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post departments exclusively): the proportion of foreign investment shall not exceed 50% (not to exceed 49% as for the express service); foreign parties shall be allowed to take the holding position no later than Dec 11, 2002; solely foreign-invested enterprises shall be allowed no later than Dec 11, 2005 3. Ocean shipping tally: limited to equity joint ventures and cooperative joint ventures 4. Advertisement: the proportion of foreign investment shall not exceed 49%, foreign parties shall be allowed to take the holding position no later than Dec 11, 2003; solely foreign-invested enterprises shall be allowed no later than Dec 11, 2005 9) insurance companies 1. Non-life insurance companies: the proportion of foreign investment shall not exceed 51%; solely foreign-invested enterprises shall be allowed no later than Dec 11, 2003 2. Life insurance companies: the proportion of foreign investment shall not exceed 50% 10) Securities companies and fund management companies 1. Securities companies: solely foreign-invested enterprises shall be allowed no later than Dec 11, 2004, and the proportion of foreign investment shall not exceed one-third 2. Fund management companies: foreign parties are allowed to make investment and the proportion of foreign investment shall not exceed 33%; and the proportion of foreign investment shall be allowed to reach 49% no later than Dec.11, 2004 11) Insurance broker companies: the proportion of foreign investment shall not exceed 50%; the proportion of foreign investment shall be allowed to reach 51% no later than Dec.11, 2004; and solely foreign-invested enterprises shall be allowed no later than Dec.11, 2006 12) Checking, appraising, attestation and notarization of import and export goods: foreign parties shall be allowed to take the holding position no later than Dec 11, 2003; solely foreign-invested enterprises shall be allowed no later than Dec 11, 2005

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 [1991] No.85 of the State Council June 30, 1991 Chapter I General Provisions Article 1 These Rules are formulated in accordance with the provisions of Article 29 of the Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises (hereinafter referred to as the "Tax Law"). Article 2 "Income from production and business operations" mentioned in Article 1, paragraph 1 and paragraph 2 of the Tax Law means income from production and business operations in manufacturing, mining, communications and transportation, construction and installation, agriculture, forestry, animal husbandry, fishery, water conservation, commerce, finance, service industries, exploration and exploitation, and in other trades. "Income from other sources" mentioned in Article 1, paragraph 1 and paragraph 2 of the Tax Law means profits (dividends), interest, rents, income from the transfer of property, income from the provision or transfer of patents, proprietary technology, income from trademark rights and copyrights as well as other non-business income. Article 3 "Enterprises with foreign investment" mentioned in Article 2, paragraph 1 of the Tax Law and "foreign companies, enterprises and other economic organizations which have establishments or places in China and engage in production or business operations" mentioned in Article 2, paragraph 2 of the Tax Law are, unless otherwise especially specified, generally all referred to as "enterprises" in these Rules. "Establishments or places" mentioned in Article 2, paragraph 2 of the Tax Law refers to management organizations, business organizations, administrative organizations and places for factories and the exploitation of natural resources, places for contracting of construction, installation, assembly, and exploration work; places for the provision of labor services, and business agents. Article 4 "Business agents" mentioned in Article 3, paragraph 2 of these Rules means companies, enterprises and other economic organizations or individuals entrusted by foreign enterprises to engage as agents in any of the following: (1) representing principals on a regular basis in the arranging of purchases and signing of purchase contracts and the purchasing of commodities on commission; (2) entering into agency agreements or contracts with principals, storing on a regular basis products or commodities owned by principals, and delivering on behalf of principals such products or commodities to other parties; and (3) having authority to represent principals on a regular basis in signing of sales contracts or in accepting of purchase orders. Article 5 "Head office" mentioned in Article 3 of the Tax Law refers to the central organization which is established in China by an enterprise with foreign investment as a legal person pursuant to the laws of China and which is responsible for the management, operations and

control over such enterprise. Income from production and business operations and other income derived by the branches within or outside China of an enterprise with foreign investment shall be consolidated by the head office for purposes of the payment of income tax. Article 6 "Income derived from sources inside China" mentioned in Article 3 of the Tax Law refers to: (1) income from production and business operations derived by enterprises with foreign investment and foreign enterprises which have establishments or places in China, as well as profits (dividends), interest, rents, royalties and other income arising within or outside China actually connected with establishments or sites established in China by enterprises with foreign investment or foreign enterprises; (2) the following income received by foreign enterprises which have no establishments or sites in China: (a) profits (dividends) earned by enterprises in China; (b) interest derived within China such as on deposits or loans, interest on bonds, interest on payments made provisionally for others, and deferred payments; (c) rentals on property leased to and used by lessees in China; (d) royalties such as those received from the provision of patents, proprietary technology, trademarks and copyrights for use in China; (e) gains from the transfer of property, such as houses, buildings, structures and attached facilities located in China and from the assignment of land use rights within China; (f) other income derived from China and stipulated by the Ministry of Finance to be subject to tax. Article 7 In respect of Chinese-foreign contractual joint ventures that do not constitute legal persons, each partner thereto may separately compute and pay income tax in accordance with the relevant tax laws and regulations of the State; income tax may, upon approval by the local tax authorities of an application submitted by such enterprises, be computed and paid on a consolidated basis in accordance with the provisions of the Tax Law. Article 8 "Tax year" mentioned in Article 4 of the Tax Law begins on January 1 and ends on December 31 under the Gregorian Calendar. Foreign enterprises that have difficulty computing taxable income in accordance with the tax year stipulated in the Tax Law may, upon approval by the local tax authorities of an application submitted by such enterprises, use their own 12-month fiscal year as the tax year. Enterprises commencing business operations in the middle of a tax year or actually operating for a period of less than 12 months in any tax year due to such factors as merger or shutdown shall use the actual period of operations as the tax year. Enterprises that undergo liquidation shall use the period of liquidation as the tax year. Article 9 "The competent authority for tax affairs under the State Council" mentioned in Article 8, paragraph 3 and Article 19, paragraph 3, subparagraph (4) of the Tax Law and Article 72 of these Rules refers to the Ministry of Finance and the State Tax Bureau. Chapter II Computation of Taxable Income Article 10 "The formula for the computation of taxable income" mentioned in Article 4 of the Tax Law is as follows: (1) Manufacturing: (a) taxable income = (profit on sales) + (profit from other operations) + (non-business income) - (non-business expenses); (b) profit on sales = (net sales) - (cost of products sold) - (taxes on sales) - [(selling expenses) + (administrative expenses) + (finance expenses)]; (c) net sales = (gross sales) - [(sales returns) + (sales discounts and allowances)]; (d) cost of products sold = (cost of products manufactured for the period) + (inventory of finished products at the beginning of the period) - (inventory of finished products at the end of the period); (e) cost of products manufactured for the period = (manufacturing costs for the period) + (inventory of semifinished products and products in process at the beginning of the period) - (inventory of semi-finished products and products in process at the end of the period); (f) manufacturing costs for the period = (direct materials consumed in production for the period) + (direct labour) + (manufacturing expenses). (2) Commerce: (a) taxable income = (profit on sales) + (profit from other operations) + (non-business income) - (non-business expenses); (b) profit on sales = (net sales) - (cost of sales) - (taxes on sales) - [(selling expenses) + (administrative expenses) + (finance expenses)]; (c) net sales = (gross sales) - [(sales returns) + (sales discounts and allowances)]; (d) cost of sales = (inventory of merchandise at the beginning of the period) + [(purchase of merchandise during the period) - (purchase returns) + (purchase discounts and allowances)] + (purchasing expenses) - (inventory of merchandise at the end of the period). (3) Service trades: (a) taxable income = (net business income) + (non-operating income) - (non-operating expenses); (b) net business income = (gross business income) - [(taxes on business income) + (operating expenses) + (administrative expenses) + (finance expenses)]. (4) Other lines of business: Computations shall be made with reference to the above formulas. Article 11 The computation of taxable income of an enterprise shall, in principle, be on an accrual basis. The following income from business operations of an enterprise may be determined by stages and used as the basis for the computation of taxable income: (1) Where products or commodities are sold by instalment payment methods, income from sales may be recognized according to the invoice date of the products or commodities to be delivered; income from sales may also be recognized according to the date of payment to be made by the buyer as agreed upon in the contract; (2) Where construction, installation and assembly projects, and provision of labour services extend beyond one year, income may be recognized according to the progress of the project or the amount of work completed; (3) Where the processing or manufacturing of

heavy machinery, equipments and ships for other enterprises extends beyond one year, income may be recognized according to the progress of the project or amount of work completed. Article 12 Where Chinese-foreign contractual joint ventures operate on the basis of product sharing, the partners thereto shall be deemed to receive income at the time of the division of the products; the amount of income shall be computed according to the price sold to third party or with reference to prevailing market prices. Where foreign enterprises are engaged in the cooperative exploration of petroleum resources, the partners thereto shall be deemed to receive income at the time of the division of the crude oil; the amount of income shall be computed according to a price which is adjusted periodically with reference to the international market prices of crude oil of similar quality. Article 13 In respect of income obtained by enterprises in the form of non-monetary assets or rights and interests, such income shall be computed or appraised with reference to prevailing market prices. Article 14 "Exchange rate quoted by the State exchange control authorities" mentioned in Article 21 of the Tax Law refers to the buying rate quoted by the State Administration of Exchange Control. Article 15 In respect of income obtained by enterprises in foreign currency, upon payment of income tax in quarterly instalments in accordance with the provisions of Article 15 of the Tax Law, taxable income shall be computed by converting the income into Renminbi according to the exchange rate quotation on the last day of the quarter. At the time of final settlement following the end of the year, no recomputation and reconversion need be made in respect of income in a foreign currency for which tax has already been paid on a quarterly basis; only that portion of the foreign currency income of the entire year for which tax has not been paid shall, in respect of the computation of taxable income, be converted into Renminbi according to the exchange rate quotation on the last day of the tax year. Article 16 Where an enterprise is unable to provide complete and accurate certificates of costs and expenses and is unable to correctly compute taxable income, the local tax authorities shall determine the rate of profit and compute taxable income with reference to the profit level of other enterprises in the same or similar trade. Where an enterprise is unable to provide complete and accurate certificates of revenues and is unable to report income correctly, the local tax authorities shall appraise and determine taxable income by the use of such methods as cost (expense) plus reasonable profits. When the tax authorities appraise and determine profit rates or revenues in accordance with the provisions of the preceding paragraph, and where other treatment is provided by the laws, regulations and rules, such other treatment shall be applicable. Article 17 Foreign air transportation and ocean shipping enterprises engaged in international transport business shall use 5% of the gross revenues from passenger and cargo transport and shipping services arising within China as taxable income. Article 18 Where an enterprise with foreign investment invests in another enterprise within China, the profits (dividends) so obtained from the enterprise receiving such investment may be excluded from taxable income of the enterprise; however, expenses and losses incurred in such abovementioned investments shall not be deducted from taxable income of the enterprise. Article 19 Unless otherwise stipulated by the State, the following items shall not be itemized as costs, expenses or losses in the computation of taxable income: (1) expenses in connection with the acquisition or construction of fixed assets; (2) expenses in connection with the transfer or development of intangible assets; (3) interest on capital; (4) various income tax payments; (5) fines for illegal business operations and losses due to the confiscation of property; (6) surcharges and fines for overdue payment of taxes; (7) the portion of losses due to natural disasters or accidents for which there has been compensation; (8) donations and contributions other than those used in China for public welfare or relief purposes; (9) royalties paid to the head office; (10) other expenses not related to production or business operations. Article 20 Reasonable administrative expenses paid by a foreign enterprise with an establishment or site in China to the head office in connection with production or business operations of the establishment or site shall be permitted to be itemized as expenses following agreement by the local tax authorities after an examination and verification of documents of proof issued by the head office in respect of the scope of the administrative expenses, total amounts, the basis and methods of allocation, which shall be provided together with an accompanying verification report of a certified public accountant. Administrative expenses in connection with production and business operations shall be allocated reasonably between enterprises with foreign investment and their branches. Article 21 Reasonable interest payments incurred on loans in connection with production and business operations shall be permitted to be itemized as expenses following agreement by the local tax authorities after an examination and verification of documents of proof, which shall be provided by the enterprises in respect of the loans and interest payments. Interest paid on loans used by enterprises for the purchase or construction of fixed assets or the transfer or development of intangible assets prior to the assets being put into use shall be included in the original value of the assets. "Reasonable interest" mentioned in the first paragraph of this Article refers to interest computed at a rate not higher than normal commercial lending rates. Article 22 Entertainment expenses

incurred by enterprises in connection with production and business operations shall, when supported by authentic records or invoices and vouchers, be permitted to be itemized as expenses subject to the following limits: (1) Where annual net sales are 15 million yuan (RMB) or less, not to exceed 0.5% of net sales; for that portion of annual net sales that exceeds 15 million yuan (RMB), not to exceed 0.3% of that portion of net sales. (2) Where annual gross business income is 5 million yuan (RMB) or less, not to exceed 1% of annual gross business income; for that portion of annual gross business income that exceeds 5 million yuan (RMB), not to exceed 0.5% of that portion of annual gross business income.

Article 23 Exchange gains or losses incurred by enterprises during pre-construction or during production and business operations shall, except as otherwise provided by the State, be appropriately itemized as gains or losses for that respective period.

Article 24 Salaries and wages, and benefits and allowances paid by enterprises to employees shall be permitted to be itemized as expenses following agreement by the local tax authorities after an examination and verification of the submission of wage scales and supporting documents and relevant materials. Foreign social security premiums paid by enterprises to employees working in China shall not be itemized as expenses.

Article 25 Enterprises engaged in such businesses as credit and leasing operations may, on the basis of actual requirements and following approval by the local tax authorities of a report thereon, provide year-by-year bad debt provisions, the amount of which shall not exceed 3% of the amount of the year-end loan balances (not including inter-bank loans) or the amount of accounts receivable, bills receivable and other such receivables, to be deducted from taxable income of that year. The portion of the actual bad debt losses incurred by an enterprise which exceeds the bad debt provisions of the preceding year may be itemized as a loss in the current year; the portion less than the bad debt provisions of the previous year shall be included in taxable income of the current year. Bad debt losses mentioned in the preceding paragraph shall be subject to approval after examination and verification by the local tax authorities.

Article 26 "Bad debt losses" mentioned in Article 25, paragraph 2 of these Rules refers to the following accounts receivable: (1) due to the bankruptcy of the debtor, collection is still not possible after the use of the bankruptcy assets for settlement; (2) due to the death of the debtor, collection is still not possible after the use of the estate for repayment; (3) due to the failure of the debtor to fulfil repayment obligations for over two years, collection is still not possible.

Article 27 Accounts receivable already itemized as bad debt losses which are recovered in full or in part by an enterprise in a subsequent year shall be included in taxable income of the year of recovery.

Article 28 Foreign enterprises with establishments or places in China may, except as otherwise provided by the State, deduct as expenses foreign income tax, which has been paid on profits (dividends), interest, rents, royalties and other income received from outside China and actually connected with such establishments or places.

Article 29 "Net assets or remaining property" mentioned in Article 18 of the Tax Law means the amount of all assets or property following deduction of various liabilities and losses upon the liquidation of an enterprise.

Chapter III Tax Treatment for Assets

Article 30 "Fixed assets of enterprises" means houses, buildings and structures, machinery, mechanical apparatus, means of transport and other such equipment, appliances and tools related to production and business operations with a useful life of one year or more. Items not in the nature of major equipment which are used for production or business operations and which have a unit value of 2000 yuan (RMB) or less, or with a useful life of two years or less may be itemized as expenses on the basis of actual consumption.

Article 31 The valuation of fixed assets shall be based on original cost. The original cost of purchased fixed assets shall be the purchase price plus transportation expenses, installation expenses and other related expenses incurred prior to the use of the assets. The original cost of fixed assets manufactured or constructed by an enterprise itself shall be the actual expenses incurred in their manufacture or construction. The original cost of fixed assets treated as investments shall, giving consideration to the degree of wear and tear of the fixed assets, be such reasonable price as is specified in the contract, or a price appraised with reference to the relevant market price plus the relevant expenses incurred prior to the use thereof.

Article 32 Depreciation of fixed assets of an enterprise shall be computed commencing with the month following the month in which they are first put into use. The computation of depreciation shall cease in the month following the month in which the fixed assets cease to be used. All investments made during the development stage by enterprises engaged in the exploitation of oil resources shall, taking the oil (gas) field as a unit, be aggregated and treated as capital expenditures; the computation of depreciation shall begin in the month following the month in which the oil (gas) field commences commercial production.

Article 33 In respect of the computation of depreciation of fixed assets, the salvage value shall first be estimated and deducted from the original cost of the assets. The salvage value shall not be less than 10% of the original value; any request for retaining a lower salvage value or not salvage value must be approved by the local tax authorities.

Article 34 Depreciation of fixed assets shall be computed using the straight-line method. Where it is necessary to use

any other method of depreciation, an application may be filed by an enterprise which, following examination and verification by the local tax authorities, shall be reported level-by-level to the State Tax Bureau for approval. Article 35 The computation of the minimum useful life in respect of the depreciation of fixed assets is as follows: (1) for houses and buildings: 20 years; (2) for railway rolling stock, ships, machinery, mechanical apparatus, and other production equipment: 10 years; (3) for electronic equipment and means of transport other than railway rolling stock and ships, as well as such fixtures, tools and furnishings related to production and business operations: 5 years. Article 36 Depreciation of fixed assets in the nature of investments during the development stage and subsequent stages of an enterprise engaged in the exploitation of oil resources may be computed on a consolidated basis without retaining salvage value; the period of depreciation shall not be less than six years. Article 37 "Houses and buildings" mentioned in Article 35, subparagraph (1) of these Rules means houses, buildings and attached structures used for production and business operations, and living quarters and welfare facilities for employees, the scope of which is as follows:— houses, including factory buildings, business premises, office buildings, warehouses, residential buildings, canteens, and other such buildings;— buildings, including towers, ponds, troughs, wells, racks, sheds (not including temporary, simply constructed structures such as work sheds and vehicle sheds), fields, roads, bridges, platforms, piers, docks, culverts, gas stations as well as pipes, smokestacks, and enclosing walls that are detached from buildings, machinery and equipment; Facilities attached to buildings and structures mean auxiliary facilities that are inseparable from buildings and structures and for which no separate value is computed, including, for example, building and structure ventilation and drainage systems, oil pipelines, communication and power lines, elevators and sanitation equipment. Article 38 The scope of railway rolling stock, ships, machinery, mechanical apparatus and other production equipment mentioned in Article 35, subparagraph (2) of these Rules is as follows:— "railway rolling stock" includes various types of locomotives, passenger coaches, freight cars, as well as auxiliary facilities on rolling stock for which no separate value is computed;— "ships" includes various types of motor ships as well as auxiliary facilities on ships for which no separate value is computed;— "machinery, mechanical apparatus and other production equipment" includes various types of machinery, mechanical apparatus, machinery units, production lines, as well as auxiliary equipment such as various types of power, transport and conduction equipment. Article 39 The scope of electronic equipment, means of transport other than railway rolling stock and ships mentioned in Article 35, subparagraph (3) of these Rules is as follows:— "electronic equipment" means equipment comprising mainly integrated circuits, transistors, electron tubes and other electronic components whose primary functions are to bring into use the application of electronic technology (including software), including computers as well as computer controlled robots, and digital control or program control systems.— "means of transport other than railway rolling stock and ships" includes airplanes, automobiles, trams, tractors, motor bikes (boats), motorized sailboats, sailboats, and other means of transport. Article 40 Where, for special reasons, it is necessary to shorten the useful life of fixed assets, an application may be submitted by an enterprise to the local tax authorities which following examination and verification shall be reported level-by-level to the State Tax Bureau for approval. Fixed assets which for special reasons as mentioned in the preceding paragraph require the useful life to be shortened include: (1) machinery and equipment subject to strong corrosion by acid or alkali and factory buildings and structures subject to constant shaking and vibration; (2) machinery and equipment operated continually year-round for the purpose of raising the utilization rate or increasing the intensity of use; (3) fixed assets of a Chinese-foreign contractual joint venture having a period of cooperation shorter than the useful life specified in Article 35 of these Rules and which will be left with the Chinese party upon termination of the cooperation. Article 41 Enterprises which acquire used fixed assets having a remaining useful life shorter than the useful life specified in Article 35 of these Rules may, following agreement by the local tax authorities after examination and verification of certifying documents so submitted, compute depreciation according to the remaining useful life. Article 42 Where expenditures incur during the course of the use of fixed assets due to increased value caused by expansion, replacement, reconstruction and technical innovation of fixed assets, the original value of fixed assets shall be increased; where the period of use of fixed assets can be extended, the useful life shall be appropriately extended and the computation of depreciation adjusted accordingly. Article 43 No further depreciation shall be allowed in respect of fixed assets which can be continued to be used after having been fully depreciated. Article 44 The balance of proceeds from the transfer or disposal of fixed assets by an enterprise shall, after deduction of the undepreciated amount or the salvage value and handling fees, be entered into the profit and loss account for the current year. Article 45 Depreciation of fixed assets received as gifts by enterprises may be computed on the basis of reasonable valuation. Article 46 Patents, proprietary technology, trademarks, copyrights, land-use rights and other intangible assets of enterprises shall be

appraised on the basis of the original value. For alienated intangible assets, the original value shall be the actual amount paid based on a reasonable price. For self-developed intangible assets, the original value shall be the actual amount of expenditure incurred in the course of development. For intangible assets used as investment, the original value shall be such reasonable price as is stipulated in the agreement or contract.

Article 47 The amortization of intangible assets shall be computed using the straight-line method. Intangible assets transferred or assigned or used as investments, where the useful life is stipulated in the agreement or contract, may be amortized over the period of that useful life; the amortization period in respect of intangible assets for which no useful life has been stipulated or which have been developed internally shall not be less than ten years.

Article 48 Reasonable exploration expenses incurred by enterprises engaged in the exploitation of petroleum resources may be amortized against income from oil (gas) fields that have already commenced commercial production. The amortization period shall not be less than one year. Where operation of a contract field owned by a foreign oil company is terminated due to failure to find commercially viable oil (gas), and where ownership of the contract for the exploitation of petroleum (gas) resources is not continued and management organizations or offices for carrying on operations for the exploitation of petroleum (gas) resources are no longer maintained in China, reasonable exploration expenses already incurred in respect of the terminated contract field shall, upon examination and confirmation and the issuance of certification by the tax authorities, be permitted to be amortized against production income of a newly owned contract field when the new contract for cooperative exploitation of oil (gas) resources is signed within ten years from the date of the termination of the old contract.

Article 49 Expenses incurred by enterprises during the period of organization shall be amortized beginning with the month following the month in which production and business operations commence; the period of amortization shall not be less than five years. The period of organization mentioned in the preceding paragraph means the period from the date of approval of the organization of the enterprise to the date of commencement of production and business operations (including trial production and trial business operations).

Article 50 Inventories of merchandise, finished products, goods in process, semi-finished products, raw materials, and other such materials of enterprises shall be valued at cost.

Article 51 Enterprises may choose one of the following such methods: first-in, first-out, moving average, weighted average or last-in, first-out as the method of computing actual costs in respect of the delivery or receipt and use of goods in stock. Once a method of valuation has been adopted for use, no change shall be made thereto. Where a change in the method of valuation is indeed necessary, the matter shall be reported to the local tax authorities for approval prior to the commencement of the next tax year.

Chapter IV Business Dealings Between Associated Enterprises

Article 52 "Associated enterprises" mentioned in Article 13 of the Tax Law refers to companies, enterprises and other economic units that have any of the following relationships with other enterprises: (1) relationships in respect of existing direct or indirect ownership of or control over such matters as finances, business operations or purchases and sales; (2) direct or indirect ownership of or control over it and another by a third party; (3) any other relationship in respect of an association of reciprocal interests.

Article 53 "Business transactions between independent enterprises" mentioned in Article 13 of the Tax Law means business dealings carried out between unassociated and unrelated enterprises on the basis of arm's length prices and common business practices. Enterprises have a duty to provide to the local tax authorities relevant materials such as standard prices and charges in respect of business dealings with their associated enterprises.

Article 54 Where prices in respect of purchase and sales transactions between an enterprise and its associated enterprises are not based on independent business dealings, adjustments may be made thereto by the local tax authorities according to the following arrangements and methods of determination: (1) based on prices of the same or similar business activities between independent enterprises; (2) based on the level of profits obtained from resales in respect of unassociated and unrelated third party prices; (3) based on costs plus reasonable expenses and profit margin; (4) based on any other reasonable method.

Article 55 Where interest paid or received in respect of accommodating financing between an enterprise and an associated enterprise exceeds or is lower than the amount that would be agreed upon by unassociated and unrelated parties, or where the rate of interest exceeds or is lower than the normal rate of interest in respect of similar business, adjustments may be made thereto by the local tax authorities with reference to normal rates of interest.

Article 56 Where labour service fees paid or received in respect of the provision of labour services by an enterprise to an associated enterprise are not based on business dealings between independent enterprises, adjustments may be made thereto by the local tax authorities with reference to the normal fee standards of similar labour activities.

