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## Preferential Corporate Income Tax Policies of China

### Background

In the past three months, Chinese State Administration of Taxation ("SAT") has issued a series of preferential Corporate Income Tax ("CIT") policies to encourage investment and economic recovery.

This newsletter aims to elaborate on the detailed contents and implications brought about by these preferential policies.

The criteria, timeline, and implications summary is listed as below for your management's reference.

### Key Content

#### 1. Preferential Corporate Income Tax policy for enterprises in key industries in Lingang New Area of Shanghai Pilot Free Trade Zone (Cai Shui [2020] No. 38)

1) Any qualified enterprise as legal person in the New Area engaging in the relevant product (technology) business in a core process step of a key industry such as **integrated circuit, artificial intelligence, biomedical, civil aviation and etc.**, and carrying out substantive production or research and development activities shall be subject to Corporate Income Tax at a reduced tax rate of 15% within five years from the date of establishment.

#### 2) Criteria

For the purpose of this Notice, a "qualified enterprise as legal person" shall satisfy all the following criteria in item (I) and item (II), and any sub-criteria in item (III) or item (IV) at the same time:

(I) Legal entities registered in the New Area since 1 January 2020

(excluding those relocate to the New Area from other areas) and mainly engaged in substantial production or R&D activities in key industries elaborated in the Catalogue of Core process in Key Industries of Integrated Circuits, Artificial Intelligence, Biomedicine, and civil Aviation in the New Area (the Catalogue", please refer to the Appendix).

\*Substantial production or R&D activities refer to the fact that the enterprise has a fixed place of business activities, regular staff, and is equipped with hardware and software supporting the production or R&D activities, and uses these to carry out the relevant business.

(II) At least 1 core product (technology) shall be included in the main R&D or sales products of the enterprise.

\*Core products (technologies) are products (technologies) that play important roles or are indispensable in core process step of a key industry such as integrated circuits, artificial intelligence. bio-medicine, civil aviation, etc.

(III) Requirements of the investors:

- i) The investor has leading international market influence in the industry, and its technical strength is ranked among the best in the industry;
- ii) The investor is in a leading position in the domestic market segment, and has cutting-edge technologies in the industry.

(IV) R&D and production conditions:

- i) The enterprise shall have leading talent and core team, and has engaged in scientific research and production in related fields at home and abroad for a long period of time;
- ii) The enterprise shall possess core technologies and has the ability to establish an intellectual property system for its main products;
- iii) The enterprise shall have the ability to promote the diversification of core suppliers in the industry chain and to lead the upgrading of domestic industries;
- iv) The enterprise shall possess high-end supply capability, and the core technical indicators is in the forefront of the international or domestic markets;

v) The R&D results (technology or product) of the enterprise have been adopted by first-tier terminal equipment manufacturers at home and abroad or have already had close and substantive cooperation with them in the areas of capital, scientific research, projects, etc.;

vi) The enterprise which have obtained special funds for technology or industrialization at national or provincial government level, or government investment funds or investment from well-known investment and financing institutions.

## **2. Notice on Preferential CIT Policies for the Hainan Free Trade Port (“FTP”) (Cai Shui [2020] No. 31)**

1) A reduced 15% CIT (China standard rate is 25%) rate applies to enterprises (i) registered in Hainan FTP; (ii) engaged in substantive business activities; (iii) in encouraged industries

Circular 31 requires establishment of the enterprise’s management body in Hainan FTP

This must exercise substantive management and control over business operations, staff, accounting, assets, etc.

“Encouraged industries” refers to sectors listed in the Guiding Catalogue for Industrial Structure Adjustment (2019 Edition), the Catalogue of Encouraged Industries for Foreign Investment (2019 Edition) and a new Hainan-specific list

Enterprise revenue from “encouraged industry” business must be at least 60% of the total

15% tax rate applies to income of head offices and branches set up in Hainan FTP

2) CIT exemption for “new” foreign-sourced income received by Hainan FTP enterprises in the tourism, modern services and high-tech industries

New foreign-sourced income refers to:

- Operating profits earned by newly established overseas branches of the Hainan company; or
- Dividends repatriated from an overseas subsidiary in which the Hainan company has a shareholding of at least 20%. The dividends must arise from new direct investment made in the overseas subsidiary.

