

Enterprise Income Tax Law of the People's Republic of China

Chapter I General Principles

Article 1

Within the territory of the People's Republic of China, enterprises and other organizations that have income (hereinafter collectively referred to as "enterprises") are taxpayers of enterprise income tax, and shall pay enterprise income tax pursuant to the provisions of this Law.

This Law does not apply to sole-proprietorship enterprises or partnership enterprises.

Article 2

Enterprises are categorized into resident enterprises and nonresident enterprises.

Enterprises established under the laws and regulations of China within Chinese territory and enterprises established under the laws and regulations of another country (region) whose de facto management bodies are located within Chinese territory are resident enterprises.

Enterprises established under the laws and regulations of another country (region) whose de facto management bodies are not within Chinese territory but which have established entities or sites within Chinese territory, as well as enterprises which have not established entities or sites within Chinese territory but have China-sourced income, are nonresident enterprises.

Article 3

Resident enterprises shall pay enterprise income tax with respect to income from sources within and outside of Chinese territory.

Nonresident enterprises which have established entities and sites within Chinese territory shall pay enterprise income tax with respect to income derived by such entities and sites within Chinese territory and with respect to income derived outside of Chinese territory but which is actually connected with such entities and sites.

Nonresident enterprises which have no entities or sites within Chinese territory, and nonresident enterprises that have entities and sites within Chinese territory with respect to income not actually connected with such entities and sites, shall pay enterprise income tax with respect to income from sources within Chinese territory.

Article 4

The rate of enterprise income tax shall be 25%. A 20% rate shall apply to income of nonresident enterprises as prescribed by Article 3(3) hereof.

Chapter II Taxable Income

Article 5

The taxable income of an enterprise for a tax year shall be its gross income minus nontaxable income, tax-exempt income, deductions and losses permitted to be carried forward from previous years.

Article 6

Gross income means the income an enterprise derives from various sources in monetary and non-monetary form, including:

- (1) income from selling goods;
- (2) income from providing labor services;
- (3) income from property transfers;
- (4) gains from equity investment such as return on stock and dividends;
- (5) interest income;
- (6) rental income;
- (7) royalty income;
- (8) income from receiving donations;
- (9) other income.

Article 7

The following items of gross income are non-taxable income:

- (1) fiscal allocations;
- (2) administrative fees and governmental funds legitimately collected and subject to budgetary administration; and
- (3) other nontaxable income stipulated by the State Council.

Article 8

Expenditures reasonably incurred by an enterprise related to its operational activities including costs, expenses, taxes, losses and other expenditures may be deducted when calculating taxable income.

Article 9

Expenditures for public-welfare donation incurred by an enterprise maybe deducted in an amount up to twelve percent of its total annual profit.

Article 10

The following may not be deducted when calculating taxable income:

- (1) equity investment earnings paid to investors;
- (2) enterprise income tax;
- (3) surcharges for late payment of tax;
- (4) fines, penalties and losses sustained through the confiscation of property;
- (5) donations other than as prescribed in Article 9 hereof;
- (6) sponsorship expenditures;
- (7) unapproved expenditures from reserve funds;

(8) other expenditures not related to the derivation of income.

Article 11

Depreciation of an enterprise's fixed assets shall be calculated pursuant to regulations.

Depreciation of the following fixed assets is not permitted:

- (1) fixed assets other than buildings or structures that are not put into use;
- (2) fixed assets leased out by means of an operational lease;
- (3) fixed assets leased out by means of a financial lease;
- (4) continuously utilized fixed assets that have been fully depreciated;
- (5) fixed assets that are not related to operational activities;
- (6) land that is evaluated separately and booked as fixed asset; and
- (7) other fixed assets that may not be depreciated.

Article 12

Amortization expenses of an enterprise's intangible assets shall be calculated pursuant to regulations.

No amortization expenses shall be made for the following intangible assets:

- (1) self-developed intangible assets the development expenses of which have been deducted for income tax purposes;
- (2) internally-developed goodwill;
- (3) intangible assets that are not related to operational activities;
- (4) other intangible assets that may not be amortized.