Article 57 Where the valuation or the receipt or payment of usage fees in respect of such business dealings as the transfer of property or the granting of rights to the use of property between an enterprise and an associated enterprise is

not based on business dealings between independent enterprises, adjustments may be made thereto by the local tax authorities with reference to amounts that would be agreed to by unassociated and unrelated parties. Article 58 Management fees paid by an enterprise to an associated enterprise shall not be expensed. Chapter V Withholding at Source Article 59 "Taxable income on profits, interest, rents, royalties and other income" mentioned in Article 19, paragraph 1 of the Tax Law shall, except as otherwise stipulated by the State, be computed on the basis of gross income. Gross royalties obtained from the provision of patents and proprietary technology include fees for blueprint materials, technical services and personnel training, as well as other related fees. Article 60 "Profits" mentioned in Article 19 of the Tax Law means income derived from the right to profits according to the proportion of investment, equity rights, stockholding, or other non-debt profit sharing rights. Article 61 "Other income" mentioned in Article 19 of the Tax Law includes gains from the transfer of property such as houses, buildings and structures and attached facilities within China and land-use rights. "Gains" mentioned in the preceding paragraph means the amount remaining from the receipt on transfer minus the original value of the property. Where foreign enterprises are unable to provide correct certification of the original value of the property, the original value of the property shall be determined by the local tax authorities according to the specific circumstances thereof. Article 62 "The amount of payment" mentioned in Article 19, paragraph 2 of the Tax Law means cash payments, payment by remittances, and amounts paid by account transfers, as well as amounts in equivalent cash value paid in noncash assets or rights and interests. Article 63 "Profits obtained from an enterprise with foreign investment" mentioned in Article 19, paragraph 3, subparagraph (1) of the Tax Law means income obtained from profits of an enterprise with foreign investment following the payment or the reduction of or exemption from income tax in accordance with the provisions of the Tax Law. Article 64 "International finance organizations" mentioned in Article 19, paragraph 3, subparagraph (2) of the Tax Law means financial institutions such as the International Monetary Fund, the World Bank, the Asian Development Bank, the International Development Association, and the International Fund for Agricultural Development. Article 65 "Chinese State banks" mentioned in Article 19, paragraph 3, subparagraph (2) and subparagraph (3) of the Tax Law means the People's Bank of China, the Industrial and Commercial Bank of China, the Agricultural Bank of China, the Bank of China, the People's Construction Bank of China, the Bank of Communications of China, the Investment Bank of China, and other financial institutions authorized by the State Council to engage in credit businesses such as foreign exchange deposits and loans. Article 66 The scope of the reduction of or exemption from income tax on royalties provided for in Article 19, paragraph 3, subparagraph (4) of the Tax Law is as follows: (1) royalties received in providing proprietary technology for the development of farming, forestry, animal husbandry and fisheries: (a) technology provided to improve soil and grasslands, develop barren mountainous regions and make full use of natural conditions; (b) technology provided for the supplying of new varieties of animals and plants and for the production of pesticides of high effectiveness and low toxicity; (c) technology provided such as to advance scientific production management in respect of farming, forestry, fisheries and animal husbandry, to preserve the ecological balance, and to strengthen resistance to natural calamities; (2) royalties received in providing proprietary technology for scientific institutions, institutions of higher learning and other scientific research units to conduct or cooperate in carrying out scientific research or scientific experimentation; (3) royalties received in providing proprietary technology for the development of energy resources and expansion of communications and transportation; (4) royalties received in providing proprietary technology in respect of energy conservation and the prevention and control of environmental pollution; (5) royalties received in providing the following proprietary technology in respect of the development of important fields of science and technology: (a) production technology for major and advanced mechanical and electrical equipment; (b) nuclear power technology; (c) production technology for large-scale integrated circuits; (d) production technology for photoelectric integrated circuits, microwave semi-conductors and microwave integrated circuits, and manufacturing technology for microwave electron tubes; (e) manufacturing technology for ultra-high speed computers and microprocessors; (f) optical telecommunications technology; (g) technology for long distance, ultra-high voltage direct current power transmission; and (h) technology for the liquefaction, gasification and comprehensive utilization of coal. Article 67 In respect of income of foreign enterprises engaged in China in construction, installation, assembly, and exploration contracting work, and provision of labour activities such as consulting, management and training, the tax authorities may designate the parties paying the contracted amounts and labour service fees as tax withholding agents. Chapter VI Tax Preferences Article 68 Pursuant to the provisions of Article 6 of the Tax Law, the granting of any necessary preferential treatment in respect of enterprise income tax to enterprises with foreign investment that are encouraged by the State shall be implemented in accordance with the provisions of the relevant laws and administrative rules and regulations of

the State. Article 69 "Special economic zones" mentioned in Article 7, paragraph 1 of the Tax Law means the special economic zones of Shenzhen, Zhuhai, Shantou and Xiamen and the Hainan Special Economic Zone established by law or established upon approval of the State Council; economic and technological development zones mentioned therein means the economic and technological development zones in the coastal port cities established upon approval of the State Council. Article 70 "Coastal economic open zones" mentioned in Article 7, paragraph 2 of the Tax Law means those cities, counties and districts established as coastal economic open zones upon approval of the State Council. Article 71 "Imposition of enterprise income tax at the reduced rate of 15%" mentioned in Article 7, paragraph 1 of the Tax Law shall be limited to income obtained by enterprises from production and business operations in the respective areas so specified in Article 7, paragraph 1 of the Tax Law. "Imposition of enterprise income tax at the reduced rate of 24%" mentioned in Article 7, paragraph 2 of the Tax Law shall be limited to income obtained by enterprises from production and business operations in the respective areas so specified in Article 7, paragraph 2 of the Tax Law. Article 72 "Enterprises with foreign investment of a production nature" mentioned in Article 7, paragraph 1 and paragraph 2 and Article 8, paragraph 1 of the Tax Law means enterprises with foreign investment engaged in the following industries: (1) machine manufacturing and electronics industries; (2) energy resource industries (not including exploitation of oil and natural gas); (3) metallurgical, chemical and building material industries; (4) light industries, and textiles and packaging industries; (5) medical equipment and pharmaceutical industries; (6) agriculture, forestry, animal husbandry, fisheries and water conservation; (7) construction industries; (8) communications and transportation industries (not including passenger transport); (9) development of science and technology, geological survey and industrial information consultancy directly for services in respect of production and services in respect of repair and maintenance of production equipment and precision instruments; (10) other industries as specified by the tax authorities under the State Council. Article 73 "Imposition of enterprise income tax at the reduced rate of 15%" mentioned in Article 7, paragraph 3 of the Tax Law applies to the following: (1) production oriented enterprises with foreign investment established in the coastal economic open zones, special economic zones and in the old urban districts of municipalities where economic and technological development zones are located and which are engaged in the following projects: (a) technology intensive or knowledge intensive projects; (b) projects with foreign investments of over US \$30 million and having long periods for return on investment; (c) energy resource, transportation and port construction projects; (2) Chinese-foreign equity joint ventures engaged in port and dock construction; (3) financial institutions such as foreign capital banks and Chinese foreign banks established in the special economic zones and other areas approved by the State Council, where the capital contribution of the foreign investor or the funds for business activities allocated by the head office bank to the branch bank exceeds US \$10 million, and where the period of operations is ten years or more; (4) production-oriented enterprises with foreign investment established in the Pudong New Area of Shanghai, as well as enterprises with foreign investment engaged in energy resource and transport construction projects such as airports, ports, railways, highways and power stations; (5) enterprises with foreign investment recognized as high or new technology enterprises established in the State high or new technology industrial development zones designated by the State Council, as well as enterprises with foreign investment recognized as new technology enterprises established in the new technology industrial development experimental zone of the municipality of Beijing; (6) enterprises with foreign investment engaged in projects encouraged by the State and established in other areas stipulated by the State Council. Enterprises with foreign investment in projects listed in subparagraph (1) of the preceding paragraph shall, following approval by the State Tax Bureau of an application submitted by such enterprises, be subject to enterprise income tax at the reduced tax rate of 15%. Article 74 "The period of business operations" mentioned in Article 8, paragraph 1 of the Tax Law means the period commencing on the date an enterprise with foreign investment actually begins production or business operations (including trial production and trial business operations) and ending on the date the enterprise ceases production or business operations. Enterprises with foreign investment that pursuant to the provisions of Article 8, paragraph 1 of the Tax Law may enjoy treatment in respect of reductions of or exemptions from enterprise income tax shall submit to the local tax authorities for examination and verification such circumstances as the lines of business in which engaged, names of major products, and the period of operations decided upon. No treatment in respect of reductions of or exemptions from enterprise income tax shall be enjoyed without examination and verification and agreement thereof. Article 75 "The relevant provisions promulgated by the State Council before the entry into force of this Law" mentioned in Article 8, paragraph 2 of the Tax Law means the following provisions in respect of exemptions from or reductions of enterprise income tax promulgated or approved for promulgation by the State Council: (1) Chinese-foreign equity joint ventures

engaged in port and dock construction where the period of operations is 15 years or more shall, following application by the enterprise and approval thereof by the tax authorities of provinces, autonomous regions, or municipalities directly under the Central Government of the location and commencing with the first profit-making year, be exempt from enterprise income tax from the first year to the fifth year and subject to enterprise income tax at a rate reduced by one half for the sixth year through the tenth year. (2) Enterprises with foreign investment established in the Hainan Special Economic Zone and engaged in infrastructure facility projects such as airports, harbours, docks, highways, railways, power stations, coal mines and water conservation, and enterprises with foreign investment engaged in the development of and operations in agriculture where the period of operations is 15 years or more shall, following application by the enterprise and approval thereof by the tax authorities of Hainan Province and commencing with the first profit making year, be exempt from enterprise income tax from the first year to the fifth year and subject to enterprise income tax at a rate reduced by one half for the sixth year through the tenth year. (3) Enterprises with foreign investment established in the Pudong New Area of Shanghai and engaged in construction projects such as airports, ports, railways, highways and power stations where the period of operations is 15 years or more shall, following application by the enterprise and approval thereof by the tax authorities of the municipality of Shanghai and commencing with the first profit making year, be exempt from enterprise income tax from the first year to the fifth year and subject to enterprise income tax at a rate reduced by one half for the sixth year through the tenth year. (4) Enterprises with foreign investment established in the special economic zones and engaged in service oriented industries where the amount of the foreign investment exceeds US \$5 million and the period of operations is ten years or more shall, following application by the enterprise and approval thereof by the tax authorities of the special economic zone and commencing with the first profit making year, be exempt from enterprise income tax in the first year and subject to enterprise income tax at a rate reduced by one half for the second and third years. (5) Financial institutions such as foreign capital banks and Chinese foreign banks established in the special economic zones and other areas approved by the State Council where the capital contribution of the foreign investor or the funds for business activities allocated by the head office bank to the branch bank exceeds US \$10 million and the period of operations is ten years or more shall, following application by the enterprise and approval thereof by the local tax authorities and commencing with the first profit making year, be exempt from enterprise income tax in the first year and subject to enterprise income tax at a rate reduced by one half for the second and third years. (6) Chinese-foreign equity joint ventures recognized as high or new technology enterprises and established in the State high or new technology industrial development zones designated by the State Council where the period of operations is ten years or more shall, following application by the enterprise and approval thereof by the local tax authorities and commencing with the first profit making year, be exempt from enterprise income tax in the first year and second year. Enterprises with foreign investment established in the special economic zones and the economic and technological development zones shall be governed by the preferential tax provisions of the special economic zones and the economic and technological development zones. Enterprises with foreign investment established in the new technology industrial development experimental zone of the municipality of Beijing shall be governed by the preferential tax provisions of the new technology industrial development experimental zone of the municipality of Beijing. (7) 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%. (8) Advanced technology enterprises invested in and operated by foreign businesses which remain advanced technology enterprises after the period of enterprise income tax exemptions or reductions has expired in accordance with the provisions of the Tax Law may continue to pay for an additional three years enterprise income tax at the tax rate specified in the Tax Law reduced by one half. (9) Implementation of other provisions in respect of exemptions from or reductions of enterprise income tax promulgated or approved for promulgation by the State Council. Enterprises with foreign investment shall, in applying for exemptions from or reductions of enterprise income tax in accordance with the provisions of subparagraph (6), subparagraph (7), or subparagraph (8) of the preceding paragraph, submit relevant documents of proof issued by departments in respect of the examination, verification and confirmation, the application shall be subjected to approval by the local tax authorities after examination and verification. Article

76" The first profit-making year" mentioned in Article 8, paragraph 1 of the Tax Law and in Article 75 of these Rules means the first tax year in which profits are obtained by an enterprise following commencement of production or business operations. Where an enterprise suffers losses during the early stages after establishment, such losses may be made up by the income of the following tax year in accordance with the provisions of Article 11 of the Tax Law. The first profit-making year shall be the year in which profits are obtained after such losses are made up. The period for exemptions from or reductions of enterprise income tax specified in the first paragraph of Article 8 of the Tax Law and Article 75 of these Rules shall be computed continuously commencing with the year in which the enterprise begins to make profits. The computation shall not be deferred because of losses incurred in any of the subsequent years. Article 77 Enterprises with foreign investment which commence operations in the middle of a year and earn profits may, where the actual period of operations is less than six months, choose to use the following year as the period in which to begin the computation of tax exemptions or tax reductions; however, income tax shall be paid in accordance with the Tax Law on profits earned during the year. Article 78 Unless otherwise provided by the State Council, the preferential tax provisions of Article 8, paragraph 1 of the Tax Law shall not apply to enterprises engaged in the exploitation of such natural resources as petroleum, natural gas, rare metals and precious metals. Article 79 Enterprises with foreign investment that have received exemptions from or reductions of enterprise income tax pursuant to the provisions of Article 8, paragraph 1 of the Tax Law and Article 75 of these Rules shall, where the actual period of operations is less than the period stipulated therein, except in the case of major losses sustained due to natural disasters or unforeseen accidents, make up the amount of the exemptions from or reductions of enterprise income tax. Article 80 "Direct reinvestment" mentioned in Article 10 of the Tax Law refers to profits received from an enterprise with foreign investment by foreign investor of that enterprise which prior to receipt are directly used to increase registered capital, or which following receipt are directly used to organize another enterprise with foreign investment. Foreign investors shall, in computing the amount of tax refundable in accordance with the provisions of Article 10 of the Tax Law, provide certificates confirming the use of the reinvested profits for the year; the local tax authorities shall adopt any reasonable method for the reckoning and determination thereof where certificates cannot be provided. Foreign investors shall, in respect of the application for a refund of tax, submit within one year of the date of the actual investment of the reinvested amount a record of the reinvested amount and a certificate for the investment period of the increased capital or contributed capital to the tax authorities in the place where the taxes were originally paid. Article 81 "Other preferential provisions of the State Council" mentioned in Article 10 of the Tax Law refers to direct reinvestment in China by foreign investors for the organization and expansion of export oriented enterprises or advanced technology enterprises, as well as profits of foreign investors earned from enterprises established in the Hainan Special Economic Zone that are directly reinvested in the Hainan Special Economic Zone in infrastructure projects and agriculture development enterprises and for which the entire portion of enterprise income tax that has already been paid on the reinvested amount may, in accordance with the provisions of the State Council, be refunded. Foreign investors that apply for a refund of tax on reinvestments in accordance with the provisions of the preceding paragraph shall, in addition to completing the requirements pursuant to Article 80, paragraph 2 and paragraph 3 of these Rules, submit certificates issued by the examining, verifying and confirming departments confirming the organization and expansion of export-oriented enterprises or advanced technology enterprises. Enterprises in which foreign investors have reinvested in respect of the organization or expansion thereof which within three years of commencing production or operations have not achieved the standards in respect of export-oriented enterprises or have not continued to be confirmed as advanced technology enterprises shall repay 60% of the amount of tax refunded. Article 82 "Tax refunds on reinvestments" mentioned in Article 10 of the Tax Law and Article 81, paragraph 1 of these Rules shall be computed according to the following formula: Amount of tax refund = Reinvestment amount / [1 - (originally applicable enterprise income tax rate + local income tax rate)] * originally applicable enterprise income tax rate * tax refund rate Chapter VII Tax Credits Article 83 "Income tax already paid abroad" mentioned in Article 12 of the Tax Law means income tax actually paid abroad by an enterprise with foreign investment on income from sources outside China and does not include taxes paid for which compensation is later received or assumed by other parties. Article 84 "The amount of tax payable computed on income from sources outside China in accordance with the provisions of this Law" mentioned in Article 12 of the Tax Law means the amount of tax payable computed on taxable income arising from income from abroad of enterprises with foreign investment, following the deduction of costs, expenses and losses allowable in accordance with the relevant provisions of the Tax Law and these Rules attributable to that income. The limit of the amount of tax payable that can be deducted shall be computed on a country-by-country basis; the method of computation

is as follows: Credit limit for tax on income derived from sources outside China = Total tax sourced inside and outside China computed in accordance with the Tax Law * Income sourced from a foreign country / Total income sourced inside and outside China. Article 85 Where the amount of income tax actually paid abroad on income from sources from abroad by enterprises with foreign investment is less than the deductible limit resulting from computation based on the provisions of Article 84 of these Rules, the actual amount of income tax paid abroad may be deducted from the amount of tax payable; where the deductible limit is exceeded, the portion in excess shall not be deducted from tax and shall not be itemized as an expense, however, the portion not exceeding the limit thereof may be used as a deduction against following year's taxes; the time limit for such supplemental deductions shall not exceed five years. Article 86 The provisions of Article 83 to Article 85 of these Rules shall apply only to enterprises with foreign investment with head offices established within China. Enterprises with foreign investment that deduct taxes in accordance with the provisions of Article 12 of the Tax Law shall provide the original tax payment certificates signed and issued by the foreign tax authorities in respect of the same year; copies or tax payment certificates of different years shall not be used as tax deduction certificates. Chapter VIII Tax Administration Article 87 Enterprises shall, within 30 days of completing business registration, complete tax registration with the local tax authorities. Enterprises with foreign investment that establish or terminate branch offices outside China shall, within 30 days of the date of establishment or termination thereof, complete with the local tax authorities procedures in respect of tax registration, amendments to the registration, or cancellation of the registration. Enterprises that complete registrations in the preceding paragraph shall, in accordance with the provisions, present relevant documents, licenses and materials. Article 88 Enterprises that undergo important registration changes such as changes of address, restructurings, mergers, spin-offs, terminations, as well as changes in the amount of capital and scope of business shall, within 30 days of the completion of the change in business registration or prior to the cancellation of registration, complete the change in registration or cancellation of registration with the local tax authorities with the relevant documents. Article 89 Foreign enterprises which establish two or more business organizations in China may use one of the selected business organizations in respect of the consolidated filing and payment of income tax. However, the business organization so selected shall meet the following conditions: (1) assumption of supervisory and management responsibility over the business operations of the other respective business organizations; (2) maintenance of complete account records and certificates which accurately reflect the income, cost, expense and profit and loss situations of the respective business organizations. Article 90 In respect of foreign enterprises which in accordance with the provisions of Article 89 of these Rules consolidate the filing and payment of income tax, the business organization so selected thereunder shall submit an application for approval according to the following provisions after examination and verification thereof by the local tax authorities: (1) consolidated filing and payment of income tax in respect of business organizations located in the same province, autonomous region, or municipality directly under the Central Government shall be subject to approval by the tax authorities of the province, autonomous region or municipality directly under the Central Government; (2) consolidated filing and payment of income tax in respect of business organizations located in two or more provinces, autonomous regions, or municipalities directly under the Central Government shall be subject to approval by the State Tax Bureau. Following approval for the filing and payment of tax on a consolidated basis by foreign enterprises, such circumstances as the establishment of additional business organizations, mergers, change of address, termination of operations, or shutdowns shall, prior to such event, be reported to the local tax authorities by the business organization responsible for the filing and payment of tax on a consolidated basis. Any change in respect of the business organization filing and paying tax on a consolidated basis shall be dealt with in accordance with the provisions of the preceding paragraph. Article 91 Where business organizations related to foreign enterprises that file and pay income tax on a consolidated basis apply different tax rates in respect of the payment of tax, the amount of taxable income of the respective business organizations shall be separately computed on a reasonable basis and income tax shall be paid on the basis of the different tax rates. Where the respective business organizations mentioned in the preceding paragraph have losses and profits, tax shall be paid on the profit remaining after the offsetting of losses against profits according to the tax rate applicable to the profitmaking business organization. A business organization which incurs losses shall offset losses using profits of the subsequent year of the business organization; tax shall be paid on the profit remaining after the offsetting of such losses according to the tax rate applicable to the business organization; tax paid on the offsetting amounts shall be based on the tax rate applicable to the business organization that offsets the losses incurred by the other business organization. Article 92 Notwithstanding the provisions of Article 91 of these Rules, where a business organization responsible for filings and payment of tax on a consolidated basis is unable to

compute separately and reasonably the taxable income of the respective business organizations, the local tax authorities may make a reasonable apportionment among the respective business organizations of the gross taxable income based on the proportion of business revenues, the proportion of cost and expenses, the proportion of capital assets, and the proportion of the number of staff or salaries and wages. Article 93 Enterprises with foreign investment which establish branch offices in China shall complete consolidated filings and payment of income tax with reference to the provisions of Article 91 and Article 92 of these Rules. Article 94 Enterprises that pay taxes in advance on a quarterly basis in accordance with the provisions of Article 15 of the Tax Law shall pay in advance on the basis of actual quarterly profits; where difficulty exists in paying in advance on the basis of actual quarterly profits, the advanced quarterly payment of tax may be made according to one fourth of the taxable income of the previous year or any other method approved by the local tax authorities. Article 95 Enterprises, whether realizing profits or losses in a tax year, shall file income tax returns and final statements of account with the local tax authorities within the time limit prescribed in Article 16 of the Tax Law, and unless otherwise provided by the State, shall include when filing the final accounting statement an audit statement of a certified public accountant registered in China. Where, for special reasons, an enterprise cannot file an income tax return and final accounting statement within the period prescribed in the Tax Law, an application shall be submitted within the filing period and, upon approval of the local tax authorities, the filing period may be extended appropriately. Article 96 Final accounting statements submitted by branches or business organizations to head offices or business organizations that file and pay income tax on a consolidated basis, shall be submitted at the same time to the local tax authorities. Article 97 Enterprises that are merged, spun off, or terminated during the year shall, within 60 days of the termination of production or business operations, complete with the local tax authorities procedures for the settlement of any liability for and payment of income tax, with refunds for overpayments or supplementary payments for deficiencies. Article 98 Enterprises which must complete procedures for tax refunds in the case of overpayments of tax may, where income in foreign currency has already been converted into Renminbi according to the foreign exchange rate, convert the amount of the tax in Renminbi to be refunded into foreign currency according to the exchange rate in effect when the tax was originally paid, and then reconvert this amount of foreign currency into Renminbi according to the foreign exchange rate at the date of issuance of the tax refund certificate. Where it is necessary to complete procedures for supplementary tax payments in the case of underpayments of tax, the amount of supplementary tax payments shall be converted into Renminbi according to the foreign exchange rate at the date of issuance of the certificate for supplementary tax payments. Article 99 Enterprises with foreign investment that undergo liquidation shall, prior to the completion of the cancellation of business registration, complete the filing of income tax returns with the local tax authorities. Article 100 Except as otherwise provided by the State, enterprises shall maintain in China accounting vouchers, books and statements that support the correct computation of taxable income. Accounting vouchers, books and statements, and reports of enterprises shall be completed in the Chinese language or completed in both the Chinese language and a foreign language. Enterprises that use electronic computers for purposes of book-keeping shall treat the accounting records in computer storage or in printed form as account books. All records on magnetic tape and diskette that have not been printed out shall be completely retained. Accounting vouchers, books and statements, and reports of enterprises shall be retained for at least 15 years. Article 101 Invoices and certificates of receipts of enterprises shall be subjected to approval by the local tax authorities prior to printing and use. Administrative measures in respect of the printing and use of invoices and certificates of receipts of enterprises shall be formulated by the State Tax Bureau. Article 102 All enterprise income tax returns and certificates of tax payments shall be printed by the State Tax Bureau. Article 103 If the final day of the period for payment of tax and the period for filing of a tax return falls on a Sunday or a legal holiday, the day following the holiday shall be used as the last day of the period. Article 104 Tax authorities may pay withholding agents as specified in Article 19, paragraph 2 of the Tax Law and Article 67 of these Rules a handling fee based on a certain proportion of the amount of tax withheld; the specific methods shall be formulated by the State Tax Bureau. Article 105 Local tax authorities may, according to the seriousness of the case, impose a fine of 5,000 yuan (RMB) or less on taxpayers or withholding agents that refuse to accept examination by the tax authorities in accordance with the relevant provisions or that refuse to pay late payment penalties within the time limit prescribed by the tax authorities. Article 106 The tax authorities may, according to the seriousness of the case, impose a fine of 5,000 yuan (RMB) or less on an enterprise which violates the provisions of Article 87; Article 90, paragraph 2; Article 95; Article 96; Article 97; Article 99; Article 100 and Article 101 of these Rules. Article 107 "Tax evasion" mentioned in Article 25 of the Tax Law means the illegal actions of a taxpayer who has intentionally violated the provisions of the Tax Law such as by: falsifying, altering or destroying account books,

receipts or accounting vouchers; falsely itemizing or overstating costs and expenses; concealing or understating taxable income or receipts; or avoiding taxes or fraudulently recovering taxes already paid. Article 108 The tax authorities shall, in punishing taxpayers or withholding agents in accordance with the provisions of the Tax Law and these Rules, serve notice of contravention. Article 109 Any entity or individual shall have the right to report a failure to comply with the Tax Law and the violators thereof. The tax authorities shall maintain confidentiality for informants and award them in accordance with the relevant provisions herein. Chapter IX Supplementary Provisions Article 110 Enterprises with foreign investment which completed business registration prior to the promulgation of the Tax Law may, in respect of the payment of income tax in accordance with the provisions of the Tax Law and where the liability for tax is higher than that prior to the entry into force of the Tax Law, use the original applicable tax rate during the approved period of operations. Where there is no established period of operations, income tax may be paid using the original applicable tax rate for five years commencing on the date of the entry into force of the Tax Law. However, in respect of the above-mentioned period, if during a tax year the tax liability is higher than that stipulated in the Tax Law, income tax shall be paid commencing with that tax year according to the tax rate stipulated in the Tax Law. Article 111 Preferential treatment in terms of exemptions from and reductions of enterprise income tax enjoyed pursuant to the laws and administrative rules and regulations prior to the entry into force of the Tax Law by enterprises with foreign investment which completed business registration prior to the promulgation of the Tax Law may continue to remain in effect until the termination of the period of exemptions and reductions. Enterprises with foreign investment which completed business registration prior to the promulgation of the Tax Law but which have not earned profits or have earned profits for less than five years may, in accordance with the provisions of Article 8, paragraph 1 of the Tax Law, be granted a corresponding period of treatment in respect of exemptions from or reductions of enterprise income tax. Article 112 Enterprises with foreign investment which completed business registration after the promulgation of the Tax Law but prior to the entry into force of the Tax Law may refer to the provisions of Article 110 and Article 111 of these Rules for implementation herein. Article 113 The Ministry of Finance and the State Tax Bureau shall be responsible for the interpretation of these Rules. Article 114 These Rules shall come into force on the effective date of the Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises. The Rules for the Implementation of the Income Tax Law of the People's Republic of China on Chinese-foreign Equity Joint Ventures and the Rules for the Implementation of the Income Tax Law of the People's Republic of China on Foreign Enterprises shall be abrogated at the same time.