The statutory CIT rate of the investee jurisdiction must not be lower than 5%

3) 100% expensing, and accelerated depreciation regimes for eligible capital expenditure applies for newly purchased fixed assets (except for immovables) and intangible assets

No limitations on industry or based on usage of assets. 100% expensing only for assets with a unit value less than RMB 5 million

In detail:

For an enterprise established in the Hainan Free Trade Port, if its newly purchased (including self-constructed and self-developed) fixed assets or intangible assets have a unit value of no more than CNY 5 million, they are allowed to be included in the current costs and expenses on a one-off basis and deducted before the calculation of taxable income, and there is no need to annually calculate depreciation and amortization; if the unit value of newly purchased (including self-constructed and self-developed) fixed assets or intangible assets exceeds CNY 5 million, the depreciation or amortization period may be shortened or the accelerated depreciation or amortization method may be adopted.

The term "fixed assets" as used in this Article means fixed assets other than houses and buildings.

This Notice shall come into force on January 1, 2020 and remain effective until December 31, 2024.

### **3. a 10-year tax exemption for enterprises or projects with IC line width of less than 28nm. The loss carry-forward period of eligible IC manufacturing enterprises is extended to 10 years (Guo Fa [2020] No.8)**

On 4 August, the State Council released a Notice (Guo Fa [2020] No 8, "the Notice") to promote the development of the integrated circuit ("IC") industry and software industry since the issuance of Guo Fa [2000] No. 18 and Guo Fa [2011] No 4. The Notice formulates the preferential policies of tax reduction and exemption across the whole industry chain It also covers other aspects, such as investment and financing, research and development (R&D), import and export, talents, intellectual property, market applications, and international cooperation to fully support the development of the IC and software industries. The Notice extends the original tax preferential policies for IC enterprises (including design manufacturing, packaging, testing, equipment, and material enterprises) and software enterprises, and newly grants a 10-year tax exemption for enterprises or projects with IC line width of less than 28nm The loss carry-forward period of eligible IC manufacturing enterprises is extended to 10 years.

**4. During the period from January 1, 2021 to December 31, 2030, CIT shall be levied at a reduced tax rate of 15% on enterprises established in the western region in encouraged industries. (an extension of old western region policy)**

Enterprises in encouraged industries referred to herein shall mean enterprises whose principal businesses are industry projects stipulated in the Catalogue of Encouraged Industries in the Western Region, and whose income from principal businesses constitutes 60% or more of their total income.

Reference: Announcement on Continuation of CIT Policies for Large-scale Development in the Western Region (Announcement [2020] No.23 of the Ministry of Finance, State Taxation Administration and National Development and Reform Commission)

**5. the Deferred Payment of Income Tax in 2020 by Small Low-profit Enterprises and Individual Businesses**

1) The State Administration of Taxation issued the "Announcement on Matters Concerning the Deferred Payment of Income Tax in 2020 by Small Low-profit Enterprises and Individual Businesses " (Announcement of the State Taxation Administration [2020] No.10). From May 1, 2020 to December 31, 2020, small low-profit enterprises may defer the payment of corporate income tax for the current period after completing the filing of tax returns with prepayment according to the provisions in the remaining filing period in 2020, and the payment of all income tax amount may be deferred to the first period for filing tax returns in 2021. When filing tax returns with prepayment, small low-profit enterprises may enjoy the policy on deferred payment of corporate income tax for small low-profit enterprises by filling in the relevant rows of the prepayment tax return form.

Among them, Small Low-profit Enterprises refer to enterprises that are engaged in non-restricted and non-prohibited industries by the state and meet the following conditions simultaneously:

- The annual taxable income does not exceed RMB 3 million,
- the number of employees does not exceed 300, and
- the total assets do not exceed RMB 50 million.

2) During the period from May 1, 2020 to December 31, 2020, upon completion of filing returns for individual income tax on income from business operation in the remaining filing period for 2020 as required, individual businesses may defer payment of individual income tax for the current period, and the payment of all income tax amount may be deferred to the first period for filing tax returns in 2021. For individual businesses adopting the simple method for filing tax returns, individual income tax will not be deducted temporarily during the period from May 1, 2020 to December 31, 2020, and the payment of all income tax amount may be deferred to the first period for filing tax returns in 2021.

This Announcement shall come into force as of May 1, 2020. Taxpayers who have paid tax amount which complies with the provisions of this Announcement on deferring tax payment during the period from May 1 to the date of promulgation of this Announcement may apply for refund and the payment of all income tax amount may be deferred to the first period for filing tax returns in 2021.