Article 13

The following expenditures of an enterprise shall be booked as long-term prepaid expenses:

- (1) improvement expenditures for fully depreciated fixed assets;
- (2) improvement expenditures for leased fixed assets;
- (3) expenditures for fixed assets innovation; and
- (4) other expenditures that shall be booked as long-term prepaid expenses.

Article 14

During the period of external investment of an enterprise, the cost of the invested assets may not be deducted when calculating the taxable income.

Article 15

For inventory consumed or sold by an enterprise, the inventory cost computed pursuant to regulations may be deducted when calculating taxable income.

Article 16

In case of asset transfer by an enterprise, the net book value of such asset may be

deducted when calculating taxable income.

Article 17

Where an enterprise calculates its enterprise income tax on a consolidated basis, it may not use the losses of its overseas operating branches to offset the profits of its operating branches within Chinese territory.

Article 18

Any losses incurred by an enterprise during a tax year may be carried forward to subsequent years to offset the profit in subsequent years. The carry-forward period shall not exceed five years.

Article 19

The following method shall be adopted in calculating the amount of taxable income with respect to the income prescribed in Article 3(3) hereof derived by nonresident enterprises:

- (1) for return on stock, dividend, interest, rental and royalty income, the taxable income shall be the total income;
- (2) for property transfer income, the taxable income shall be the total income minus the net book value;
- (3) for other income, the taxable income shall be the amount calculated with reference to the above two methods.

Article 20

The detailed scope and criteria in relation to Article 10 through 20 hereof shall be formulated by the finance departments of the State Council and the competent tax authorities.

Article 21

Where an enterprise's financial or accounting method in calculating taxable income is different from that of tax laws or administrative regulations, the provisions of tax laws or administrative regulations shall prevail.

Chapter III Tax Payable

Article 22

The tax payable for an enterprise is its taxable income multiplied by the applicable tax rate, minus tax reductions and tax credits prescribed by the provisions of this Law on preferential tax treatment.

Article 23

Tax payments made outside of Chinese territory with respect to the following income derived by an enterprise may be credited against the current tax payable up to the amount of tax payable on such income calculated pursuant to this Law. The portion exceeding the credit limit may be used in the subsequent five years to offset the balance between the credit limit and the credited [foreign] tax payment of each year:

- (1) taxable income of resident enterprises from sources outside of Chinese territory;
- (2) taxable income of nonresident enterprises which have established entities or sites that has occurred outside of Chinese territory but is actually connected with their entities or sites within Chinese territory.

Article 24

Where a resident enterprise receives such income from equity investments as return on stock or dividends which is from sources outside Chinese territory and distributed by a foreign enterprise controlled directly or indirectly by such resident enterprise, the portion of foreign income tax actually paid by the foreign enterprise which is attributable to such income may be used as an creditable income tax payment of such resident enterprise to credit its tax liabilities within the limitations set forth in Article 23 hereof.

Chapter IV Preferential Tax Treatment

Article 25

Preferential enterprise income tax treatment shall be granted to key industries and projects that are supported and encouraged by the State.

Article 26

The following income of an enterprise shall be tax-exempt income:

- (1) interest income from national bonds;
- (2) gains from equity investments such as return on stock or dividends derived between qualified resident enterprises;
- (3) gains from equity investments such as return on stock or dividends which are actually connected with nonresident enterprises' entities or sites within Chinese territory and which are derived by such nonresident enterprises from resident enterprises; and
- (4) income of qualified non-profit public welfare organizations.

Article 27

The following income may be reduced or exempted from enterprise income tax:

- (1) income derived from activities in farming, forestry, animal husbandry and fishery projects;
- (2) income derived from investment or operation in key infrastructure projects supported by the State
- (3) income derived from qualified environmental protection, energy or water-saving projects;
- (4) income from qualified technology transfer; and
- (5) income prescribed in Article 3(3) hereof.

Article 28

Enterprise income tax shall be levied at a reduced rate of 20% for qualified small-scale enterprises with low profit margins.

Enterprise income tax shall be levied at the reduced rate of 15% for hi-tech enterprises supported by the State.

Article 29

An enterprise income tax reduction or exemption may be granted to the enterprises located in the autonomous region for the portion that is shared by the local government. The reductions or exemptions granted by the autonomous regions or counties should be subject to approval by the People's governments of the provinces, autonomous regions or directly administered cities of the autonomous places.