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BEFORE THE
INTERNATIONAL TRADE ADMINISTRATION
UNITED STATES DEPARTMENT OF COMMERCE
AND THE
UNITED STATES INTERNATIONAL TRADE COMMISSION

In the Matter of)

ALUMINUM EXTRUSIONS FROM)
THE PEOPLE'S REPUBLIC OF)
CHINA)

PETITION FOR THE IMPOSITION
OF ANTIDUMPING AND
COUNTERVAILING DUTIES

VOLUME III: COUNTERVAILING DUTY ALLEGATIONS

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- EXHIBIT III-57** Questions from the United States to China concerning Subsidies and Price Controls under the WTO Transitional Review Mechanism
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- EXHIBIT III-66** *Implementation Rules of the Income Tax Law of the People's Republic of China of Foreign Investment Enterprises*
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- EXHIBIT III-80** *Administrative Measures on Enterprise Income Tax Credits for Purchase of Domestic Equipment by FIEs and Foreign Enterprises*
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- EXHIBIT III-82** China's Notification to the World Trade Organization Pursuant to Article XVI:1 of the GATT 1994 and Article 25 of the Agreement on Subsidies and Countervailing Measures
- EXHIBIT III-83** Profile of Asia Aluminum (China) Co., Ltd.
- EXHIBIT III-84** *Catalogue of High and New Technology Products*
- EXHIBIT III-85** Kam Kiu Aluminum Extrusion Co. Was Designated as 'Guangdong Provincial Export Famous Brand,' *China Aluminum Net*
- EXHIBIT III-86** *Notification on Providing Transitional Preferential Tax Treatments to High-tech Enterprises Newly Set up in Special Economic Zones and in Pudong New District of Shanghai*
- EXHIBIT III-87** *Regulations for Implementation of the Enterprise Income Tax Law*
- EXHIBIT III-88** *Administrative Measures Governing the Recognition of High or New Technology Enterprises*
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- EXHIBIT III-90** *Circular on Certain Issues Regarding Expenses on Research and Development to Be Offset from Taxable Income of FIEs*
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- EXHIBIT III-102** *Circular Concerning the Adjustment in the Taxation Policy of Import Equipment*
- EXHIBIT III-103** Xingfa Company Website Printout
- EXHIBIT III-104** *Interim Administrative Measures on Purchase of Domestic Equipment by Projects with Foreign Investment*
- EXHIBIT III-105** Introduction to Zhaoqing, Zhaoqing Government
- EXHIBIT III-106** *Circular of the Administrative Measures on the State Key Technology Renovation Projects and the Administrative Measures on Special Fund Generated by Treasury Bonds for the State Key Technology Renovation Projects*
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I. NAME OF THE COUNTRY IN WHICH THE SUBJECT MERCHANDISE IS MANUFACTURED OR PRODUCED

The name of the country in which the subject merchandise is manufactured or produced is the People's Republic of China ("China").

II. ALUMINUM EXTRUSION IMPORTS FROM CHINA ARE BENEFITTING FROM COUNTERAVAILABLE SUBSIDIES

For several years, exports of aluminum products from China have been disrupting markets around the world. Chinese aluminum products other than extrusions have been subject to trade remedy investigations in at least Argentina (aluminum phosphide),¹ Europe (foil and wheels),² India (sheets, foil, wheels),³ and South Africa (hollowware).⁴ In addition, both Canada and Australia have investigated the dumping and subsidization of aluminum extrusions from China. Canada found that aluminum extrusions exported to Canada were subsidized at an estimated weighted average amount of 47 percent *ad valorem*.⁵ The Australian authorities have

¹ "Argentina launches antidumping against aluminum phosphide," *China Chemical Reporter* (Feb. 2003), **Exhibit III-1**.

² "EU imposes anti-dumping tariffs on Chinese aluminum foil," *People's Daily Online* (Sept. 24, 2009), **Exhibit III-2**; "EU to launch anti-dumping investigations on China Aluminum Alloy Wheel," *Dow Jones* (Aug. 7, 2009), **Exhibit III-3**.

³ "India slaps safeguard duties on Chinese aluminum, soda ash," *domain-b.com* (Mar. 16, 2009), **Exhibit III-4**; "China-Made Wheels Under Ministry Scanner," *Financial Express* (Nov. 9, 2006), **Exhibit III-5**.

⁴ South Africa Government Gazette (June 29, 2007), **Exhibit III-6**.

⁵ See Canadian Border Services Agency, Statement of Reasons concerning the making of final determinations with respect to the dumping and subsidizing of *Certain Aluminum Extrusions Originating in or exported from the People's Republic of China* (Mar. 3, 2009) ("Canadian Statement of Reasons"), **Exhibit III-7**.

preliminarily found that Chinese aluminum extrusion exports to Australia are subsidized at rates of up to 9.2 percent *ad valorem*.⁶

As chronicled in the findings of the governments of Canada and Australia, and as set forth below, the Government of China ("GOC") maintains an extensive support system for aluminum extruders. The resulting subsidies are so great that Chinese extrusions often can be purchased for less than the cost of the aluminum that they contain. These abnormally low prices are not the result of the invisible hand but rather the GOC's thumb on the scale. In light of this extensive subsidization, the Department should initiate an investigation of subsidies benefitting Chinese producers and exporters of aluminum extrusions as quickly as possible.

The Department should note that for purposes of 19 C.F.R. § 351.524(d)(2), the average useful life of renewable physical assets in the aluminium extrusion industry is twelve years.⁷ Accordingly, assuming that the appropriate period of investigation ("POI") is calendar year 2009, Petitioners respectfully request the Department investigate any allocable, non-recurring subsidies granted during the period 1998 through 2009, and any outstanding loans or recurring subsidies provided during the presumptive POI.

III. NAMES AND ADDRESSES OF CHINESE ALUMINIUM EXTRUSION PRODUCERS AND EXPORTERS BELIEVED TO BENEFIT FROM COUNTERAVAILABLE SUBSIDIES

Petitioners have identified numerous Chinese producers or exporters of aluminum extrusions that Petitioners believe benefit from countervailable subsidies provided by national, provincial, and local governments in China. The names and contact information for these

⁶ Australian Customs and Border Protection Service, *Review of Preliminary Dumping and Subsidy Margins For Exporters Selected For Further Investigation* (Jan. 21 2010) ("Australia Preliminary Determination"), **Exhibit III-8**.

⁷ See Internal Revenue Service, "How to Depreciate Property" (2009), **Exhibit III-9**.

companies are listed in **Exhibit I-8**. The information provided represents the information reasonably available to Petitioners. Petitioners have been unable to obtain information regarding the proportion of total exports to the United States for individual producers during the most recent 12-month period.

IV. BACKGROUND ON CHINESE GOVERNMENT DIRECTION OF THE DEVELOPMENT AND EXPANSION OF CHINA'S ALUMINUM AND ALUMINUM EXTRUSION INDUSTRIES

China's rapid growth in aluminum extrusion exports can be traced to several policies enacted by the GOC. China's five-year plans, for example, set out the nation's broadest economic and industrial goals.⁸ As the Department has explained, "{i}n its five-year plans, China decides well in advance on the aggregate, economywide {sic} amount of investment that will be made over the period and locations to specific industries and sectors."⁹ The five-year plans identify favored industries, enumerate the types of preferences to be provided to such industries, establish production targets, and in many instances identify individual enterprises for special treatment.¹⁰ Issued by elite planning agencies with input from the highest levels of the Communist Party, the plans serve as economic and industrial instructions for the GOC's

⁸ See generally *Memorandum from Shauna Lee-Alaia and Lawrence Norton to Assistant Secretary David Spooner* (Mar. 29, 2007) at 9, **Exhibit III-10** ("Instead of directly allocating all financial resources in the economy, the PRC central and local government's primary levers of economic and financial control lie in its use of administrative measures (which allow for *ad hoc* discretionary policy implementation), five-year plans and industrial policies which may serve as guidance for lending and growth, and decentralized (local) control over the banking sectors").

⁹ Department of Commerce Report to the President—Global Steel Trade (2000) at 147, **Exhibit III-11**.

¹⁰ See "New Five-Year Plan Called 'Revolutionary,'" *Asia Times Online* (Oct. 13, 2005), **Exhibit III-12**; see also *Report of the Working Party on the Accession of the People's Republic of China to the World Trade Organization*, WT/MIN(01)3 (Nov. 10, 2001) at paras. 171-176, **Exhibit III-13**.

operating units, including provincial planning agencies, local governments, banks, and SOEs, all of which are beholden to the requirements of the plans.¹¹

China's *National Economic and Social Development 10th Five-Year Plan* (the "*10th Five-Year Plan*") established the development of alumina as a national objective and first step in the promotion of the aluminum and aluminum products industries generally.¹² To implement this and other policies contained in the *10th Five-Year Plan*, the GOC announced that it would "comprehensively utilize planning, fiscal, financing and other means, exert the functions of pricing, taxation, interest rate, exchange rate and other levers, and strengthen and improve the macro control."¹³

By the end of the *10th Five Year Plan* in 2005, China was the largest producer of aluminum in the world.¹⁴ In light of this success, the focus of the *National Economic and Social Development 11th Five-Year Plan* (the "*11th Five-Year Plan*") turned to upgrading industrial and product structures to increase industry competitiveness during the period 2006-2010. Toward this end, the GOC announced in the plan that it would "{c}ontrol the total quantity of electrolytic aluminum, moderately develop alumina, encourage the development of aluminum deep processing and new types of alloy material, and enhance the comprehensive utilization level of

¹¹ GOC guidance to industries has a history of remarkable effectiveness. See generally WTO, Trade Policy Review Body, *Trade Policy Review*, Report by the Secretariat, People's Republic of China, WT/TPR/S/161 (Feb. 28, 2006) at xiii-xiv, **Exhibit III-14**.

¹² See *10th Five-Year Plan*, **Exhibit III-15**.

¹³ See *id.*

¹⁴ See "China Becomes Largest Aluminum Producer and Consumer in the World," *Liaoning Daily* (Jul. 11, 2007), **Exhibit III-16**.

aluminum industrial resources.”¹⁵ The GOC also called for the development of several secondary aluminum “enterprises with annual production capacities of more than 300,000 tons”¹⁶ and specifically identified the manufacture of aluminum extrusion products as “encouraged.”¹⁷ The 11th Five-Year Plan further provided that the GOC would use various economic means including taxation, credit, and land to promote the development of the aluminum industry.¹⁸

National level five-year plans cover the economy of China as a whole and are often general in nature. Additional details are provided in derivative plans for specific jurisdictions and industries. There are several additional industrial policies and pronouncements relevant to the production and sale of aluminum extrusion products. For example, the *Circular of the State Development Planning Commission on Printing and Distributing 10th Five-Year Development Guidelines for Aluminum Industry of China* (the “10th Five-Year Development Guidelines for Aluminum Industry”)¹⁹ declared that the GOC would:

Accelerate the strategic adjustment and reorganization of the aluminum industry, and via the development and structure adjustment, increase the overall operating quality of the aluminum industry.²⁰

¹⁵ See 11th Five-Year Plan, **Exhibit III-17**. The information available to Petitioners indicates that the GOC considers extrusions to be processed aluminum products. See e.g., “Aluminum Exports Slightly Increased at Shandong Port in the Previous Two Months,” *Qingdao Customs Website* (Apr. 11, 2007), **Exhibit III-18**; “Brief Introduction of Aluminum Processing Project,” *Zunyi County Bureau of Investment Promotion Website* (Sep. 5, 2007), **Exhibit III-19**.

¹⁶ See *id.*

¹⁷ See *id.*

¹⁸ See *id.*

¹⁹ The State Development Planning Commission is the predecessor of the National Development and Reform Commission.

²⁰ See 10th Five-Year Development Guidelines for Aluminum Industry (Sep. 11, 2001), **Exhibit III-20**.

The plan also encouraged the production of processed aluminum products.²¹

The GOC announced additional policies for the aluminum extrusion industry in the *Notice of Guidelines on Accelerating the Adjustment of Aluminum Industry Structure* (the “*Aluminum Industry Structure Notice*”). This document urges the development of high value-added aluminum products, calls for increasing the proportion of aluminum extrusion products relative to total aluminum production, and further singles out aluminum extrusions as among those products eligible for preferences including policy loans.²² The *Aluminum Industry Structure Notice* also calls on financial institutions to allocate credit in conformity with the state’s industrial policies -- that is, to provide policy loans to aluminum extrusion producers.²³ Similarly, the *Special Development Plan for the Aluminum Industry* and the *Industrial Development Policy for the Aluminum Industry* call for cooperation with electricity companies in order to promote the development of processed aluminum products like extrusions.²⁴

The GOC’s issuance of policies relevant to aluminum extruders continued into the presumptive POI with the *Nonferrous Metal Industry Adjustment and Revitalization Plan*. The purpose of this document was to provide additional assistance to the Chinese non-ferrous metal industry during the financial crisis, and to further boost the already rapid development and

²¹ *See id.*

²² *Notice of Guidelines on Accelerating the Adjustment of Aluminum Industry Structure*, Fa Gai Yun Xing (2006) No. 589 (Apr. 11, 2006), **Exhibit III-21**.

²³ *See id.*

²⁴ *See Standing Meeting of the State Council Passes Special Development Policy for the Aluminum Industry and Others* (Sep. 8, 2005), **Exhibit III-22**. The texts of the *Special Development Plan for the Aluminum Industry* and the *Industrial Development Plan for the Aluminum Industry* are not reasonably available to Petitioners. The Department should request that the GOC provide these two plans, because they play an important role in the GOC’s planning to develop the aluminum extrusion industry.

expansion of China's aluminum industry.²⁵ The *Nonferrous Metal Industry Adjustment and Revitalization Plan* provides that the GOC will build between three and five large metal producers by 2011, with the largest ten companies controlling 70 percent of aluminum production in China.²⁶ To accomplish these goals, the GOC stated that it will facilitate mergers and restructurings.²⁷ The plan also states that the GOC will support exports of processed aluminum products through special tax rates, policy loans, interest subsidies, electricity subsidies, and funds for research.²⁸ In addition, the State Council instructs the entities subordinate to it to "enrich and perfect policies and measures, speed up the innovation of systems and mechanisms and fully carry out and implement the industrial adjustment and revitalization plan(s) in a bid to make new breakthrough progress on the basis of raising the quality and efficiency of industrial growth."²⁹

As the Department is aware from its several countervailing duty investigations involving Chinese products, China's five-year plans and other industrial planning documents are implemented at all levels of government. The GOC's administrative system ensures that provincial and local policy goals and objectives are in conformity with the central government's

²⁵ See "State Council Executive Meeting Deliberated to Further Implement the Revitalization Plan for Key Industries," *Xinhua Net* (Feb. 26, 2010), **Exhibit III-23**.

²⁶ See *Wen Jiabao Hosts Standing Meeting to Review Nonferrous Industry and Logistics Industry Plans* (Feb. 25, 2009), **Exhibit III-24**; see also *Nonferrous Metal Industry Adjustment and Revitalization Plan* (May 11, 2009), **Exhibit III-25**.

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.*

policy goals and objectives.³⁰ This is particularly important because local governments have significant influence over banks and use that influence to ensure that the country's industrial plans and programs, including those for the aluminum extrusion industry, are carried out.³¹ For this reason, the Department has considered five-year plans to be "a central government policy or program that local governments adopt and implement."³²

The information available to Petitioners indicates that the GOC's directives to support the aluminum industry generally and aluminum extrusion producers specifically have been implemented by provincial and local officials. For example, the *National Economic and Social Development 11th Five-Year Plan of Liaoning Province* (the "*Liaoning Province 11th Five-Year Plan*") states that the province should develop aluminum products, and that the government will support several key aluminum projects including a project undertaken by Zhongwang.³³ This provincial plan further indicates that support for identified projects will come through special financing opportunities and tax benefits, among other means.³⁴

The *National Economic and Social Development 11th Five-Year Plan of Guangxi Zhuang Autonomous Region* (the "*Guangxi Autonomous Region 11th Five-Year Plan*") calls for the development and expansion of the aluminum industry through economic, legal, and

³⁰ See *Coated Free Sheet Paper From the People's Republic of China: Final Affirmative Countervailing Duty Determination*, 72 Fed. Reg. 60645 (Oct. 25, 2007), Issues and Decision Memo ("*China CFS Paper I&D Memo*") at 53.

³¹ See *Coated Free Sheet Paper From the People's Republic of China: Amended Preliminary Affirmative Countervailing Duty Determination*, 72 Fed. Reg. 17484 (Apr. 9, 2007) ("*China CFS Paper Preliminary Determination*") at 17493.

³² See *China CFS Paper Preliminary Determination* at 17492.

³³ See *Liaoning Province 11th Five-Year Plan*, **Exhibit III-26**.

³⁴ *Id.*

administrative means, including preferential treatment for financing and land allocation.³⁵ In particular, the *Guangxi Autonomous Region 11th Five-Year Plan* states that the government will “give priorities to develop alumina, reasonably develop electrolytic aluminum, and actively develop aluminum deep processing,” and further build aluminum “production bases.”³⁶

It should be clear from the preceding paragraphs that the aluminum industry is particularly encouraged by the GOC, especially with regard to the production of downstream aluminum products. Moreover, the evidence available to Petitioners indicates that, even among the universe of aluminum products, extrusions are particularly favored. The National Department and Reform Commission (“NDRC”), for example, periodically publishes a *Directory Catalogue on Readjustment of Industrial Structure* listing “encouraged” industries (and products) eligible for special government preferences. The most recent version of list, the *Directory Catalogue on Readjustment of Industrial Structure (Version 2005)* (the “*Directory Catalogue on Readjustment*”), identifies several aluminum-related projects as encouraged.³⁷ In particular, the directory specifies two typical uses for aluminum extrusions: railways³⁸ and doors and windows.³⁹

³⁵ See *Guangxi Autonomous Region 11th Five-Year Plan*, **Exhibit III-27**.

³⁶ See *id.*

³⁷ See *Directory Catalogue on Readjustment* (Dec. 2, 2005), **Exhibit III-28**.

³⁸ China’s largest aluminum extrusion producer, Zhongwang, produces aluminum extrusions widely used in railway systems, among other things. See *Profile of China Zhongwang Holdings Limited*, **Exhibit III-29**. The company is one of the few qualified suppliers of such products designated by the Ministry of Railways. *Id.*

³⁹ The Chinese aluminum producer and exporter Kam Kiu is a leading company in designing and producing doors and windows. See “Product Center,” *Kam Kiu Website*, **Exhibit III-30**.

The GOC has in the past invited foreign entities to participate in the growth and development of China's aluminum extrusion industry. In this regard, the NDRC and the Chinese Ministry of Commerce ("MOFCOM") jointly publish the *Catalogue for the Guidance of Foreign Investment Industries*. This catalogue specifies whether certain projects are encouraged, restricted, or prohibited for foreigners.⁴⁰ The GOC's most recent version of the catalogue, the *2007 Catalogue for the Guidance of Foreign Investment Industries*, designates numerous aluminum projects as encouraged, including the manufacture of forged aluminum products, automobile components, and "extrusion moulds of aluminum."

These references to aluminum projects related to extrusion products have a number of consequences in China's industrial planning regime. Among other things, *Decision No. 40 of the State Council on Promulgating and Implementing the "Temporary Provisions on Promoting Industrial Structure Adjustment"* ("Decision No. 40") calls for providing financing and other benefits to the designated projects.⁴¹ *Decision No. 40* is explicit regarding the mandates for all levels of government to assist in the development of China's encouraged industries including the aluminum industry:

The people's governments of all provinces, autonomous regions, and municipalities directly under the Central Government shall take the promotion of industrial structure adjustment as an important reform and development task at present and within a

⁴⁰ See *2007 Catalogue for the Guidance of Foreign Investment Industries* (Oct. 31, 2007), **Exhibit III-31**.

⁴¹ See *Decision No. 40, Exhibit III-32*. The *Catalogue for the Guidance of Foreign Investment Industries* applies to foreign invested enterprises, and the *Directory Catalogue on Readjustment of Industrial Structure* covers all other kinds of enterprises in China. The Department has found that this list of encouraged industries serves as "important basis for guiding investment decisions, and for the governments to administer investment projects." See, e.g., *China CFS Paper I&D Memo* at 52-53; *Certain Oil Country Tubular Goods From the People's Republic of China: Final Affirmative Countervailing Duty Determination*, 74 Fed. Reg. 64045 (Dec. 7, 2009), Issues and Decision Memo ("China OCTG I&D Memo") at 101.

period in the future... lay emphasis on implementation and shall, in accordance with the "Interim Provisions"... formulate specific measures, rationally guide the investment directions, encourage and support the development of advanced production capacities, restrict and eliminate outdated production capacities... All relevant administrative departments shall speed up the formulation and amendment of policies on public finance, taxation, credit, land, import, export, etc., effectively intensify the coordination and cooperation with industrial policies, and further improve and promote the policy system on industrial structure adjustment.⁴²

Taken as a whole, the policies described above demonstrate that the manufacture and sale of aluminum extrusions is especially encouraged by the GOC and, as a result, eligible for a number of subsidy benefits. Given this support, it should be no surprise that annual aluminum extrusion capacity in China tripled between 1997 and 2010, and now stands at nearly 7 million tons.⁴³

V. SUBSIDY PROGRAMS

A. Lending Programs

1. Policy loans to aluminum extrusion producers

The Department has previously found policy lending programs in China to be countervailable.⁴⁴ In particular, the Department has found that where there is a policy for state-owned banks to lend to particular industries, the resulting loans constitute government-provided loans within the meaning of Section 771(5)(D)(i) of the Act.⁴⁵ The Department has also found

⁴² See *Decision No. 40* at Preamble, **Exhibit III-32**.

⁴³ China Strategies LLC, "China's Extrusion Industry" (Sep. 19, 2007), **Exhibit III-33**.

⁴⁴ See e.g., *Coated Free Sheet Paper From the People's Republic of China: Final Affirmative Countervailing Duty Determination*, 72 Fed. Reg. 60645 (Oct. 25, 2007), Issues and Decision Memo ("*China CFS Paper I&D Memo*") at 9-10; *Certain Oil Country Tubular Goods From the People's Republic of China: Final Affirmative Countervailing Duty Determination*, 74 Fed. Reg. 64045 (Dec. 7, 2009), Issues and Decision Memo ("*China OCTG I&D Memo*") at 12.

⁴⁵ *Id.*

that these lending programs are *de jure* specific within the meaning of Section 771(SA)(D)(i) of the Act.⁴⁶ Moreover, the loans provide a benefit to recipients equal to the difference between what the recipient paid on a loan and the amount the recipient would have paid on a comparable commercial loan consistent with Section 771(S)(E)(ii) of the Act.⁴⁷

To determine whether the GOC has a program of policy lending to support a particular industry, “the Department generally looks to whether government plans or other policy directives lay out objectives or goals for developing the industry and call for lending to support objectives or goals. Where such plans or policy directives exist, then we will find a policy lending program that is specific to the named industry (or producers that fall under that industry).”⁴⁸ As detailed above, the GOC maintains numerous plans and policies that call for the support of the Chinese aluminum industry and aluminum extrusion producers specifically.

