

China Tax Alert

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Shanghai Municipal Government Released the Incentive Scheme for the Establishment of Regional Headquarters

Regulations discussed in this issue:

- The modified version of the *Incentive Scheme for the Establishment of Regional Headquarters by Multinational Companies in Shanghai (Hufufa [2017] No. 9)* was issued by the Shanghai Municipal Government on 27 January 2017, which took effect on 1 February 2017 and will expire on 31 January 2022.

Background

On 27 January 2017, the Shanghai Municipal Government promulgated the modified version of the Incentive Scheme for the Establishment of Regional Headquarters by Multinational Companies in Shanghai (hereinafter referred to as “the Incentive Scheme”, which took effect on 1 February). The modification aims to extend, optimise and integrate the 2011 version of the Incentive Scheme (*Hufufa [2011] No. 98, expired on 19 December 2016*) and its supplementary policies. The essence of the *State Council Announcement on Opening-up Expansion and Encouraging Foreign Investment (Guofa [2017] No. 5, hereinafter referred to as Announcement No.5)* is also followed and implemented by the municipal government in this modification.

By the end of 2016, a cumulative number of 580 regional headquarter institutions, including Regional Headquarters (“RHQs”) and Headquarter Establishment, had been set up in the city of Shanghai. The Joint Annual Report on Foreign Investment staged a rosy picture of the data, showing that with only 1.26% of foreign-invested enterprises (“FIEs”) being regional headquarter institutions, 17.37% of net profit and 10.59% of tax revenue were contributed by the regional headquarter institutions. Apparently, the headquarter economy has been playing a major role in the regional economic development and fiscal revenue growth of Shanghai.

This issue of China Tax Alert highlights and analyses the major adjustments and hot topics regarding the modification of the Incentive Scheme. Meanwhile, we also share our observations for your reference.

Modification Highlight

The modified Incentive Scheme basically follows the logical sequence and concepts adopted in the previous version, with adjustments to and simplification of certain requirements, and integrates a series of later incentives and policies developed at the state and regional level. The highlights of the modified Incentive Scheme are summarised as below:

1. [Expansion of incentive coverage](#)

A key modification of the Incentive Scheme is the integration of the concept of Headquarter Establishment, which was first introduced by the *Supplementary Regulations Governing the Incentive Scheme for Headquarter Institutions* (hereinafter referred to as “Supplementary Regulations”, jointly released by four government bodies at the Shanghai municipal level). The integration of the concept aims to officially expand the incentive coverage to the multinational companies and branches that in substance assume roles of regional decision-making, fund management, sales and procurement, but fall short of the accreditation criteria.

2. [Removal of requirement on company form](#)

The previous version of Incentive Scheme prescribed that a RHQ can only be established in the form of a China Holding Company (“CHC”) or a Management Company. This modification removes such requirement, giving multinational enterprises more autonomy in determining the form and function to be assumed by headquarters.

3. [Adjustments to accreditation requirements](#)

As mentioned above, the modified Incentive Scheme covers RHQ and Headquarter Establishment. Some adjustments have also been made to their respective accreditation criteria.

- **RHQ**

The minimum total assets required of the parent company of a RHQ in a service industry has been reduced from USD 400 million to USD 300 million. Meanwhile, a CHC can no longer be accredited as a RHQ automatically.

- **Headquarter Establishment**

Compared with the Supplementary Regulation released in 2014, the modification loosens some of the accreditation requirements:

- ✓ The minimum number of existing investments by the parent company of the Headquarter Establishment has been reduced from 3 to 2.
- ✓ Senior management personnel are no longer required to be based in Shanghai. Furthermore, the requirements on minimum area of operation premises and headcount of employees acting in managerial capacities are also removed from the Incentive Scheme.

An additional threshold of minimum registered capital (operation fund in the case of a branch) of USD 2 million for an entity to apply for the headquarter accreditation is introduced in the modified Incentive Scheme.

4. [An assortment of supplementary policies for fund management](#)

Benefiting from a package of recent policies, qualified RHQs and Headquarter Establishments are able to carry out various fund management activities, such as centralised intra-group foreign exchange management, an assortment of cross-border RMB transactions and opening free trade accounts for cross-border RMB and foreign exchange settlement.

In addition, optimisation of cross-border remittance under non-trade items and a fast track for related contract registration and tax assessment are also brought up in the modified Incentive Scheme.

5. No more limits on business scope

The previous version of Incentive Scheme provided a list of 7 allowable business operations (e.g., investment decision-making and financial management) for a RHQ, which has been removed by the modification.

6. Simplified documents and expediting of approval process

Capital verification report and a set of documents for the legal representative, including the appointment letter, resume and identification, have been removed from the revised application document request list. Also, the allowed timeline for the government authority to review an application and provide feedback has been reduced from 10 working days to 8 working days.

7. Introduction of discretionary incentive at the district level

Another salient point of this modification is that the district-level government for the first time is officially allowed to devise its own incentive plans to support the headquarter economy. The introduction of such discretionary incentives corresponds with the motif of Announcement No. 5, giving district governments more leeway in policy-making to attract business and boost the local economy.

KPMG Observations

With the regulatory adjustments in this modification, we have summarised below the areas worthy of your attention:

- In the modified version of the Incentive Scheme, fiscal subsidy still expressly remains exclusive to RHQ. Headquarter Establishments, not eligible for fiscal subsidy, are granted with other preferential treatments including but not limited to talent attraction and visa facilitation. Such differences in incentive plans between the two types of headquarter institution should be well noted by enterprises in determining the headquarter business plan.
- Based on our communication with policy makers, there has yet to exist any supplementary incentive plan on a district level. However, according to our experience with the previous policy practice, it is highly likely that the district level of incentive policies will be rolled out soon.
- The modified Incentive Scheme does not specify any regulatory facilitation or support for fund management that is exclusive to enterprises with RHQ or Headquarter Establishment accreditation. Instead, it incorporates a selection of existing policies in this realm as a supplement to the incentive package.
- That being said, the accreditation of headquarter institutions may be factored into some comprehensive evaluation mechanism. For instance, the headquarter accreditation may help lift the applicant's profile and fasten the assessment and approval in a cross-border RMB cash pool application.
- Similar to its previous version, the modified Incentive Scheme does not elaborate on fiscal incentive plans in detail. The *Implementation Opinion and Method (Hufubanfa [2012] No. 51)*, which serves as the official explanation and detailed implementation plan for the previous version of Incentive Scheme, will not expire until 30 June 2017. We learned that the modification of the *Implementation Opinion and Method* is underway and is expected to be released before the aforesaid expiration date. We suggest that enterprises can study the current version for reference, proactively communicate with the relevant governmental authority, as well as keep a close eye on the update of the fiscal incentive plans in this respect.

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