Article 30

Super deductions are allowed for the following expenditures of an enterprise:

- (1) research and development expenditures incurred in the development of new technology, new products and new processes; and
- (2) salary paid to disabled employees or other employees encouraged by the State for employment.

Article 31

Where a venture capital enterprise engages in venture capital investment supported and encouraged by the State, a certain percentage of the investment amount may be used to offset the taxable income.

Article 32

Where an enterprise's fixed assets require accelerated depreciation due to reasons such as advances of technology, the term of depreciation may be reduced, or an accelerated depreciation method may be adopted.

Article 33

Income derived by an enterprise through producing products that complies with the national industry policies by comprehensive utilization of resources may be reduced in calculating taxable income.

Article 34

A certain percentage of investment amount that is spent for purchasing equipment for the purpose of environmental protection, energy saving, water saving and safety production may be credited against the tax payable.

Article 35

The detailed measures of preferential tax treatment provided by this Law shall be formulated by the State Council.

Article 36

Pursuant to the demand of national economy and social development, or in case any emergency accidents cause considerable impact to the enterprises' business operations,

the State Council may formulate ad hoc enterprise income tax preferential policies and report to the National People's Congress for filing.

Chapter V Withholding at Source

Article 37

Withholding at source shall apply to taxes payable on income set forth in Article 3(3) hereof derived by nonresident enterprises. The payer shall be the withholding agent. Tax shall be withheld by the withholding agent from the amount of each payment or payable due by the payer.

Article 38

Withholding at source shall apply to nonresident enterprises' receipt of any income within Chinese territory through undertaking of engineering projects and provision of labor services. Tax authorities may appoint the party paying for the engineering projects or the labor services to act as a tax withholding agent.

Article 39

Where the withholding agent fails to withhold income tax according to laws or unable to fulfill its withholding obligations with respect to the income tax of the nonresident enterprises to be withheld at source pursuant to Article 37 or 38 hereof, the taxpayer shall pay the tax at the place where the income occurred. Where taxpayer fails to pay tax according to laws, tax authorities may pursue and collect tax payables of such enterprises from payables that will be paid by payers of other income items within Chinese territory.

Article 40

The withholding agent shall, within seven (7) days of withholding, turn the amount of taxes withheld on each payment over to the State Treasury and submit a withholding income tax return to the local tax authorities.

Chapter VI Special Tax Adjustments

Article 41

Where an enterprise engages in business transactions with a related party that do not comply with the arm's length principle, thereby reducing the taxable income of such enterprise or that of the related party, tax authorities shall have the power to make adjustments [to their respective tax obligations] through reasonable means.

Where an enterprise and a related party jointly develop or license intangible assets, or jointly provide for or bear services costs, [the joint costs] shall be divided based on the arm's length principle when calculating [their respective] taxable income.

Article 42

An enterprise may propose to the relevant tax authority the pricing principles and calculation methods it has used in business transactions with its related parties, the tax authority may enter into and advance pricing agreements with the enterprise upon

consultation and confirmation.

Article 43

Enterprises shall submit annual related-party transaction reports with the related parties along with the submission of annual tax returns to the tax authority.

When the tax authority carries out any investigation into the related-party transactions, both the enterprises and the related parties as well as other enterprises that are related to the related-party transactions shall supply information pursuant to regulations.

Article 44

Where an enterprise fails to supply information or provide false or incomplete information with respect to its transactions with the related party, thus fails to provide true information reflecting related-party transactions, the tax authority has the right to deem the taxable income of such enterprise according to the Law.

Article 45

Enterprises established and controlled by resident enterprises, or jointly controlled by resident enterprises and Chinese individual in the countries (regions) that the effective tax burden of which is apparently lower than that of Article 4(1) hereof, and failed to make profit distribution or made unreasonable profit distribution other than out of reasonable business consideration, the aforesaid profit that attributable to the resident enterprises shall be included in their current income.

Article 46

No interest expenditure shall be deducted from the taxable income if the ratio of an enterprise's debt financing and equity financing accepted from its related party exceeds the stipulated standard.

Article 47

Where an enterprise implements any other arrangement with no reasonable commercial purpose to reduce its taxable income or profit, the tax authority shall have the right to make reasonable adjustment.

