

September, 2011

**Provisions on the implementation of the security review system for mergers and acquisitions of domestic enterprises by foreign investors** ("MOFCOM Provisions") (商务部实施外国投资者并购境内企业安全审查制度的规定), issued by the Ministry of Commerce (MOFCOM)

Further to the *Circular on the launching of the security review system for mergers and acquisitions of domestic enterprises by foreign investors* ("State Council Circular") (see our newsletter of February 2011), issued by the General Office of the State Council on February 3, 2011, and the *Interim provisions on issues related to the implementation of the security review system for mergers and acquisitions of domestic enterprises by foreign investors* ("MOFCOM Interim Provisions") (see our newsletter of March 2011), issued by MOFCOM on March 4, 2011, MOFCOM issued these Provisions based on its Interim Provisions, after more than five months of implementing the State Council Circular and the MOFCOM Interim Provisions. They will replace the Interim Provisions starting September 1, 2011.

According to the MOFCOM Provisions, the scope of the mergers and acquisitions security review is set out in the State Council Circular. The detailed documentation requirements for filing an application for a security review are the same as those in the MOFCOM Interim Provisions.

The main development of the MOFCOM Provisions is a new provision under which the authorities must decide whether M&A transactions carried out by foreign investors fall under the scope of a national security review based on the substantial content and actual impact of the concerned transactions. Foreign investors are not allowed to evade the national security review, which includes nominative shares, trusts, multi-level re-investments, leasing, loans, contractual arrangements, overseas transactions, etc.

With the establishment of the national security review system, M&A transactions carried out by foreign investors must pass three thresholds: industry access approval (based on the Industry Catalogue for Guiding Foreign Investment), anti-monopoly investigation and a national security review.

However, further clarification of the definition of national security, a more detailed scope of review and a more detailed list of industries falling under the scope of review are expected.

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**Notice on issues concerning Renminbi cross-border direct investment (draft for comments)** (商务部关于跨境人民币直接投资有关问题的通知), issued by the Ministry of Commerce (MOFCOM)

Further to the *Proposed Policies on Foreign Direct Investment (FDI) in Renminbi* (see our newsletter of April 2011) and the *Circular on clarifying issues relating to cross-border Renminbi transactions* (see our newsletter of June 2011), following the trend of facilitating FDI in Renminbi under the precondition of risk control, this proposed notice establishes the following:

Renminbi proceeds that are lawfully obtained by foreign investors from overseas may be invested back into China if these cross-border Renminbi FDI and re-investment by a Foreign Invested Enterprise (FIE) invested by such foreign investors comply with the PRC FIE laws and regulations, Industry Catalogue for guiding foreign investment, anti-monopoly laws and M&A national security review rules.

Lawfully obtained Renminbi proceeds from overseas are:

- 1) Renminbi that foreign investors obtain from overseas, including Renminbi proceeds obtained from cross-border trade settlements and overseas issues of Renminbi bonds and shares; and
- 2) Renminbi profits gained and Renminbi proceeds obtained from share transfers, capital decreases, liquidations and early recoveries of investments from FIEs invested by foreign investors in China and transferred overseas.

The notice clearly bans cross-border Renminbi FDI from investing directly or indirectly in securities and financial derivatives in China, providing entrustment loans or paying domestic or overseas loans.

It also clarifies the approval authorities for Renminbi cross-border FDIs (the central MOFCOM and its local subsidiaries), documentation requirements and approval procedures.

Date of issue: August 22, 2011. Deadline for submitting comments: September 20, 2011.

**Administrative measures for registering debt-for-equity swaps (draft for comments)** (公司债权转股权登记管理办法), issued by the State Administration for Industry and Commerce (SAIC)

These draft measures mainly establish the scope, procedure and documentation requirements for registering debt-for-equity swaps.

