

Enterprise income tax (“EIT”) preferential treatment for Small low-profit enterprises and super deduction of R&D expenses



CHINA

On March 26, 2023, the Ministry of Finance (MOF) and the State Administration of Taxation (SAT) made two joint announcements concerning “preferential EIT policies for Small low-profit enterprise”, i.e. SAT Bulletin [2023] No. 6 (“Bulletin No.6”), and “super deduction of R&D expenses”, i.e. SAT Bulletin [2023] No. 7 (“Bulletin No.7”). These two bulletins both change the current policies and below please find the introduction of these two bulletins.

1. CHANGES ON PREFERENTIAL EIT POLICIES FOR SMALL LOW-PROFIT ENTERPRISE:

Small low-profit enterprises are those that meet all of the following criteria:

- i. engaged in business activities not restricted or prohibited by the PRC government,
- ii. annual taxable income is no more than RMB 3 million,
- iii. employees are no more than 300, and
- iv. total assets amount is no more than RMB 50 million.

1) EIT preferential treatment before the issuance of Bulletin No. 6

Based on EIT law, the EIT rate for Small low-profit enterprises is 20% instead of 25% (a normal EIT rate), however, the additional following tax incentives are applied to promote the business of Small low-profit enterprise:

Annual taxable income	Effective EIT rate Jan 1, 2022 – Dec 31, 2022	Effective EIT rate Jan 1, 2023 – Dec 31, 2024
The portion of amount no more than RMB 1 million	2.5% (i.e. EIT = 20% * 12.5% annual taxable income)	N/A until the issuance of Bulletin No. 6
The portion of amount between RMB 1 million and 3 million	5 % (i.e. EIT= 20 % * 25% annual taxable income)	

2) Change indicated in Bulletin No. 6

From January 1, 2023, the tax incentives for Small low-profit enterprises are as follows:

Annual taxable income	Effective EIT rate Jan 1, 2023 – Dec 31, 2023	Effective EIT rate Jan 1, 2024 – Dec 31, 2024
The portion of amount less than RMB 3 million	5 % (i.e. EIT= 20 % * 25% annual taxable income)	

In addition, the effective period of Bulletin No. 6 is from Jan 1, 2023 to Dec 31, 2024, as such, whether such EIT preferential treatment can be applied after Dec 31, 2024 is uncertain.

2. SUPER DEDUCTION OF R&D EXPENSES BEFORE EIT

The super deduction of R&D expenses refers to deducting R&D expenses before EIT not according to their actual cost, but using a multiple of the actual cost. In this way, the company’s EIT annual taxable income is reduced, and it pays less EIT.

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The scope of R&D expenses allowed for super deduction includes the followings:

- i. Staff and labour expenses
- ii. Direct costs
- iii. Depreciation of assets
- iv. Amortization of intangible assets
- v. Design fees for new products, fees for formulation of new processes, clinical trial fees for new drugs, and onsite testing fees for exploration and development technologies
- vi. Other relevant expenses, of which the total amount of these expenses shall not exceed 10% of the total amount of R&D expenses allowed for super deduction

1) Super deduction of R&D expenses before EIT before the issuance of Bulletin N° 7

Before the publication of Bulletin No. 7, the policy of super deduction is implemented based on the following table:

Industries	Deduction of R&D expenses
Manufacturing industry	200% of the actual amount of R&D expenses
Tobacco manufacturing, accommodation and catering industries, wholesale and retail industries, real estate, leasing and commercial services, and entertainment industries	100% of the actual amount of R&D expenses, i.e. no super deduction
Other industries excluding the above two types	175% of the actual amount of R&D expenses

2) Change indicated in Bulletin No. 7

Following the publication of Bulletin No. 7, effective from January 1, 2023, the scope of application of the 200% super deduction is no longer limited to the manufacturing industries, but is open to all industries with the exception of those still subject to restriction according to the table below:

Industries	Deduction of R&D expenses
Tobacco manufacturing, accommodation and catering industries, wholesale and retail industries, real estate, leasing and commercial services, and entertainment industries	100% of the actual amount of R&D expenses, i.e. no super deduction
Other industries excluding the above type	200% of the actual amount of R&D expenses



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