Article 48

Where tax authorities make any adjustment pursuant to the provisions of this Chapter and levy additional tax, additional tax should be charged and interest should be paid in accordance with the State Council's regulations.

Chapter VII Administration of Tax Collection

Article 49

In addition to provisions of this Law, administration for collection of enterprise income tax shall be implemented in accordance with the relevant provisions of the *Law of the People's Republic of China concerning the Administration of Tax Collection*.

Article 50

Except otherwise stipulated by tax laws or administrative regulations, a resident enterprise's place of incorporation shall be the tax payment place. Where its place of incorporation is outside China, the place of its de facto management body shall be the tax payment place.

The enterprise income tax of a resident enterprise that have established operating establishment in China with no legal person capacity shall be computed and paid collectively.

Article 51

The tax payment place for a nonresident enterprise that has derived any income prescribed in Article 3(2) hereof shall be the place where the entities or establishments locates. Where a nonresident enterprise establishes two or more business bodies in China, upon review and approval of tax authorities, it may elect to collectively pay the enterprise income tax through the principal business body.

The tax payment place for a nonresident enterprise that has derived any income prescribed in Article 3(3) hereof shall be the place where the withholding agent is located.

Article 52

Except otherwise stipulated by the State Council, no enterprise shall pay the enterprise income tax on a consolidated basis.

Article 53

Enterprise income tax should be calculated on an enterprise income tax year basis. An enterprise income tax year shall refer to the period from January 1 to December 31 of the Gregorian calendar.

An enterprise commences or ceases operation in the middle of a tax year and consequently its de facto operation period in a tax year is less than 12 months shall regard its actual period of operations as a tax year.

Where an enterprise enters into liquidation, the liquidation period shall be regarded as a tax year.

Article 54

Provisional enterprise income tax payments shall be made on a monthly or quarterly basis.

Enterprises shall submit tax returns to the tax authorities within fifteen (15) days of the end of the month or quarter and prepay the tax.

Enterprises shall file annual enterprise income tax returns within five (5) months of the

end of each year and make final settlement to settle any excess tax payment or deficiency.

When enterprises submit enterprise income tax returns, they shall also submit financial statements and other information according to regulations.

Article 55

Where an enterprise ceases its operation in the middle of a year, the enterprise shall conduct enterprise income tax final settlement for the current period with tax authority within 60 days of after actually ceases the operation.

Enterprises shall file tax returns to the tax authorities and make settlement for its liquidation income according to the law prior to its registration of cancellation.

Article 56

Any enterprise income tax paid under this Law shall be computed in Renminbi. Where any income derived is calculated in foreign currency, the tax shall be calculated and paid in Renminbi through currency conversion.

Chapter VIII Miscellaneous

Article 57

Enterprises established prior to the promulgation of this Law eligible for low tax rate preferential treatment in accordance with the then prevailing tax laws and administrative regulations shall, pursuant to regulations of the State Council, over a five-year transition period from the implementation of this Law, gradually become subject to the tax rate provided by this Law.

Enterprises eligible for regular tax reductions or exemptions may, pursuant to regulations of the State Council, continue to enjoy tax preferential treatment after the implementation of this Law until their preferential treatment expire. The preferential-treatment period of enterprises which have not enjoyed any preferential treatments for the reason of not having made any profits, however, shall be deemed as starting from the implementation of this Law.

The specific regions established for purpose of developing foreign economic cooperation and technical exchange pursuant to laws, as well as key high technology enterprises supported by the State newly established in aforesaid regions that have implemented the above preferential policies may enjoy transitional preferential tax treatment; the detailed regulations shall be formulated by the State Council.

Enterprises under the encouraged category determined by the State may enjoy tax reductions or exemptions according to the provisions of the State Council.

Article 58

Where any tax treaties concluded between the government of the People's Republic of China and any foreign governments contain provisions different from this Law, the

provisions of the respective treaties shall apply.

Article 59

Rules for implementation of this Law shall be formulated by the State Council in accordance with this Law.

Article 60

This Law shall come into force on January 1, 2008. The *Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises* adopted by the 4th Conference of the National People's Congress on April 9, 1991 and the *Provisional Regulations of the People's Republic of China on Enterprises Income Tax* published by the State Council on December 13, 1993 shall be repealed on the same date.