

Notice of the Implementation of Royalty Provisions in Tax Treaty

September 14th, 2009

Notice of the Implementation of Royalty Provisions in Tax Treaty "Notice"

In order to facilitate the avoidance of double taxation relating to the implementation of tax provisions, the State Administration of Taxation recently issued the "Notice of the implementation of royalty provisions in tax treaty "(the notice), which will come into effect on October 1st, according to agreements of avoiding the double taxation between China and foreign countries.

The main points of the notice are as follows:

1. If the definition of royalty in the corresponding tax treaty explicitly includes the funds for use of industrial, commercial and scientific equipment, the profit of the royalties shall be regulated by the royalty provisions in such tax treaty. If the tax rate in the tax treaty is lower than the rate in the relating tax law of PRC, the former shall be applied.
2. In the service agreement, if the provider uses some know-how and technologies in the process of service but does not transfer or license them, this kind of service agreement does not belong to the scope of royalty.
3. If the staffs from technology licensor charge the service fee for providing the support and instruction in the process of transfer or license of know-how and technologies, the service fee will be regarded as the royalty and regulated by the royalty provisions in the tax treaty. However, if the service corresponds to a contribution to an existing entity, the profit from service shall apply the provisions of business profit in the tax treaty.
4. The following income or profit shall be considered as labor income rather than royalty:
 - 1) The income of the service after selling in the trade of goods;
 - 2) The income of the service provided by the seller to the buyer during the guarantee period;
 - 3) The income of the service from the professional organizations such as engineering, management and consulting companies;
 - 4) Other similar incomes regulated by the State Administration of Taxation.

The announcement of the notice specifies the definition and the implementation of the royalty provisions in the tax treaty, which will make the procedures relating to the taxation more transparent and efficient.