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Reference: SAT Announcement [2017] No. 40
Issuance date: 8 November 2017
Effective date: Apply to 2017 annual CIT filing and subsequent years

Relevant industries: Industries involved R&D activities
Relevant companies: Enterprises involved R&D activities
Relevant taxes: CIT

Potential impacts on businesses:

- Compliance costs due to regulatory uncertainties reduced

You may click here to access full content of the circular.

R&D super deduction implementation rules

On 8 November 2017, the State Administration of Taxation (SAT) issued Announcement [2017] No. 40 ("Announcement 40"). This clarifies which expenses qualify as research and development (R&D) expenses for super deduction purposes (under this eligible R&D expenses are entitled 150% deduction for CIT purposes; 175% for science and technology SMEs). It also addresses practical issues arising from the two 2015-issued R&D super deduction circulars Cai Shui [2015] No. 119 ("Circular 119") and SAT Announcement [2015] No. 97 ("Announcement 97"). Announcement 40 applies to corporate income tax (CIT) filings from (and including) 2017.

Super deductions are now clarified as available for:

- Wages and salaries directly paid to outsourcing companies undertaking R&D activities;
- Equity incentives provided to R&D staff;
- R&D expenses related to failed R&D activities.

Clarifications are also made in relation to depreciation/amortization on tangible or intangible fixed assets which are used for R&D activities. Announcement 40 clarifies that, where such assets are depreciated/amortized on an accelerated basis (for tax purposes), the depreciation / amortization expenses can be included in the total expenses for super-deduction purposes. This replaces the Announcement 97 provision that the eligible depreciation expense can be claimed for super deduction purposes if the accounting treatment has been followed for tax purposes (this would limit the amount deductible from a tax perspective). For example, if accelerated tax depreciation is 100, and accounting depreciation is 30, Announcement 97 says only 30 can be taken into the super deduction, but Announcement 40 allows 100.

Furthermore, Announcement 40 also clarifies the treatment of government subsidies, multi-year special income (e.g., from selling scrap, faulty or trial products, etc.) and expenses, and outsourcing of R&D projects for super deduction purposes.

* For more information about the R&D "super deduction" policy, you may access the following KPMG publications:

- *China Tax Alert: Notice of the State Administration of Taxation on Further Implementation of the R&D Expenses Super Deduction Policy (Issue 6, February 2017)*
- *China Tax Alert: 150% Super Deduction Regulation Update (Issue 3, January 2016)*
- *China Tax Alert: R&D Super Deduction Regulation Update (Issue 31, November 2015)*

Reference: N/A
Issuance date: 20 November 2017
Effective date: N/A

Relevant industries: Resource related industries
Relevant companies: Resource related companies
Relevant taxes: Resource tax

Potential impacts on businesses:
- Compliance risks due to regulatory uncertainties reduced

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Resource Tax Law in development

On 20 November 2017, the Ministry of Finance (MOF) and SAT issued the Draft Resource Tax Law ('the draft RT law") to solicit the public comments before 20 November 2017.

On 9 May 2016, MOF, SAT and the Ministry of Water Resources (MWR) had issued three circulars, to comprehensively implement the RT reform across China beginning on 1 July 2016 (see KPMG *China Tax Weekly Update (Issue 18, May 2016)* for details). The reform aims to expand the scope of collection of the RT, from a volume based to a price based tax and establish a more fair and efficient RT system.

To this end, the government has now decided to place the existing RT on a statutory basis, i.e., RT is currently based on 1993 State Council-issued rules and it will be replaced by statutory law issued by the National People's Congress. The draft RT law mainly clarifies the following:

- Minerals and salts will be subject to RT. MOF and SAT listed more than 20 major minerals and other minerals that shall be subject to RT which may be determined by provincial-level governments.
- A majority of taxable items will be taxed on price basis while a few items may be taxed either on a price basis or volume basis. The RT collection method may be selected by provincial-level governments and is subject to approval by the standing committee of the people's congress at the same provincial level.
- The water resources tax reform is still in the pilot phase and the existing regulations will not be replaced by statutory law at this stage. Furthermore, China will not currently impose RT on other natural resources such as forests and grassland. At present, pilot program of water resources tax reform is being carried out by the State Council**.**
- Chinese enterprises and foreign enterprises that are currently subject to mining royalties on Sino-foreign cooperative exploration of crude oil and natural gas, will be levied with RT, instead of mining royalties, when the draft RT law is finalized and goes into effect.

* See KPMG *China Tax Weekly Update* (Issue 30, August 2016), (Issue 25, July 2016) for more information about RT reform.

Reference: N/A
Issuance date: N/A
Effective date: N/A

Relevant industries: All
Relevant companies: Group enterprises that fall under TEI
Relevant taxes: CIT / VAT

Potential impacts on businesses:

- Risks of being challenged due to non-compliance issued increased

You may click here to access full content of the circular.

Tax risk management for TEI-covered group enterprises

On 24 November 2017, Mr. Wang Fukai, deputy director of the SAT Large Enterprise Department ("LED"), shared details of the SAT's progress with tax risk management for group enterprises listed in the "Thousand Enterprises Initiative" ("TEI"). This took place through an online discussion (webcast) with taxpayers. Mr. Wang highlighted the following:

- The LED has started to perform a tax risk analysis for each TEI-covered group enterprise and their member enterprises. Based on the analysis, the identified tax risks of each member enterprise will be sent to the state/local tax bureaus, via the Golden Tax III system, for further consideration and action. This will improve overall tax administration efficiency by providing better support for taxpayers who are proactive in tax risk management, as well as by helping tax officers to screen audit targets and risk areas.
- SAT is looking to set up a communication mechanism to tackle inconsistency issues arising from the diverse application of individual tax policies, by different local authorities. Under this mechanism, SAT will communicate with the headquarters of the involved group enterprise to reach an agreement on the tax treatment of an issue, before it is sent to local tax authorities for resolution.
- Tax risk analysis on TEI-covered enterprises focuses on completed transactions, rather than transactions which are still in progress. However, SAT may conduct tax risk analysis for an enterprise on its in-progress and more complex transactions (such as mergers and acquisitions transactions) upon receipt of relevant information and data. The identified tax risks will be alerted to the enterprise to ensure that tax filing for the transaction is accurately performed. This may reduce the enterprise's risk of late payment surcharges and penalties.
- In collaboration with provincial-level tax authorities, the Fifth Branch of the Beijing State Tax Bureau has been assigned to support the SAT to work on the analysis of the TEI information.
- In the past two years, LED has set up a risk indicator system and completed its upgrade from Version 1.0 to 3.0. The key features of Version 3.0 include:
  - Use of accounting indicators to measure enterprise operation status;
  - Use of tax collection indicators to monitor enterprise tax compliance performance;
  - Use of industry indicators to identify enterprise tax risks.

* For more information about the policies in relation to TEI-covered group enterprises and improvement of tax services for large enterprises, please read KPMG *China Tax Weekly Update* (Issue 4, February 2016) , (Issue 42, November 2016) and (Issue 14, April 2017).

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