As one example, the *Notice of Guidelines on Accelerating the Adjustment of Aluminum Industry Structure* was issued by nine central government agencies including the NDRC, the People’s Bank of China, MOFCOM, and the Ministry of Finance (“MOF”). It calls for the development of high value-added processed aluminum products including aluminum extrusions, and further mandates that “financial institutions shall properly allocate credit loans, in conformity of the state’s macro control and industrial policies, as well as the credit loan principles.”⁴⁹

⁴⁶ *Id.*

⁴⁷ *Id.*

⁴⁸ *Citric Acid and Certain Citrate Salts From the People’s Republic of China: Final Affirmative Countervailing Duty Determination*, 74 Fed. Reg. 16836 (Apr. 13, 2009), Issues and Decision Memo (“*China Citric Acid and Citrate Salts I&D Memo*”) at 52-53.

⁴⁹ See *Notice of Guidelines on Accelerating the Adjustment of Aluminum Industry Structure*, Exhibit III-21.

The GOC's more recently issued *Nonferrous Metal Industry Adjustment and Revitalization Plan* also provides that the government should "increase the support to backbone nonferrous enterprises in financing, and provide support in issuance of stocks, enterprise bonds and corporate bonds, and in bank loans, for projects that are in conformity with the industrial policy, environmental protection and land laws and regulations, and investment regulations, and for enterprises that undertake M&A, restructuring, 'going abroad,' and technology reform."⁵⁰

Following the lead of the central authorities, provincial governments have also targeted aluminum extruders for policy loans. For example, the *Industrial Economy Development 11th Five-Year Plan of Liaoning Province* (the "*Liaoning Province Industrial Development Plan*") sets as a government objective the development of processed aluminum products including aluminum extrusions, and offers support for Zhongwang specifically.⁵¹ The plan continues that designated projects and companies should receive loans, interest subsidies, and other benefits.⁵² More subsidies for aluminum extruders in Liaoning Province are discussed in Section V.A.4 below.

One example of the GOC's policy loan program in action relates to Guangxi Baise's Pingguo aluminum facility. The China Development Bank, a declared policy bank, has provided more than 2.6 billion RMB in loans to support the growth of Pingguo's aluminum production

⁵⁰ See *Nonferrous Metal Industry Adjustment and Revitalization Plan*, **Exhibit III-25**. These policy documents further prohibit providing loans to backward manufacturers inconsistent with the GOC's industrial policy, effectively directing loans to producers that the policy favors. See *Notice of Guidelines on Accelerating the Adjustment of Aluminum Industry Structure*, **Exhibit III-21**; see also *Nonferrous Metal Industry Adjustment and Revitalization Plan*, **Exhibit III-25**.

⁵¹ See *Liaoning Province Industrial Development Plan*, **Exhibit III-34**.

⁵² See *id.*

from 1995 to 2007.⁵³ An additional indication of the existence of policy lending for aluminum extrusion producers includes the Agricultural Bank of China entering into a strategic cooperation relationship with Xingfa Aluminum.⁵⁴ Public information also indicates that Asia Aluminum benefited from the GOC's policy lending program. In 2007, for example, seven Chinese banks provided loans totaling approximately 4 billion RMB to the company and, in 2009 the Bank of China and China Construction Bank agreed to provide 6 billion RMB in loans notwithstanding the company's monumental credit default (which will be discussed in greater detail in the Section V.A.2, *infra*).⁵⁵

The evidence available to Petitioners also indicates that the GOC continues to control lending decisions and interest rates in China. In the final determination of *China Citric Acid and Citrate Salts*, the Department stated that

Once we identify government plans or other policy directives laying out objectives or goals for developing or promoting an industry and the plans or directives call for lending to support the objectives or goals, the Department relies upon the analysis undertaken in *CFS Paper from the PRC* to further conclude that national and local government control over the SOCBs results in the loans being a financial contribution by the GOC, and that the relevant loans are provided pursuant to the governmental plans.⁵⁶

⁵³ See *Promoting Sustainable Development of Baise Aluminum Industry with Developing Finance* (Nov. 1, 2007), **Exhibit III-35**.

⁵⁴ See *Agricultural Bank of China Yichun City Branch Services Local Economic Development with Innovative Model* (Feb. 4, 2010), **Exhibit III-36**. The Agricultural Bank of China is 100 percent owned by the GOC and has a policy lending function.

⁵⁵ See "To Prevent Bankruptcy Asia Aluminum Is to Restructure, Bank of China and China Construction Bank Provide 6 Billion Loans," *China Finance Online* (Mar. 16, 2009), **Exhibit III-37**.

⁵⁶ *China Citric Acid and Citrate Salts I&D Memo* at 56.

Among the considerations in *China CFS Paper* was whether the GOC maintains a floor on lending rates and a ceiling on deposit rates for Chinese banks, which indicates that those banks cannot independently price loans or set interest rates on a market basis.⁵⁷ The evidence available to Petitioners shows that the GOC continues to maintain control over the deposit and lending rates in China. The GOC has established, for example, a mechanism for “controlling the cap for deposit rate, and controlling the floor for lending rate.”⁵⁸ Through such mechanisms, the GOC is able to control the interest rates banks charge borrowers. As China’s central bank explains, the deposit and lending interest rates are the retail rates that financial institutions offer to their customers. The benchmark deposit and lending interest rates are published by PBOC, and are an important policy tool.⁵⁹

Because the GOC maintains both a policy to provide financial assistance to China’s aluminum extrusion producers through bank loans, and the means to control the interest rates charged, Petitioners request that the Department find that loans to aluminum extrusion producers from state-owned banks constitute countervailable subsidies.

a) Financial contribution

The provision of loans by banks owned or controlled by the GOC constitutes a direct transfer of funds within the meaning of Section 771(5)(D)(i) of the Act. As the Department noted in *China CFS Paper*, it is the Department’s policy to consider loans provided by declared

⁵⁷ *China CFS Paper I&D Memo* at 68.

⁵⁸ *China Monetary Policy Report (2009 Quarter 2)* at 8, **Exhibit III-38**.

⁵⁹ *China Monetary Policy Report (2008 Quarter 4)* at 12, **Exhibit III-39**.

policy banks such as the China Development Bank as loans provided directly by the government and thus as direct financial contributions under the Act.⁶⁰

In determining whether a loan from a nominally commercial bank in China provides a financial contribution, the Department has examined in past countervailing duty cases the extent to which the Chinese banking sector remains under State control, thus undermining the ability of SOCBs to operate in a commercial fashion, and resulting in a situation where loans are based on government policy rather than on commercial considerations.⁶¹ To determine whether the GOC retains control over its banking sector, the Department relies to a large extent on the level of government ownership.⁶² In the case of China, the four largest nominally commercial banks are essentially all owned by the GOC. State owned shares of China Construction Bank, for example, amount to 58.50 percent.⁶³ State-owned shares of Industrial and Commercial Bank of China and the Bank of China are 70.7 and 70.95 percent, respectively.⁶⁴ The GOC owns 100 percent of the shares in Agricultural Bank of China.⁶⁵

The Department also considers that the legal framework under which China's banking sector operates indicates strong government control.⁶⁶ In this regard, Article 34 of the *Law of the*

⁶⁰ See *China CFS Paper I&D Memo* at 55.

⁶¹ See *China CFS Paper I&D Memo* at 55.

⁶² See *China CFS Paper I&D Memo* at 58.

⁶³ See *2009 Third Quarterly Report of China Construction Bank Corporation* at 4, **Exhibit III-40**.

⁶⁴ See *2009 Third Quarterly Report of Industrial and Commercial Bank of China Ltd.* at 5, **Exhibit III-41**, and *2009 Third Quarterly Report of Bank of China Ltd.* at 5, **Exhibit III-42**.

⁶⁵ See *2008 Annual Report of Agricultural Bank of China Ltd.* at 18, **Exhibit III-43**.

⁶⁶ See *China CFS Paper I&D Memo* at 58.

People's Republic of China on Commercial Banks requires even nominally commercial banks in China to "conduct their business of lending in accordance with the needs of the national economic and social development and under the guidance of the industrial policies of the State."⁶⁷

In *China CFS Paper* and subsequent investigations of Chinese subsidies programs, the Department has found that there is sufficient information to demonstrate pervasive government influence and control over the banks which are owned and/or controlled by the GOC.⁶⁸ Specifically, the Department looked to the fact that China's SOCBs suffer from a legacy of complete state control, the vestiges of which allow for continued government control on lending.⁶⁹ In addition, the Department found that dominant state ownership of these banks enables the GOC to use the SOCBs as policy instruments.⁷⁰ Therefore, the Department concluded that the PRC policy banks and SOCBs should be considered government authorities and loans from these institutions are financial contributions within the meaning of 771(5)(D)(i) of the Act.⁷¹

Petitioners believe that loans from the SOCBs and government policy banks provide a financial contribution to aluminum extrusion producers in China based on the Department's findings in prior countervailing duty investigations on Chinese products, as well as the ample

⁶⁷ See *Law of the People's Republic of China on Commercial Banks (amended on Dec. 27, 2003)*, **Exhibit III-44**.

⁶⁸ See e.g., *China CFS Paper I&D Memo* at 61; *China OCTG I&D Memo* at 96.

⁶⁹ See, *China CFS Paper I&D Memo* at 56.

⁷⁰ See *id.* at 58.

⁷¹ See e.g., *China CFS Paper I&D Memo* at 61; *China OCTG I&D Memo* at 96.

additional evidence presented in this Petition, which shows that the Chinese government has a policy to provide aluminum extrusion producers with below-market loans.

b) Benefit

Pursuant to 19 C.F.R. § 351.505 and Section 771(5)(E)(ii) of the Act, the benefit of any loan from the GOC or a GOC-owned bank is equal to the difference between what the recipient paid on the government-provided loan and the amount the recipient would have paid for a comparable commercial loan that it could actually have obtained on the market.

Petitioners note that pursuant to Article 15 of China's WTO Accession Protocol, the Department may "use methodologies for identifying and measuring the subsidy benefit which take into account the possibility that prevailing terms and conditions in China may not always be available as appropriate benchmarks."⁷² The Department found in *China CFS Paper* that "the GOC's intervention in the banking sector creates significant distortions, even restricting and influencing private and foreign banks within the PRC. Therefore, loans from private and foreign banks in the PRC do not provide a suitable benchmark" for policy lending.⁷³ Consequently, the Department has used an external benchmark computed from the inflation-adjusted interest rates of countries with similar per capita gross national income to the PRC.⁷⁴

c) Specificity

Policy loans to aluminum extrusion producers are specific as a matter of law because, as described above, the GOC has established a comprehensive program to encourage and support the growth of the aluminum industry in China and encourage the production of aluminum

⁷² See *China's WTO Accession Protocol* at art. 15(b), **Exhibit III-45**.

⁷³ *China CFS Paper I&D Memo* at 5-6.

⁷⁴ See e.g., *China CFS Paper I&D Memo* at 6; *China OCTG I&D Memo* at 10.

extrusions. Each of the industrial planning documents identified specifies either the aluminum sector or the aluminum extrusion industry as the beneficiary of the program. In addition, as explained in China's WTO Accession Protocol, loans from Chinese policy banks are by their very nature discretionary and, consequently, specific.⁷⁵ Therefore, the GOC's policy lending program for aluminum extrusion producers is *de jure* specific pursuant to Section 771(5A)(D)(i) of the Act.⁷⁶

2. Debt forgiveness for Asia Aluminum

In 2006, the NDRC announced that it would restructure China's aluminum processing industry so that it would be more competitive.⁷⁷ In prior CVD investigations involving products from China, the Department has found that debt forgiveness provided by the GOC, Chinese policy banks, and SOCBs can constitute a countervailable subsidy.⁷⁸ For example, a countervailable debt forgiveness program exists where the GOC forgives debts in connection with a corporate restructuring or where SOCBs do not enforce debt agreements.⁷⁹

⁷⁵ See Annex 5A to *China's WTO Accession Protocol* at IX, **Exhibit III-45**. Petitioners further note that pursuant to Article 10.2 of China's WTO Accession Protocol, subsidies provided to SOEs are deemed specific if SOEs are the predominant recipients of such subsidies or receive disproportionately large amounts of such subsidies. See *China's WTO Accession Protocol* at art.10.2, **Exhibit III-45**.

⁷⁶ See e.g., *China CFS Paper I&D Memo* at 10; *China OCTG I&D Memo* at 12.

⁷⁷ "China 06 Aluminum Pdt Capacity To Be 11.6M Tons-Official," *Dow Jones Newswire* (Apr. 25, 2006), **Exhibit III-46**.

⁷⁸ See e.g., *Circular Welded Carbon Quality Steel Pipe From the People's Republic of China: Final Affirmative Countervailing Duty Determination*, 73 Fed. Reg. 31966 (June 5, 2008), Issues and Decision Memo ("*China CWP I&D Memo*") at 15-16; *Certain New Pneumatic Off-the-Road Tires From the People's Republic of China: Final Affirmative Countervailing Duty Determination*, 73 Fed. Reg. 40480, Issues and Decision Memo ("*China OTR Tires I&D Memo*") at 15-19; *China OCTG I&D Memo* at 22.

⁷⁹ *OCTG I&D Memo* at 22.

The evidence available to Petitioners indicates that the GOC and its SOCBs have forgiven the debts of certain Chinese aluminum extrusion producers in furtherance of industrial policies calling for the consolidation of the industry. In 2004, for example, Asia Aluminum financed an expansion by issuing nearly \$45 million in senior notes and accepting another \$500 million in additional investments relating to a buyout.⁸⁰ In early 2009, to the surprise of most creditors, the company announced that it would buy back this debt at just a fraction of its face value.⁸¹ The company did not go any formal legal procedure such as bankruptcy -- it simply announced that it would no longer honor its obligations to foreign note holders.

In most circumstances, a debtor's unilateral declaration that it will not repay its obligations results in liquidation of the company with the proceeds paid to creditors. The GOC, however, was adamant that foreign interests would not gain control over the assets of one China's national champions. First, it offered to fund the "buyout" of the bondholders.⁸² After this effort failed, the GOC prevented a foreign entity from purchasing Asia Aluminum for nationalistic reasons. Specifically, in June 2009 Norsk Hydro made a "strong commitment" to buy company's assets, but local government officials informed the foreign company that its bid would not be considered.⁸³ Consequently, the Chinese government permitted the former

⁸⁰ See Peter Stein and Laura Santini, "Asia Debt Holders Squirm," *The Wall Street Journal* (Aug. 25, 2009), **Exhibit III-47**.

⁸¹ See *id.*

⁸² See "Asia Aluminum Will Show Bankruptcy Prospects to Win Investors," *Bloomberg News* (Mar. 2, 2009), **Exhibit III-48**.

⁸³ See Peter Stein, "Norsk Hydro Drops China Bid," *The Wall Street Journal* (June 24, 2009), **Exhibit III-49**.

managers of Asia Aluminum to buy the assets of the company free of the bond obligations at a price lower than that offered by Norsk Hydro through an entity called Golden Concord Pacific.⁸⁴

The circumstances surrounding the creation of a new entity from the ashes of Asia Aluminum indicate that the new entity received a countervailable subsidy. In essence, the local government delivered the assets of Asia Aluminum to the same people who had been running it, and perhaps owned some of it, free of debt owed to foreign interests and thus at a significant discount.⁸⁵ The GOC's actions effectively forgave debt and in the process conferred a benefit on the new entity. The Department has encountered similar fact patterns in other subsidies investigations involving China.⁸⁶ In light of the NDRC's instructions to restructure the aluminum sector, it is likely that this type of debt forgiveness for an aluminum extrusion company was not limited to the example described above.⁸⁷

a) Financial contribution

By allowing the managers of Asia Aluminum to buy the company's assets free of certain obligations and by prohibiting the original debt holders from enforcing their legal rights, the GOC provided a financial contribution in the form of debt forgiveness within the meaning of Section 771(5)(D)(i) of the Act.

⁸⁴ See Peter Stein and Laura Santini, "Asia Debt Holders Squirm," *The Wall Street Journal* (Aug. 25, 2009), **Exhibit III-47**; see also "Asia Aluminum Restructuring Is Expected to Pass Hong Kong Court Today," *P5W Net* (June 25, 2009), **Exhibit III-50**.

⁸⁵ Under the restructuring plan, the new company pays 20 cents on every dollar for the senior notes, and 1 cent on every dollar for the pay-in-kind notes. See Peter Stein and Laura Santini, "Asia Debt Holders Squirm," *The Wall Street Journal* (Aug. 25, 2009), **Exhibit III-45**.

⁸⁶ See *China OTR Tires I&D Memo* at 19.

⁸⁷ See *Nonferrous Metal Industry Adjustment and Revitalization Plan* (May 11, 2009), **Exhibit III-25**.

b) Benefit

In accordance with Section 771(5)(E) of the Act and 19 C.F.R. 351.508(a), debt forgiveness provides a benefit in the amount of debt forgiven. In this case, when the GOC allowed the assets of the company to be sold to the company's managers free of certain obligations, the purchasers received a benefit in the amount of the debt effectively forgiven.

c) Specificity

This debt forgiveness is *de facto* specific under Section 771(5A)(D)(iii)(I) of the Act because it is limited to Asia Aluminum. This program is also specific within the meaning of Section 771(5A)(D)(iii)(IV) in that the government officials exercise discretion in determining whether and how to effectively forgive debt.

3. Debt-to-equity swaps for companies in the aluminum sector

The GOC has long maintained a debt-for-equity swap program to help loss-making enterprises rid themselves of debt.⁸⁸ This program has been examined in several academic studies,⁸⁹ and is relevant to this investigation because a number of companies in the aluminum industry have used it.⁹⁰ For example, China Development Bank and two state-owned asset management corporations traded approximately 3.4 billion of debt owed by Aluminum Corporation of China for equity.⁹¹ The China Development Bank and China Construction Bank

⁸⁸ The World Bank, *China Gets Read for Debt-Equity Swaps*, Exhibit III-51.

⁸⁹ See, e.g., Edward Steinfeld, "China's Program of Debt-Equity Swaps: Government Failure or Market Failure?", Massachusetts Institute of Technology (2001), Exhibit III-52.

⁹⁰ Professor Steinfeld, for example, examines the case of a debt-for-equity swap involving a non-ferrous metal company. See *id.*

⁹¹ See *Profile of Aluminum Corporation of China*, Exhibit III-53.

also traded debt owed by Pinguo Aluminum for equity in the company.⁹² When state-owned or controlled banks such as those identified above trade debt for equity in a failing firm, a countervailable subsidy can result because the equity "investment" is inconsistent with commercial considerations.⁹³

a) Financial contribution

A debt-to-equity swap constitutes a financial contribution under Section 771(5)(D)(i) in that the provision of equity by state-owned and controlled banks and asset management companies constitutes a direct transfer of funds. This program can also provide a financial contribution within the meaning of Section 771(5)(D)(ii) because it involves the forgiveness of debt owed to the government.

b) Benefit

The exchange of non-performing debt for equity in a failing firm confers a benefit under Section 771(5)(E)(i) of the Act. Moreover, under 19 C.F.R. § 351.507, a debt-for-equity swap provides a benefit to the extent that the investment decision is inconsistent with the usual investment practice of private entities in the country where the equity infusion is made. In this case, the purpose of the GOC's program is to assist failing companies by relieving them of debt, indicating that any such swap would not be consistent with normal commercial considerations.

c) Specificity

China's debt-to-equity swap program is *de facto* specific under Section 771(5A)(D)(iii)(I) of the Act because it is limited to a small number of recipients. Clearly, the GOC does not

⁹² See "Pinguo Aluminum Receives 1.5 Billion RMB Debt-to-Equity Swap," *Chinavista Net* (Nov. 19, 1999), **Exhibit III-54**.

⁹³ See, e.g., *Dynamic Random Access Memory "DRAM" Semiconductors from the Republic of Korea* Final Affirmative Countervailing Duty Determination, 68 Fed. Reg. 37122 (June 23, 2003).

forgive the debt of all companies in China but rather carefully selects those it wishes to support through this program. This program is also specific within the meaning of Section 771(SA)(D)(iii)(IV) in that the state-owned or controlled banks and asset management corporations involved exercised discretion in determining which failing companies can utilize the program.

4. Loans and interests subsidies provided pursuant to the Northeast Revitalization Program

In 2003, the GOC established a program to revitalize the industrial base of three Northeastern provinces – Heilongjiang, Jilin, and Liaoning.⁹⁴ This area is often referred to as China's "rust belt" because it contains much of the country's older manufacturing infrastructure. The "Northeast Revitalization Program," as it is called, provides advantages to business located in the provinces designated by the GOC.⁹⁵

As part of its program to revitalize China's rust belt, the GOC established a special purpose bank⁹⁶ to "provide financial support for the revitalization of northeastern China's old heavy industrial hub."⁹⁷ The bank is controlled by the States Council,⁹⁸ and in 2007 was re-

⁹⁴ "China's Old Industrial Base Eyes Bright Future with Ambitious Plan," *People's Daily Online* (Jan. 9, 2004), **Exhibit III-55**; see also *Opinions of the Central Committee of CPC and the State Council on the Implementation of Revitalization Strategy of the Old Industrial Bases in Northeast China*, *Zhong Fa* (2003) No.11, **Exhibit III-56**.

⁹⁵ See *Transitional Review Mechanism Pursuant to Section 18 of the Protocol on the Accession of the People's Republic of China, Questions from the United States to China concerning Subsidies and Price Controls*, G/SCM/Q2/CHN/14 (Sep. 29, 2005) at 2, **Exhibit III-57**.

⁹⁶ "New Bank Set to Revitalize Northeast China," *China Daily* (May 31, 2004), **Exhibit III-58**.

⁹⁷ *Id.*

⁹⁸ *Id.*

named Shengjing Bank.⁹⁹ This special purpose bank has injected billions of dollars into the Northeast region as part of the GOC's plan.¹⁰⁰

Consistent with the overall goals of the Northeast Revitalization Program, the *Liaoning Province 11th Five-Year Plan* designated both the aluminum extrusion industry and its largest producer, Zhongwang, as "key."¹⁰¹ Such designations open the gate to policy loans under the Revitalization Plan.¹⁰² Reports indicate Zhongwang received 80 million RMB in loans with interest subsidies under the program in connection with a technological reform project.¹⁰³ The interest subsidies themselves are substantial -- 9.22 million RMB for 2004 and 2005.¹⁰⁴

The Department has previously investigated loans and interest subsidies provided pursuant to this program but has not, to Petitioners' knowledge, found any respondent that benefitted from this countervailable program.¹⁰⁵ In this case, however, the GOC has admitted

⁹⁹ See "'Northeast Revitalization Bank' Gets Approved, Shengjing Bank Debuts in New Wear," *People's Daily Online* (Mar. 2, 2007), **Exhibit III-59**.

¹⁰⁰ See "Introduction of Shengjing Bank," Shengjing Bank Website, **Exhibit III-60**.

¹⁰¹ See *Liaoning Province 11th Five-Year Plan*, **Exhibit III-26**.

¹⁰² *Id.*

¹⁰³ See "Liaoning Zhongwang Group Aluminum Extrusion Production Line Technological Renovation: Develop High-quality Products, Grasp Market Opportunities," MOFCOM Website (Dec. 29, 2006), **Exhibit III-61**.

¹⁰⁴ See *id.* See "Global Perspective of A Grass-root Enterprise," *Gongkong News* (Jan. 7, 2010), **Exhibit III-62**.

¹⁰⁵ See e.g., *China CWP Pipe I&D Memo* at 18; see also Transitional Review Mechanism Pursuant to Section 18 of the Protocol on the Accession of the People's Republic of China, Questions from the United States to China concerning Subsidies and Price Controls, G/SCM/Q2/CHN/14 (Sep. 29, 2005) at 2, **Exhibit III-57**; see also "China Export-Import Bank Offers Loan of Five Billion to Help Enterprises in Northeast China Go Abroad," MOFCOM Website, (Mar. 29, 2005), **Exhibit III-63**.

that subsidies provided under the Northeast Revitalization Program have facilitated the growth of Zhongwang.¹⁰⁶

a) Financial contribution

As explained in the other lending allegations above, the provision of loans by GOC-owned or controlled banks constitutes a direct transfer of funds within the meaning of Section 771(D)(i) of the Act. Based on the Department's findings in prior investigations and the evidence of GOC policies requiring loans to enterprises in China's Northeast, Petitioners believe that policy loans from GOC-owned and controlled banks provide a financial contribution to aluminum extrusion producers in the three designated provinces. To the extent that the GOC may provide interest subsidies in the form of cash payments, those payments also would qualify as direct financial contributions under Section 771(5)(D)(i) of the Act.

b) Benefit

As described more fully in the sections above, pursuant to 19 C.F.R. § 351.505 and Section 771(5)(E)(ii) of the Act, the benefit from any loan from the GOC or a GOC-owned bank is equal to the difference between what the recipient paid on the government-provided loan and the amount the recipient would have paid for a comparable commercial loan that it could actually have obtained on the market. Moreover, because of the GOC's pervasive interventions in the Chinese financial sector, a commercial loan benchmark can only come from outside of China.¹⁰⁷

c) Specificity

Petitioners allege that this program is specific under Section (5A)(D)(iv) of the Act because, under the terms of the Northeast Revitalization Program, benefits are available only to

¹⁰⁶ See "Global Perspective of A Grass-root Enterprise," *Gongkong News* (Jan. 7, 2010), Exhibit III-62.

