, the demonstration below will break the stereotype. The internal controller is the link at the surface or underlying between BRI and the rule changes, and it plays a fundamental rule in making the general analysis defensible. If a rule change has no link with BRI, it does then make no sense to count it in the follow-up analysis. It is not necessary to enumerate here all the forms of that link. Instead, the link will be explained when inspecting the rule changes.

D. Top-Level Policy Design of BRI

1. Phase I: Vision and Actions

The so-called 'top-level' refers to the policy documents issued by the Party or central government, in contrast to those by the provincial governments. During the period 2013-2015, the major policy reference to BRI is the milestone document ('Decision')[12] by the Party who led the government at all levels. The *Decision* is the programmatic plan for China's reform in the next 5-10 years. And it positions BRI as one of the plans for the objective of constructing a new *open economy* system.[13]

Before the State Council authorized NDRC[14], MOF[15], and MOFCOM to issue the first top-level BRI action plan[16] ('Vision and Actions') in 2015, there are no global guiding principles of BRI. Therefore, the *Vision and Actions* is the critical file to comprehending the guiding lights for the construction of BRI, in particular of taxation.

In the Vision and Actions, taxation is seen as one of the aspects regarding smooth trade and investment facilitation, among the priorities of cooperation. Specifically, in terms of taxation, the document calls on the parties to push forward the negotiation of DTAs. In this regard, the international tax treaty is saluted for its functions of eliminating investment barriers as well as protecting the interests of investors. Going further, considering China's advantageous positions to most of other BRI parties, either barrier elimination or investor protection gains more realistic significance for Chinese outbound investments and investors than their counterparties.

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12 'Decision of the Central Committee of the Communist Party of China on Several Major Issues Concerning Comprehensively Deepening Reform', 12 November 2013, available at http://www.gov.cn/jrzg/2013-11/15/content_2528179.htm, accessed 3 May 2019.

13 Ibid, chapter 7, point 26.

14 National Development and Reform Commission.

15 Ministry of Finance.

16 'Vision and Actions on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road', available at http://en.ndrc.gov.cn/newsrelease/201503/t20150330_669367.html, accessed 3 May 2019.

2. Phase II: Comprehensive Policymaking

After the guiding light shed by the Vision and Actions, there has been a clear boost of BRI policymaking. At the central government level, such policymaking has been comprehensively contributed by both the State Council and almost all the ministries. The below Chart 1 shows the policy fields covered, and Chart 2 shows the monthly issued quantity of BRI policies.[17] As shown in Chart 1, tax policy is obviously not among the champions of fields issuing new BRI policies. However, that does not undermine the primacy of taxation in constructing BRI, as already evidenced by the Vision and Actions. The following will focus on the stance of State Administration of Taxation (SAT) in the BRI.

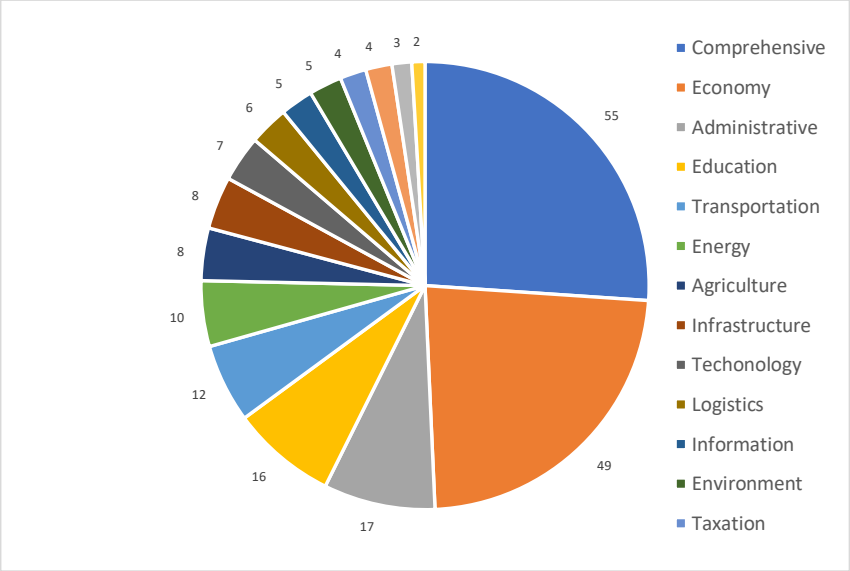

Chart 1

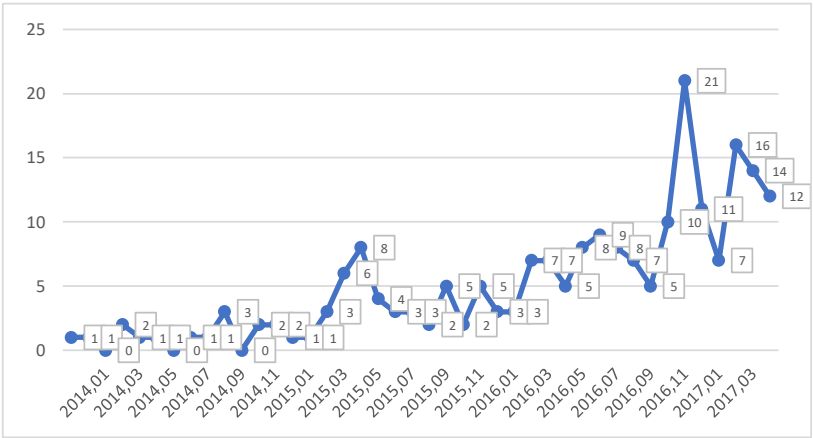

Chart 2

2.1. SAT: Two Directions of Efforts

The SAT is the quasi-legislative as well as the administrative organ of taxation in China.[18] Its legislative power is broad, especially for the implementation matters of taxation 'laws', of which the legislation is the reserved authority of the National People's Congress. As a result, for both the top-level tax policy orientation and the detailed tax rules, one must consult with the SAT. This article is not an exception,

17 The Chart is processed from the data in the research '黄凯丽, 赵频, 一带一路倡议的政策文本量化研究——基于政策工具视角, 情报杂志 37.1 (2018): 53-58.' The authors collected the policy documents with the theme of BRI from the end of 2013 to May 2017.

18 Supra note 9, 2.5.1.

so that it extracts its 'macro' role as a source of knowing the policy trend, while leaves the 'micro' role for further analysis in later parts.

SAT does not release a legislation plan for BRI, so there is no straightforward way to know whether the SAT has a coherent strategy for the rule changes. However, a Notice published soon after the announcement of the Vision and Actions in 2015 may serve a similar purpose. The recipients of this Notice[19] are the provincial branches of SAT. According to the Notice, the general requirement of SAT is that taxation should serve BRI proactively. In concrete, the local SATs should adopt 10 specific measures from three aspects. These aspects are, safeguarding the interests by implementing tax treaties, seeking development by improving services, and promoting compliance by standardizing management. Although these are mostly in the level of tax administration, they equally show at the macro level the work priorities of SAT towards BRI. These 10 measures can be aligned by two directions of SAT's efforts with regards to BRI, which are shown below.

