**In brief**

To further stimulate the growth of foreign capital and create a higher level of open environment for foreign investors, the State Council issued the 22 Measures¹ in August 2017, setting forth a series of objectives for formulating fiscal and tax incentives, including: extending the corporate income tax (CIT) incentives for Technological Advanced Service Enterprises (TASEs) in China. Later on, on 2 November 2017, the Ministry of Finance (MOF), State Administration of Taxation (SAT), Ministry of Commerce (MOC), Ministry of Science and Technology (MST) and National Development and Reform Commission (NDRC) (the “Five Ministries”) jointly issued the “Notice on Nation-wide Implementation of the Preferential CIT Treatment for TASEs (Caishui [2017] No.79 or Circular 79)” to extend this CIT incentive nationwide effective from 1 January 2017.

The release of Circular 79 will allow more high-tech and high-value-added service enterprises to enjoy this preferential tax policies. In this issue of China Tax and Business News Flash, we will review the process of extending the preferential CIT policies for TASEs, introduce the applicable criteria and preferential policies, and summarize several key points for enterprises’ reference.

**In detail**

**Policy review**

The preferential CIT policies for TASEs were firstly piloted in Suzhou Industrial Park in 2006. The Chinese government then extended these policies to 20 Service Outsourcing Demonstration Cities (SODCs) (the “Pilot Cities”) from 1 January 2009, and further clarified the scope of qualified technological advanced services, the related preferential policies and applicable criteria. One of the key criteria is that the TASE’s income derived from offshore outsourcing services should account for no less than 50% of its total income².

Later on, with the release of Caishui [2010] No.65 ³, Caishui [2014] No.59 ⁴, and Caishui [2016] No.108 ⁵, the valid period for TASE’s preferential policies was continuously extended, the scope of pilot SODC’s was further expanded, and the applicable criteria were further relaxed. Currently, enterprises in 31 Pilot Cities are eligible for the preferential CIT treatment. Meanwhile, the minimum requirement for income derived from offshore outsourcing services is lowered from 50% to 35%.

To implement the 22 Measures, further increase foreign capital, and create an improved open environment, the Five Ministries jointly issued Circular 79 to roll out this CIT incentive nationwide.

**Preferential policies**

From 1 January 2017, recognized TASEs can enjoy the following preferential CIT policies nationwide:

- A reduced CIT rate of 15% (the statutory CIT rate for general enterprises is 25%); and
- An increase in the deduction cap for employee education expenses for CIT purpose from 2.5% to 8% of total wages and salaries (the deduction cap for general enterprises is 2.5%) with the excess allowed to be carried forward to subsequent tax years.
Applicable criteria
TASEs wishing to enjoy the preferential CIT policies mentioned above have to satisfy all of the following criteria:

- Company profile - corporate enterprises registered within the territory of China (excluding Hong Kong, Macao and Taiwan);
- Service scope – enterprises have to engage in the provision of qualified technological advanced services set out in the Recognition Scope of Qualified Technological Advanced Services (the “Scope”), i.e. information technology outsourcing (ITO), business process outsourcing (BPO) and knowledge process outsourcing (KPO), and adopt advanced technologies or possess strong R&D capability;
- Headcount – more than 50% of the total headcount of the company has to have a college degree or above;
- Income derived from qualified technological advanced services - income generated by the enterprise from the provision of qualified technological advanced services should not be less than 50% of its annual total income; and
- Offshore outsourcing service income – income generated by the enterprise from the provision of qualified offshore outsourcing services should not be less than 35% of its annual total income. “Offshore outsourcing service income” refers to income derived by an enterprise from its overseas entity under a subcontract arrangement where the enterprise or its directly subcontracted enterprise provides ITO, BPO and KPO services stipulated in the above Service scope.

The takeaway

Tax incentives and criteria inherited from Caishui [2014] No.59

The extension in Circular 79 aims to allow eligible high-tech and high-value-added service enterprises across the country to enjoy the preferential tax policies for TASEs, in order to further ensure that the trade in service structure would help China to become more competitive. The preferential policies, applicable criteria and the Scope provided under Circular 79 basically follow the tax policies for TASEs in the current Pilot Cities as prescribed in Caishui [2014] No.59. As such, the existing TASEs recognized for year 2017 in the current 31 Pilot Cities are still eligible. Since Circular 79 took effect from 1 January 2017, enterprises previously located outside the Pilot Cities can now apply for the qualification for the year 2017, and enjoy the preferential policies in the 2017 annual CIT filing.