While local governments have already issued various local rules on debt-for-equity swap registration before the issuance of these draft measures, the draft measures unify those local rules at the national level and, more importantly, broaden the scope of debt-for-equity swap registration by including foreign creditors and foreign invested enterprises (FIEs) as debtors in the debt-for equity swap scheme. When a creditor asks

to register equity in FIEs converted from indebtedness owed by such FIEs, or when a foreign creditor swaps loans that are already registered with the State Administration of Foreign Exchange (SAFE) as foreign debts for equity, such swaps must be approved by relevant authorities under the FIE laws, regulations and rules before their registration.

As debt-for-equity swap is a form of non-cash capital contribution, the total amount of the value of such capital contribution together with other forms of non-cash capital contribution must not exceed 70% of the total amount of the company's registered capital.

Date of issue: August 18, 2011. Deadline for submitting comments: September 2, 2011.

**Announcement of the State Administration of Taxation on relevant issues concerning value-added tax ("VAT") payment obligations** (Announcement of the State Administration of Taxation [2011] No.40)(国家税务总局关于增值税纳税义务发生时间有关问题的公告), issued by the State Administration of Taxation ("SAT")

When a taxpayer sells goods directly for money and has delivered the goods to the buyer without having received payment, the VAT obligation arises when the taxpayer receives the payment or issues the invoice, whichever is earlier.

Date of issue: July 15, 2011. Effective date: August 1, 2011.

**Circular on issues concerning tax policies for in-depth implementation of western development strategy** (Caishui [2011] No.58)(关于深入实施西部大开发战略有关税收政策问题的通知), issued by the State Administration of Taxation ("SAT"), Ministry of Finance ("MOF") and General Administration of Customs ("GAC")

The Circular introduced preferential tax treatment for companies located in the western region of China.

Equipment imported for self use within the aggregate total project investment of domestic encouraged industries, foreign-invested encouraged industries and advantageous industries in the western region will be exempt from tariffs.

From January 1, 2011, to December 31, 2020, enterprise income tax may be levied at a reduced tax rate of 15% for enterprises in encouraged industries that are established in the western region.

These are enterprises whose principal business focuses on the industrial projects listed in the Catalogue of Encouraged Industries in the Western Region, the income of which accounts for more than 70% of the total income of such enterprises. The Catalogue of Encouraged Industries in the Western Region will be issued separately.

Enterprises in transportation, electricity, water, postal services and broadcasting and television established in the western region before December 31, 2011, which benefit from a "tax exemption for two years and a 50% tax reduction for three years" on enterprise income tax under Paragraph 3, Article 2 of the Circular of the Ministry of Finance, the State Administration of Taxation and the General Administration of Customs on Issues Concerning Preferential Tax Policies for the Western Development (Cai Shui [2001] No. 202), may continue to benefit from this preference until it expires.

The western region includes Chongqing municipality, Sichuan province, Guizhou province, Yunnan province, Tibet autonomous region, Shanxi province, Gansu province, Ningxia Hui autonomous region, Qinghai province, Xinjiang Uyghur autonomous region, Xinjiang Production and Construction Corps, Inner Mongolia autonomous region, and Guangxi Zhuang autonomous region. Xiangxi Tujia and Miao autonomous prefecture in Hunan province, Enshi Tujia and Miao autonomous prefecture in Hubei province and Yanbian Korean autonomous prefecture in Jilin province will follow the tax policy for the western region.

Date of issue: July 27, 2011. Effective date: January 1, 2011.

**Announcement of the State Administration of Taxation on issues related to implementing the revised Individual Income Act** (SAT Public Notice [2011] No.46)( 国家税务总局关于贯彻执行修改后的个人所得税法有关问题的公告), issued by the State Administration of Taxation ("SAT")

This Announcement clarifies the calculation of individual income tax ("IIT") from September 2011, after the implementation of the new IIT Act.

For wages and salary income earned by taxpayers from September 1, 2011, individual income tax must be calculated and paid according to the standards for deducting expenses and the tax rates under the new IIT Act.