Directions	Measures
Facilitating Outbound Investment	Establishing a country-by-country tax information center
	Creating BRI tax service website
	Tax training for outbound investors
	Setting up a 'going out' seat on 12366 Hotline
	Encouraging intermediary agencies going out
	Enhancing the implementation of tax treaties
	Strengthening tax-related disputes resolution by bilateral negotiation
Managing the Risks	Perfecting the management of overseas tax Information declaration
	Reporting annually the tax analysis of outbound investors
	Establishing risk pre-warning mechanism

Table 2

Through these two directions of efforts in terms of BRI, it is known that SAT intends to, on one hand, smooth the tax experiences for Chinese companies to investing overseas, on the other, to control the tax risks brought by the outbound investment. Even though for the latter point, the form and substance of the tax 'risks' are not specified.

E. BRI-driven Reforms of Domestic Tax Law

Compared to the investigation of China's DTAs that often requires to see things behind the articles, the adjustments of Chinese domestic tax laws are more transparent. Even though there are many more changes in law enforcement, however, the following will only focus on the rule-based reforms. To testify the claim, one of the characteristics of ROT is that a state is taking tax actions encouraging its residents to invest overseas. On the mirror side, the growing outbound investment may also challenge the effectiveness of the home country's RBT. The countering tax measures, therefore, constitute another thread demonstrating the claim. Accordingly, two aspects of rule changes will be introduced and discussed. The first is the perfected and activated controlled foreign Corporation (CFC) regime, the second is the improved foreign tax credit system.

19 SAT, 'Notice of the State Administration of Taxation on Implementing the Action Plan on the Belt and Road Initiative and Effectively Conducting the Taxation Service and Administration', April 2015.

1. Improved Foreign Tax Credit System

China's foreign tax credit (FTC) system has undergone substantial reform against the background of BRI. The tenet of the reform is to facilitate the going out of Chinese companies by providing more thorough credit of foreign tax. The original FTC system was effectively built up in 2009[20], which had imposed considerable restrictions on the sufficiency of tax credit. In 2017, SAT reshaped the FTC system so as to adapt to the new situation brought about by BRI,[21] and that has released the restrictions tit for tat. Here the restrictions and the countering reforms are grouped as horizontal and vertical.

The horizontal feature of the old system marking those restrictions is the per-country credit mechanism. Under this mechanism, resident company deriving incomes from more than one country is not allowed to combine and reuse the credit balance across countries. As a result, taxpayers' credit balances in low tax countries cannot be reused for the credit of high tax countries. On the other hand, foreign tax paid to high tax countries that exceed the credit limit as calculated by the Chinese tax rate cannot be credited currently. Therefore, insufficient credit exists under the per-country credit mechanism, which will adversely affect the cash flow of the taxpayer. The situation will be worse if one of the foreign branches has suffered losses, for under the mechanism such losses cannot be manipulated into calculating the taxable income in China or third countries.

The vertical restriction in the old FTC system is the three-layer credit mechanism, regarding the indirect credit for tax paid by the multi-layered foreign subsidiaries. Ideally, a perfect FTC system should provide unlimited credit to the end of the holding chain. But apparently, this cannot be the case in reality. In China's old FTC system, the taxpayer can file credit for foreign tax at most until the third layer subsidiary. There are detailed standards to identify the qualified layer and subsidiary.[22] With the popularity of outbound investment, the business model that extends further than three-layer holding becomes common as well.[23] Restricting the credit chain to three layers makes the FTC halfway to its purpose, for double taxation is only partially exempt.

The new system aiming at facilitating outbound investment has targeted loosening both the horizontal and vertical restrictions. First of all, the per-country credit is supplemented by a global credit mechanism, which provides combined FTC regardless of the countries of source. In this case, the FTC obtained by the taxpayer will be more sufficient. The same spirit is found in the reform of the five-layer credit. It literally means that resident company can credit the foreign tax it has indirectly born all the way to the fifth-layer subsidiary. Although it raises higher standards of tax administration and compliance, the elimination of double taxation will be achieved to a greater extent.

The two measures, in horizontal and vertical aspects, have the direct effect of easing the tax burden of outbound Chinese investors. Besides these, there are also peripheral actions serving the same purpose. For instance, SAT abolished the ex-ante approval procedure for FTC in 2015[24], now taxpayer only needs to file for record of FTC. Another example is a BRI-tailored policy relevant to FTC. In general, or sub-contracting or consortium engineering project, the entity that actually earns the foreign income is not who actually pays the foreign tax. The first entity then may not be eligible for Chinese FTC. SAT issued a circular in 2017 to solve this inconsistency problem by adopting the principle of 'substance over form'[25]. These actions taken together have formed robust policy support for improving the FTC system, to the direction of facilitating the outbound investment of resident companies.

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20 MOF, SAT, Notice on Issues Concerning the Foreign Income Tax Credit of Enterprises, No.125 [2009].

21 MOF, SAT, Notice on Issues concerning Improving the Tax Credit Policy for Overseas Income of Enterprises, No. 84 [2017].

22 Ibid, articles 5 and 6.

23 See official reading of the new FTC policy at, 'Senior Officials of SAT and MOF Answering Questions on Improving the Tax Credit Policy for Enterprises' Overseas Income' http://m.mof.gov.cn/czxw/201712/t20171229_2790745.htm, accessed 10 June 2019.

24 SAT, Announcement on Issues concerning the Follow-up Administration after the Cancellation of the Approval Item of Confirmation of the Application of Simple Collection and Tax Sparing Credit to the Overseas Income of Enterprises, No. 70 [2015].

25 SAT, Announcement on Issues concerning the Tax Credit Vouchers for Overseas Contracted Engineering Projects of Enterprises, No. 41 [2017].

According to the conceptual approach and the table 1, the foreign tax credit system should firstly be classified into the group of RBT rules. For that the FTC is a basic method to eliminate double taxation, which is the key consideration for cross-border factor movement. Secondly, in the level of completeness, the above reform of China's FTC system has made it more competent to achieve its normative goal. The reform can also pass the test of factual approach as well. Because SAT had expressly alleged that the reform is to serve the "the need for new developments"[26]. Therefore, the improvement of FTC system has added weight to the RBT. Taken individually, it conforms to the trend in the research claim regarding the ITSC's transformation to ROT.

2. Activated and Patched CFC Regime

CFC regime is designed to combat the artificial tax avoidance of resident companies by using foreign controlled entities, especially in low tax jurisdictions. CFC denies the potential tax deferral or avoidance by taxing currently the resident's proportionate income share in its controlled foreign subsidiaries. CFC regime is not sensitive to the worldwide or territorial tax system, in that in either system resident companies have the incentive to abuse the tax laws. On the other hand, the CFC regime is rooted in the rightfulness of residence taxing right, and the unreasonable tax deferral or tax avoidance by using CFC challenge such rightfulness. In this sense, the CFC regime maintains the RBT, and the development of it may manifest the changing weight of RBT.

