

**CHINA – CERTAIN MEASURES GRANTING REFUNDS, REDUCTIONS OR
EXEMPTIONS FROM TAXES AND OTHER PAYMENTS**

Communication from China and the United States

The following communication, dated 19 December 2007, from the delegation of China and the delegation of the United States, is circulated at the request of those delegations.

The Governments of the People's Republic of China and the United States of America wish to notify the Dispute Settlement Body that we have reached an agreement with respect to the matter raised by the United States in the dispute *China – Certain Measures Granting Refunds, Reductions or Exemptions from Taxes and Other Payments* (WT/DS358).

Please find attached the text of the agreement, in the form of a memorandum of understanding. We ask that you circulate this notification and the attachment to the Dispute Settlement Body.

**Memorandum of Understanding between the United States of America
and the People's Republic of China Regarding Certain Measures
Granting Refunds, Reductions or Exemptions from Taxes or Other Payments**

Whereas the United States of America ("United States") filed requests for consultations with the People's Republic of China ("China") on 2 February 2007 and 27 April 2007 pursuant to Articles 1 and 4 of the World Trade Organization (WTO) Understanding on Rules and Procedures Governing the Settlement of Disputes, Article XXII:1 of the WTO General Agreement on Tariffs and Trade 1994, Articles 4 and 30 of the WTO Agreement on Subsidies and Countervailing Measures, and Article 8 of the WTO Agreement on Trade-Related Investment Measures, regarding certain measures granting refunds, reductions or exemption from taxes or other payments (DS358);

Whereas the United States and China held constructive consultations in Geneva on 20 March and 22 June 2007;

The United States and China have agreed as follows:

1. During the consultations, the United States described its concerns about the WTO-consistency of tax preferences provided under:

- (a) the *Circular of the Ministry of Finance and the State Administration of Taxation Concerning the Issues of Tax Credit To Enterprise Income Tax for Purchase of Domestically Produced Equipment by Enterprises with Foreign Investment and Foreign Enterprises*, CaiShuiZi [2000] No. 49, issued on 14 January 2000, and the *Circular of the State Administration of Taxation on Printing and Issuing the Measures On Tax Credit To Enterprise Income Tax for Purchase of Domestically Produced Equipment by Enterprises with Foreign Investment and Foreign Enterprises*, GuoShuiFa [2000] No. 90, issued on 18 May 2000; and
- (b) the *Circular on Printing and Issuing the Interim Measures on Credit and Exemption of Enterprise Income Tax for Investment in Domestically Made Equipment for Technological Renovation*, CaiShuiZi [1999] No. 290, issued by the Ministry of Finance and the State Administration of Taxation on 8 December 1999.

In this regard, China has explained that legal instruments of at least equal legal stature to the circulars identified in sub-paragraphs (a) and (b) above, will contain provisions stating that these circulars are repealed, and will be issued by the competent authorities, by 31 December 2007, effective no later than 1 January 2008. China confirms that the tax preferences under the circulars identified in sub-paragraphs (a) and (b) above will not be reinstated.

2. During the consultations, the United States described its concerns about the WTO-consistency of tax preferences provided under:

- (a) Article 9 of the *Provisions of the State Council on the Encouragement of Foreign Investment*, GuoFa [1986] No. 95, issued on 11 October 1986 (hereinafter "*State Council Provisions*"); Article 6 of the *Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises*, Order No. 45, promulgated on 9 April 1991 (hereinafter "*FIE Income Tax Law*"); and Article 75, paragraph 1, section 8 of the *Rules for the Implementation of the Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises*, Decree No. 85, issued by the State Council on 30 June 1991 (hereinafter "*FIE Income Tax Implementing Rules*");

- (b) Article 8 of the *State Council Provisions*; Article 6 of the *FIE Income Tax Law*; and Article 75, paragraph 1, section 7 of the *FIE Income Tax Implementing Rules*; and
- (c) Article 10 of the *State Council Provisions*; Articles 6 and 10 of the *FIE Income Tax Law*; and Article 81 of the *FIE Income Tax Implementing Rules*.

China confirms that, effective 1 January 2008, the *Enterprise Income Tax Law of the People's Republic of China*, Order No. 63, promulgated on 16 March 2007 (hereinafter "*Enterprise Income Tax Law*"), repeals the *FIE Income Tax Law*. In addition, China has explained that legal instruments to be issued by, and made effective no later than, 1 January 2008, will contain provisions stating that the *FIE Income Tax Implementing Rules* are repealed. With the abolition of the *FIE Income Tax Law* and the *FIE Income Tax Implementing Rules*, Articles 8, 9 and 10 of the *State Council Provisions* will no longer be valid. China has further explained that, in accordance with its schedule of administrative regulations revision, Articles 8, 9 and 10 of the *State Council Provisions* will be eliminated by a legal instrument no later than 1 January 2009. The legal instruments repealing the *FIE Income Tax Implementing Rules* and Articles 8, 9 and 10 of the *State Council Provisions* will be issued by the competent authorities and be of at least equal legal stature to the legal instruments being repealed. China confirms that the tax preferences under the legal provisions identified in sub-paragraphs (a), (b) and (c) above will not be reinstated.

