CHINA HIGH- AND NEW-TECHNOLOGY ENTERPRISES

QUALIFICATION

To qualify as a high- and new-technology enterprise, an enterprise must meet all of the following requirements.

1. The enterprise must be a resident enterprise that has been registered in China (excluding Hong Kong, Macau, and Taiwan) for at least one year.

2. The enterprise must own the proprietary intellectual property right of core technology in connection with the main products (services) of the enterprise. The enterprise may obtain the IP right within last three years through self-R&D activities, purchase, donation, merger, etc. The enterprise may also satisfy this requirement by acquiring an exclusive right to use the IP right for a period of at least five years. It is not clear under the Measures whether the right can be exclusive to China or must encompass a broader area.
3. The products or services of the enterprise must be within the scope of the Catalogue. The Catalogue lists more than 200 categories of technologies, products, and services in eight large technological areas. Those areas are:

- Electronic information technology
- Biological and medical technology
- Aviation and space technology
- New materials technology
- High-tech services
- New energy and energy conservation technology
- Resources and environmental technology
- Transformation of traditional sectors through new high-tech

4. At least 30 percent of the enterprise’s employees should be college graduates (three-year program or above); among the qualified staff, at least 10 percent of the total number of employees should be engaged in R&D activities.

5. R&D expenditures for the last three accounting years should reach a certain percentage of the enterprise’s total revenue

<table>
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<tr>
<th>Total revenue in preceding year</th>
<th>R&amp;D expenses at least as % of revenue</th>
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<tbody>
<tr>
<td>Below RMB 50 million</td>
<td>6%</td>
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<tr>
<td>RMB 50 million - 200 million</td>
<td>4%</td>
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<tr>
<td>Above RMB 200 million</td>
<td>3%</td>
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At least 60 percent of the minimum R&D expenditure must be incurred in China.

6. Current-year income from high- and new-technology products (services) is at least 60 percent of the total revenue of the enterprise.

7. The enterprise should meet the requirements respecting the rating of R&D management, the capacity to convert R&D outcomes, the number of IP rights, and the growth of sales and total assets as provided in Administrative Working Guidelines of Assessment of High- and New-Technology Enterprises. Such working guidelines will be issued separately.

**CERTIFICATION PROCEDURES**

An applicant should conduct a self-assessment in accordance with the above criteria on an official web site. If the enterprise believes that it satisfies the certification requirements, it may then submit a written application together with all of the required documents to the local assessment administrative authority. The local assessment authority is generally formed at the provincial level. The Science and Technology Bureau, Finance Bureau, and State Tax Bureau in charge of each area will jointly form the assessment authority for its jurisdiction. At the central government level, MST, MOF, and SAT will jointly form a leadership group that will supervise the assessment work.

A technical expert pool will be set up by the local assessment authority from which the local assessment authority will select expert(s) to review the application. The leadership group at the central government will be in charge of administration of expert qualifications and registrations. Upon the approval of the local assessment authority, the enterprise will be listed on the official web site for 15 days for public comments. If no objections are raised, the local assessment authority will file the approval with the leadership group, issue a high- and new-technology enterprise certificate to the enterprise, and release the certification result on the official web site. The certificate will be valid for a period of three years from the issuance date.
APPLICATION FOR TAX INCENTIVES

Once an enterprise is certified as a high- and new-technology enterprise, it may apply the tax incentives under the CIT Law and regulations, including the reduced 15 percent CIT rate. However, the certification does not guarantee three years of tax benefits. The enterprise needs to continue to meet the qualification requirements each year during the period of validity of the certificate.

EXISTING HIGH- AND NEW-TECHNOLOGY ENTERPRISES

High- and new-technology enterprise certificates were issued to many enterprises under the old regulations. The Measures have replaced the old rules. As the new rules provide for more strict criteria, the enterprises that received such certificates under the old regime may not necessarily qualify as a high- and new-technology enterprise under the Measures. As such, those high- and new-technology enterprises certified under the old regulations will need to go through the new certification procedures to predetermine whether or not they still qualify as high- and new-technology enterprises.

IMPACT ON MULTINATIONAL CORPORATIONS

Under the Measures, a Chinese subsidiary of a multinational corporation can qualify as a high- and new-technology enterprise without owning the IP right to the core technology. Rather, the subsidiary may satisfy the IP requirement by obtaining a five-year exclusive licensing. Although “exclusive” is not defined in the Measures, one school of thought posits that an exclusive right within China should be sufficient. Hopefully, this ambiguity will be clarified when the Administrative Working Guidelines of Assessment of High- and New-Technology Enterprises is issued. Alternatively, the Chinese subsidiary may obtain a territory IP right through a cost-sharing arrangement. Again, the qualification and permissibility of such an arrangement needs to be answered in future regulations and tested in practice.

The tax policy clearly encourages R&D activities in China. In order to enjoy the tax benefits, enterprises must continue to meet the requirements as provided in the Measures, including R&D expenditures in China. As such, acquisition of an IP right without continuing R&D activities would not qualify an enterprise as a high- and new-technology enterprise.

Due to the specific requirements such as high-tech revenue percentage and college graduate percentage, multinational corporations may need to restructure their China operations in order to take advantage of the tax benefits granted to high- and new-technology enterprises. These companies should also consider other tax issues in connection with such a restructuring, including transfer pricing and potential business tax on revenue received by a technology company (if the R&D company is separated from the production company).

LAWYER CONTACT

For further information, please contact your principal Firm representative or the lawyer listed below. General e-mail messages may be sent using our “Contact Us” form, which can be found at www.jonesday.com.

Full Cao
86.10.5866.1223
fcao@jonesday.com