

# China Tax Alert

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## Upgraded tax incentives show China's determination in stabilizing employment - Are you prepared to enjoy the benefits?

### Summary :

- On 2 August 2023, China's Ministry of Finance, State Taxation Administration, Ministry of Human Resources and Social Security, and Ministry of Agriculture and Rural Affairs jointly issued Notice No. 15 ("Circular 15"), which sets out the rules for incentives that aim to stabilize employment for qualified groups of people.

### Background

Over the past several decades of rapid socio-economic development, the Chinese government has recognized that certain groups of people are less privileged, and the government has introduced an array of incentive programs that aim to help them. Some of these incentives have taken the form of cash given to individuals, while others have been set up as tax credits/refunds for enterprises that hire members of the relevant groups of people. The categories of incentives that have been set out in Circular 15 were first introduced in 2019 (in Caishui [2019] No. 22), with a view to stabilizing employment for people from poverty-stricken geographical areas as well as people who have suffered prolonged periods of unemployment.

Amid the current challenging economic environment, Chinese authorities have upgraded and renewed the above-mentioned incentives with the goal of stabilizing and stimulating the employment market. We should point out that the incentives are based on the concerted efforts of multiple Chinese government departments. We have set out the key features of Circular 15's incentives below:

- Each "qualified" employee can generate a maximum of RMB 23,400 (approximately USD 3,300) worth of tax benefits. These tax benefits will be received in the form of successive refunds/reductions in Value-added Tax (VAT), Urban Maintenance and Construction Tax (UMCT), Educational Levy (EL), Local Educational Levy (LEL) and Corporate Income Tax (CIT)
- "Qualified" employees refer to employees with employment contracts of more than one year for whom social security premiums are paid. "Qualified" individuals are employees who are 1) persons in need of poverty-relief as identified by the National Anti-Poverty Retracement Monitoring System 全国防止返贫监测信息系统 and the Rural Revitalization Information System 乡村振兴信息系统; or 2) persons who have been registered as unemployed for over six months with the Human Resources and Social Security Department / Public Employment Agency
- The tax benefits could be applied retrospectively. Each "qualified" employee may produce tax benefits for up to a maximum of three years. "Qualified" employees who have already been "utilized" previously (e.g., N months) can continue to generate tax benefits under Circular 15 for up to three years (e.g., 36 - N months)
- A database that collates the information for "qualified" personnel has been set up. The Ministry of Human Resources and Social Security, Ministry of Agriculture and Rural Affairs / Rural Revitalization Bureau, and State Taxation Administration will facilitate the smooth sharing of this information; and specifically, information will be shared from the central to local level

- Circular 15 is effective from 1 January 2023, and taxpayers can enjoy the tax benefits until 31 December 2027. Over this five-year period, each existing and new employee may generate tax benefits for up to three years of their employment period.

## KPMG observations

As mentioned above, the employment stabilization tax benefits set out in Circular 15 represent an “upgrade” from the prior incentive policy. The rationale behind setting up the policy is likely to incentivize employers to hire certain target groups of people who are in needs. Perhaps more importantly, these “targets” can gain skills over a significant period of employment (i.e., three years), which should help them become more self-sustainable in the future.

In KPMG China’s experience in helping enterprises secure the previous generation of employment stabilization incentives, we learned the following:

- Only a handful of enterprises have set specific hiring criteria to encourage the hiring of “qualifying” personnel; in other words, many companies’ workforces have been built without considering these tax incentives as a factor in hiring
- Generic historical data (from a manufacturing enterprise) showed a hit rate of 8% to 14% among the entire employee population. In a recent case, RMB 100 million worth of tax credits/refunds were identified for a consumer electronics group’s OEM factory with 4,300+ qualifying employees (out of a total of 40,000+ employees, mainly blue-collar workers)
- The above “hit rate” would vary depending on the sector, geographic region, wage level, etc. For instance, an IT business would likely have a low hit rate, while an OEM factory for consumer electronics in Suzhou (i.e., an affluent city in central China) could possibly have a high hit rate
- Many tax bureaus do not have experience in handling this specific type of tax credit/refund, even though this tax incentive was first introduced in 2019 (in Caishui [2019] No. 22). For this reason, efforts should be made to educate enterprises/taxpayers, as well as tax officials
- Typically, enterprises need to follow a three-step process before they can obtain the incentives:

Step 1: Screen & Quantify	Enterprises need to screen their employees to identify qualifying individuals. Then, enterprises need to reconcile the employees’ employment history and social security payments to quantify the dollar amount of incentives available
Step 2: Prepare & Apply	<p>As the incentive application must be submitted through the employers’ tax returns, enterprises need to amend their relevant VAT and/or CIT return. The adjusted tax returns, together with the list of qualifying employees, should be submitted to the employers’ corresponding in-charge tax bureaus to formally launch the incentive application process</p> <p>For enterprises with a nationwide footprint, an implementation plan will need to be designed in order to prioritize efforts and generate “returns” in an efficient manner</p>
Step 3: Track & Obtain	The application usually needs to be escalated to upper-level tax authorities (e.g., at the provincial level) so that the list of qualifying employees can be verified against the database hosted by the Ministry of Human Resources and Social Security / Ministry of Agriculture and Rural Affairs. Therefore, enterprises need to follow up with different levels of tax authorities to ensure the application is processed in a timely manner. For applications that trigger tax refund payments, enterprises may also need to follow up with their local finance bureaus in order to actually obtain the payment

- Assuming the process runs smoothly, it will typically take two to four months, and some applications will involve multiple government authorities. Certain resources (i.e., a project team that organizes internal and external resources) will need to be deployed in order to secure the incentives

## Conclusion

Observers have noted that Circular 15 was introduced at an opportune time as the employment market has been severely impacted by the post-COVID-19 economic environment. Many companies have been proactively looking for incentives to subsidize their business, and we recommend that suitable resources be deployed and implementation actions be planned in order to obtain benefits in relation to qualifying employees. In addition to the financial rewards, Circular 15's incentives also offer ESG benefits in that under-privileged persons will be "looked after" by enterprises, and these individuals can learn self-sustaining skills during their period of employment.

KPMG has been using the above-mentioned three-step approach to assist enterprises in securing the employment stabilization incentives. Based on the experience the firm has gained in the application process, we believe that we are well-positioned to help enterprises benefit from the upgraded Circular 15 incentives. We are more than happy to help companies start their journey from now to the end of 2027. KPMG will also continue to closely follow up on the latest local practices and developments related to the incentives, and we will provide timely updates to enterprises so that they can stay up-to-date on any changes that might affect how and to what extent they can secure tax refunds or deductions under Circular 15.

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