3. During the consultations, the United States described its concerns about the WTO-consistency of tax and other preferences provided under:

- (a) Article 7 of the *FIE Income Tax Law*; Article 73, paragraph 1, section 6 of the *FIE Income Tax Implementing Rules*; and Section XIII of the *Catalogue of Encouraged Foreign Investment Industries* (hereinafter "*Encouraged Catalogue*") within the *Catalogue for the Guidance of Foreign Investment Industries*, Order [2004] No. 24, issued by the National Development and Reform Commission and the Ministry of Commerce on 30 November 2004 (hereinafter "*Catalogue*"); and
- (b) the *Circular of the State Council Concerning the Adjustment in the Taxation Policy of Imported Equipment*, GuoFa [1997] No. 37, issued on 29 December 1997; and Section XIII of the *Encouraged Catalogue*.

In this regard, China has explained that, in accordance with its economic and social development, it revised the *Catalogue* on 31 October 2007, which revision will take effect as of 1 December 2007. China confirms that Section XIII of the *Encouraged Catalogue* dated 30 November 2004 will not be reinstated.

4. During the consultations, the United States described its concerns about the WTO-consistency of the *Enterprise Income Tax Law*, including Articles 25, 28, 31 and 57 thereof. China has explained that these provisions do not provide for the offering of any income tax preference contingent upon the use of domestic over imported goods or upon export performance. China has further explained that, notwithstanding the fact that Article 57 of the *Enterprise Income Tax Law* authorizes the continuation of certain income tax preferences beyond 1 January 2008, it will not be implemented or applied so as to introduce or permit the continuation of the income tax preferences being repealed by virtue of the actions described in paragraphs 1 through 3 of this Memorandum of Understanding. These limitations will be made explicit under fully authoritative legal measures, and will be effective, no later than 1 January 2008.

5. During the consultations, the United States described its concerns about the WTO-consistency of an exemption for certain foreign-invested enterprises from payments to the State for worker allowances, provided under Article 3 of *State Council Provisions*.

China has explained that, at the time the State Council promulgated the *State Council Provisions*, Article 11 of the *State Council Regulations on Labor Management in Sino-Foreign Joint Ventures*, GuoFa [1980] No. 199 (26 July 1980), required foreign-invested enterprises to make such payments to the State. China has confirmed, however, that because this requirement was eliminated by the *State Council Decision on Abolition of Certain Administrative Regulations Promulgated Prior to the End of 2000*, Order No. 319 (6 October 2001), the exemption provided under Article 3 of the *State Council Provisions* is no longer operative. China confirms that Article 3 of the *State Council Provisions* may no longer serve as a legal basis to exempt foreign-invested enterprises from making payments required by Chinese law, regulation, or other official measure.

6. During the consultations, the United States described its concerns about the WTO-consistency of value-added tax (VAT) refunds provided under the *Circular of the State Administration of Taxation on Printing and Issuing the Interim Measures for the Administration of Tax Refund to Enterprises with Foreign Investment for the Purchase of Domestically Produced Equipment*, GuoShuiFa [1999] No. 171, issued on 20 September 1999, and the *Circular of the State Administration of Taxation and National Development and Reform Commission on Printing and Issuing the Interim Measures for the Administration of Tax Refund for the Purchase of Domestically-Produced Equipment in Foreign Investment Projects*, GuoShuiFa [2006] No. 111, issued on 24 July 2006.

In this regard, China has stated that these circulars do not create a preference, either in law or on a *de facto* basis, for the use of domestic over imported goods in connection with purchases of domestically-produced equipment when viewed in relation to the *Circular of the State Council Concerning the Adjustment in the Taxation Policy of Imported Equipment*, GuoFa [1997] No. 37, issued on 29 December 1997, in connection with purchases of imported equipment. China has confirmed that, in implementing the above-mentioned legal instruments as well as any new legal instruments that affect the operation of the above-mentioned legal instruments, it will ensure that imported equipment receives VAT treatment under terms and conditions no less favorable than those applicable to domestically-produced equipment.

7. The United States and China agree to communicate in a timely manner with respect to the implementation of the actions described above, including provision of related new legal instruments.

8. This Memorandum of Understanding is without prejudice to the rights and obligations of the United States and China under the WTO Agreement.

Done in Geneva, on 29 November 2007, in two copies in English and Chinese respectively, each text being equally authentic.

(signed)
For the Government
of the United States of America

(signed)
For the Government
of the People's Republic of China