The evolvement of China's CFC regime in recent years corresponds to the trend of strengthening RBT. The regime was introduced by China's first Enterprise Income Tax Law (EITL) in 2008[27], and materialized by SAT later on in 2009[28], but that was still far from perfection, for it lacks operational guidelines on various elements. For instance, there are no comprehensive standards of 'control'[29] in identifying controlled foreign entities. The same situation is there for 'reasonable business operation'. In addition, although the EITL refers to the individual holding CFC, SAT cannot deal with the individual tax avoidance on behalf of Individual Income Tax Law (IITL). The IITL then did not intend to cooperate with EITL on this point. Furthermore, at the practical level, SAT lacked the experiences of tackling the tax avoidance of residents using overseas resources.

Due to the incompleteness of legislation and also the lack of realistic urgency, China's CFC regime had been frozen for a significant period of time. SAT had never administered a CFC case, until 2014 and 2015 when SAT improved the tax information collection of residents investing overseas.[30] The reform was enacted expressly to serve the construction of BRI, signaling that the increasing outbound investment is the factual impetus. Later on, in 2018, the new IITL also filled up the hole in CFC regime with respect to individual controlling cases.[31] While more patches can be put on the regime, the existing one can already basically function. It is found then a boost of CFC cases filed by SAT since 2014[32], and by now SAT has managed to administer CFC regime on a regular basis.

The above reforms around the CFC regime, either SAT's legislative and administrative measures that have activated CFC or the patch made by IITL, have increased the effectiveness and competency of the regime. Being the rule of RBT in itself, the CFC regime, through the improvements, has contributed to the weighted RBT. As for the considerations of the factual approach, the link with BRI and the timing requirement are

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26 Supra note 23.

27 See article 45.

28 SAT, Notice on Issuing the Measures for the Implementation of Special Tax Adjustments (for Trial Implementation), No. 2 [2009]

29 In the above regulation, it is provided only the case of control by shareholding.

30 SAT, Announcement on Issues concerning Resident Enterprises' Reporting of Information Relating to Overseas Investment and Income, No.38 [2014]; Notice on Effectively Conducting the Work of Resident Enterprises' Reporting of Information about Overseas Investment and Income, No.327 [2015].

31 Article 8 of Individual Income Tax Law (2018).

32 The first CFC case appeared in 2014, handled by Shandong Local Tax Bureau. There is an 'outburst' of CFC cases ever since investigated by SAT branches of, for example, Hai Nan and Xin Jiang (2015), Su Zhou (2016), Beijing and JinZhou (2017), Kun Shan and Qingdao (2018).

convincing as well. In conclusion, the reforms of the CFC regime have added the persuasiveness of the research claim, affirming again the ITSC's transformation to ROT.

F. Changes in Bilateral Tax Agreements

The bilateral tax treaty is entered traditionally for the purpose of eliminating double taxation and tax evasion. But that purpose has extended to objectives like developing economic relationship and improving cooperation on tax matters[33]. The proactive intent of the contracting parties whatsoever must be triggered by the realistic economic intercourse of the two countries. This is the fundamental reason for their delegates to sit down and argue. The same applies to BRI, which aims to (re)build the economic ties along the Belt and Road. Consequently, with the revival of the Belt and Road, there must come the need to establish the 'tax ties' as well.

When questioning the implications of BRI for the general ITSC, and for now in terms of tax treaties, both the breadth and depth of China's DTAs should be considered. In this article, the inspection of breadth, which refers to the extensiveness of China's tax treaty network, intends to explore the expansion of the treaty network. While for depth, the specific changes of treaties' articles are viewed as substantial evidence to knowing the tendency of ITSC under the influences of BRI. Only through the combination of both the breadth and depth aspects can we master the global transformation of China's stance on international taxation from the treaty perspective. However, what needs to be explained is that the breadth part and depth part are not always and do not need to be aligned by the same tax treaties. In other words, the treaties that signify the specific tendency of expansion do not necessarily show the noticeable content changes, which may lie elsewhere. This article views the two aspects as on equal foot and organically connected.

1. The Breadth of China's Tax Treaty Network

This section will be unfolded by three charts, which are in turn processed with the data regarding China's DTAs and the development of BRI.[34]

Chart 3 shows (in green area) the countries signing tax treaties with China. As can be seen, China's tax treaty network is already very comprehensive so far. With a few still not into force, China has signed bilateral tax agreements with 107 countries in the world, which makes China's tax treaty network one of the largest in the world. From the map in Chart 3, there are only two noteworthy grey areas, meaning that those are countries without tax agreements with China. One is in Africa, and another is in South America.

Chart 4 shows the number of tax treaties that China signed or updated with other countries each year from 1983 to 2019. This Chart supplements Chart 1 in that it introduces the time dimension into the analysis of China's DTA network evolution.

Combining the Chart 3 and Chart 4, the first thing to note is that over 30 years and of such extensive coverage, China's international tax treaty network is still growing, through either extending to new jurisdictions or refreshing the old treaties. Narrowing the lens down to only the period since the launch of BRI, it is found that even within only 6 years, BRI has clear influences on the expansion of China's treaty network. Since 2015, China's treaty network extends to eight new countries, who are at the same time the new members of BRI as well.[35] And even in the first five months of 2019, the tax treaties with New Zealand and Italy, being the new BRI countries respectively in 2017 and 2019, were totally renegotiated both in 2019.

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33 See article 6 of 'Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS', https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm.

34 See 'List of Countries that Have Signed 'Belt and Road' Cooperation Document with China' https://www.yidaiyilu.gov.cn/gbjg/gbgk/77073.htm; SAT, 'List of Double Taxation Agreements Signed by China', see http://www.chinatax.gov.cn/n810341/n810770/index.html, accessed 1 May, 2019.

35 They are Chile, Zimbabwe, Cambodia, Kenya, Gabon, The Republic of Congo, Angola and Argentina. Argentina does not officially sign the BRI cooperation documents with China, yet it already has substantial projects going on in the name of constructing BRI.

Then, on the historical dimension, there are three more points of time shown in Chart 4 that are worth considering. The first is 2001, when China joined the WTO, marking its integration into the world and its twenty-year rapid growth of the economy. The new century is literally the new age of the economic China. The second point of time is that after 7 years of attracting foreign capital, China's dual corporate income tax system ended in 2008.[36] The third one is 2016, two years after the announcement of BRI, China has transformed from a capital importing country to net capital exporting country. And as can be seen in Chart 4, nearly 70 out of 107 tax treaties were signed before 2001, when China has fewer capital outputs. The little triangle symbolizing the launch of BRI rests after the first two blue dash lines and ahead of the third one.

This has two aspects of instructions. For one thing, the status quo of China's tax treaties falls behind the fast-changing reality, both economic and legal, in that the basis of those treaties have shifted dramatically. The second instruction relates to how should we view BRI's role in China's evolving tax treaties. When evaluating the implications of BRI for both the scope and content of China's tax treaty network, the efforts of isolating BRI from its general economic and legal background are futile. The changes brought by BRI must be seen in conjunction with the background it grows in. Thus, it can be said that BRI has been accelerating the change of reality along the existed route, and in turn making the tax rule changes faster and more observable.

