



China Tax Newsletter

September 2017

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1. Preferential Tax Policies in the Law of the People's Republic of China on Promotion of Small and Medium-sized Enterprises

The Law of the People's Republic of China on Promotion of Small and Medium-sized Enterprises (hereinafter referred to as "new Law on Promotion of SMEs") was revised and adopted at the 29th Session of the Standing Committee of the 12th National People's Congress of the People's Republic of China on September 1, 2017 and will be put into implementation as of January 1, 2018.

Compared to the existing Law on Promotion of SMEs, the new Law expands from 7 chapters to 10 chapters, with articles increased from 45 to 61. The new Law on Promotion of SMEs features not only the relevant refined measures on promoting financing and relevant chapters on protection of rights and interests and on special supervision and inspection, but also parts of the current preferential tax policies which upgrades these tax policies to tax laws (see below):

- Article 11 The State shall adopt tax policies conducive to the development of small and micro enterprises, take measures such as the postponement of the imposition of, reduction of or exemption from enterprise income tax, value-added tax, etc. for eligible small and micro enterprises as per provisions, simplify the tax collection and administration procedures, and reduce the tax burden on small and micro enterprises.
- Article 12 The State shall implement favorable policies such as reduction of or exemption from administrative fees for small and micro enterprises to reduce the burden on them.
- Article 25 Any graduate of an institution of higher education, ex-serviceman, unemployed person or disabled person that starts a small and micro enterprise shall enjoy tax preferences and the reduction of or exemption from charges as per the state provisions.
- Article 26 The State shall take measures to support social funds to participate in the investment in SMEs. Where a venture capital enterprise or individual investor invests in an innovative enterprise for science and technology at the start-up stage, it or he shall enjoy tax preferences as per the state provisions.
- Article 32 Where it is necessary to accelerate the depreciation of the fixed assets of SMEs for the reason of technical progress, etc., the depreciation period may be shortened or the accelerated depreciation method may be adopted.

The State shall improve the additional deduction policy for the research and development (R&D) expenses of SMEs in order to support their technical innovation.

Preferential tax policies in the new Law of Promotion of SMEs are briefly summarized as follows:

(1) Income Tax Preferential Policies for Small Low-Profit Enterprises

The Ministry of Finance and the State Administration of Taxation issued the circular on Widening the Coverage of Income Tax Preferential Policies for Small Low-Profit Enterprises (Cai Shui [2017] No. 43) on June 6, 2017.

Per the circular, from January 1, 2017 to December 31, 2019, for a small low-profit enterprise of which the annual taxable income is less than CNY500,000 (inclusive), its income is included in the taxable income at the reduced ratio of 50%, and the enterprise income tax is levied at the reduced tax rate of 20%.

▲ Supporting Policy on Tax Levy and Administration

Announcement of the State Administration of Taxation on Tax Levy and Administration Matters concerning the Implementation of Enterprise Income Tax Preferential Policies with Widened Coverage for Small Low-profit Enterprises (Announcement of the State Administration of Taxation [2017] No. 23)

(2) VAT Exemption for Qualified Small-Scale VAT Taxpayers

Per the Announcement of the State Administration of Taxation on Issues concerning Exempting Small and Micro Enterprises from Value-added Tax and Business Tax (Announcement of the State Administration of Taxation [2014] No. 57) and Article 50 of the Implementation Measures for the Pilot Program of the Collection of Value-added Tax in Lieu of Business Tax (Appendix 1 of Circular Cai Shui [2016] No. 36):

Enterprises or non-enterprise entities that are small-scale VAT taxpayers whose monthly sales amount is not more than CNY30,000 (or CNY90,000 for quarterly sales) may be temporarily exempted from VAT.

(3) Relevant Policies on Widening the Exemption Scope of Governmental Funds on Small and Micro Enterprises

Per the circular on Widening the Exemption Scope of Relevant Governmental Funds (Cai Shui [2016] No. 12) which is effective from February 1, 2016, small and micro enterprises that meet the following criteria shall be exempted from relevant governmental funds:

For payment obligors whose monthly taxable sales amount is not more than CNY100,000 (CNY300,000 for quarterly taxable sales), they are exempted from education surcharges, local education surcharges and water conservancy construction funds.

According to the Notice of the Ministry of Finance and the State Administration of Taxation on Issues concerning Policies and Levying and Administration of Development Fee for Cultural Undertakings in the Pilot Program of the Collection of Value-added Tax in Lieu of Business Tax (Cai Shui [2016] No. 25), from January 1, 2015 to December 31, 2017, the development fee shall be waived for payment obligators with a monthly sales of not more than CNY30,000 (inclusive) in case of paying tax on a monthly basis, or with a quarterly sales of CNY90,000 (inclusive) in case of paying tax on a quarterly basis.

Per Article 2 of the Notice on Exempting Small and Micro Enterprises from Relevant Government Funds (Cai Shui [2014] No. 122), small and micro enterprises which have no more than 20 employees and which fail to achieve the required percentage of employment for the disabled within three years from the date of registration with the industrial and commercial bureau shall be exempted from employment security funds for the disabled.

(4) Tax Incentives on Supporting and Promoting the Entrepreneurship and Employment of the Graduates of Institutions of Higher Education and the Unemployed

Per the Notice on Continuing the Implementation of Relevant Tax Policies for Supporting

and Promoting the Entrepreneurship and Employment of Key Groups (Cai Shui [2017] No. 49):

From January 1, 2017 to December 31, 2019, for an individual who holds an Employment and Entrepreneurship Certificate or an Employment and Unemployment Registration Certificate and engages in individual business, taxes and surcharges including value-added tax, urban maintenance and construction tax, education surcharges, local education surcharges and individual income tax payable for the current year shall be reduced in sequence by up to CNY8,000 per household annually within three years. The quota of such tax incentives may float upward by 20% at maximum for local implementation.

