

**TRANSITIONAL REVIEW MECHANISM PURSUANT TO  
SECTION 18 OF THE PROTOCOL ON THE ACCESSION  
OF THE PEOPLE'S REPUBLIC OF CHINA**

Questions from the EUROPEAN COMMUNITIES to  
CHINA with regards to China's Transitional Review  
Mechanism on Subsidy Practices

The following communication, dated 20 September 2005, is being circulated at the request of the Delegation of the European Commission.

1. Despite the assurances given by China to the SCM Committee that it would do its best to provide a New and Full Subsidy Notification, to date, nearly four years after China's accession to the WTO, there is still no such notification. The EC reiterates its dissatisfaction that China has so far not fulfilled this obligation resulting from its accession to the WTO and strongly urges China to provide a subsidy notification as soon as possible.
2. EC noted with great disappointment in April this year that the VAT reimbursement scheme for the import of copper raw material has been prolonged for the current year. Although some explanation had been provided by the delegate of China during last year's TRM exercise, no exact legal reference nor amounts of VAT reimbursed have been provided. The EC wants to point out again that in regard to the distortions caused by this system to the world market, the overall figures of raw material imports showed a strong upward trend. The figures available to the EC showed that 30 per cent of China's copper scrap imports and 50 per cent of the copper concentrate imports had benefited from the system. The effective price reduction for Chinese smelters obtained through the VAT refund is substantial and enables them to pay higher buying prices for raw materials which are not reflected in equally higher prices for the finished product. The EC reiterates its strong concerns that this trade distorting subsidy practice had and continues to cause adverse effects to its and other Members' industries and should therefore be eliminated.
3. The EC wants to point out that it still has not received any satisfying replies to its questions 3 to 7 of last years TRM questionnaire (G/SCM/Q2/CHN7 – see attachment) in regard to certain subsidy schemes. The EC asks China to provide a response to these questions, and in particular, whether or not such subsidy programmes exist, and if they exist to describe them in more detail.
4. The EC has become aware that the following legal provisions are apparently still in force:
  - Article 7 Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises (passed on 9 April 1991 on the 4<sup>th</sup> meeting of the 7<sup>th</sup>

National Congress, and Promulgated by Decree No. 45 of the Chairman's instruction of the People's Republic of China on the same day):

*“The income tax on enterprises with foreign investment established in Special Economic Zones, foreign enterprises which have establishments or places in Special Economic Zones engaged in production or business operations, and enterprises with foreign investment of a production nature in Economic and Technological Development Zones, shall be levied at the reduced rate of fifteen percent.*

*The income tax on enterprises with foreign investment of a production nature established in coastal economic open zones or in the old urban districts of cities where the Special Economic Zones or the Economic and Technological Development Zones are located, shall be levied at the reduced rate of twenty four percent.*

*The income tax on enterprises with foreign investment in coastal economic open zones, in the old urban districts of cities where the Special Economic Zones or the Economic and Technological Development Zones are located or in other regions defined by the State Council, within the scope of energy, communications, harbor, wharf or other projects encouraged by the state, may be levied at the reduced rate of fifteen percent. The specific rules shall be regulated by the State Council.”*

- Article 75 (7) Rules for the implementation of the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises (Promulgated by Decree No. 85 of the State Council of the People's Republic of China on 30 June 1991 and effective as of 1 July 1991)

*“Export-oriented enterprises invested in and operated by foreign businesses for which in any year the output value of all export products amounts to 70% or more of the output value of the products of the enterprise for that year may pay enterprise income tax at the tax rate specified in the Tax Law reduced by one half after the period of enterprise income tax exemptions or reductions has expired in accordance with the provisions of the Tax Law. However, export-oriented enterprises in the special economic zones and economic and technological development zones and other such enterprises subject to enterprise income tax at the tax rate of 15% that qualify under the above-mentioned conditions shall pay enterprise income tax at the tax rate of 10%.”*

Can China please confirm whether these provisions are still in force and if not provide the exact legal reference by which they have been amended?

If they are still in force:

1. Can China please specify - with reference to the respective legal provision - which are the conditions for a company to settle in the special zones mentioned in the tax law and whether there exist any export requirements?
2. Can China please explain how the subsidy provided in Article 75 (7) of the implementing rules is compatible with Article 3 ASCM and when it will bring its legislation into conformity with the WTO subsidy rules?

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