



Jesa Consulting Ltd.

NEWSLETTER

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What is Jesa?

Jesa is a service company headquartered in Shanghai specializing in facilitating start-up of new industrial productions while providing reliable management and control solutions. We operate 4 main branches in China and a foreign office in Ulaan Baatar (Mongolia). Since 1998, Jesa has built a team of 70 specialized employees in addition to 25 engineers following "in loco" projects. Commercial relationships are exclusive and strictly confidential, ensuring the highest expertise on each single commercial and technical issue. Jesa is a leader in managing manufacturing processes and eliminating any industrial and regulatory problems while helping our clients save financial resources. Jesa is currently expanding its services to provide support to those companies seeking to develop environmental projects in china, such as alternative energies and environmental management.

New Tax Preference Policy for Hiring Disabled Workers

Starting July 1st of this year China has implemented a new tax preference policy for both foreign and local companies aimed at hiring disabled people all across the country. Since July 1st this year, China will implement new tax preference policy for hiring the disabled people across the country.

The chief of the National Tax Bureau highlighted that the company which decides to employ disabled persons will enjoy preferential tax polices towards turnover taxes and business taxes.

In terms of turnover tax, depending on the number of disabled persons that a company employs, the tax bureau will give back value added tax to a certain extent or decrease the overall turnover tax. The limits of value added tax returned and turnover tax released for every person is set as 6 times the local minimum wage; however, the maximum returned can not exceed 35 thousand RMB (\approx 3.5 thousand Euro) per year for every person.

For business income tax, the business income tax of the company which employs the disabled person will be deducted for twice as much as the true salary of the disabled worker. Meanwhile, the enterprise income tax will be exonerated for VAT, refunded legally, or the revenue of the business tax will be decreased.

In this preferential policy, a disabled person is defined as a person with eyesight impairment, auditory impairment, language impairment, intellectual impairment, or mental impairment; all of which are marked in PRC disabled certificates and/or people who hold PRC disabled soldier certificates (levels 1-8). Compared to past polices, this new policy adds intellectual impairment and mental impairment to enlarge the scope of protection for disabled people.

To enjoy the tax preference, the enterprises which employ the disabled should satisfy the following five conditions:

1. Sign labour contract or service agreement for more than one year with every handicapped, and each one should work in the position assigned;
2. The proportion disabled workers accounts for more than 25% of the total staff and the quantity of the disabled workers actually employed must be more than 10 individuals. Enterprises for which the proportion of disabled is more than 1.5% but less than 25% and the disabled actually employed is more than 5 individuals, are entitled to enjoy

the policy but can't enjoy the added value tax or turnover tax preference policy;

3. They must pay social insurance, including: basic endowment insurance, basic hospitalization insurance, unemployment insurance, and injury insurance (according to the county government regulation) for every handicapped;
4. They must pay wages which are not less than local lowest wage standard for every handicapped through proper banking means;
5. Follow basic establishment regulations to employ disabled persons.

Compared to the old tax preference policy, the new policy has the following characteristics:

1. It has enlarged the scope of enterprises which can enjoy the preference (different kinds of ownership enterprisers) and the scope of disabled people (by including intellectual and mental impairments);
2. It has established further protection for the rights and interests of the disabled. In order to enjoy the tax preference, enterprises have to sign a labour contract, pay every kind of social insurance according to the local government regulation, pay salary which is no less than local salary level through a financial institution, and have basic physical means in their facilities to employ disabled employees;
3. It has continued to maintain this favourable policy. Employing 1.5% of disabled employees is the duty and responsibility of every enterprise and it is necessary to implement this tax preference in order to encourage enterprises to employ the adequate amount of disabled workers. The policy creates a win-win situation for the enterprise since the disabled workers create

value for the company while at the same time enabling it to reactive financial allowance.

To avoid that enterprises and individuals cheat this tax preference system, the policy prescribes the following punishment:

If enterprises and individuals sign false labour contracts or service agreements, forge or reuse disabled certificates or disabled soldier certificates, make a false report of the proportion of disabled employees, employ the disabled without paying them (or paying them less than minimal wage), take back salary of disabled employees to cheat tax preferences - the enterprises and individuals will be forced to pay the tax immediately and they will not be allowed to enjoy this tax preference for a period of three years.

This new tax preference policy contributes to creating equitable competition within the tax environment and encourages more enterprises to employ disabled persons. At the same time, proper regulations have been put in place such that enterprise will not take advantage of the policy for their own means. For foreign companies, the new policy also gives them the same chance to enjoy tax preferences and gives them the opportunity to demonstrate positive corporate social responsibility practices. All foreign enterprises may enjoy these business income tax preferences starting January 1st, 2008.