Chart 3

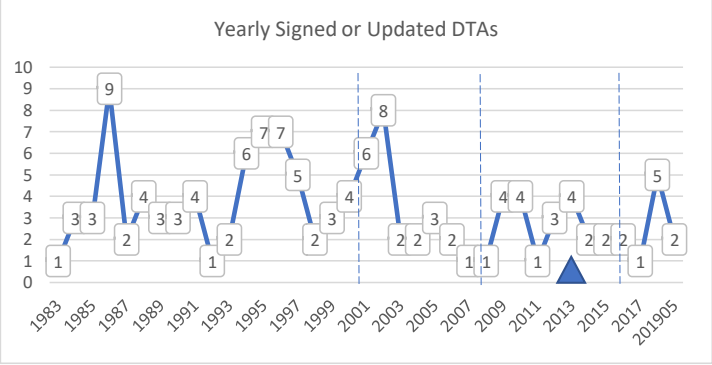

Chart 4[37]

36 See the evolution of China's enterprise income tax law at para. 2.2.1 of Jinyan Li, International Taxation in China: A Contextualized Analysis, IBFD.

37 The 'updated' includes the re-negotiated ones.

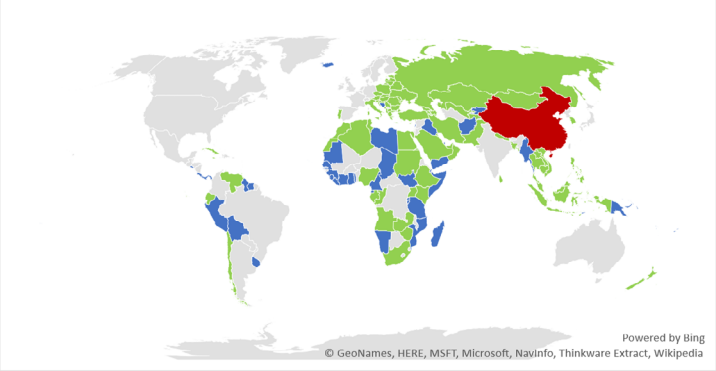

Chart 5

Chart 5 painted all the countries signing the BRI cooperation documents ('BRI Countries') with China either blue or green. The green areas in the map are the BRI countries with which China has a DTA, while the blue areas are the BRI countries without a DTA with China. By May 2019, the pained areas altogether consisted of 131 countries, which covered the majority of Africa and Euro-Asia continent. The BRI countries are mostly developing countries, for the noteworthy grey areas are all rich North America, Australia, and West and North Europe. See Chart 6 for detailed information about the distribution of BRI countries across the continents.

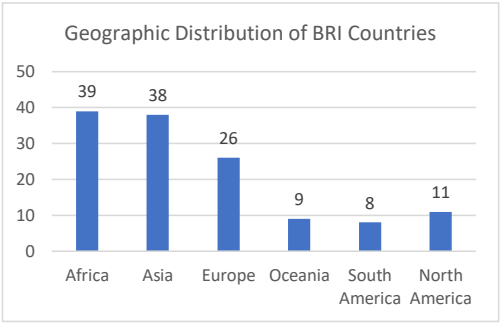

Chart 6

In terms of the distribution of DTAs in the BRI countries, it can be found that the majority of BRI countries, both in absolute number and geographic coverage, has already had bilateral tax treaties with China. That is attributed to the work done by SAT largely before BRI. However, the blue areas in Africa and South America imply that China's tax treaty network may further extend into these two continents.

1.1. Summary

The above analysis around the three diagrams has shown the network of China's current international tax treaties, and the evident role of BRI in its expanding scope. The analysis also touches upon why a transition of ITSC in terms of tax treaties is destined to happen. This part only deals with the breadth of the ITSC, and the next session will turn to focus on the depth, the content of tax treaties so as to reveal the material changes. But that does not mean the scope change of DTAs is of trivial significance. The key lies in that firstly, the bilateral tax treaty is critical to distributing income between countries by allocating taxing rights; secondly, bilateral tax treaty is itself an instrument to removing barriers to cross-border investment, which has been pointed out in the top design of BRI; thirdly, BRI has made a difference in the expanding tax treaty network, for the increased treaty partners may be attracted in by BRI.

The first decade in the chronicle of China's international treaties witnessed the agreements with most of OECD countries.[38] Through the latter two decades and under the influences of BRI, the network has included more capital-poor countries than capital-rich countries, with China as a benchmark. Even though

38 Supra note, Jinyan Li, para. 4.2.2.

sometimes the tax treaties are called 'international', it is in fact only 'bilateral'. Yet China's international tax treaties seen as a whole, the general position of China in the DTAs must have been different from it ever was.

2. The Depth of China's Tax Treaties

As said, the depth part will deal with the content changes of China's DTAs, under the implications of BRI, with an aim to shed some light on the research claim of this article. This part is not going to do a blanket search of all the article changes of DTAs, but only to identify the key articles that are relevant to the claim. The direct objective of a bilateral tax treaty, as usually stated in its preamble, is to eliminate double-taxation and combat tax avoidance. To those ends, tax treaty determines the two contracting parties as either source or residence, and then divides the taxing rights between them. The identification of ITSC as SOT or ROT, while manifested in tax treaty, is firstly dependent upon China's position as source or residence, and further on the interests vested in the source or residence by the treaty. In general, the taxing right of the source is prioritized, and the residence state has the residual right to tax. According to this judgment, this article does find proof of the ITSC's move from SOT to ROT.

2.1. The Flexible Sparing Credit

Normally, in the double tax agreement, article 23 specifies the methods adopted by the two contracting states for eliminating double taxation. In cases where they choose credit method, there are options for the residence state to decide whether to view the *de facto* unpaid tax as the payable tax in the other state, for the purpose of calculating foreign tax credit. The unpaid tax is the tax that would have been paid but otherwise is spared (exempted or reduced) as tax incentives to attract foreign investment.

Neither OECD or UN Model Tax Conventions provide sparing credit in its articles as an option for double-tax elimination. However, sparing credit has been common for the DTAs between developed and developing countries. However, being counterproductive for the popular propositions of neutrality and equity, sparing credit has lost its appeal for developed countries.[39] But sparing credit may still attract those countries, mainly in that it increases the competitiveness of their outbound investors.

For developing countries, however, the inclusion of sparing credit in its DTAs prevents the other contracting state from nullifying their tax incentives under the top-up effect of credit method. The incentive benefits then will be accrued to investors, rather than the treasury of their home states.[40] So that the sparing credit method has been embraced as a tool for attracting and competing for capital from developed countries.