¹⁰⁷ See e.g., *China CFS Paper I&D Memo* at 6; *China OCTG I&D Memo* at 10.

companies in a limited geographic area, *i.e.*, the three designated Northeastern provinces. In addition, as explained in China's WTO Accession Protocol, loans from Chinese policy banks are by their very nature discretionary and, consequently, specific.¹⁰⁸

B. Income Tax Programs

I. Tax exemptions and reductions for "productive" FIEs

In order to attract foreign capital to develop designated industrial sectors, the GOC provides a variety of incentives to foreign companies establishing businesses in China. As the Department is aware from its past investigations, companies in China with more than 25 percent foreign investment are known as foreign invested enterprises ("FIEs").¹⁰⁹ During the presumptive POI, these entities were entitled to special tax treatment.

Under Article 8 of the *Foreign Invested Enterprise and Foreign Enterprise Income Tax Law* (the "*FIE Tax Law*"), FIEs that are "productive" and scheduled to operate for not less than 10 years are exempt from income tax in their first two profitable years and pay half of their applicable tax rate for the following three years.¹¹⁰ FIEs are "productive" if they meet the conditions set forth in Article 72 of the *Implementation Rules of the Income Tax Law of the*

¹⁰⁸ See Annex 5A to *China's WTO Accession Protocol* at IX, **Exhibit III-45**. Petitioners also note that pursuant to Article 10.2 of China's WTO Accession Protocol, subsidies provided to SOEs are deemed specific if SOEs are the predominant recipients of such subsidies or receive disproportionately large amounts of such subsidies. See *China's WTO Accession Protocol* at art.10.2, **Exhibit III-45**.

¹⁰⁹ See *China CFS Paper I&D Memo* at 85.

¹¹⁰ See *FIE Tax Law*, **Exhibit III-64**; see also *China Line Pipe I&D Memo* at 12. In March 2007, China's National People's Congress adopted a new tax law, the *Enterprise Income Tax Law of the PRC* (the "*Enterprise Income Tax Law*"), effective January 1, 2008. The new *Enterprise Income Tax Law* unifies the enterprise tax rate for domestic and foreign enterprises at 25 percent, although companies previously enjoying a preferential rate would continue to do so. See *Notification of the State Council on Carrying out the Transition Preferential Policies concerning Enterprise Income Tax*, Guo Fa 2007 No. 39, **Exhibit III-65**.

People's Republic of China of Foreign Investment Enterprises (the "Implementation Rules of the FIE Tax Law").¹¹¹ This provision lists a number of industries, primarily connected to manufacturing, in which FIEs must operate in order to qualify as "productive." This provision includes, *inter alia*, the light industrial and metallurgical industries, and thus Chinese producers of aluminum extrusions.¹¹² The GOC has reported to the Department that if an FIE meets the conditions laid out in the provision, the amount exempted appears on the enterprise's tax return.¹¹³ County-level State Administration of Tax ("SAT") offices administer the program.¹¹⁴

China implemented a new tax regime on January 1, 2008 intended to eliminate the discrepancies between tax rates for domestically-owned companies and FIEs. Notwithstanding this new law, FIE tax subsidies continued into 2009. Article 57 of the new *Enterprise Income Tax Law* grandfathered benefits for FIEs that were entitled to special tax rates under the previous

¹¹¹ See *Implementation Rules of the Income Tax Law of the People's Republic of China of Foreign Investment Enterprises* (June 30, 1991), **Exhibit III-66**; see also *China Line Pipe I&D Memo* at 12.

¹¹² See *id.* Article 72 of the *Implementation Rules of the FIE Tax Law* specifies a list of "productive" enterprises, including "(1) machine manufacturing and electronics industries; (2) energy resource industries (excluding exploitation of oil and natural gas); (3) metallurgical, chemical and building material industries; (4) light industries, and textiles and packaging industries; (5) medical equipment and pharmaceutical industries; (6) agriculture, forestry, animal husbandry, fisheries and water conservation; (7) construction industries; (8) communications and transportation industries (excluding passenger transport); (9) development of science and technology, geological survey and industrial information consultancy directly for services in respect of production and services in respect of repair and maintenance of production equipment and precision instruments; and (10) other industries as specified by the tax authorities under the State Council."

¹¹³ See *id.*

¹¹⁴ See *Countervailing Duty Investigation of Coated Free Sheet from the People's Republic of China*, Questionnaire Response of the Government of China, January 31, 2007 at 49, **Exhibit III-67**.

regime.¹¹⁵ Moreover, the GOC issued separate rules clarifying how it would continue to provide the tax breaks notwithstanding the new law. These rules provide in pertinent part:

Enterprises that have enjoyed preferential tax rates shall be taxed at rates to be increased from the current rate to the full rate under the Enterprise Income Tax Law within a period of 5 years. Among others, the enterprises that have been taxed at 15 percent shall be taxed at 18% in 2008, 20% in 2009, 22% in 2002, 24% in 2011 and 25% in 2012; the enterprises that have been taxed at 24% under the old income tax law shall be taxed at 25% as from 2008.¹¹⁶

As a result, the benefits of this program remained available during the presumptive POI.

Petitioners have developed information indicating that a number of the companies producing aluminum extrusions in China qualify as FIEs and therefore are likely to benefit from this program. For example, certain subsidiaries of Asia Aluminum reported enjoying income tax exemptions and reductions from 2001 to 2005.¹¹⁷ In addition, Zhongwang reports benefitting from his program from 2005 to 2007, leaving several years of potential benefits remaining.¹¹⁸ Further, certain subsidiaries of Xingfa benefited from this program in 2006 and 2007.¹¹⁹ Petitioners believe that Xingfa and its affiliated companies continue to be eligible for tax deductions under this program from 2008 to 2010.¹²⁰ Other aluminum extrusion producers that

¹¹⁵ See *Enterprise Income Tax Law*, **Exhibit III-68**.

¹¹⁶ See *Notification of the State Council on Carrying out the Transition Preferential Policies Concerning Enterprise Income Tax*, Guo Fa 2007 No. 39, **Exhibit III-65**.

¹¹⁷ See Asia Aluminum 2002 Annual Report at 53, **Exhibit III-69**; Asia Aluminum 2003 Annual Report at 59, **Exhibit III-70**; Asia Aluminum 2006 Interim Report at 18, **Exhibit III-71**.

¹¹⁸ See Liaoning Zhongwang Prospectus at I-22, **Exhibit III-72**.

¹¹⁹ See Xingfa Aluminum 2007 Annual Report at 16, **Exhibit III-73**.

¹²⁰ Government publications indicate that FIEs that qualified for preferential tax treatment under the previous Tax Law on Foreign-Invested Enterprises, and that still meet the conditions imposed under the prior Tax Law, remain eligible to receive the preferential treatment.

are FIEs and may benefit from this program include Kam Kiu, Pingguo, and Tai-Ao.¹²¹ This program was found to be countervailable by CBSA in its investigation of aluminum extrusion products from China¹²² and also found to be preliminarily countervailable by Australia.¹²³

a) Financial contribution

The reduction or exemption of income tax for a productive FIE provides a countervailable subsidy. In particular, it provides a financial contribution in the form of revenue foregone by the GOC, consistent with Section 771(5)(D)(ii) of the Act.

b) Benefit

This program provides a benefit to the recipient in the amount of the tax savings from the program. 19 C.F.R. § 351.509(a)(1).

c) Specificity

The program is specific within the meaning of Section 771(5A)(D)(i) of the Act because the exemption/reduction is limited as a matter of law to a group of enterprises or industries, "productive FIEs."

2. Provincial tax exemptions and reductions for "productive" FIEs

Under Article 9 of the *FIE Tax Law*, provincial governments have the authority to grant exemptions or reductions on local income taxes to productive FIEs.¹²⁴ As one example of this

See Circular of the State Administration of Taxation on How to Deal with Related Issues after Cancellation of Several Previous Tax Preferential Policies on Foreign-Invested Enterprises and Foreign Enterprises, Guo Shui Fa 2008 No. 23, Exhibit III-74.

¹²¹ See Zhongwang Prospectus at 80-82, **Exhibit III-72**; An Introduction to Zhaoqing, **Exhibit III-75**; Company Profile of Xingfa Aluminum Co., Ltd., **Exhibit III-76**; Kam Kiu Newsletter (May/June 2005), **Exhibit III-77**; Company Profile of PanAsia Enterprise Group Ltd., **Exhibit III-78**; Company Profile of Taiao Aluminum (Taishan) Co., Ltd., **Exhibit III-79**.

¹²² See *Canadian Statement of Reasons*, **Exhibit III-7**.

¹²³ *Australia Preliminary Determination*, **Exhibit III-8**.

program in action, Article 2 of the *Rules of Exemption and Deduction of Local Income Tax of FIEs in Guangdong Province* exempts "productive" FIEs from provincial income taxes during the period covered by the "Two Free, Three Half" program described above. As indicated above, tax breaks under this program remained available in the presumptive POI notwithstanding changes in the corporate income tax law.¹²⁵

CBSA found this program provided countervailable benefits to producers of aluminum extrusion products in its recent investigation.¹²⁶ Aluminum extrusion producers eligible for this program, based on their status as FIEs that manufacture, include at least Asia Aluminum, Kam Kiu, PanAsia, Tai-Ao, Xingfa and Zhongwang.¹²⁷

a) Financial contribution

An income tax reduction or exemption is a financial contribution in the form of revenue forgone by the government. Section 771(5)(D)(ii) of the Act.

b) Benefit

The exemption provides a benefit to the recipient in the amount of the tax savings pursuant to 19 C.F.R. § 351.509(a)(1).

¹²⁴ See the *FIE Tax Law*, **Exhibit III-64**; see also *Issues and Decision Memorandum for the Final Determination in the Countervailing Duty Investigation of Certain Kitchen Appliance Shelving and Racks from the People's Republic of China* (Jul. 20, 2009) ("Kitchen Shelving I&D Memo") at 12.

¹²⁵ See *Notification of the State Council on Carrying out the Transition Preferential Policies concerning Enterprise Income Tax*, Guo Fa 2007 No. 39, **Exhibit III-65**.

¹²⁶ See CBSA's *Statement of Reasons* at 66, **Exhibit III-7**.

¹²⁷ See An Introduction to Zhaoqing, **Exhibit III-75**; Kam Kiu Newsletter (May/June 2005), **Exhibit III-77**; Company Profile of PanAsia Enterprise Group Ltd., **Exhibit III-78**; Company Profile of Taiiao Aluminum (Taishan) Co., Ltd., **Exhibit III-79**; Company Profile of Xingfa Aluminum Co., Ltd., **Exhibit III-76**; Zhongwang Prospectus at 80-82, **Exhibit III-72**.

c) **Specificity**

The program is specific within the meaning of Section 771(SA)(D)(i) of the Act because the exemption/reduction is limited as a matter of law to certain enterprises, "productive FIEs."

3. Tax reductions for FIEs purchasing Chinese-made equipment

China's tax rules provide certain incentives to FIEs investing in new equipment. In *China CFS Paper*, the Department found that the *Administrative Measures on Enterprise Income Tax Credits for Purchase of Domestic Equipment by FIEs and Foreign Enterprises* and the *Circular of the Ministry of Finance and the State Administration of Taxation on Enterprise Income Tax Credits for Purchase of Domestic Equipment by Foreign Invested Enterprises and Foreign Enterprises* permits FIEs to obtain tax credits of up to 40 percent of the purchase value of domestically-produced equipment in certain circumstances. Specifically, the credit is available to FIEs (and other firms with foreign ownership) engaged in projects which are classified in either the Encouraged or Restricted B categories of the *Catalog of Industrial Guidance for Foreign Investment*. The credit applies to any domestically-produced equipment so long as the equipment is not listed in the *Catalog of Non-Duty-Exemptible Articles of Importation*. The program has been in effect since 1999 and its purpose, according to the GOC, is to attract foreign investment.¹²⁸

To receive a tax credit under this program, the requesting enterprise must submit an application to the local tax authority within two months of purchasing equipment. Once approved, the credit can be claimed on the enterprise's income tax return. The amount of the

¹²⁸ See the *Administrative Measures on Enterprise Income Tax Credits for Purchase of Domestic Equipment by FIEs and Foreign Enterprises*, Guo Shui Fa 2000 No. 90 (May 18, 2000), **Exhibit III-80**; see also *Circular of the Ministry of Finance and the State Administration of Taxation on Enterprise Income Tax Credits for Purchase of Domestic Equipment by Foreign Invested Enterprises and Foreign Enterprises*, (Cai Shui Zi 2000 No. 49) (Jan. 14, 2000), **Exhibit III-81**; *China CFS Paper Preliminary Determination* at 17495.

credit is limited to the lesser of 40 percent of the purchase price of the domestically-produced equipment or the incremental increase in income taxes owed over the previous year.¹²⁹ As indicated above, tax breaks under this program remained available in the presumptive POI notwithstanding changes in the law.¹³⁰

Reasonably available information indicates that several aluminum extrusion producers in China qualify as FIEs. These aluminum extrusion producers include but are not limited to Asia Aluminum, Kam Kiu, PanAsia, Tai-Ao, Xingfa and Zhongwang.¹³¹ Information relating to the equipment purchases of these entities is not reasonably available to Petitioners.

a) Financial contribution

An income tax reduction is a financial contribution in the form of revenue forgone by the government. Section 771(5)(D)(ii) of the Act.

b) Benefit

This program provides a benefit to the recipient in the amount of the tax savings from the program. 19 C.F.R. § 351.509(a)(1).

c) Specificity

The income tax credit is specific under Section 771(5A)(C) of the Act because it is contingent on the use of domestic over imported goods.

¹²⁹ *Id.*

¹³⁰ See Notification of the State Council on Carrying out the Transition Preferential Policies concerning Enterprise Income Tax, Guo Fa 2007 No. 39, **Exhibit III-65**.

¹³¹ See An Introduction to Zhaoqing, **Exhibit III-75**; Kam Kiu Newsletter (May/June 2005), **Exhibit III-77**; Company Profile of PanAsia Enterprise Group Ltd., **Exhibit III-78**; Company Profile of Taiao Aluminum (Taishan) Co., Ltd., **Exhibit III-79**; Company Profile of Xingfa Aluminum Co., Ltd., **Exhibit III-76**; Zhongwang Prospectus at 80-82, **Exhibit III-72**.

4. Tax reductions for FIEs in designated geographic locations

The GOC uses special tax rates to encourage FIEs to locate in designated coastal economic development zones, special economic zones, and economic and technical development zones.¹³² This program was originally created in 1988 under the *Provisional Rules on Exemption and Reduction of Corporate Income Tax and Business Tax of FIEs in Coastal Economic Zone* of the MOF, and it is currently administered under the *FIE Tax Law*, and *Decree 85 of the State Council of 1991* ("Decree 85").¹³³ Under Article 7 of the *FIE Tax Law* and Article 71 of *Decree 85*, "productive" FIEs located in the designated economic zones pay enterprise income tax at a reduced rate of either 15 or 24 percent, depending on the zone.¹³⁴ As indicated above, these benefits continued into the presumptive POI notwithstanding the changes to China's tax regime.¹³⁵

Based on the addresses available to Petitioners, it appears that several producers of aluminum extrusions are located in designated geographical areas and, therefore, eligible to benefit from the tax breaks available under this program.¹³⁶ In particular, Zhongwang reported in its prospectus that the company is located in Liao Yang City, which is a coastal economic

¹³² See *China's Notification Pursuant to Article XVI:1 of the GATT 1994 and Article 25 of the Agreement on Subsidies and Countervailing Measures* at X, G/SCM/N/123/CHN (Apr. 13, 2006) ("*GOC WTO Notification*"), **Exhibit III-82**.

¹³³ See the *FIE Tax Law*, **Exhibit III-64**; see also *Decree 85*, **Exhibit III-66**.

¹³⁴ See *id.*; see also *China CFS Paper I&D Memo* at 11; see also *China Rectangular Pipe and Tube Memo*, at 10-11.

¹³⁵ See *Notification of the State Council on Carrying out the Transition Preferential Policies concerning Enterprise Income Tax*, Guo Fa 2007 No. 39, **Exhibit III-65**.

¹³⁶ See Zhongwang Prospectus at 80-82, **Exhibit III-72**; An Introduction to Zhaoqing, **Exhibit III-75**; Company Profile of Xingfa Aluminum Co., Ltd., **Exhibit III-76**; Kam Kiu Newsletter (May/June 2005), **Exhibit III-77**; Company Profile of PanAsia Enterprise Group Ltd., **Exhibit III-78**; Company Profile of Taiao Aluminum (Taishan) Co., Ltd., **Exhibit III-79**.

open zone.¹³⁷ Xingfa's 2007 Annual Report indicates that Foshan Xingfa Aluminum Profiles Co., Ltd., one of Xingfa's subsidiaries, is located in the coastal economic open zone of Foshan City, and has benefited from this program.¹³⁸ Also, Asia Aluminum (China) Co., Ltd. is located at the Zhaoqing High and New Tech Development Zone in Guangdong Province.¹³⁹ Notably, CBSA found that this program provided countervailable subsidies to aluminum extrusion producers in its recent investigation.¹⁴⁰

a) Financial contribution

An income tax reduction is a financial contribution in the form of revenue forgone by the government. Section 771(5)(D)(ii) of the Act.

b) Benefit

This program provides a benefit to the recipient in the amount of the tax savings under 19 C.F.R. § 351.509(a)(1).

c) Specificity

The income tax credit is specific under Section 771(5A)(D)(iv) of the Act because it is limited to enterprises located in designated geographical regions.

5. Tax reductions for technology or knowledge-intensive FIEs

This subsidy program is available to FIEs that qualify as technology-intensive or knowledge-intensive and have major products listed in the *Catalogue of High and New Technology Products of China* promulgated by the Ministry of Science and Technology

¹³⁷ See Zhongwang Prospectus at 1-22, **Exhibit III-72**.

¹³⁸ See Xingfa Aluminum 2007 Annual Report at 111, **Exhibit III-73**.

¹³⁹ See Company Profile of Asia Aluminum (China) Co., Ltd., **Exhibit III-83**.

¹⁴⁰ See CBSA's *Statement of Reasons* at 60-61, **Exhibit III-7**.

("MOST").¹⁴¹ Article 73 of the *Implementation Rules of the Income Tax Law of the People's Republic of China of Foreign Investment Enterprises* authorizes a reduced income tax rate of 15 percent for "productive" FIEs located in coastal economic zones, special economic zones, or economic and technical development zones if they undertake, among other things, technology-intensive or knowledge-intensive projects.¹⁴² Additionally, FIEs that have been established in zones specified by the State Council and that engage in projects encouraged by the GOC may qualify for the reduced income tax rate of 15 percent upon approval of SAT.¹⁴³ FIEs having qualified products that account for 50 percent or more of total revenue pay a reduced income tax rate of 15 percent.¹⁴⁴ As indicated above, these benefits continued into the presumptive POI notwithstanding the changes to China's tax regime.¹⁴⁵

MOST's catalogue identifies a number of relevant products as eligible for this program including aluminum fibers, alloy plates, and extrusion equipment.¹⁴⁶ Petitioners believe that a number of Chinese aluminum extrusion producers are designated as high-tech enterprises by the

¹⁴¹ See *GOC WTO Notification* at VI, **Exhibit III-82**.

¹⁴² See *Implementation Rules of the Income Tax Law of the People's Republic of China of Foreign Investment Enterprises* (June 30, 1991) ("Decree 85"), **Exhibit III-66**; see also *Citric Acid I&D Memo* at 16.

¹⁴³ *Id.*

¹⁴⁴ *Id.* Petitioners understand that in 2009 China unified the enterprise tax rate and local enterprise tax rate for domestic and foreign enterprises at 25 percent, although companies previously enjoying a preferential rate would continue to do so. See *Notification of the State Council on Carrying out the Transition Preferential Policies concerning Enterprise Income Tax*, Guo Fa 2007 No. 39, **Exhibit III-65**; see also *Enterprise Income Tax Law*, **Exhibit III-68**.

¹⁴⁵ See *Notification of the State Council on Carrying out the Transition Preferential Policies concerning Enterprise Income Tax*, Guo Fa 2007 No. 39, **Exhibit III-65**.

¹⁴⁶ See *Catalogue of High and New Technology Products of China (2006)* ("MOST Catalogue"), **Exhibit III-84**.

GOC and have received benefits under this program.¹⁴⁷ Producers that have been designated as high- and new-technology companies by the relevant authorities include: Kam Kiu, Tai-Ao, Xingfa, and Zhongwang.¹⁴⁸ Consequently, the information available to Petitioners indicates that many Chinese producers and exporters of aluminum extrusions are eligible for this program.

a) Financial contribution

An income tax reduction is a financial contribution in the form of revenue forgone by the government. Section 771(5)(D)(ii) of the Act.

b) Benefit

This program provides a benefit to the recipient in the amount of the tax savings under 19 C.F.R. § 351.509(a)(1).

c) Specificity

The program is specific within the meaning Section 771(5A)(D)(i) of the Act because the exemption/reduction afforded by this program is limited as a matter of law to certain enterprises, "productive FIEs."

6. Tax reductions for FIEs that are also HNTEs

The GOC provides tax benefits to FIEs recognized as high or new technology enterprises ("HNTEs") established in State high or new technology industrial development zones, and for advanced technology enterprises with foreign investment.¹⁴⁹ This program is conducted under

¹⁴⁷ This program was investigated by CBSA. See CBSA's *Statement of Reasons* at 74, **Exhibit III-7**.

¹⁴⁸ See "Kam Kiu Aluminum Extrusion Co. Was Designated as 'Guangdong Provincial Export Famous Brand,'" *China Aluminum Net* (Aug. 20, 2009), **Exhibit III-85**; Company Profile of Tai-Ao Aluminum (Taishan) Co., Ltd, **Exhibit III-79**; Xingfa Aluminum 2007 Annual Report at 111, **Exhibit III-73**; Zhongwang Prospectus at 127, **Exhibit III-72**.

¹⁴⁹ See *GOC WTO Notification* at VIII-IX, **Exhibit III-82**.

the auspices of MOF, SAT, MOFCOM and MOST.¹⁵⁰ As indicated above, these benefits continued into the presumptive POI notwithstanding the changes to China's tax regime.¹⁵¹

China reported to the WTO that the program works as follows: FIEs designated as HNTes established in high or new technology industrial development zones pay income tax at the reduced rate of 15 percent.¹⁵² In addition, Sino-foreign joint ventures scheduled to operate for at least ten years and designated as HNTes established in high or new technology industrial development zones pay no income tax for their first two years of profitability and at half the normal rate for the next three years.¹⁵³ FIEs in high and new technology industrial development zones are also eligible to benefit from additional tax preferences administered by the governments of the zones themselves.¹⁵⁴

As previously reported, several Chinese aluminum extrusion producers have been designated as HNTes and are located in the designated development. These companies include Kam Kiu, Tai-Ao, Xingfa, and Zhongwang.¹⁵⁵ The Department should investigate this and similar programs at the national, provincial, and local levels.

¹⁵⁰ *See id.*

¹⁵¹ *See Notification of the State Council on Carrying out the Transition Preferential Policies concerning Enterprise Income Tax*, Guo Fa 2007 No. 39, **Exhibit III-65**.

¹⁵² *See id.*

¹⁵³ *See id.*

¹⁵⁴ *See id.*

¹⁵⁵ *See* "Kam Kiu Aluminum Extrusion Co. Was Designated as 'Guangdong Provincial Export Famous Brand,'" *China Aluminum Net* (Aug. 20, 2009), **Exhibit III-85**; Company Profile of Tai-Ao Aluminum (Taishan) Co., Ltd, **Exhibit III-79**; Xingfa Aluminum 2007 Annual Report at 111, **Exhibit III-73**; Zhongwang Prospectus at 127, **Exhibit III-72**.

a) Financial contribution

An income tax reduction is a financial contribution in the form of revenue forgone by the government. Section 771(5)(D)(ii) of the Act.

b) Benefit

This program provides a benefit to the recipient in the amount of the tax savings from the program. 19 C.F.R. § 351.509(a)(1).

c) Specificity

The program is specific within the meaning Section 771(5A)(D)(i) of the Act because the exemption/reduction is limited as a matter of law to certain enterprises, in this case FIEs that are also HNTES.

7. Tax reductions for HNTES involved in designated projects

Under China's new tax regime, enterprises that are qualified as HNTES are entitled to a reduced tax rate of 15 instead of 25 percent.¹⁵⁶ Additional tax benefits may also be available to HNTES. For example, *Circular Guofa 2007 No. 40* provides that certain HNTES that locate a special economic zone (*i.e.* Shenzhen, Zhuhai, Shantou, Xiamen or Hainan Special Economic Zone) or in the Pudong New District of Shanghai are exempt from income taxes for the first two years after earning income from production and pay only half of the standard tax rate for the next three years.¹⁵⁷ There are certain additional requirements related to how long a company has been in existence.¹⁵⁸

¹⁵⁶ See *Enterprise Income Tax Law*, **Exhibit III-68**.

