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Go West - New Round of Fiscal Incentives for China's Western Region

On July 27, 2011, the Ministry of Finance, General Administration of Customs ("GAC") and State Administration of Taxation ("SAT") jointly issued circular Caishui [2011] No. 58 ("Circular 58") providing fiscal incentives to further support China's go-west strategy.

These incentives have a retroactive date of January 1, 2011.

Background

- Since the previous fiscal incentives for China's Western Region¹ expired at the end of 2010, the market has been waiting eagerly for the Chinese government to launch a new round of incentives for the Western Region.

¹ "Western Region" covers one municipality, Chongqing, six provinces (Gansu, Guizhou, Qinghai, Shanxi, Sichuan and Yunnan) and five autonomous regions (Guangxi, Inner Mongolia, Ningxia, Tibet and Xinjiang). The other three autonomous prefectures include certain prefectures in Hunan, Hubei and Jilin provinces.

- In general Circular 58 extends the following corporate income tax ("CIT") and customs duty incentives for the Western Region:
 - CIT - qualified enterprises in encouraged industries are eligible for a reduced CIT rate of 15% (the standard rate is 25%);
 - Customs Duty - equipment imported within the total investment of qualified projects for self-use are exempt from customs duty.
- The following table further summarizes the new round of fiscal incentives under Circular 58:

		New Round of Fiscal Incentives (Circular 58)
Reduced CIT Rate	Rate	Reduced to 15%
	Qualified Enterprises	Qualified enterprises include entities that satisfy the following conditions: <ul style="list-style-type: none"> • The major business of the enterprise falls within the encouraged industries that will be identified in the upcoming Catalogue of Encouraged Industries in Western Region; and • Over 70% of the enterprise's revenue is derived from such business.
Customs Duty/Import Value Added Tax ("VAT")	Incentives	Customs duty is exempt, but not import VAT.
	Qualified Projects	<ul style="list-style-type: none"> • Both domestic and foreign-invested projects in the encouraged industries; • Foreign-invested projects in the competitive industries²
CIT Holidays		Not applicable, but qualified enterprises established prior to December 31, 2010 are eligible to continue enjoying the unused tax holidays until they expire.
Effective Period		10 years (from January 1, 2011 to December 31, 2020)

² Catalogue of Competitive Industries for Foreign Investment in Central and Western Regions (2008)

Our Observations

- **Import VAT exemption is removed** - With the VAT transformation rolled out nationwide on January 1, 2009, all input VAT (including import VAT) for equipment are now creditable by VAT taxpayers. As a result, all previous incentives on import VAT exemptions have been revoked nationwide since 2009 as the import VAT will no longer be a cost to such VAT taxpayers.
- **Circular 58 is silent on the implementation details** - The SAT and GAC likely will be working on the implementation guidelines for tax and customs duty respectively.
- **The upcoming Catalogue of Encouraged Industries in Western Region** - The upcoming Catalogue referred to in Circular 58 currently is being assembled by relevant departments of the Central government, e.g. the National Development and Reform Commission, Ministry of Commerce, etc.

Conclusion

The development of the Western Region continues to be a priority in China's regional economic development strategy for the next five years. Circular 58 earmarks another milestone in China's sustaining support to the Western Region from fiscal perspectives. The extended tax and customs duty incentives demonstrate the Central government's determination to further promote the Western Region development and narrow the gap between the eastern and western areas.

With the official announcement of this new round of fiscal incentives, enterprises eligible for the previous round of incentives are encouraged to initiate discussions with the relevant in-charge tax authorities to secure the benefits under the new round of incentives.

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