The sparing credit thus implicitly links SOT and ROT, for that different countries or a country in different phases may adopt sparing credit from different starting points. When a country adopts sparing credit in its DTAs, it is not difficult to identify its purpose as attracting foreign investment or facilitating outbound investment. Based on that, sparing credit adds weight to either SOT or ROT, and is able to show dynamically the transformation process between SOT and ROT.

2.2. The Redirected Role of Sparing Credit

The historical trajectory of sparing credit in tax treaties echoes the evolution of China's DTAs and is in concert with the tendency of ITSC from SOT to ROT.

Sparing credit was introduced by China as early as in its first DTA in 1983, which was with Japan. Since then, sparing credit has sprung up in its tax treaty network. Put that against the system background, China has operated a dual tax system which gives institutional incentives to foreign investors until 2008.

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39 Xiong Yan, Thinking Over Questions Relevant to Sparing Credit, International Taxation, vol. 12, 2016, p. 36(. (2016). 对饶让抵免有关问题的思考. 国际税收, (12), p. 36.).

40 Kristian Reinert Haugland Nilsen, The Concept of Tax Sparing, p. 9, available at https://www.jus.uio.no/ior/english/research/projects/global-tax-tranparency/publications/the-concept-of-tax-sparing.pdf.

Consequently, by the end of 2007, forty-nine in all ninety-two China's DTAs contain the sparing credit provisions, and most of them are treaties with developed countries.

In 2008, the first *Enterprise Income Tax Law* canceled the systematic preferential treatment of foreign investors, and only sectorial and regional incentives exist thereafter. The institutional basis thus falls away. After 2008, only 2 among the 33 newly signed or updated tax treaties contain the sparing credit provisions. The first one with Ethiopia included a restricted sparing credit, which was claimed to be a reluctant compromise made by China in 2009.[41] The second one, however, came late on 2016 with Cambodia, which used a standard clause of sparing credit.

This article holds that the tax treaty with Cambodia manifests a shifted role of sparing credit, and to a certain extent, it marks a new stance of China's tax treaty negotiation, in contrast to that a decade ago.

Although rather unlikely the treaty would specify its link to BRI in its text, that link, however, is genuine. The bilateral tax treaty and BRI cooperation agreement between China and Cambodia were negotiated along the same track and were signed simultaneously on 13th October 2016. The process is the reflection of the tenet of the *Vision and Actions* that China's tax treaty should be in proactive service of BRI. As a result, it can be said that the consideration of sparing credit can pass the test of the factual approach.

Needless to say, the mutual sparing credit, will gain more attractiveness for Cambodia as an investment destination among other Southeast Asian countries. For China, the taxable income that would have accrued to the Chinese treasury, due to the credit mechanism, turns to be the income of the Chinese investors in Cambodia. What makes this even more meaningful for those investors is that China has operated a per-country credit mechanism until 2017. The credit balance for a specific country cannot be reused for another country's tax credit. Sparing credit thus reduces the 'waste' of credit balance, and in a certain way alleviates the double taxation caused by the inadequate foreign tax credit. Therefore, the sparing credit included in the Cambodia-China DTA plays a redirected role from its predecessors that started from China being the location of investment, rather than an exporter of capital.

Following the conceptual approach, the classification of sparing credit is flexible. And the way to classify is not to look at the content of provisions, but to look through the motives of adopting it. As analyzed above, the redirected role of sparing credit renders itself into the category of RBT from the former SBT, which echoes China's shifted motives to facilitating outbound investment from attracting foreign investment. Compared to the arguments in part E that prove more the destination of the trend, the analysis here has shown where the transformation comes from and where it leads to.

2.3. Lowered Withholding Tax

In international taxation, the way to tax income of foreign investors is generally aligned with the categorization of incomes as active income or passive income.[42] The country of source can tax the active or business income on a net basis with a normal corporate tax rate, while passive incomes are taxed at a reduced rate on a gross basis. More particularly, the source tax on passive incomes is paid by the payer rather than the recipient. The scope and the special way of taxing the international passive incomes result in a unique category within the corporate income tax, that is, the withholding tax.

2.3.1. Withholding Tax and RBT/SBT

Withholding tax is a key design for international income sharing. For business income derived by the permanent establishment, the source country has abundant resources to tax such income. In contrast, the earner of passive incomes does not need to have a significant presence in the source country. Letting the payers pay the source tax out of the dividend, interest, or royalties to be received by foreign earner seems to be the best option. Withholding tax is thus key to realizing source taxing rights, leaving the residence country to tax the residual incomes. Withholding tax, together with other tax allocation regimes,

41 Supra note 39, p. 35.

42 Avi-Yonah, Reuven S. International Tax as International Law: An Analysis of The International Tax Regime. Cambridge University Press, 2007, p. 1.

affect the balance of income sharing between source and residence. The heavier liability of withholding tax results in the larger share in the source, and less income will accrue to the residence. Being a gross-based mechanism, withholding tax is more succinct than typical corporate income tax. Among others, the decisive factors of withholding tax liability are the scope and the tax rate, which is also simpler than the case of net-basis income tax.

On the other side of the mirror, the income sharing of residence and source concerns directly the interests of taxpayers. In the case where the residence state adopts the credit method, the withholding tax affects the cash flow of the taxpayer. Or when the residence state uses exemption method to eliminate double taxation, the withholding tax will directly affect the overall tax burden. In either case, withholding taxation influences the interest of cross-border taxpayer.

Based on the above, it is reasonable to gauge the changing position of a country by looking into the trend of withholding tax in its tax treaties. The trend can be a rising, declining or stable withholding taxation. If over a certain period of time, a tax treaty has provided lower withholding tax liability in the source state, then that means the residence state has been sharing larger pie of the cross-border income. The residence country has gained stronger position than the source state in the game of international tax sharing. Translate that to contact the conceptual approach, the residence country that achieved lower withholding tax liability in a DTA obtains greater benefits for its residents. Consequently, residence country has the motive to reduce the withholding tax liability for both the treasury and to facilitate overseas investment. In short, lower withholding tax liability adds weight to RBT.

For the theme of this article, a preliminary conclusion can be drawn that the residence country may be transforming to ROT, if multiple such treaties can be found. Because any tax liability in a DTA is bilateral, the changing position as reflected by inspecting withholding tax should be considered with the underlying fact - the general stance of the contracting parties as exercising more source or residence taxing rights. For the tax treaties between China and BRI countries, as analyzed above, China plays more as the residence states. Consequently, the trend of lower or higher withholding tax liability prescribed by the treaty means the larger or smaller income pie share of China, which in turn renders China closer to ROT or SOT.

2.3.2. Cases of Lowered Withholding Tax

Through inspecting some of the recent DTAs of China, a clear trend of lower withholding tax liability can be found, and that will further back the claim that the ITSC is heading towards ROT. Such a trend also has an indelible connection with the construction of BRI. The following will introduce the details.