¹⁵⁷ See *Notification of the State Council on Providing Transitional Preferential Tax Treatments to High-tech Enterprises Newly Set up in Special Economic Zones and in Pudong New District of Shanghai*, Guo Fa 2007 No. 40, **Exhibit III-86**.

¹⁵⁸ See *Regulations of Implementation of the Enterprise Income Tax Law*, **Exhibit III-87**; see also *Administrative Measures Governing the Recognition of High or New Technology*

Companies must be engaged in certain fields to receive support under this program.¹⁵⁹ There are, however, more than 200 categories of projects that confer eligibility.¹⁶⁰ The projects include the use of certain technologies such as “deep processing technology of alloy materials of aluminum, magnesium and titanium” and “low-cost and high performance processing technology of composite metal materials.” There are additional requirements related to revenue streams, intellectual property rights, and R&D.¹⁶¹

As indicated in the section above, several Chinese aluminum extrusion producers have been designated as having high or new technology, making these companies eligible for tax reductions under this program. These companies include Kam Kiu, Tai-Ao, Xingfa, and Zhongwang.¹⁶²

a) Financial contribution

An income tax exemption or reduction qualifies as financial contribution in the form of revenue forgone by the government. Section 771(5)(D)(ii) of the Act.

b) Benefit

This program provides a benefit to the recipient in the amount of the tax savings from the program. 19 C.F.R. § 351.509(a)(1).

Enterprises, Exhibit III-88; Circular of the State Administration of Taxation on the Issues Concerning Implementation of the Preferential Income Tax for High or New Technology Enterprises, Exhibit III-89.

¹⁵⁹ *See id.*

¹⁶⁰ *See id.*

¹⁶¹ *See id.*

¹⁶² *See* “Kam Kiu Aluminum Extrusion Co. Was Designated as ‘Guangdong Provincial Export Famous Brand,’” *China Aluminum Net* (Aug. 20, 2009), **Exhibit III-85**; Company Profile of Tai-Ao Aluminum (Taishan) Co., Ltd, **Exhibit III-79**; Xingfa Aluminum 2007 Annual Report at 111, **Exhibit III-73**; Zhongwang Prospectus at 127, **Exhibit III-72**.

c) **Specificity**

The program is specific within the meaning Section 771(SA)(D)(i) of the Act because it is limited as a matter of law to only certain enterprises, HNTes.

8. Tax offsets for research and development at FIEs

According to China's 2006 subsidies notification to the WTO, the GOC maintains preferential tax policies for research and development at FIEs. The program is authorized by SAT Circular Guo Shui Fa 1999 No. 173 and is administered by MOF and SAT.¹⁶³ According to China's WTO notification, "the actual expenses of foreign-invested enterprises on research and development conducted in China, which have increased ten per cent or more from the previous year, may be offset by 50 percent from the taxable income of the year."¹⁶⁴ As indicated above, these benefits continued into the presumptive POI notwithstanding the changes to China's tax regime.¹⁶⁵

Petitioners believe that one or more Chinese aluminum extrusion producers may have received tax benefits under this program. Kam Kiu, Tai-Ao, Xingfa, and Zhongwang have all been recognized as high and new technology companies and would therefore appear to be eligible for benefits due to their investments in technology.¹⁶⁶ Consequently, the Department should investigate this and similar programs on the national, provincial, and local levels.¹⁶⁷

¹⁶³ See *GOC WTO Notification* at XXVII, **Exhibit III-82**.

¹⁶⁴ See *id.*

¹⁶⁵ See *Notification of the State Council on Carrying out the Transition Preferential Policies concerning Enterprise Income Tax*, Guo Fa 2007 No. 39, **Exhibit III-65**.

¹⁶⁶ See *Supra* Section B.6.

¹⁶⁷ CBSA recently investigated this program relative to aluminum extrusion producers. See *CBSA's Statement of Reasons* at 74, **Exhibit III-7**.

a) Financial contribution

Pursuant to Section 771(5)(D)(ii) of the Act, income tax offsets constitute financial contributions in the form of revenue forgone by the government.

b) Benefit

This program provides a benefit to the recipient in the amount of the tax savings from the program. 19 C.F.R. § 351.509(a)(1).

c) Specificity

The program is specific within the meaning of Section 771(5A)(D)(i) of the Act because the offset is limited as a matter of law to certain enterprises, *i.e.*, FIEs.¹⁶⁸

9. Tax credits for domestically-owned companies purchasing Chinese-made equipment

According to China's WTO subsidies notification, the GOC offers preferential income tax policies to domestic enterprises if these enterprises upgrade their manufacturing operations with Chinese-made equipment.¹⁶⁹ The notification explains that domestic enterprises which upgrade technology consistent with the GOC industrial policies may deduct 40 percent of the cost of equipment from their next year's income tax obligation.¹⁷⁰ In those circumstances where the income tax due is less than the 40 percent of the cost of the machinery, the remainder of the cost may be deducted in subsequent years, for a period up to five years.¹⁷¹

¹⁶⁸ See SAT's Circular on Certain Issues Regarding Expenses on Research and Development to Be Offset from Taxable Income of FIEs, Guo Shui Fa 1999 No. 173, Exhibit III-90.

¹⁶⁹ See GOC WTO Notification at LIX, Exhibit III-82.

¹⁷⁰ See *id.*

¹⁷¹ See *id.*

During the Department's investigation of welded line pipe, the GOC stated that this program was terminated effective January 1, 2008 pursuant to the *Circular on Relevant Issues with Respect to Ceasing Implementing of Income Tax Credit to Purchase of Domestically Produced Equipment by Enterprises*.¹⁷² The Department should, however, examine whether benefits under this program have actually terminated, were grandfathered, or continue under a new name.¹⁷³ Petitioners respectfully request that the Department investigate whether Chinese-owned producers of aluminum extrusions in China, including but not limited to, Guangdong Fenglu, Guangdong Hao Mei and Shandong Nanshan, benefitted from countervailable subsidies provided under this program in the presumptive POI.

a) Financial contribution

Pursuant to Section 771(5)(D)(ii) of the Act, income tax credits constitute financial contributions in the form of revenue forgone by the government.

b) Benefit

This program provides a benefit to the recipient in the amount of the tax savings from the program. 19 C.F.R. § 351.509(a)(1).

c) Specificity

The income tax credit is deemed specific under Section 771(5A)(C) of the Act because it is contingent upon the use of domestic over imported goods.

¹⁷² *Welded Line Pipe I&D Memo* at 79.

¹⁷³ CBSA investigated this program in its recent inquiry into subsidies conferred on the production and sale of aluminum extrusions. See *CBSA's Statement of Reasons* at 74, **Exhibit III-7**.

10. Tax reductions for export-oriented FIEs

An FIE may continue to pay income tax at half the standard rate following the expiration of the five-year term of the "Two Free, Three Half" program if its exports constitute 70 percent of sales.¹⁷⁴ Export-oriented enterprises in special economic and other specially designated zones already eligible to pay half the standard income tax rate may have their rate further reduced through this program pursuant to the *Rules for the Implementation of the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises*.¹⁷⁵ As indicated above, these benefits continued into the presumptive POI notwithstanding the changes to China's tax regime,¹⁷⁶ and CBSA found this program to be countervailable in its recent investigation.¹⁷⁷

Several Chinese aluminum extrusion producers qualify as FIEs¹⁷⁸ and, to the extent that they satisfy the requisite export levels, likely benefit from this program. For example, Kam Kiu declares that it exports more than 80 percent of its production.¹⁷⁹

¹⁷⁴ See Article 75 of the *Rules for the Implementation of the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises* (the "*Rules for the Implementation of FIE Tax Law*"), **Exhibit III-66**; Article 6 and 8 of the *FIE Tax Law*, **Exhibit III-64**; see also *GOC WTO Notification*, **Exhibit III-82**.

¹⁷⁵ See *Rules for the Implementation of FIE Tax Law*, **Exhibit III-66**.

¹⁷⁶ See *Notification of the State Council on Carrying out the Transition Preferential Policies Concerning Enterprise Income Tax*, Guo Fa 2007 No. 39, **Exhibit III-65**.

¹⁷⁷ See *CBSA's Statement of Reasons* at 65, **Exhibit III-7**.

¹⁷⁸ See Zhongwang Prospectus at 80-82, **Exhibit III-72**; An Introduction to Zhaoqing, **Exhibit III-75**; Company Profile of Xingfa Aluminum Co., Ltd., **Exhibit III-76**; Kam Kiu Newsletter (May/June 2005), **Exhibit III-77**; Company Profile of PanAsia Enterprise Group Ltd., **Exhibit III-78**; Company Profile of Taiao Aluminum (Taishan) Co., Ltd., **Exhibit III-79**.

¹⁷⁹ See *Company Profile of Kam Kiu Aluminum Group*, **Exhibit III-91**.

a) Financial contribution

Pursuant to Section 771(5)(D)(ii) of the Act, tax reductions constitute financial contributions in the form of revenue forgone by the government.

b) Benefit

This program provides a benefit to the recipient in the amount of the tax savings from the program. 19 C.F.R. § 351.509(a)(1).

c) Specificity

This program is deemed specific pursuant to Section 771(5A)(B) of the Act because it is contingent upon export performance.

11. Tax refunds for reinvestment of FIE profits in export-oriented enterprises

FIEs that re-invest profits into the same FIE, or use those profits to establish another FIE (or high-technology company), are eligible for complete refunds of the corporate income tax already paid on the invested amount, so long as the recipient of the investment is export-oriented and scheduled to operate for at least five years. This program is authorized by *The Ministry of Finance and State Administration of Taxation's Notice on Preferential Tax Policies for Supplementary Investment of Foreign Invested Enterprises*¹⁸⁰ and *The State Administration of Taxation's Supplementary Notice on Preferential Tax Policies for Supplementary Investment of*

¹⁸⁰ See *Ministry of Finance and State Administration of Taxation Notice on Preferential Tax Policies for Supplementary Investment of Foreign Invested Enterprises* (June 1, 2002), Exhibit III-92.

Foreign Invested Enterprises.¹⁸¹ As indicated above, these benefits continued into the presumptive POI notwithstanding the changes to China's tax regime.¹⁸²

Aluminum extrusion producers with foreign investment are eligible for this program provided the entities in which they invest meet the export threshold. Given the substantial imports of aluminum extrusions into the United States, and demonstrated export orientation of certain producers,¹⁸³ Petitioners have every reason to believe that some of the companies that are the focus of this Petition benefit from this program.¹⁸⁴

a) Financial contribution

Consistent with Section 771(5)(D)(ii) of the Act, income tax exemptions are financial contributions in the form of revenue forgone by the government.

b) Benefit

This program provides a benefit to the recipient in the amount of the tax savings from the program. 19 C.F.R. § 351.509(a)(1).

c) Specificity

This program is deemed specific because it is contingent upon export performance. Section 771(5A)(B) of the Act.

¹⁸¹ See *Supplementary Circular Concerning the Preferential Policy for Enterprises with Foreign Investment*, Guo Shui Han 2003 No. 368, **Exhibit III-93**.

¹⁸² See *Notification of the State Council on Carrying out the Transition Preferential Policies concerning Enterprise Income Tax*, Guo Fa 2007 No. 39, **Exhibit III-65**.

¹⁸³ See *Company Profile of Kam Kiu Aluminum Group*, **Exhibit III-91**.

¹⁸⁴ See *CBSA's Statement of Reasons at 74*, **Exhibit III-7**.

12. Tax exemptions and reductions for enterprises that utilize recycled materials

As China reported to the WTO, the GOC has implemented a program to assist companies that recycle.¹⁸⁵ The stated policy objective of this program is to “protect the environment and encourage the recycling of resources.”¹⁸⁶ According to the GOC, the authority for this legislation is *MOF Circular Cai Shui Zi No.001 of 1994*, and the program is administered under the auspices of MOF and SAT.¹⁸⁷ Under this program, enterprises that use waste materials (such as scrap) for production are eligible for exemptions or reductions of income tax for five years.¹⁸⁸ For the reasons indicated above, these benefits likely continued into the presumptive POI notwithstanding the changes to China’s tax regime.¹⁸⁹

The information available to Petitioners indicates that aluminum extruders are eligible for this program based on their use of scrap metals in production. For example, Chalco Nanhai Alloy Co., Ltd. reportedly recycles aluminum scrap.¹⁹⁰ The China Nonferrous Metals Industry Association also has indicated that the “Chinese government will continue to support recycling

¹⁸⁵ See *GOC WTO Notification at XIX, Exhibit III-82*.

¹⁸⁶ See *id.*

¹⁸⁷ See *id.*

¹⁸⁸ See *MOF & SAT Circular on Several Preferential Corporate Income Tax Policies, Circular, Cai Shui Zi 1994 No. 001, Exhibit III-94*.

¹⁸⁹ See *Notification of the State Council on Carrying out the Transition Preferential Policies concerning Enterprise Income Tax, Guo Fa 2007 No. 39, Exhibit III-65*.

¹⁹⁰ See “Scraps Recycled into Aluminum Billets to Build Renewable Economy,” *Foshan Daily* (Feb. 3, 2010), *Exhibit III-95*.

businesses and scrap metals."¹⁹¹ The Department should investigate the extent to which this program benefitted producers of the subject merchandise.

a) Financial contribution

Tax exemptions and reductions for enterprises utilizing waste materials qualify as financial contributions in the form of revenue foregone by the GOC under Section 771(5)(D)(ii) of the Act.

b) Benefit

The program provides a benefit to the recipient in the amount of tax savings. 19 C.F.R. § 351.509(a)(1).

c) Specificity

This program is *de facto* specific under Section 771(5A)(D)(iii)(I) of the Act because it is limited to a small number of recipients. This program is also specific within the meaning Section 771(5A)(D)(i) of the Act because the exemptions or reductions it affords are limited as a matter of law to certain enterprises -- those that use waste or recycling materials for production.

13. Accelerated depreciation for enterprises located in the Northeast Region

The Department has previously investigated preferential income tax policies for enterprises located in China's Northeast.¹⁹² Under the Northeast Tax Preference Policy, enterprises located in the Heilongjiang, Jilin, and Liaoning Provinces may:

- Reduce the depreciation life of fixed assets by up to 40 percent for tax purposes, thereby increasing the annual amount of depreciation expense which may be deducted from the company's income tax;¹⁹³ and

¹⁹¹ "China Scrap Metals Output Up Quickly Jan-Sep - Indus," *Worldal.com* (Nov. 17, 2006), **Exhibit III-96**.

¹⁹² See *China OCTG I&D Memo* at 26.

- Shorten the period of amortization of intangible assets by up to 40 percent for tax purposes, resulting in a larger annual tax deduction for amortization expense.¹⁹⁴

As the GOC has emphasized, the Northeast Tax Preference Policy significantly reduces an enterprise's tax liability. The GOC's official news agency, *Xinhua*, reported that tax exemptions granted to the first company to receive benefits under the policy totaled 96.84 million RMB for a single quarter alone.¹⁹⁵

Information concerning the income taxes paid and the tax deductions taken by aluminum extrusion producers located in the Northeast Region is not reasonably available to Petitioners. It is, however, likely that aluminum extrusion producers benefited from the Northeast Tax Preference Policy as a consequence of their involvement in an industry that requires significant investment in plant and machinery, resulting in significant depreciation. For example, Zhongwang is located in the Northeast and reported that during the first half of 2009, its depreciation of its property, plant, and equipment amounted to 161.753 million RMB.¹⁹⁶

a) Financial contrition

The Northeast Tax Preference Policy provides a financial contribution in the form of revenue foregone within the meaning of 771(5)(D)(ii) of the Act. Specifically, the program

¹⁹³ See *Circular of the Ministry of Finance and the State Administration of Taxation on Preferential Enterprise Income Tax Policies for Revitalization of Northeast Old Industrial Bases*, Cai Shui 2004 No.153, **Exhibit III-97**; see also *Circular of the Ministry of Finance and the State Administration of Taxation on the Assets Depreciation and the Implementation Caliber of Amortization Policy in the Northeast Old Industrial Bases*, Cai Shui 2005 No.17, **Exhibit III-98**.

¹⁹⁴ See *id.*

¹⁹⁵ See "Northeast Preferential Enterprise Income Tax Policy Became Effective, First Claimant Got 96.48 million Yuan of Taxes Waived," *Xinhua Net*, (Oct. 22, 2004), **Exhibit III-99**.

¹⁹⁶ See 2009 Interim Report of China Zhongwang Holding Limited at 31, **Exhibit III-100**.

permits a company in the Northeast Region to deduct a larger amount of depreciation and amortization expenses, thereby reducing the company's income tax otherwise due to the government.

b) Benefit

The effect of the Northeast Tax Preference Policy is to lower the tax burden for eligible companies. In this manner, it confers a benefit on the recipient within the meaning of Section 771(S)(E) of the Act.¹⁹⁷

c) Specificity

The subsidies provided by the Northeast Tax Preference Policy are available only to companies located in Heilongjiang, Jilin, and Liaoning Provinces. As a result, such benefits are limited to a designated geographical region within the jurisdiction of the authority providing the subsidy, *i.e.*, the GOC, and are specific under Section 771(5A)(D)(iv) of the Act.

14. Tax forgiveness for enterprises in the Northeast Region

Pursuant to the *Circular of the Ministry of Finance and the State Administration of Taxation on Exempting the Tax Arrears of the Enterprises in Northeast Old Industrial* (the "*Northeast Tax Forgiveness Program*"), the GOC directs provincial and local governments to forgive the tax arrears of enterprises located in China's Northeast.¹⁹⁸ Although the tax returns and payments of potential respondents are not reasonably available to Petitioners, Zhongwang is located in the Northeast region and is therefore eligible for this program.¹⁹⁹

¹⁹⁷ See *Countervailing Duties (Final Rule)*, 63 Fed. Reg. 65348 (Nov. 25, 1998), at 65375-65376.

¹⁹⁸ See *Circular of the Ministry of Finance and the State Administration of Taxation on Exempting the Tax Arrears of the Enterprises in Northeast Old Industrial*, Cai Shui 2006 No.167, **Exhibit III-101**.

¹⁹⁹ See *Company Profile of Liaoning Zhongwang*, **Exhibit III-29**.

a) Financial contribution

The Northeast Tax Forgiveness Program provides a financial contribution under Section 771(5)(D)(ii) of the Act in the form of revenue foregone by the GOC.

b) Benefit

The amount of the benefit from this program is the amount of the tax forgiveness under Section 771(5)(E) of the Act.

c) Specificity

The subsidies provided by the Northeast Tax Forgiveness Program are available only to companies located in the Heilongjiang, Jilin, and Liaoning Provinces in Northeast China. Thus, such subsidies are limited to a designated geographical region within the jurisdiction of the authority providing the subsidy, *i.e.*, the GOC, and are therefore specific within the meaning of Section 771(5A)(D)(iv) of the Act.

C. Other Tax Programs

1. VAT and tariff exemptions on imported equipment

The State Council's *Circular on Adjusting Tax Policies on Imported Equipment* (Guofa No. 37) exempts both FIEs and certain domestic enterprises in encouraged industries from paying VAT and tariffs on imported equipment not for resale.²⁰⁰ The objective of this program is to encourage foreign investment and to introduce advanced equipment from abroad into China and upgrade domestic industrial technology.²⁰¹ The Department has countervailed this program in past investigations.²⁰² This program also was found to be countervailable by both the

²⁰⁰ See *Circular of the State Council Concerning the Adjustment in the Taxation Policy of Import Equipment*, Guo Fa 1997 No. 37, **Exhibit III-102**; see also *CFS I&D Memo* at 13.

²⁰¹ *Id.* See also *GOC WTO Notification* at LX, **Exhibit III-82**.

²⁰² See *e.g.*, *China OTR Tires I&D Memo* at 22-23.

Canadian and Australian authorities in their subsidies investigations of aluminum extrusion products from China.²⁰³

The information reasonably available to Petitioners indicates that a number of companies that produce aluminum extrusions in China, including Asia Aluminum, Kam Kiu, PanAsia, Tai-Ao, Xingfa and Zhongwang, imported foreign-made equipment. For instance, Xingfa states on its website that its workshops and production lines are "armed with first-rate equipments imported from Britain, U.S.A., Switzerland, Italy, and Taiwan."²⁰⁴ Zhongwang's prospectus also indicates that the company's "machinery and equipment are primarily purchased and imported from manufacturers in Japan, Germany, Italy, Switzerland and Spain."²⁰⁵

a) Financial contribution

Import tariff and VAT exemptions provide a financial contribution in the form of revenue foregone by the GOC. Section 771(5)(D)(ii) of the Act.

b) Benefit

This program provides a benefit to the recipient in the form of the tax savings from the program. 19 C.F.R. § 351.510(a)(1).

c) Specificity

The Department has found this program to be specific on a *de facto* basis under Section 771(5A)(D)(iii)(I) of the Act because the actual recipients of the subsidy are limited in

²⁰³ See CBSA's *Statement of Reasons* at 66-67, **Exhibit III-7**; *Australia Preliminary Determination*, **Exhibit III-8**.

²⁰⁴ Xingfa website, **Exhibit III-103**.

²⁰⁵ See Zhongwang Prospectus at 2, **Exhibit III-72**.

number.²⁰⁶ It is also specific because it is essentially limited to FIEs. Section 771(5A)(D)(i) of the Act.

2. VAT rebates on FIE purchases of Chinese-made equipment

As outlined in the *Interim Administrative Measures on Purchase of Domestic Equipment by Projects with Foreign Investment* (the "1999 VAT Measures"), the GOC refunds the VAT on FIE purchases of certain domestically-produced equipment. Article 3 of the *1999 VAT Measures* specifies that this program is limited to FIEs. Article 4 defines the type of equipment eligible for the VAT exemption, which includes equipment falling under the "Encouraged" and "Restricted B" categories listed in the *Notice of the State Council Concerning the Adjustment of Taxation Policies for Imported Equipment* and equipment for projects listed in the *Catalogue of Key Industries, Products and Technologies Encouraged for Development by the State*. VAT rebates on domestically-produced equipment are granted to FIEs upon presentation of documents showing their FIE status.²⁰⁷

Based on publicly-available information, the following Chinese aluminum producers qualify as FIEs: Asia Aluminum, Kam Kiu, PanAsia, Tai-Ao, Xingfa and Zhongwang.²⁰⁸ Because certain producers of aluminum extrusions are likely to have purchased machinery used to manufacture subject merchandise from domestic sources in China, there is a reasonable basis

²⁰⁶ See *China OTR Tires I&D Memo* at 22; see also *China CFS Paper I&D Memo*, at 87-88.

²⁰⁷ See *Interim Administrative Measures on Purchase of Domestic Equipment by Projects with Foreign Investment*, Guo Shui Fa 1999 No. 171, **Exhibit III-104**; see also *Notice of the State Council Concerning the Adjustment of Taxation Policies for Imported Equipment*, 1997 No. 37, **Exhibit III-102**; *China CFS Paper I&D Memo* at 13.

²⁰⁸ See An Introduction to Zhaoqing, **Exhibit III-75**; Kam Kiu Newsletter (May/June 2005), **Exhibit III-77**; Company Profile of PanAsia Enterprise Group Ltd., **Exhibit III-78**; Company Profile of Taiao Aluminum(Taishan) Co., Ltd., **Exhibit III-79**; Company Profile of Xingfa Aluminum Co., Ltd., **Exhibit III-76**; Zhongwang Prospectus at 80-82, **Exhibit III-72**.

to believe that some producers of aluminum extrusions have benefited from the VAT rebate program.²⁰⁹

a) Financial contribution

The VAT refund program for purchases of domestic equipment qualifies as a financial contribution under 19 U.S.C. § 1677(5)(D)(ii) because it involves revenue foregone by the Chinese government.

b) Benefit

This program provides a benefit to the recipient in the form of the tax savings from the program. 19 C.F.R. § 351.510(a)(1).

c) Specificity

The Department has found this program to be specific on a *de facto* basis under Section 771(5A)(D)(iii)(I) of the Act because the actual recipients of the subsidy are limited in number.²¹⁰ It is also specific because it is limited to FIEs. Section 77195A)(D)(i) of the Act.

3. City tax and surcharge exemptions for FIEs

In *Certain Kitchen Shelving and Racks from the People's Republic of China: Final Affirmative Countervailing Duty Determination* ("Kitchen Shelving"), the Department found a program that provides exemptions from city construction and education taxes for FIEs.²¹¹ Pursuant to the *Circular on Temporarily Not Collecting City Maintenance and Construction Tax and Education Fee Surcharge for FIEs and Foreign Enterprises* (Guo Shui Fa 1994 No. 38), the

²⁰⁹ See CBSA's *Statement of Reasons* at 74, **Exhibit III-7**.

²¹⁰ *CFS Paper I&D Memo* at 13.