Reduction of Export VAT Refunds

One of the most highlighted issues with regards to the Chinese market has been its consistent increase of its foreign trade surplus. In yet another move to counteract this rising figure, the PRC announced on June 19th of this year that it will impose major downward adjustments to export VAT refund rates; consequently lowering profits of exporters in many industries. This is because the reductions and complete elimination (in some cases) of the export VAT refunds will apply to a broad range of products; including socially/environmentally harmful products, low value-added industries, and even strong export products.

This article is based on official documents released by Deloitte Group Asia and it outlines the major changes which we will see and the actions exports can take who have been negatively affected.

- 1) The VAT export tax refund has been fully repealed for 533 "high energy consuming, high polluting, and scarce resource-consuming" products. This means that there will be no refund of VAT paid on inputs. For these commodities, it is expected as well that output VAT will be required despite they're being exports. Such products previously had export refund rates between 5% and 13%.
- 2) The VAT export refund rate has been reduced for 2,268 commodities likely to trigger trade disputes. These products will have their VAT export refund rates reduced by percentages ranging from 2% to 8%.
- 3) The VAT export tax refund has been fully repealed for 10 items, but their export sale will still be VAT exempt (these products include peanut kernels and oil paintings).

- 4) All changes have been effective since July 1st 2007.

Refer to the table below for a brief summary of the changes:

Changes in Export Rebate Rates – Categories of Goods Most Affected

Commodity	Rate before Adjustment	Rate Post-adjustment	Rate Change
Clothing	13%	11%	2%
Certain electronic machinery, machine tools, auto vehicles	17% / 13%	11% / 9%	2% / 8%
Toys	13%	11%	2%
Plastics, rubber and their products	13%	5%	8%
Leas and shoes	13%	11%	2%
Certain base metals and their products, such as copper, zinc, molybdenum	13%	5%	8%
Certain Chemical Products	13% / 11%	9% / 5%	2% / 8%
Vegetable oils	13% / 11%	5%	6% / 8%

It is important to note that there will not be any transitional rules which will apply except for one exception: for contracts covering the export of ships and equipment and building materials involved in long term construction projects.

The changes will significantly raise tax costs for many exporting enterprises. Some of the decreases are so large (up to 8%) that the profit and loss of some exporters could be quite deleterious to the sustainability of their business practices.

Deloitte outlines a number of things which exports negatively affected by these changes can do to minimize their impact. Thus apart from simply increasing prices to foreign costumers, the following can also be done:

- *Tariff coding:* the description and tariff codes of the exported goods should be reviewed to ensure that all commodities are correctly labelled;
- *Supply chain model:* the tax efficiency of the currently used export business model in the supply chain should be evaluated, e.g. the effect of contract manufacturing verses toll manufacturing;

- *Functions and risks:* the functions and risks undertaken by the China operation should be revisited to see if some functions could be performed and risks assumed outside China in order to lower FOB prices of related-party exports;
- *Transfer pricing:* some benchmarking exercise could be conducted on the functions and risks undertaken in China to ensure that the existing transfer pricing policy for related-party exports is proper;
- *Special purpose vehicles:* special purpose vehicles, e.g. the use of Chinese foreign-invested commercial enterprises could potentially reduce the impact of the refund reductions;
- *Designated zones:* designated special purpose zones, e.g. export processing zones could be considered to reduce the potential impact;
- *Increase of bonded imports:* increase of imports or conversion of domestic purchases into imports can also reduce the VAT cost increase (the use of bonded logistics parks can help facilitate this process);
- *Vertical integration/segregation:* changes in the operations undertaken in China potentially may change the exported products and, hence, the applicable tariff code for each product.

We can consider these solid changes as positive for the overall future stability of China's financial system and we urge all exporters hurt by these changes to seek professional advice on how to ameliorate their situation.

Highlights from Around China

NDRC issues warning over food-price lifts

China warned local governments to be alert to recent rising consumer price. The consumer price index grew 4.4 percent in June and 3.2 percent in the first half from a year earlier, driven by the surging cost of food. About 10 major Chinese instant noodle makers began to add up to 20 percent on the price.

Polluting industries lose their loan access

SEPA (State Environmental Protection Administration of China) has submitted to the financial institutions a blacklist of 30 companies that violated environmental rules. Companies that fail to pass environmental assessments or implement environmental protection regulations are disqualified from getting loans from any bank or financial institution.

China warns economy on brink of overheating

Industrial added-value rose 18.5% over the first half of the year, while new loans have added up to 2.54 trillion RMB (\approx 254 billion Euro) in just six months. M1 (cash and demand deposits) keeps increasing but with little effect on prices.

Steps to rein in steel exports expected to gain traction soon

Steel export may rise only 20 percent this year, due to new trade policies. A new batch of taxes will try to bound industry growth, to smooth trade frictions. US has indeed complained China was selling too cheaply last year.

China tightens bank credit to cool economy

For a sixth time this year, banks have been ordered to increase reserves, after the economy grew 11.9% last quarter. The pool of money available for lending has risen to 12% from 11.5%. The currency has showed no significant reaction.



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