Non-exhaustively, this article has found some recent tax treaties that exhibit dynamically or statically the decreasing withholding tax liability. For the dynamical demonstration, the DTAs with Russia and Romania are good examples. China's first tax treaty with Russia was signed in 1994, in which the rates set for the passive incomes dividend, interest and royalties were all 10%. In 2014, the DTA with Russia was renegotiated, and the same rates were reduced. For dividend, a 5% rate applies with a modest threshold, otherwise, the rate is 10%. For interest and royalties, the rates were also reduced to 5% and 6%. This is not the end. In 2015, when China and Russia signed the BRI cooperation document[43], the delegates of the two sides also signed a tax protocol amending the new DTA. According to the protocol, the withholding taxing right on interest payment was exclusively conferred upon the residence state, while the source state gives up its taxing right. All in all, from 1994 to 2015, China has gained more and more residence taxing rights relative to the source taxing rights of Russia. The same conclusion can be drawn based on the observation of the DTA with Romania, which has reduced the withholding rate to around 3%. For static demonstration, the first DTAs with BRI countries Gabon, Argentina, and the Republic of Congo all set the withholding tax rate to a relatively low level.

Besides the above, there are proofs demonstrating that the aforesaid trend is real and that such trend is affected by BRI to a large extent. The proofs are the provisions in a number of DTAS exempting or lowering

43 'Joint statement between the People's Republic of China and the Russian Federation on the construction of Silk Road Economic Belt and the construction of Eurasian Economic Union', https://www.yidaiyilu.gov.cn/zchj/sbwj/2427.htm, accessed 1 June 2019.

the withholding tax liability of the Silk Road Fund of China (SRF). Established in 2014, SRF is a state-owned fund with a focus on financing BRI projects. In DTAs with BRI countries Italy (2019)[44], Argentina (2018), Kongo (2018), Spain (2018), and Malaysia (2016), the withholding tax liabilities of SRF in those countries are set low or lowered, wholly or partially exempt. Although the preferential treatment can be attributed to sovereign immunity, that does not hinder it adding strength to the trend and reflecting the straightforward role of BRI in ITSC.

2.4. Most-Favored-Nation Clause

This part aims to link the changing position of the most-favored-nation (MFN) clause in China's tax treaties over the years with the research claim. The analysis in the following is expected to contribute to the claim that China is indeed gaining more dominance in negotiating tax treaties, and the ITSC is in turn heading towards ROT.

In plain words, MFN clause is to ensure in a bilateral agreement between A and B that party A will not be subjected to a less favorable treatment than what B accords to C in their agreement of the same kind. In international trade or investment law, MFN is a 'standard' clause[45], for that the major multilateral trade agreements including GATT, GATS, TRIPS, and NAFTA all contain it, and so do most of bilateral investment treaties.[46] However, it is well known that these agreements virtually do not touch upon tax especially direct tax issues.

Narrowing down the lens to tax treaties, the MFN clause has independent significance than that in international trade or investment law. For one thing, in international taxation, it is less possible for MFN to be a rule of customary international law. Unlike the popularity among international trade or investment agreements, MFN only exhibits limited existence in the global tax treaty network. Countries do not feel obliged to provide MFN treatment to its counterparty when negotiating bilateral tax agreement. As a matter of fact, either in academia or practice, the stances on MFN are far from united.[47] For another, taxation has direct and immediate impact on national welfare, which explains partly why tax issues are usually reserved in trade or investment agreements, and why a multilateral tax agreement is still staggering on its way. Therefore, it should be understood that the MFN clause enjoys different status and serves different purposes in a tax treaty than those in a trade or investment agreement.

2.4.1. MFN and Non-discrimination: Deviated but Connected

As reported by the International Law Commission, MFN clause does not stem from a country's general right to non-discrimination.[48] The OECD Model Tax Convention (MTC) has never accepted MFN clause in its articles, while only considered it in the commentary for a while and later on removed it without substitution.[49] The OECD in Article 24 has provided four forms of non-discrimination in five paragraphs.[50] They are the non-discrimination of nationality, permanent establishment, payment and capital. Being separate aspects, the four lack an overarching rationale behind them.[51] The prevalence

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44 The renegotiated DTA with Italy was also signed simultaneously with the BRI document.

45 Most-Favored-Nation-Treatment in International Investment Law, OECD working paper on international investment, No. 2004/2, September 2004, p. 16.

46 See Art. I of GATT, Art. II of GATS, Art. 4 of TRIPS, and the Art. 1103 (investment), Art.1203 (services) and Art. 1403 (financial services) of the North American Free Trade Agreement (NAFTA).

47 See generally the discussions in Daniel Dürrschmidt, Tax Treaties and Most-Favoured-Nation Treatment, particularly within the European Union, Bulletin for international taxation 60.5 (2006): 202; Cordewener, Axel, and Ekkehart Reimer. The Future of Most-Favoured-Nation Treatment in EC Tax Law-Did The ECJ Pull the Emergency Brake without Real Need?-Part I." European Taxation 46.6 (2006): 239-249, and Most-Favoured-Nation Treatment under Tax Treaties Rejected in the European Community: Background and Analysis of the D Case, Intertax 33.10 (2005): 429-444.

48 Report of the ILC on the work of its thirtieth session, A/33/10, 1978, Chapter II, paras. 47 to 50.

49 Art. 24 OECD Commentary 1977, No. 55, 2nd sentence, and it was deleted in the 1992 commentary. Hofbauer, Ines. Most-Favoured-Nation Clauses in Double Taxation Conventions-A Worldwide Overview. Intertax 33.10 (2005), p. 445.

50 OECD MTC 2018, available at https://www.oecd.org/tax/treaties/model-tax-convention-on-income-and-on-capital-condensed-version-20745419.htm.

51 Guglielmo Maisto, Pasquale Pistone, Dennis Weber, Non-Discrimination in Tax Treaties: Selected Issues from a Global Perspectiv, IBFD, p. 4.

of non-discrimination clauses in tax treaties has contributed little to the status of MFN clause in tax treaties, simply because a third state cannot require the most-favored-nation treatment on account of the non-discrimination provisions. The status quo is that, among the MFN clauses that are included in the worldwide tax treaties, almost none of them are aligned with the non-discrimination article. Under most circumstances, instead of being applied overarchingly, MFN treatments are provided only to particular aspects of international taxation, like for the transportation income or permanent establishment.[52] Resting uncomfortably among the general non-discrimination provisions, the current status of MFN clause is closer to being an exception to them. For example, the tax treaty between country A and B contains the standard non-discrimination article, which enumerates several situations where both parties shall not discriminate the residents of each other. A's tax treaty with country C also has similar non-discrimination arrangement. Now B has negotiated a more favorable condition in its treaty with A, the question arises that whether C is reasonable to claim for its residents the same treatment that B's residents are newly having in A. The answer, under the existing development of treaty law, is obviously negative.[53]

Consequently, the o*pinio juris* of countries to include MFN clause in their tax treaties barely exist. And the autonomous revision of treaty conditions that may be triggered by MFN treatment with a third state poses risks to the reciprocal basis of tax treaty, unless the MFN clause is expressly provided in the treaty. In the above example, the claim of C will be justifiable if the A-C tax treaty has the MFN provisions written regarding its claim. Otherwise, the MFN treatment inappropriately deducted from non-discrimination will blur the border of the 'two-sidedness' or 'privity' of tax treaty.