²¹¹ *Certain Kitchen Shelving and Racks from the People's Republic of China: Final Affirmative Countervailing Duty Determination*, 74 Fed. Reg. 37012 (July 27, 2009) ("*Kitchen Shelving Final Determination*"), and *Kitchen Shelving I&D Memo* at 13.

tax authorities exempted all FIEs and foreign enterprises from the city maintenance and construction taxes and the education fee surcharges.²¹² The city maintenance and construction tax is normally seven percent of a company's VAT payable, while the education fee surcharge is normally three percent of a company's VAT payable.²¹³ The Department also preliminarily countervailed this program in its investigation of *Certain Coated Paper* from China.²¹⁴

Potential respondents Asia Aluminum, Kam Kiu, PanAsia, Tai-Ao, Xingfa and Zhongwang are FIEs that would be exempt from the relevant charges and fees under this program.²¹⁵

a) Financial contribution

Consistent with Section 771(5)(D)(ii) of the Act, exemptions from various government taxes, fees, and surcharges are financial contributions in the form of revenue forgone by the government.

b) Benefit

The exemptions provided under the program confer a benefit in the amount of the taxes or charges otherwise due but not collected. 19 C.F.R. § 351.509(a)(1).

²¹² *Id.*

²¹³ *Id.*

²¹⁴ See *Certain Coated Paper Suitable for High-Quality Print Graphics Using Sheet-Fed Presses from the People's Republic of China: Initiation of Countervailing Duty Investigation*, 74 Fed. Reg. 53703 (Oct. 20, 2009) ("*Certain Coated Paper Initiation Notice*").

²¹⁵ See An Introduction to Zhaoqing, **Exhibit III-75**; Kam Kiu Newsletter (May/June 2005), **Exhibit III-77**; Company Profile of PanAsia Enterprise Group Ltd., **Exhibit III-78**; Company Profile of Taiao Aluminum (Taishan) Co., Ltd., **Exhibit III-79**; Company Profile of Xingfa Aluminum Co., Ltd., **Exhibit III-76**; Zhongwang Prospectus at 80-82, **Exhibit III-72**.

c) Specificity

The exemptions afforded by this program are limited as a matter of law to certain enterprises -- FIEs, and are therefore specific under Section 771(5A)(D)(i) of the Act.

4. Exemptions from administrative charges for companies in industrial zones

The Zhaoqing High-Tech Industry Development zone where Asia Aluminum is located proclaims on its website that its residents are exempt from any administrative charge that might be levied by municipal authorities.²¹⁶ In addition, "operative charges" are imposed at only half the normal rate and certificates are issued for only the cost of production.²¹⁷ These exemptions from government fees are countervailable subsidies.

a) Financial contribution

Consistent with Section 771(5)(D)(ii) of the Act, exemptions from the municipal government fees and taxes constitute financial contributions in the form of revenue forgone by the government.

b) Benefit

The exemptions provided under the program confer a benefit in the amount of the exemption or reduction of taxes otherwise due. 19 C.F.R. § 351.509(a)(1).

c) Specificity

The exemption or reduction of fees due is specific because the municipal authorities have designated certain geographical region within their jurisdictions for disparate treatment within the meaning of Section 771(5A)(D)(iv) of the Act.

²¹⁶ An Introduction to Zhaoqing, **Exhibit III-105**.

²¹⁷ *Id.*

D. Grant Programs

1. The State Key Technology Renovation Project Fund

The Department has countervailed the State Key Technology Renovation Project Fund program in past investigations.²¹⁸ The program was created pursuant to state circular *Guojingmao Touzi (1999) No. 886* ("Circular No. 886"), and operates under regulatory guidelines including the *Measures for the Administration of National Debt Special Fund for National Key Technology Renovation Project* (the "Special Fund Measures"), *Guojingmao Touzi (1999) No. 122*, *Guojingmao Touzi (1999) No. 1038*, and *Guojingmao Touzi (2000) No. 822*.²¹⁹ According to the GOC, the program is intended to promote: (a) technological renovation in key industries, enterprises, and products; (b) technology upgrades; (c) improvements in product structure; (d) improvements in quality; (e) increases in supply; (f) the expansion of domestic demand; and (g) further development of the state economy.²²⁰

Under this program, companies apply for funds to cover the cost of financing specific renovation projects. Under Paragraph 9 of the *Special Fund Measures*, payments are disbursed in the form of "project investment facility" grants covering two years of interest payments on loans to fund the project, or up to three years for enterprises located in the northeast, central or western areas of China.²²¹ The total amount of the grant is not to exceed 15 percent of the

²¹⁸ See e.g., *China OTR I&D Memo* at 23-24; *China OCTG I&D Memo* at 15-16.

²¹⁹ See *Coated Free Sheet Paper From the People's Republic of China: Amended Preliminary Affirmative Countervailing Duty Determination* ("China CFS Paper Preliminary Determination"), 72 Fed. Reg. 17484 (Apr. 9, 2007) at 17491.

²²⁰ See *id.*

²²¹ See *Circular of the Administrative Measures on the State Key Technology Renovation Projects and the Administrative Measures on Special Fund Generated by Treasury Bonds for the State Key Technology Renovation Projects*, Guo Jing Mao Touzi 1999 No. 886 at 10, **Exhibit III-106**.

project cost.²²² Under Article 11 of the *Special Fund Measures*, Key Technology Program funds may also be disbursed as “loans interest grants,” which are calculated with reference to the amount of the project loans and prevailing interest rates during a period of one to two years.²²³

Article 4 of *Circular No. 886* states that the recipients of these funds will be selected primarily from large state-owned enterprises and large-sized state holding enterprises among the 512 key enterprises, 120 pilot enterprise groups, and other leading enterprises.²²⁴ Article 4 also states that preference in recipient selection will be given to the “old industrial bases in north-east, central, and western areas.”²²⁵

As companies engaged in an industry strongly encouraged and supported by the GOC, leading Chinese aluminum extrusion producers should be eligible for this program. *Zhongwang's 2009 Interim Report*, for example, shows that the company received 9.24 million RMB from the GOC in 2009 for its technology research projects (and market development).²²⁶ Xingfa was also granted government subsidies totaling 2.927 million RMB in 2008 for certain research projects and other activities.²²⁷

²²² *See id.*

²²³ *See id.*

²²⁴ *See id.*

²²⁵ *See id.*

²²⁶ *See 2009 Interim Report of China Zhongwang Holdings Limited at 54, Exhibit III-100.*

²²⁷ *See 2008 Annual Report of Xingfa Aluminium Holdings Limited at 99, Exhibit III-107.*

a) Financial contribution

This program provides a financial contribution through a direct transfer of funds within the meaning of Section 771(5)(D)(i) of the Act.

b) Benefit

This program provides a benefit in the amount of the grant(s) according to 19 C.F.R. § 351.504(a).

c) Specificity

This program is specific under Section 771(5A)(D)(i) of the Act because it is limited as a matter of law to certain enterprises, *i.e.*, large-sized state-owned enterprises and large-size state holding enterprises among the 512 key enterprises, 120 pilot enterprise groups and the leading enterprises in industries.²²⁸ Petitioners further note that pursuant to Article 10.2 of China's WTO Accession Protocol, subsidies provided to SOEs are deemed specific when SOEs are the predominant recipients of such subsidies or receive disproportionately large amounts of such subsidies.²²⁹

2. The State Science and Technology Support Scheme

As explained in the *Circular of Ministry of Science and Technology and Ministry of Finance on Printing and Distributing Interim Measures on Administration of State Science and Technology Support Scheme*, the State Science and Technology Scheme was established to implement the *National Mid-term and Long-term Science and Technology Plan (2006-2020)*.²³⁰

²²⁸ See *China CFS Paper Preliminary Determination* at 17491

²²⁹ See *China's WTO Accession Protocol*, art. 10.2, **Exhibit III-45**.

²³⁰ See *Circular of Ministry of Science and Technology and Ministry of Finance on Printing and Distributing Interim Measures of Administration State Science and Technology Support Scheme*, Guo Ke Fa Ji Zi 2006 No.331, **Exhibit III-108**.

Supervised by MOST and MOF, the State Science and Technology Scheme supports research aimed at resolving scientific or technological problems in the area of economic and social development through grants from the central government.²³¹

The information available to Petitioners indicates that aluminum extruders are eligible for this program because extrusions are encouraged and supported by the GOC. Moreover, the GOC uses the goals espoused in its industrial policies to select grant recipients.

Zhongwang announced at the start of 2009 that the company's technology research project for complex aluminum products was selected by the MOST as a project under the State Science and Technology Scheme.²³² As a result, the evidence available to Petitioners indicates that this program provides benefits to producers of the subject merchandise.

a) Financial contribution

This program provides a financial contribution because it represents a direct transfer of funds in the form of a grant consistent with Section 771(5)(D)(i) of the Act.

b) Benefit

Grants provided under the State Science and Technology Scheme provide a benefit in the amount of the grant(s) according to 19 C.F.R. § 351.504(a).

c) Specificity

The information available to Petitioners indicates that this program is specific because recipients are selected based on the GOC's designation of certain industries for development in its industrial planning documents. As discussed in the sections above, the GOC has developed a

²³¹ See *id.*

²³² See Zhongwang, "Our Company's Research and Development Project Is Selected by 'the State Science and Technology Scheme of the 11th Five-Year'" (May 13, 2009), **Exhibit III-109**.

series of policies and measures to encourage and support aluminum extrusion producers to develop high-value-added and technology-intensive extrusion products through various means including funds for technology research.²³³ In this instance, the funding is intended to resolve problems in producing technology-intensive products such as aluminum extrusions. As the experience of Zhongwang shows, this program is specific as a matter of law pursuant to Section 771(5A)(D)(i) of the Act.

Additionally, subsidies provided under State Science and Technology Support Scheme are specific because of the discretion the GOC exercises in selecting beneficiaries.²³⁴ Only those entities that MOST considers "excellent" may participate in this program.²³⁵ As a result, the program is also specific under Section 771(5A)(D)(ii)(I) of the Act as well as Section 771(5A)(D)(ii)(III) because there are no clear, objective selection criteria.

3. "Famous Brands" awards

The Department has previously found that famous brand awards confer countervailable subsidies.²³⁶ The purpose of the program is to raise the competitiveness of Chinese industries, and it is implemented at both the national and provincial levels.²³⁷ In addition, a number of local

²³³ See e.g., *Nonferrous Metal Industry Adjustment and Revitalization Plan* (May 11, 2009), **Exhibit III-25**.

²³⁴ See *Circular of Ministry of Science and Technology and Ministry of Finance on Printing and Distributing Interim Measures of Administration State Science and Technology Support Scheme*, **Exhibit III-108**.

²³⁵ *Id.*

²³⁶ See *China Citric Acid and Citrate Salts I&D Memo* at 13-14.

²³⁷ See AQSISQ, *China Famous Brand Strategy Development Report* (Dec. 2006), **Exhibit III-110**.

governments have formulated various policies to reward enterprises with designated "famous" brands.²³⁸

Public information indicates that Chinese aluminum extrusion producers have benefited from this program. For example, Xingfa reported that the company received a subsidy for maintaining its brand name "Xingfa" as a well-known trademark in the PRC.²³⁹ Kam Kiu also was designated a "Famous Export Brand of Guangdong Province" for the year 2009-2010.²⁴⁰ Zhongwang has also been designated a "Famous Brand of China" and received assorted other accolades from the GOC including recognition as a "well-known Trademark" and thus may have benefited from this program.²⁴¹ Available information also indicates that Dali has four enterprises that produce "China Famous Products."²⁴²

Although Petitioners understand that China agreed to abolish this subsidy program following a WTO challenge, the agreement did not occur until more than halfway through the presumptive POI.²⁴³ As a result, it is unclear when the GOC has or will stop making grants under this program or if it made any grants in 2009 prior to agreeing to stop the program at the end of July.

²³⁸ See *id.*

²³⁹ See *2008 Annual Report of Xingfa Aluminium Holdings Limited* at 99, **Exhibit III-107**.

²⁴⁰ See "Taishan Kam Kiu Aluminium Extrusion Receives 'Famous Export Brand of Guangdong Province,'" *China Aluminum Net* (Aug. 20, 2009), **Exhibit III-111**.

²⁴¹ See Zhongwang, "Brand Excellence," **Exhibit III-112**.

²⁴² China Strategies LLC, "China's extrusion industry" (Sep. 19, 2007), **Exhibit III-33**.

²⁴³ United States Trade Representative, "United States Wins End to China's 'Famous Brand' Subsidies after Challenge at WTO; Agreement Levels Playing Field for American Workers in Every Manufacturing Sector" (Dec. 18, 2009), **Exhibit III-113**.

a) Financial contribution

As the Department has previously found, awards under the Famous Brand programs constitute a financial contribution in the form of a direct transfer of funds within the meaning of 771(5)(D)(i) of the Act.²⁴⁴

b) Benefit

The benefit from this program is the amount of any grant, as set forth in 19 C.F.R. § 351.504(a).

c) Specificity

In *Citric Acid*, the Department determined that very few enterprises received Famous Brands award and, as a result, the program was *de facto* specific within the meaning of Section 771(5A)(D)(iii)(I) of the Act.²⁴⁵

4. Grants to cover legal fees in trade remedy cases

According to submissions filed at the WTO by the European Union, the Shenzhen World Trade Organization Office (the "Shenzhen WTO Office") has a fund of more than RMB 10 million to reimburse up to 30 percent of legal fees to local companies facing anti-dumping investigations abroad.²⁴⁶ Shenzhen is an important industrial center in Guangdong Province, and the Shenzhen WTO Office is a government entity.²⁴⁷ The European Union's submission notes

²⁴⁴ *Citric Acid I&D Memo* at 14.

²⁴⁵ *Citric Acid I&D Memo* at 14.

²⁴⁶ See Transitional Review Mechanism Pursuant to Section 18 of the Protocol on the Accession of the People's Republic of China, Questions from the European Union to China concerning Subsidies and Price Controls, G/SCM/Q2/CHN/24 (Oct. 20, 2006) at 2, **Exhibit III-114**.

²⁴⁷ "Government fund helps firms face anti-dumping charges," *China Daily* (Feb. 16, 2004), **Exhibit III-115**.

that the fund aims to "encourage local export companies to aggressively strive for their legal rights in the anti-dumping cases through legal action."²⁴⁸

As indicated in Section II, *supra*, Chinese aluminum products including extrusions have been subject to antidumping and countervailing duty investigations in several jurisdictions in recent years.²⁴⁹ Consequently, it is likely that they have benefited from this program.

a) Financial contribution

This program provides a financial contribution in the form of a direct transfer of funds from a government source in accordance with Section 771(5)(D)(i) of the Act.

b) Benefit

This program provides a benefit in the amount of the grants according to 19 C.F.R. § 351.504(a).

c) Specificity

This program is a prohibited export subsidy within the meaning of Section 771(5A)(B) of the Act because it is limited to companies that export.

5. Special fund for energy saving technology reform

The Circular of the Ministry of Finance and National Development and Reform Commission on Printing and Distributing Interim Measures on Administration of Energy Saving

²⁴⁸ *See id.*

²⁴⁹ *See* "Argentina launches antidumping against aluminum phosphide," *China Chemical Reporter* (Feb. 2003), **Exhibit III-1**; "EU imposes anti-dumping tariffs on Chinese aluminum foil," *People's Daily Online* (Sep. 24, 2009), **Exhibit III-2**; "EU to launch anti-dumping investigations on China Aluminum Alloy Wheel," *Dow Jones* (Aug. 7, 2009), **Exhibit III-3**; "India slaps safeguard duties on Chinese aluminum, soda ash," *domain-b.com* (Mar. 16, 2009), **Exhibit III-4**; "China-Made Wheels Under Ministry Scanner," *Financial Express* (Nov. 9, 2006), **Exhibit III-5**; South Africa Government Gazette (June 29, 2007), **Exhibit III-6**; *Canadian Statement of Reasons*, **Exhibit III-7**; and *Australia Preliminary Determination*, **Exhibit III-8**.

Technology Reform Awards Fiscal Funds provides awards to support certain enterprises undertaking energy saving technology reform projects.²⁵⁰ In addition to the MOF and the NDRC, local government agencies also supervise the implementation of this program and the construction of funded projects.²⁵¹

A number of local governments have adopted regulations to implement the policies described above. In particular, the Guangdong provincial government, through the *Interim Measures on Administration of Guangdong Province Energy Saving Special Fund*, will pay 200 RMB for every metric ton of coal saved through a participating project.²⁵²

In 2009, Guangdong Province rewarded 112 enterprises with grants from the Energy Saving Special Fund, including two Chinese aluminum extrusion producers: Xingfa and Asia Aluminum.²⁵³ According to reports, Xingfa's project involved saving 5,174 metric tons of coal, and Asia Aluminum's project saved 5,879 metric tons.²⁵⁴ According to the formula established in the *Interim Measures on Administration of Guangdong Province Energy Saving Special Fund*, these two companies should have received 1,034,800 and 1,175,800 RMB, respectively.

²⁵⁰ See *Circular of Ministry of Finance and National Development and Reform Commission on Printing and Distributing Interim Measures on Administration of Energy Saving Technology Reform Awards Fiscal Funds*, Cai Jian 2007 No. 371, **Exhibit III-116**.

²⁵¹ See *id.*

²⁵² See *Interim Measures on Administration of Guangdong Province Energy Saving Special Fund*, Yue Cai Gong 2008 No. 126, **Exhibit III-117**.

²⁵³ See *Publication of 2009 Guangdong Province Energy Saving Fund Projects Plan*, **Exhibit III-118**.

²⁵⁴ See *id.*

a) Financial contribution

This program confers a financial contribution through a direct transfer of funds within the meaning of Section 771(5)(D)(i) of the Act.

b) Benefit

Grants made under the Energy Saving Special Fund program provide a benefit in the amount received according to 19 C.F.R. § 351.504(a).

c) Specificity

This program is specific on a *de facto* basis within the meaning of Section 771(5A)(D)(iii)(I) of the Act, because as noted above, the actual recipients of the grant are limited to a small number of enterprises. Guangdong is one of China's most economically vibrant provinces and thus the 112 eligible companies represent only a miniscule portion of the companies in the province.

6. The Clean Production Technology Fund

As the Department has found, the Clean Production Technology Fund program entered into force in October 2004 pursuant to the *Provisional Measures on Clean Production Inspection*.²⁵⁵ The purpose of program is to decrease pollution through incentives including monetary rewards presented to companies that pass an environmental inspection.²⁵⁶ This program is implemented at the local government level.²⁵⁷

As part of this program, the Liaoning provincial government promulgated the *Implementation Rules on Key Enterprise Compulsory Clean Production Inspection*, which

²⁵⁵ *China CFS Paper I&D Memo* at 15.

²⁵⁶ *See id.*

²⁵⁷ *See Provisional Measures on Clean Production Inspection*, Decree No. 16 (Aug. 16, 2004), **Exhibit III-119**.

provide for financial support to enterprises that have the inspections performed.²⁵⁸ Liaoning Province designated 249 key enterprises to participate in the inspection process.²⁵⁹ Publicly available information indicates that Zhongwang was one of the companies selected by the provincial government.²⁶⁰ As a result, the information available to Petitioners indicates that Zhongwang benefited from this program during the presumptive POI.

a) Financial contribution

This program provides a financial contribution in the form of a direct transfer of funds within the meaning of Section 771(5)(D)(i) of the Act.

b) Benefit

The amount of the benefit from this program is the amount of the grant. 19 C.F.R. § 351.504(a).

e) Specificity

This program is *de facto* specific pursuant to Section 771(5A)(D)(iii)(I) of the Act because, as documented above, the number of recipients is small. Only 251 companies in the entire province of Liaoning were selected to participate, for example. The program is also specific under Section 771(5A)(D)(iii)(IV) because of the discretion exercised by the government when selecting companies to participate.

²⁵⁸ See *Liaoning Province Implementation Rules on Key Enterprise Compulsory Clean Production Inspection* (Dec. 31, 2006), **Exhibit III-120**.

²⁵⁹ See "More Than Thousand Liaoning Enterprises Have Realized "Clean Production," *Xinhua Net* (Dec. 11, 2009), **Exhibit III-121**.

²⁶⁰ See *Notice of Key Enterprises Implementing Liaoning Province Compulsory Clean Production Inspection (Second Batch)* (Jun. 15, 2007), **Exhibit III-122**; see also Liaoning City Environmental Protection Bureau, "Three Enterprises of Our City Smoothly Passed Provincial-level Clean Production Inspection Evaluation" (Sep. 30, 2009), **Exhibit III-123**.

7. Grants for listing shares

Press reports indicate the Liaoyang City rewarded Zhongwang with a grant of 1 million RMB for publicly listing shares.²⁶¹ The grant appears to have been made during the presumptive POI.²⁶²

Grants from local governments to companies that list shares appear to be common in China. For example, one municipality facilitates public offerings by

offering a “green passage to listing”, providing assistance in areas such as licensing, land use applications and foreign exchange. Furthermore, each enterprise is provided with incentives specific to its circumstances. If the incorporation of a joint stock company involves the transfer of land use rights or property ownership, then the expenses involved in the transfer can be cut in half. After reorganizing into a stock company, the tax increment will be returned in full after the enterprise goes public. When the “tutoring” period is completed and the enterprise is listed, it is awarded RMB300,000 (US\$42,000) by the municipal government. In {a nearby} city, local companies receive an additional bonus of RMB3 million (US\$420,000) when they list.²⁶³

Publicly available information indicates that a number of Chinese aluminum extrusion producers are trading shares on stock exchanges. For example, Zhongwang and Xingfa are trade on the Hong Kong Stock Exchange, and Nanshan is traded on the Shanghai Stock Exchange.²⁶⁴ The Department should investigate this program for any respondent company that has listed shares.

²⁶¹ Zhongwang, “Liaoyang Zhongwang Group on the road to becoming the world’s advanced aluminum extrusion enterprise” (Nov. 4, 2009), **Exhibit III-124**.

²⁶² *Id.*

²⁶³ See “Listing Frenzy,” *China Business Feature* (Feb. 27, 2008), **Exhibit III-125**.

²⁶⁴ See 2009 Interim Report of China Zhongwang Holdings Limited at 2, **Exhibit III-100**, 2009 Interim Report of Xingfa Aluminium Holdings Limited at 3, **Exhibit III-126**, and 2009 Interim Report of Shandong Nanshan Aluminium Co., Ltd. at 3, **Exhibit III-127**.

a) Financial contribution

This program provides a financial contribution in the form of a direct transfer of funds from a government source in accordance with Section 771(5)(D)(i) of the Act.

b) Benefit

This program provides a benefit in the amount of the grants according to 19 C.F.R. § 351.504(a).

c) Specificity

The program is *de facto* specific under Section 771(5A)(D)(iii)(I) of the Act because only a small number of Chinese companies are allowed to list on bourses.²⁶⁵ It is also specific under Section 771(5A)(D)(i) because it is limited to companies with listed shares.

8. The Northeast Region Foreign Trade Development Fund

This program provides grants for up to 50 percent of the expense of an eligible project to support exporting enterprises. In particular, the aims of the program are to help companies "develop an export processing base . . . support the registration of trademarks in foreign countries . . . support the training of foreign trade professional, and . . . explore international markets."²⁶⁶ Only companies in China's Northeastern provinces are eligible for this program.²⁶⁷

Zhongwang is located in Liaoning Province, and thus is eligible for benefits under this program. Moreover, as Zhongwang's 2009 *Interim Report* reveals, the company received 9.24 million RMB from the Finance Bureau of Liao Yang City in connection with expenditures for

²⁶⁵ See *Administrative Measures for the Initial Public Offering and Listing of Stocks*, China Securities Regulatory Commission Order No. 32 (May 17, 2006), **Exhibit III-128**.

²⁶⁶ See *China Line Pipe I&D Memo* at 20-21.

²⁶⁷ See *id.* at 21.

market exploration, among other things.²⁶⁸ The Department has found this program countervailable in prior investigations.²⁶⁹

a) Financial contribution

This program provides a financial contribution in the form of a direct transfer of funds from the government under Section 771(5)(D)(i) of the Act.²⁷⁰

b) Benefit

As the Department has found previously, this program bestows a benefit in the amount of the grant(s) within the meaning of Section 771(5)(E) of the Act.²⁷¹

c) Specificity

Because the receipt of the export interest subsidies is contingent upon export performance, this program is deemed specific under Section 771(5A)(A) of the Act.²⁷²

9. The Northeast Region Technology Reform Fund

The GOC's Northeast Revitalization Program provides, among other things, funds to support enterprises located in China's old industrial bases that undertake technological reforms and research & development activities in order to "strengthen technical transformation of

²⁶⁸ See 2009 Interim Report of China Zhongwang Holding Limited at 54, Exhibit III-100.

²⁶⁹ See *Circular Welded Carbon Quality Steel Line Pipe From the People's Republic of China: Final Affirmative Countervailing Duty Determination*, 73 Fed. Reg. 70961 (Nov. 24, 2008), Issues and Decision Memo ("China Line Pipe I&D Memo") at 20-21.

²⁷⁰ See *China Line Pipe I&D Memo* at 21.

²⁷¹ See *id.*

²⁷² See *id.*

enterprises" and "improve independent innovation capability."²⁷³ To implement policy, the Liaoning Province Financial Bureau earmarks 300 million RMB annually for loan interest subsidies.²⁷⁴ As mentioned above, Zhongwang in 2009 received 9.24 million RMB from the Finance Bureau of Liao Yang City in connection with a number of activities including technological research.²⁷⁵ Some of these funds were likely provided under this program.

a) Financial contribution

This program confers benefits in the form of direct transfer of funds, *i.e.*, grants, from the government to eligible recipients, and thus confers a financial contribution within the meaning of Section 771(5)(D)(i) of the Act.

b) Benefit

This benefit from this program is the amount of grant received. Section 771(5)(E) of the Act.

c) Specificity

Because this subsidy program is available only to companies located in the Heilongjiang, Jilin, and Liaoning Provinces in Northeastern China, subsidies under this program are available only within a designated geographical region within the jurisdiction of the authority providing the subsidy, *i.e.*, the GOC. As a result, this program is specific within the meaning of Section 771(5A)(D)(iv) of the Act.