(5) Tax Incentives on Supporting Entrepreneurship and Employment of Ex-Servicemen Seeking Employment on Their Own

According to the Notice on Continuing the Implementation of Related Tax Policies for Supporting Entrepreneurship and Employment of Ex-Servicemen Seeking Employment on Their Own (Cai Shui [2017] No. 46), for ex-servicemen seeking employment on their own who engage in individual business, taxes and surcharges including value-added tax, urban maintenance and construction tax, education surcharges, local education surcharges and individual income tax payable for the current year shall be reduced in sequence by up to CNY8,000 per household annually within three years. The quota of such tax incentives may float upward by 20% at maximum for local implementation.

The period of execution of the Notice is from January 1, 2017 to December 31, 2019.

(6) Tax Incentives on Encouraging Entrepreneurship and Employment of Disabled Persons

According to the Provisions on Transitional Policies for the Pilot Program of the Collection of Value-added Tax in Lieu of Business Tax (Appendix 3 of Circular Cai Shui [2016] No. 36), services provided by the disabled for the public can be exempted from VAT.

According to Article 36 of the Law of the People's Republic of China on the Protection of Disabled Persons, the State exempts self-employed disabled persons from administrative fees.

In addition, according to Article 5 of the Individual Income Tax Law of the People's Republic of China, individual income tax levied on income of the disabled may be reduced upon approval.

(7) Income Tax Incentives for Venture Capital Enterprises and Individual Angel Investors Investing in Science and Technology Enterprise at Seed Stage or Early Stage

To further implement the innovation-driven development strategy, the Ministry of Finance and the State Administration of Taxation released the Notice on Promulgation of the Pilot Tax Policies for Venture Capital Enterprises and Individual Angel Investors (Cai shui [2017] No. 38) which notifies relevant pilot preferential tax policies for venture capital enterprises and individual angel investors, see below:

Where a venture capital enterprise of corporate nature or under a limited partnership has made direct equity investment in a science and technology enterprise at seed stage or early stage (hereinafter referred to as the "tech startup") for two or more than two years (24 months, the same below), it may deduct 70% of its investment amount from its

taxable income (i.e. taxable income of the venture capital enterprise of corporate nature, income distributed to the corporate partner from the partnership venture capital enterprise, and business income distributed to the individual partner from the partnership venture capital enterprise) of the current year when the equity has been held for 2 years; if the taxable income of the current year is insufficient to be deducted, the deduction may be carried forward to the subsequent tax year.

Where an individual angel investor has made direct equity investment in a tech startup for two or more than two years, he/she may deduct 70% of the investment amount from his/her taxable income obtained from transfer of the equity of such tech startup; if his/her taxable income for the current period is insufficient to be deducted, the deduction may be carried forward to the future when he/she obtains taxable income from transfer of the equity of such tech startup.

Where an individual angel investor has invested in multiple tech startups in pilot areas among which some of the tech startups are going through the deregistration formalities, if the 70% of the investor's investment amounts in these tech startups have not been fully deducted, the deduction balance may be carried forward to be deducted from the taxable income obtained by the individual angel investor from the transfer of the equity of other tech startups within 36 months from the date of the aforesaid deregistration.

The enterprise income tax policies stipulated in this Notice shall be implemented from January 1, 2017, and the individual income tax policies shall come into effect on July 1, 2017. The pilot areas in this Notice cover 8 comprehensive innovative and reformative pilot areas including Beijing-Tianjin-Hebei, Shanghai, Guangdong, Anhui, Sichuan, Wuhan, Xi'an and Shenyang, and the Suzhou Industrial Park.

▲ Supporting Policy on Tax Levy and Administration

Announcement of the State Administration of Taxation on Issues Concerning the Pilot Tax Policies for Venture Capital Enterprises and Individual Angel Investors (Announcement of the State Administration of Taxation [2017] No. 20)

(8) Proportion of Additional Pre-tax Deduction of R&D Expenses Raised from 50% to 75% for SME Science and Technology Enterprises

According to the Notice on Increasing the Proportion of Additional Pre-tax Deduction of Research and Development Expenses for Small and Medium-sized Science and Technology Enterprises (Cai Shui [2017] No. 34) issued by the Ministry of Finance, the State Administration of Taxation and the Ministry of Science and Technology, regarding the actual R&D expenses incurred by a SME science and technology enterprise from its R&D activities, an additional 75% of the actually incurred expenses may be deducted before tax from January 1, 2017 to December 31, 2019, on the basis of actual deductions as required, provided that no intangible asset has been formed and balanced into its current gains and losses; where any intangible asset has been formed, such expenses may be amortized at the rate of 175% of the intangible asset's costs before tax during the above-mentioned period.

Other policy criteria for SME science and technology enterprise to enjoy the policy of additional pre-tax deduction of R&D expenses shall be subject to the provisions set out in the Notice of the Ministry of Finance, the State Administration of Taxation and the Ministry of Science and Technology on Improving the Policy on Additional Pre-tax Deduction of Research and Development Expenses (Cai Shui [2015] No. 119).

▲ Supporting Policy on Tax Levy and Administration

Announcement of the State Administration of Taxation on Issues concerning Increasing the Proportion of Additional Pre-tax Deduction of Research and Development Expenses of Small and Medium-sized Science and Technology Enterprises (Announcement of the State Administration of Taxation [2017] No. 18)

Notice of the Ministry of Science and Technology, the Ministry of Finance and the State Administration of Taxation on Promulgation of the Measures for Evaluating Small and Medium-sized Science and Technology Enterprises (Guo Ke Fa Zheng [2017] No. 115)

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