While the realities of the non-discrimination article and MFN clause deviate, their underlying connections are touchable. First of all, the loosely aligned provisions of non-discrimination in the MTC are targeting the same negative consequences with that the general DTA aims to counter. Economic distortions can be caused by both double taxation and discriminatory taxation.[54] The equal tax treatment of nationals and non-nationals advocated by non-discrimination reflects part of the capital import neutrality (CIN).[55] Discriminatory tax treatment in the source state hinders the free movement of capital and investment, and so do the double taxation of residence and source states.

Secondly, both non-discrimination in the MTC and MFN clause lead to equal treatment, while only the former is for resident and non-resident, and the latter is for non-residents. In the same vein with the first point above, what is justifying MFN is that discriminatory treatment among non-residents of different nationalities also creates distortions and reduces efficiency. Through the application of MFN clause, the differential tax treatment in a certain aspect will be eliminated, and that aspect will not be a factor for foreign investors in their business decisions. As a result, the efficiency will be safeguarded for both the investor and source state. In this regard, the MFN clause and non-discrimination article are connected by their common rationale and objective.

2.4.2. Driving Forces Behind MFN

Questioning why a country is driven to adopt MFN clauses in their tax treaties leads us to the purposes of those countries doing so. And more importantly, the inquiry of the driving forces of MFN clause will also provide fulcrums to think out the claim of this article. Since the relative scarcity of MFN clauses in the global tax treaty network, MFN is not a reliable instrument to achieving international tax harmonization, as what MFN can effectively do in international trade and investment system. And the deviated nature of MFN and non-discrimination also decides their different 'destiny' in practice. But as discussed above,

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52 For illustration, see the distribution of MFN clauses through the treaty articles at Hofbauer, Ines. Most-Favoured-Nation Clauses in Double Taxation Conventions-A Worldwide Overview. Intertax 33.10 (2005, pp. 449-453.

53 'As tax conventions are based on the principle of reciprocity, a tax treatment that is granted by one Contracting State under a bilateral agreement to a resident or national of another Contracting State party to that agreement by reason of the specific economic relationship between those Contracting States may not be extended to a resident or national of a third State under the non-discrimination provision of the tax convention between the first State and the third State.', OECD Commentary 2007 on Article 24 Concerning Non-discrimination.

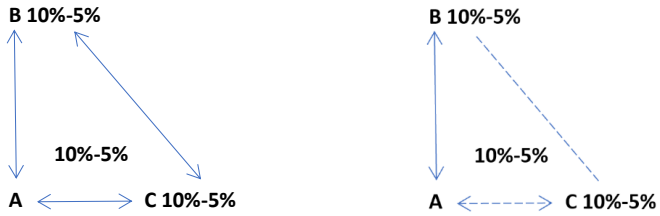
54 Richman, P. (1963). Taxation of Foreign Investment Income, an Economic Analysis. Baltimore, MD: Johns Hopkins Press.

55 CIN aims to lay down a level playing field for residents and non-residents, in the sense of the general international tax system, which is wider than equal treatment in the source. Non-discrimination in the source states is necessary but not sufficient.

MFN shares the value of non-discrimination. So that even though MFN gains far less application, the situation does not prevent MFN from radiating its appeal to a single state. It is held that the MFN clause especially the unilateral type is relied upon by a state as a tool to attracting foreign investment.

To illustrate this point, the base case will be concretized by adding more details and another version. First of all, suppose that in the base case 1, A, B and C are all having tax treaties among each other, and all those treaties include MFN clause regarding the withholding tax rate on interest. The original rates in the three treaties are identically 10%. Now C has negotiated such rate as lowered to 5% with A in their DTA, which means A will impose a preferable rate on investors of C. The MFN clause between A and B will then be triggered, the same rate will apply to B's investors in A. If these MFN clauses in this triangle scenario all provide the two-way treatment, the same change will happen to B and C as the source states. The cross-border investments from and to either A, B and C will face only a 5% withholding tax on interest, so that the overall tax burden on investment within the group of ABC will be decreased. The consideration of taxation will be less weighted in capital movement.

However, a more realistic version of the base case is that the 'conduction chain' of MFN clauses is often broken. When the mutual or group MFN treatment is not available, the unilateral MFN clause in a state's tax treaty with another country will especially attract investment from that country, for its the preferable treatment will be maintained in the state. For example, in the base case 2, A provides unilateral MFN treatment to B in their DTA, while C has MFN arrangements with neither A nor B. In this new situation, if A provides lower rate from 10% to 5% to C, A will also accord such rate to B. In contrast, if the rate for B further drops to 3%, C is not entitled to such favorable treatment. The base case 2 has identified that in the real world where bilateral or multilateral MFN is rare[56], a unilateral MFN can guarantee the target country is treated no worse than any other countries in the source state. The source country can thus gain an advantage over its competitors attracting the target country's investment.



2.4.3. New Developments of MFN in China

In general, China has few MFN clauses in its extensive tax treaty network, consistent with the overall situation in the world. But the recent move in the DTA with Chile provides us with a new window to think through the implications of MFN. China and Chile signed their first tax treaty in 2015, and Chile officially endorsed BRI in 2018. The China-Chile tax treaty is annexed to a protocol, of which the article 10 has prescribed an MFN clause regarding the withholding rate on interest.[57] The MFN treatment is provided unilaterally by Chile to China, saying that in the case that Chile applies lower rate in the treaty with a third country for interest payment from Chile, the same low rate will then be provided to China as well. In 2018, two years after the China-Chile DTA took effect, the MFN clause was triggered since Chile had negotiated

56 For the comprehensive collection of the existing MFN clauses in the global bilateral tax treaty network, see IBFD-Tax Research Platform-Treaties-MFN.

57 'In the event that pursuant to an Agreement concluded with a country after the date of signature of this Agreement, Chile agrees to a lower rate of tax in paragraph 2 of Article 11, such new rate shall automatically apply under the same conditions as established in that other Agreement, for the purposes of this Agreement when the provision of the first-mentioned Agreement becomes applicable, in particular with reference to financial institutions wholly owned by the government. In such case, the competent authorities shall by mutual agreement settle the mode of application of this paragraph.', available at http://www.chinatax.gov.cn/n810341/n810770/c1644352/part/1659942.pdf.

lower rate with Japan and Italy.[58] As a result, the two countries through the exchange of notes modified the original interest article in 2018.

The implications of this new development should be considered from both signatory parties. On one hand, it should be noted that before the treaty with China, Chile has already been veteran in adopting MFN clause in its DTAs. By now, there are 22 DATs that contain the MFN clause,[59] and the majority of them are with OECD countries. Combining the earlier analysis, the intention of Chile embracing the MFN is clear, especially considering most of OECD countries use the exemption method to eliminate double taxation. Chile aims to level the playing field at least in terms of certain tax aspects for those capital-exporting countries, the economic efficiency will be enhanced probably at the cost of reciprocity. And the MFN clauses will increase the horizontal attractiveness over its fellow South American countries as well.