Revised tax rates:

Bracket	Monthly taxable income		Tax rate (%)	Quick calculation deduction
	Including taxation band	Excluding taxation band		
1	Less than 1,500 yuan	Less than 1,455 yuan	3	0
2	Between 1,500 yuan and 4,500 yuan	Between 1,455 yuan and 4,155 yuan	10	105
3	Between 4,500 yuan and 9,000 yuan	Between 4,155 yuan and 7,755 yuan	20	555
4	Between 9,000 yuan and 35,000 yuan	Between 7,755 yuan and 27,255 yuan	25	1005
5	Between 35,000 yuan and 55,000 yuan	Between 27,255 yuan and 41,255 yuan	30	2755
6	Between 55,000 yuan and 80,000 yuan	Between 41,255 yuan and 57,505 yuan	35	5505
7	More than 80,000 yuan	More than 57,505 yuan	45	13505

Notes:

1. The amounts in the sections "including taxation band" and "excluding taxation band" refer to the income from which relevant expenses have been deducted under tax laws.

2. The section "including taxation band" applies to wages and salary income on which taxpayers should pay tax; the section "excluding taxation band" applies to wages and salary income on which others (employers) should pay tax on behalf of taxpayers.

For wages and salary income earned by taxpayers before September 1, 2011, individual income tax must be calculated and paid according to the standards for deducting expenses and the tax rates in place before the IIT Act was reviewed, regardless of whether the tax will be turned over to the state treasury on September 1, 2011.

Income earned by investors (partners) of individual industrial and commercial households, sole proprietorships and partnerships from production and business operations will be subject to the new standards for deducting expenses and the tax rates after the revision of the IIT Act.

Under the provisions of tax laws, regulations and documents, the annual taxable income must be calculated before the annual tax payable. The following method is used to calculate the annual tax payable for 2011:

Tax payable for the first 8 months = (annual taxable income \* corresponding tax rate before the revision of the Tax Act - quick calculation deduction) \* 8/12.

Tax payable for the second 4 months = (annual taxable income \* corresponding tax rate after the revision of the Tax Act - quick calculation deduction) \* 4/12.

Annual tax payable = tax payable for the first 8 months + tax payable for the second 4 months.

Within three months of the close of the year, taxpayers must calculate and pay the annual tax payable for 2011 according to this method.

Date of issue: July 29, 2011. Effective date: September 1, 2011.

**Announcement of the State Administration of Taxation on printing and distributing the Administrative Measures for income tax on Chinese-controlled resident enterprises incorporated overseas (trial implementation)** (SAT Public Notice [2011] No.45) (国家税务总局关于印发《境外注册中资控股居民企业所得税管理办法(试行)》的公告), issued by the State Administration of Taxation ("SAT")

This Announcement regulates overseas companies controlled mainly by PRC companies while being regarded PRC tax-resident enterprises ("TRE") because their place of effective management is in China ("Chinese-controlled TRE incorporated overseas"). These Chinese-controlled TRE incorporated overseas could apply for PRC TRE status with the responsible tax authority, which may also decide to carry out onsite inspections if it thinks the Chinese-controlled TRE incorporated overseas should apply for this status.

Chinese-controlled TRE incorporated overseas should register for tax with the responsible tax authority within 30 days of receiving the TRE verification letter from this tax authority.

Chinese-controlled TRE incorporated overseas must declare and pay income tax on a quarterly basis under the prepayment method, and settle this on a yearly basis. When a TRE verification letter exists, payers do not have a withholding obligation when paying dividends, bonuses or other equity investment income, as well as interest, rent, royalties, property transfer income and other income, to Chinese-controlled TRE incorporated overseas.

Chinese-controlled TRE incorporated overseas must report to the responsible tax authority and provide the equity transfer agreement and relevant materials if its share is transferred by a Non-TRE within 30 days of entering into the equity transfer agreement.

Chinese-controlled TRE incorporated overseas that are tax residents of China are subject to the tax treaty between China and the country (region) in which they are incorporated, and must follow the procedures for preferential treatment under the corresponding tax treaty. If it is necessary to prove they are tax residents in China, they may apply to the responsible tax authority for the corresponding certificate, and this tax authority must deal with this request within 10 working days of the date on which it accepts the application.

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