Provincial-level authority is in-charge of TASE’s determination and administration

According to Caishui [2014] No.59, eligible TASEs should lodge an application to the science and technology departments in their Pilot Cities, and the municipal science and technology departments, commerce department, finance department, tax department as well as the development and reform department shall jointly review the application. Now Circular 79 sets forth that the provincial department instead of the municipal authorities shall be in-charge of TASE’s recognition and administration so as to ensure centralized management. On one hand, it means enterprises in different areas within one province would receive an equitable treatment under a consistent administrative standard, which shows the commitment of relevant authorities to extend the TASE’s CIT incentive nationwide. On the other hand, provinces have to formulate their respective administrative measures for TASE determination by the end of 2017. Due to differences in industry structures and technical administration levels of the different provinces, one cannot rule out the possibility of differences among the administrative measures to be released by the provinces. As such, cross-provincial service groups should pay attention and understand whether there are differences in local-level measures when applying for the determination of the TASE status for group companies in different locations. In the meantime, it is recommended that existing TASEs should pay close attention to the possible modifications in the procedure of application in the future.

A new set of platform and information system for TASE administration

Under Circular 79, the list of recognized enterprises and relevant information shall all be filed for record through the MST’s “Administrative Platform for TASEs in China”, and the filed information are exchanged among the five Ministries. In addition, eligible TASEs should fill in the enterprise’s basic information in the MOC’s “Information Management System for Supervising the Statistics of the Trade and Services Sector” (information of the outsourcing service part) and timely submit them. The above two provisions lead to a more transparent and open administration of enterprise’s information. According to the previous experience, a new set of platform and information system would generally be followed by a smart supervision method based on automatic correlation, logic verification, and early warning, etc. It is therefore recommended that enterprises should ensure that the data submitted regarding TASE application substantially demonstrates the enterprise’s true technological capacity and financial condition. In case there is a difference between their data and other information submitted to the authorities through different platforms, enterprises should be able to reasonably explain such difference.

Types of trade in services not covered in this extension

In 2016, the Five Ministries jointly issued Caishui [2016] No.122, allowing enterprises engaged in business that falls within the “Scope of Qualified Technological Advanced Services (Trade in Services)” (the “Catalogue of Trade in Services”) in 15 pilot areas to enjoy the preferential policies of TASEs from 1 January 2016 to 31 December 2017. The Scope of Trade in Services includes cross-border licensing of intellectual properties, digitalization of cultural products and medical care of traditional Chinese medicine, etc. It is important to note that the extension under Circular 79 this time does not cover the Scope of Trade in Services stipulated under Circular 122. It remains to be seen whether the preferential policies in Circular 122 would be extended and/or whether the Scope would be expanded after the expiry at the end of 2017.

Endnote

1. Notice Issued by the State Council Regarding Measures on Promoting the Growth of Foreign Capital in China (Guo Fa [2017] No.39). For the details and observations, please refer
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2. For details please refer to the “Notice Regarding Relevant Policies for Technology Advanced Service Enterprises” (Cai Shui [2009] No.63).

3. Notice Jointly Issued by the MOF, SAT, MOC, MST and NDRC Regarding CIT Treatments for Technology Advanced Service Enterprises (Cai Shui [2010] No.65)

4. Notice Jointly Issued by the MOF, SAT, MOC, MST and NDRC Further Refining the CIT Treatments for Technology Advanced Service Enterprises (Cai Shui [2014] No.59)

5. Notice Jointly Issued by the MOF, SAT, MOC, MST and NDRC Expanding the List of Service Outsourcing Demonstration Cities Eligible for the CIT Treatments of Technology Advanced Service Enterprises (Cai Shui [2016] No.108)
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Let’s talk

For a deeper discussion of how this issue might affect your business, please contact a member of PwC’s China Research and Development Incentive Services Team:

Roger Di  
China R&D Incentive Services Leading Partner  
+86 (10) 6533 2268  
roger.di@cn.pwc.com

Landa Guo  
Central China R&D Incentive Services Partner  
+ 86 (21) 23233016  
landa.guo@cn.pwc.com

Yali Chen  
Southern China R&D Incentive Services Director  
+86 (10) 6533 3383  
yali.chen@cn.pwc.com

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For more information, please contact:
Matthew Mui  
+86 (10) 6533 3028  
matthew.mui@cn.pwc.com

Please visit PwC’s websites at http://www.pwccn.com (China Home) or http://www.pwchk.com (Hong Kong Home) for practical insights and professional solutions to current and emerging business issues.

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