On the other hand, at the side of China, because the successful application of MFN clause with Chile, its competitive advantage of tax policy is sealed. The treaty with Chile is not the first that contains an MFN clause, even though the total number is indeed tiny. What makes the MFN clause with Chile of significance is not about the content, but it is the first of such being effectively activated and unilaterally given to China, which also denotes the willingness of China to innovate in DTA design.[60] The earlier MFN clauses are either bilateral like with Philippine[61], or unilaterally given to other countries like the Netherlands[62]. In any event, the MFN clauses remain on the paper. The activated MFN clause will further add forces to the position of China as both the largest trade partner of and exporter to Chile, among other capital exporters including Japan and Italy. And that particularly relates to BRI which is expected to deepen the economic relationship of the two countries.

2.4.4. The Shifted Position of China

MFN clause has a special status in the general institutions of international tax law. Under the current circumstances that a multilateral or regional tax treaty is not around the corner, the reciprocity and privity of DTA are material obstacles to the acceptance of MFN clause. The adoption and practice of MFN clause in the global tax treaty network are thus not common. In contrast, the non-discrimination article, which shares the equal treatment principle with MFN, is routine in DTAs. The deviated reality of non-discrimination and MFN, however, does not cut the link that they both target the negative economic effect of unequal treatment. Based on that, countries should have been obsessed with MFN clause. Due to the restrictions though, countries may retreat to providing unilateral MFN treatment utilizing MFN clause as an instrument to attracting investment. On the mirror side, there may also be countries that demand the MFN treatment proactively in that it maintains their relative competitiveness.

The above case roughly echoes the track of MFN clause in China, which sheds some lights on the task of this article, for that the shifted position of China corresponds to the transition of ITSC from SOT to ROT. Before the China-Chile treaty, though remaining deactivated and with exceptions[63], the MFN clauses of China are introduced for the sake of its value of attracting capital. For example, China provides MFN treatment unilaterally to the Netherlands in 1987. The case of the United States is not that straightforward, but according to 'substance over form', the MFN clause with the United States that specifies the sparing

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58 'I hereby inform you that the condition for this (MFN) clause to apply has been fulfilled, since Chile concluded after the date of signature of the Convention with China, a convention with Japan and another with Italy that contemplates lower source tax rates for interests than those contained in the Convention between Chile and China.', Exchange of Notes of China and Chile tax authorities in 2018, available at http://www.chinatax.gov.cn/n810341/n810770/c1644352/part/3562025.pdf.

59 IBFD Tax Research Platform.

60 'Coming of age – China's leveraging of BEPS', available at https://www.internationaltaxreview.com/Article/3848525/Coming-of-ageChinas-leveraging-of-BEPS.html?ArticleId=3848525.

61 Art. 2 of the Protocol to the Agreement Between the Government of The People's Republic of China and the Government of the Republic of the Philippines for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, available at http://www.chinatax.gov.cn/n810341/n810770/c1153616/part/1153618.pdf.

62 Article IX of Protocol to the Agreement between the Government of the People's Republic of China and the Kingdom of the Netherlands for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, http://www.chinatax.gov.cn/n810341/n810770/c1153196/part/1153200.pdf.

63 For example, the exception is that with Vietnam, in which the MFN treatment is given unilaterally to China by Vietnam, see Exchange of Notes, available at http://www.chinatax.gov.cn/n810341/n810770/c1153436/part/1153443.pdf.

credit in their 1984 Exchange of Notes serves the same purpose for China.[64] In this phase, MFN is one of the characteristics that contribute to the so-called SOT system, when the focus of SAT was to attract foreign capital or safeguarding its source taxing rights. In the more recent times, China either withdrawn the unilateral MFN treatment to other countries, for example, the unilateral MFN treatment to the Netherlands was canceled in their renegotiated treaty in 2014, or as discussed, China was taking MFN treatment from Chile. Especially for the latter, SAT opened a new door out of the sights of OECD or UN MTC serving the redirected goals of ITSC towards ROT against the background of BRI.

G. Conclusion

The changes surveyed and analyzed in accordance with the approach illuminated earlier have verified the claim made in part B of this article. The international tax system of China, propelled by the forces of BRI, has a clear trend of transforming from source-oriented to residence-oriented tax system. The SAT, either in formulating domestic tax policies or negotiating double tax agreements, bears more and more residence than source thinking.

As explained in part C, China has formed at the top level the systematic design for developing BRI, in which SAT was assigned for advancing BRI in both facilitating outbound investment and managing the risks therein. This two-direction guideline can also basically cover the rule-based efforts made in domestic and DTA aspects. From domestic rule-making perspective, the improved tax credit system and CFC regime respectively ease the burden and defend against base erosion. More domestic measures that are not rule-based as seen in table 2 are skipped by this article, which operate along this same two-lane route as well. From the perspective of bilateral tax treaty, the expanding breadth of China's tax treaty network, among other dimensions, are paving the way for Chinese companies going global. In terms of depth, the changes of sparing credit, withholding tax liability and the MFN clause are both signaling the transformation of China's position in tax treaties.

The trend is real, and this article further holds that such transformation to residence-oriented taxation is an ongoing process. And that does not mean China is loosening its taxing rights as the state of source. Actions have also been taken to attract foreign investment or combat source base erosion, but mostly they stay at the level of rule-administration rather than rule-making.[65] In contrast, it has been revealed from top to the bottom the rule-based changes that lead to residence-oriented taxation, and the construction of BRI has accelerated the transformation and made it more observable.

64 As analyzed earlier regarding the function of sparing credit, here the MFN clause is a tool for China to attract investment from the United States. 'Both sides agree that a tax sparing credit shall not be provided in Article 22 of this Agreement at this time. However, the Agreement shall be promptly amended to incorporate a tax sparing credit provision if the United States hereafter amends its laws concerning the provision of tax sparing credits, or the United States reaches agreement on the provisions of a tax sparing credit with any other country.', Exchange of Notes of DTA between China and the United States, available at http://www.chinatax.gov.cn/n810341/n810770/c1153055/part/1153063.pdf.

65 An exception is the Announcement of SAT on Issues Concerning Expanding the Applicable Scope of the Policy of Temporary Exemption of Withholding Tax on the Direct Investment Made by Overseas Investors with Distributed Profits, No.53 [2018].

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***Abstract*:** The Belt and Road Initiative (BRI), as one of the most remarkable events of international economic cooperation nowadays, has noticeable implications for many areas of study. This article is to explore how BRI, an initiative proposed and championed by China, has influenced China's international tax system. To answer the question, the article sets two poles for depicting a country's position of international taxation, namely, the source-oriented tax system and residence-oriented tax system. Based on that, this article puts forward the proposition that there is a trend that China's international tax system is transforming from source-oriented to residence-oriented. In the end, the article is concluded by rendering the proposition as tenable.

Keywords: Belt and Road Initiative, China, international tax system

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