²⁷³ "China's Old Industrial Base Eyes Bright Future with Ambitious Plan," *People's Daily Online* (Jan. 9, 2004), **Exhibit III-55**; see also *Opinions of the State Council on Further Implementing the Strategy of Revitalizing the Old Industrial Bases Including Northeast China*, Guo Fa 2009 No. 33, **Exhibit III-129**.

²⁷⁴ See *Liaoning Province Policies and Opinions on Supporting the Reform and Development of Enterprise by the Financial Bureau* (Nov. 24, 2004), **Exhibit III-130**.

²⁷⁵ See *2009 Interim Report of China Zhongwang Holding Limited* at 54, **Exhibit III-100**.

E. Government Provision Of Goods Or Services For Less Than Adequate Remuneration

1. Land

The evidence available to Petitioners indicates that that Chinese producers of aluminum extrusions benefit from the government provision of land use rights for less than adequate remuneration. As the Department is aware, all land in China is the property of the State, and owned by some level of government or a township or village "collective."²⁷⁶ As a result, the GOC has exceptional control over how land is used in China, as well as prices.²⁷⁷ Although private entities may purchase land-use rights from a government or from certain classes of other entities holding land-use rights, the Department has found that the GOC's ability to control land allocations and grants, combined with policies that restrict the ability of tenants to determine how to use land, result in severe price distortions.²⁷⁸

a) Land use rights in industrial and other special economic zones

The GOC provides land at preferential rates to enterprises located in special economic zones, where many of the companies producing aluminum extrusions are located. The provision of land to companies located such zones has been found countervailable in prior investigations.²⁷⁹

The information available to Petitioners indicates Asia Aluminum, for example, paid essentially nothing for its land use rights in the Zhaoqing City High-Tech Development Zone. Specifically, Asia Aluminum agreed to acquire 50-year land use rights for 10,300 *mu*

²⁷⁶ See *Line Pipe I&D Memo* at 15.

²⁷⁷ See, e.g., *OTR Preliminary Determination* at 71368.

²⁷⁸ See *Line Pipe I&D Memo* at 16.

²⁷⁹ See, e.g., *LWS I&D Memo* at 14-18, and *Thermal Paper I&D Memo* at 22.

(approximately 6.8 million square meters) of land located in the zone for 288 million RMB. The Zhaoqing City government, however, agreed to return the payment to the company as compensation for the construction of infrastructure.²⁸⁰

Other government-designated zones advertise their “preferential” land prices in order to entice companies to locate within their borders. For example, the Liaoyang High-Tech Industry Development Zone, where Zhongwang is located,²⁸¹ says that companies that locate within its borders can receive a “preferential” price of between 80 and 100 RMB per square meter, with the possibility of discounts.²⁸² While the zone does not specify in what manner its prices are preferential, considering that the local government is responsible for determining all land prices within its jurisdiction, the price can only be preferential relative to the price of other land use rights in the same area.

(i) Financial contribution

As the Department has found in prior investigations, including *Laminated Woven Sacks* and *Line Pipe*,²⁸³ the provision of land use rights constitutes a financial contribution from the GOC within the meaning of Section 771(5)(D)(iii) of the Act.

(ii) Benefit

The GOC provision of land use rights at below market prices (including for free) confers

²⁸⁰ Asia Aluminum Holdings Ltd. 2006 Interim Report at 22, **Exhibit III-71**.

²⁸¹ See Introduction to Liaoyang High-Tech Industry Development Zone (May 17, 2006), **Exhibit III-131**.

²⁸² See Preferential Policies in Liaoyang High-Tech Industry Development Zone (Nov. 11, 2009), **Exhibit III-132**.

²⁸³ See, e.g., *LWS I&D Memo* at 14 (“we continue to find the sale of land-use rights constitutes a financial contribution from a government authority in the form of providing goods or services pursuant to section 771(5)(D)(iii) of the Act.”), and *Line Pipe I&D Memo* at 14.

a benefit within the meaning of 19 CFR § 351.511(a)(2) and Section 771(5)(E)(iv) of the Act.²⁸⁴

Due to government predominance in the land market in China, there are no commercial land benchmarks available within China. As a result, Petitioners believe that the Department should rely on an external benchmark to measure the benefit conferred by this program, consistent with the statute, the Department's regulations, and the Department's prior practice.²⁸⁵ The benefit will be the difference between the price paid and the amount the recipient would have paid in reference to the market benchmark.

(iii) Specificity

This program is specific under Section 771(5A)(D)(iv) of the Act because the land use rights at issue are located within designated geographical regions of the jurisdictions providing them. Because these jurisdictions treat entities located within the zones differently, the resulting subsidy is specific.²⁸⁶

b) Allocated land use rights for SOEs

In addition to below-market prices in development zones, the GOC also provides preferential land use rights to SOEs. As the Department has found in prior investigations, SOEs are eligible to receive "allocated" land use rights (as opposed to "granted" or "conveyed" land use rights). Allocated land use rights are transferred from the State to an SOE for a nominal one-

²⁸⁴ Petitioners note that pursuant to Article 15 of *China's WTO Accession Protocol* the Department may "use methodologies for identifying and measuring the subsidy benefit which take into account the possibility that prevailing terms and conditions in China may not always be available as appropriate benchmarks," **Exhibit III-45**.

²⁸⁵ See, e.g., *LWS I&D Memo* at 14-18.

²⁸⁶ See, e.g., *Line Pipe I&D Memo* at 14; see also *OTR Tire I&D Memo* at 20-21.

time charge and annual fee, and do not expire.²⁸⁷ In the *OTR Tires Preliminary Determination*, the Department noted that “the information on the record indicates that allocated land-use rights, which can only be transferred to state entities and which are subject to significantly different terms than granted land-use rights, are specific to SOEs pursuant to section 771(5A)(D)(i) of the Act.” The fees associated with allocated land use rights do not approximate or even reflect market values, and, as a result, recipients of this type of land use rights benefit from a countervailable subsidy. Fenglu is an SOE and would therefore appear to be eligible for benefits under this program.²⁸⁸

(i) Financial contribution

As the Department has found in its prior investigations, the provision of land use rights constitutes a financial contribution from the GOC within the meaning of Section 771(5)(D)(iii) of the Act.

(ii) Benefit

For the reasons described in the benefit section immediately above, the information available to Petitioners indicates that the GOC provides allocated land use rights to SOEs for only nominal fees, providing a benefit within the meaning of 19 CFR § 351.511(a)(2) and Section 771(5)(E)(iv) of the Act.²⁸⁹ Because of the market distortions resulting from the GOC’s ownership and control all land in China, the Department should calculate the amount of the

²⁸⁷ *Certain New Pneumatic Off-the-Road Tires from the People’s Republic of China: Preliminary Affirmative Countervailing Duty Determination*, 72 Fed. Reg. 71360, 71368 (Dec. 17, 2008) (“*OTR Preliminary Determination*”).

²⁸⁸ See Company Profile of Guangdong Fenglu Aluminum Co, Ltd., **Exhibit III-133**.

²⁸⁹ Petitioners note that pursuant to Article 15 of *China’s WTO Accession Protocol* the Department may “use methodologies for identifying and measuring the subsidy benefit which take into account the possibility that prevailing terms and conditions in China may not always be available as appropriate benchmarks,” **Exhibit III-45**.

benefit through a comparison to land use values in a market economy at a similar stage of economic development that is reasonably proximate to China.²⁹⁰ The benefit will be the difference between the price paid and the amount the recipient would have paid in reference to the market benchmark.

(iii) **Specificity**

“Allocated” land use rights are only available to SOEs, a group of enterprises, making the government provision of allocated land use rights at below market prices specific under Section 771(5A)(D)(i) of the Act.²⁹¹ Petitioners further note that pursuant to Article 10.2 of China’s WTO Accession Protocol, subsidies provided to SOEs are deemed specific when SOEs are the predominant recipients of such subsidies or receive disproportionately large amounts of such subsidies.²⁹²

2. Primary aluminum

Aluminum extrusion producers in China have long enjoyed the benefit of obtaining primary aluminum from state-owned aluminum producers at below market prices under several GOC policies. Investigations conducted by Customs officials in both Canada and Australia have confirmed that SOEs provide primary aluminum to extrusion producers for less than adequate remuneration.²⁹³

²⁹⁰ See, e.g., *LWS I&D Memo* at 14-18.

²⁹¹ *OTR Preliminary Determination* at 71368.

²⁹² See *China’s WTO Accession Protocol*, art. 10.2, **Exhibit III-45**.

²⁹³ See *Canadian Statement of Reasons* at 70-72, **Exhibit III-7**; *Australia Preliminary Determination*, **Exhibit III-8**.

As indicated in the dumping and injury sections of this Petition, Primary aluminum is the main input in the manufacture of extruded aluminum.²⁹⁴ In China, state-owned aluminum producers dominate in the production of primary aluminum.²⁹⁵ In 2008, for example, SOEs accounted for nearly half of China's total aluminum production.²⁹⁶ The state-owned Aluminum Corporation of China Limited ("Chalco") alone produced almost one-fourth of China's total primary aluminum output in 2008.²⁹⁷

To ensure sufficient supply for the benefit of producers of downstream products such as aluminum extruders, the GOC has implemented several policies to manage primary aluminum prices. For example, the *Notice of Guidelines on Accelerating the Adjustment of Aluminum Industry Structure* is the government's effort to manage supply and demand in electrolytic aluminum (*i.e.*, primary aluminum).²⁹⁸ It requires China's financial institutions to support electrolytic aluminum enterprises through lending.²⁹⁹ Moreover, as one industry journal reports, the Chinese government "has been keen to control exports of the upstream product primary

²⁹⁴ See Australian Customs and Border Protection Service, *Preliminary Report on Existence of Countervailable Subsidies – Alleged Subsidization of Aluminum Extrusion Exported from the People's Republic of China* (Feb. 19, 2010) ("*Australia Preliminary Report*") at 8, **Exhibit III-134**.

²⁹⁵ See *Canadian Statement of Reasons* at 70, **Exhibit III-7**; see also *Australia Preliminary Report* at 6, **Exhibit III-134**.

²⁹⁶ See *Australia Preliminary Report* at 6, **Exhibit III-134**.

²⁹⁷ See *2008 Annual Report of Aluminum Corporation of China Limited* at 27, 37, and 39, **Exhibit III-135**.

²⁹⁸ *Notice of Guidelines on Accelerating the Adjustment of Aluminum Industry Structure*, Fa Gai Yun Xing 2006 No. 589, **Exhibit III-21**.

²⁹⁹ *Id.*

aluminum in order to increase domestic supply.³⁰⁰ In the presumptive POI, the GOC imposed export tariffs as high as 15 percent.³⁰¹ This is contrary to China's policy on most products, which receive a VAT rebate upon export.

Publicly available information supports the findings of the Canadian and Australian authorities that extruders in China purchase aluminum from SOEs at below-market prices. For example, the average price of spot aluminum on the London Metals Exchange ("LME") in 2008 was \$2,572 per metric ton, whereas the price on the Shanghai Futures Exchange ("SHFE") was nearly 4 percent lower, *i.e.*, \$2,479.57 per metric ton.³⁰² The table below shows that monthly spot prices and three-month futures prices in 2008.

Table 1: Comparison of 2008 LME and SHFE Aluminum Prices

	Spot Price (USD / Metric Ton)			3-Month Future (USD / Metric Ton)		
	LME	SHFE	Difference	LME	SHFE	Difference
Jan. 2008	2,445.00	2,570.29	5.12%	2,491.00	2,628.29	5.51%
Feb. 2008	2,776.00	2,685.86	-3.25%	2,816.00	2,763.71	-1.86%
Mar. 2008	3,005.00	2,818.14	-6.22%	3,047.00	2,916.14	-4.29%
Apr. 2008	2,959.00	2,721.43	-8.03%	3,009.00	2,775.43	-7.76%
May 2008	2,902.00	2,659.14	-8.37%	2,949.00	2,713.14	-8.00%
June 2008	2,957.00	2,670.14	-9.70%	3,005.00	2,724.29	-9.34%
July 2008	3,071.00	2,716.86	-11.53%	3,121.00	2,785.43	-10.75%
Aug. 2008	2,764.00	2,660.14	-3.76%	2,817.00	2,694.29	-4.36%
Sept. 2008	2,525.00	2,472.43	-2.08%	2,577.00	2,489.86	-3.38%
Oct. 2008	2,121.00	2,096.57	-1.15%	2,178.00	2,110.43	-3.10%
Nov. 2008	1,852.00	1,962.71	5.98%	1,905.00	1,988.00	4.36%
Dec. 2008	1,490.00	1,720.71	15.48%	1,536.00	1,677.43	9.21%
2008 Average	2,572.00	2,479.57	-3.59%	2,621.00	2,522.14	-3.77%

(Source: China Commodity Net)

³⁰⁰ "Growing aluminum alloy exports inviting attention from Chinese ...," *China Metals Weekly* (Jul. 18, 2008), **Exhibit III-136**.

³⁰¹ See *Customs Export Tariff of the People's Republic of China (Enforced from Jan. 1, 2009)*, **Exhibit III-137**; see also *Customs Import Tariff of the People's Republic of China (2009)*, **Exhibit III-138**.

³⁰² See "Overview of 2008 Aluminum Market and the Outlook for 2009," *China Commodity Net* (Mar. 12, 2009), **Exhibit III-139**.

A review of 2009 pricing data reveals evidence of a subsidy benefit from the purchase of aluminum from SOEs. On average, the SHFE price was nearly 3 percent lower than the LME price adjusted for import duties and VAT.³⁰³ This difference is especially pronounced in the latter half of the year, after a GOC program to protect aluminum companies like Chalco from the effects of the global economic crisis by stockpiling aluminum in a government reserve.³⁰⁴ Even with this temporary program to support primary aluminum producers, however, SHFE prices for the presumptive POI were still lower than the adjusted LME average.

³⁰³ The MFN import duty and VAT for primary aluminum in China for 2009 were 5 percent and 17 percent, respectively. See *Customs Import Tariff of the People's Republic of China (2009)*, **Exhibit III-138**. Petitioners note that it is consistent with the Department's regulations and prior practice to adjust the comparison price by adding fees such as import duties and delivery charges, so as to reflect the price a firm would pay if it imported the product. See *19 CFR 351.511(a)(2)(iv)*; see also *Light-Walled Rectangular Pipe and Tube From People's Republic of China: Final Affirmative Countervailing Duty Investigation Determination*, 73 Fed. Reg. 35642 (June 24, 2008), Issues and Decision Memo ("*China LRPT I&D Memo*") at 37.

³⁰⁴ See generally Aluminum Association, "China's State Reserve Agency Stockpile to Buoy Aluminum Sector" (Dec. 29, 2008), **Exhibit III-140**.

Table 2: Comparison of 2009 LME and SHFE Adjusted Aluminum Prices

	LME (USD / Metric Ton)	Adjusted LME ³⁰⁵ (USD / Metric Ton)	SHFE ³⁰⁶ (USD / Metric Ton)	Percentage ³⁰⁷
Jan. 2009	1,413.12	1,724.01	1,742.71	1.09%
Feb. 2009	1,330.20	1,622.84	1,714.35	5.64%
Mar. 2009	1,335.84	1,629.72	1,727.99	6.03%
Apr. 2009	1,420.85	1,733.44	2,016.64	16.34%
May 2009	1,460.45	1,781.75	1,840.50	3.30%
June 2009	1,573.73	1,919.95	1,915.97	-0.21%
July 2009	1,667.96	2,034.91	1,941.88	-4.57%
Aug. 2009	1,933.75	2,359.18	2,157.01	-8.57%
Sept. 2009	1,834.11	2,237.61	2,142.66	-4.24%
Oct. 2009	1,878.57	2,291.86	2,127.86	-7.16%
Nov. 2009	1,949.29	2,378.13	2,134.03	-10.26%
Dec. 2009	2,180.10	2,659.72	2,242.14	-15.70%
2009 Average	1,664.83	2,031.09	1,975.31	-2.75%

(Source: LME and SHFE)

Public information also indicates that, in addition to the macroeconomic controls described above, the GOC intervenes directly in the purchasing process to assist aluminum product manufacturers. For example, the Fuzhou Development Zone Development and Reform Bureau helped at least one aluminum product manufacturer procure low-priced aluminum ingot during the POI.³⁰⁸

Based on the information documented above and the affirmative determinations by the Canadian and Australian authorities in investigations involving the same subject merchandise, Petitioners believe that Chinese aluminum extrusion producers have benefited from the

³⁰⁵ The "Adjusted LME" price includes the 17 percent VAT and 5 percent tariff, *i.e.*, Adjusted LME price = LME price * (100%+17%+5%). Petitioners note that the Department's normal comparison methodology would also add transportation costs.

³⁰⁶ The monthly SHFE price is an arithmetical average of SHFE daily prices of the month, *i.e.*, the monthly SHFE price = sum of daily prices / number of days.

³⁰⁷ The "Percentage" shows the percentage by which the SHFE price is lower than the "Adjusted LME" price.

³⁰⁸ See Mawei District Government "Fuzhou Development Zone 'Bites' on Scientific Development Tightly" (May 4, 2009), **Exhibit III-141**.

government provision of this key input for less than adequate remuneration during the presumptive POI.

a) Financial contribution

Information reasonably available to Petitioners demonstrates that aluminium extrusion producers in China receive low-priced primary aluminium from the GOC, through state-owned aluminium suppliers. The Department has found that the provision of goods by state-owned enterprises in China constitutes a financial contribution within the meaning of Section 771(5)(D)(iii) of the Act in prior investigations of Chinese products.³⁰⁹ In addition, China agreed when it acceded to the WTO that its state-owned enterprises will be considered to be government actors, and therefore that they may confer countervailable subsidies, when they do not act in a commercial manner.³¹⁰ Hence, by selling aluminum for less than adequate remuneration, the SOEs are not behaving as commercial actors but rather arms of the GOC.

b) Benefit

Pursuant to Section 771(5)(E)(iv) of the Act, Chinese producers of aluminum extrusions receive a benefit to the extent that the price paid for the primary aluminum from state-owned and controlled aluminum producers constitutes less than adequate remuneration. To determine the amount of benefit, the Department's regulations at 19 C.F.R. § 351.511(a)(2)(i) require the use of a market-determined price for the good resulting from actual transactions in the country in question as the benchmark, where applicable. As described above, however, the GOC's domination and subsidization of Chinese aluminum producers have distorted the price of primary

³⁰⁹ See, e.g., *China CWP I&D Memo* at 9-11; *China OCTG I&D Memo* at 13.

³¹⁰ See *Report of the Working Party on the Accession of China, World Trade Organization*, WT/MIN(01)/3 (Nov. 10, 2001) ("*Working Party Report*") at para. 172, **Exhibit III-13**.

aluminum in China. In the Canadian and Australian investigations of this product, both authorities failed to find an appropriate market benchmark in China due to the domination of the industry by SOEs and the GOC's market interventions.³¹¹ Consequently, both authorities used a world market price, *i.e.*, the LME price, as the market benchmark.³¹² Petitioners are similarly unable to locate a market-determined price for primary aluminum in China that is not distorted by the GOC's policies and ownership of the means of production.

In situations such as these where no internal commercial benchmarks are available, measuring the benefit conferred by this program with reference to an external benchmark is consistent with the statute, the Department's regulations, and the Department's prior practice.³¹³ For the purpose of this allegation, Petitioner reviewed the information reasonably available to make the comparison called for under 19 C.F.R. § 351.511(a)(2)(ii), *i.e.*, to compare the China price to a "world market price." Because primary aluminum is a commodity product traded worldwide, such a comparison can be easily made. Following the practice of Canadian and Australian authorities, Petitioners adopted the LME price as a suitable world market price, adjusted as appropriate. For the GOC price of primary aluminum, Petitioners use the publicly-available SHFE price, notwithstanding that the target companies are major consumers that likely do not purchase on the spot market but rather through long-term contracts. As noted in Table 2, based on the LME price for primary aluminum, Petitioners estimate that this program provided

³¹¹ See *Canadian Statement of Reasons* at 71-72, **Exhibit III-7**; see also *Australia Preliminary Report* at 6-7, **Exhibit III-134**.

³¹² See *id.*

³¹³ See, e.g., *China LRPT I&D Memo* at 35-37. Petitioners further note that, pursuant to Article 15 of China's WTO Accession Protocol, the Department may "use methodologies for identifying and measuring the subsidy benefit which take into account the possibility that prevailing terms and conditions in China may not always be available as appropriate benchmarks." See *China's WTO Accession Protocol* at Article 15, **Exhibit III-45**.

substantial benefits to Chinese aluminum extrusion producers during the POI.

c) Specificity

The manufacture of aluminum extrusions is one of main uses of primary aluminum in China.³¹⁴ The provision of primary aluminum at less than adequate remuneration is therefore specific within the meaning of Section 771(5A)(D)(iii)(I) of the Act.

F. Government Purchase Of Goods For More Than Adequate Remuneration

As noted in Section III, *supra*, the GOC has created and implemented a comprehensive policy directing the development of the Chinese aluminum extrusions industry. As part of its policy to assist directly in the development and expansion this industry, the GOC has implemented a program to purchase aluminum extrusions from Chinese producers at prices that exceed world market prices. Such procurements are financial contributions, which are specific and result in a significant benefit to China's aluminum extrusion producers.

Several of China's largest aluminum extrusion manufacturers have expansive and, in some cases, nearly exclusive procurement arrangements with government-owned companies in the transportation and construction sectors of the Chinese economy. For example, Zhongwang is a significant supplier to government-owned railcar, subway, aircraft, automobile, and machinery manufacturers throughout China.³¹⁵ Since 2004, the company has been designated as one of only

³¹⁴ See *2008 Annual Report of Aluminum Corporation of China Limited* at 45 (stating the primary aluminum is used for "the production and sales of seven main aluminum fabricated products, including casts, planks, screens, extrusions, forges, powder and die castings"), **Exhibit III-135**; see also *Australia Preliminary Report* at 8, **Exhibit III-134**.

³¹⁵ "China Zhongwang Announces Proposed Listing on the Main Board of the HKEx," *ecplaza.net* (Apr. 23, 2009), **Exhibit III-142**. China South Locomotive & Rolling Stock company was co-founded by China South Locomotive and Rolling Stock Industry Group Corporation ("CSR Group") and Beijing Railway Industry Economic and Trade Company with a total equity capital of 7 billion RMB. See *Profile of China South Locomotive and Rolling Stock Corporation Limited*, **Exhibit III-143**. According to CSR Ltd.'s 2008 Annual Report, CSR

a few qualified suppliers by the Ministry of Railways, to which it supplies aluminum extrusion products for the manufacture of train cars.³¹⁶ As Zhongwang itself notes, the Ministry of Railways has “consistently designated China Zhongwang as one of the few qualified suppliers for the manufacture of cargo and passenger carriages in the mainland since 2004.”³¹⁷ In addition, China South Locomotive & Rolling Group Limited and China Northern Locomotive & Rolling Stock Industry (Group) Corporation are major customers of Zhongwang.³¹⁸ Zhongwang has strategic agreements with China South Locomotive & Rolling Co. Ltd., China North Locomotive & Rolling Co. Ltd and other major metropolitan rail manufacturers and operators in China.³¹⁹ It is reported that Zhongwang has contracts to supply 70,000 tons of aluminum extrusions to several train manufacturers supervised by the Ministry of Railways.³²⁰

Zhongwang has been a beneficiary of China’s 4 trillion RMB stimulus package, much of which is being spent on infrastructure projects such as railways.³²¹ Of the 4 trillion RMB in the stimulus spending, 31.5 billion RMB is projected to be spent on public infrastructure, such as

Group, which is a state-owned entity, owns 56.75 percent shares of CSR Ltd. See *2008 Annual Report of CSR Ltd.* at 13 and 16, **Exhibit III-144**. China Northern Locomotive & Rolling Stock Industry (Group) Corporation (“CNR Group”) is a large state-owned enterprise. See *China CNR Corporation Limited Prospectus* at 33, **Exhibit III-145**.

³¹⁶ “PE Explores Industries Benefiting From The 4000 Billion Investment,” *21cbh Website* (May 27, 2009), **Exhibit III-146**.

³¹⁷ “China Zhong Wang Announces Proposed Listing on the Main Board of the HKEx,” *eplaza.net* (Apr. 23, 2009), **Exhibit III-142**.

³¹⁸ *Id.*

³¹⁹ *Id.*

³²⁰ MOFCOM, “China Zhongwang Chairman Liu Zhongtian Accumulates 24 Billion Yuan Within 15 Years, Becomes Richest in China” (Sep. 22, 2009), **Exhibit III-147**.

³²¹ “China Zhong Wang IPO to Raise up to \$1.6b,” *China Daily* (Apr. 20, 2009), **Exhibit III-148**.

electricity, water, and roads and 27.5 billion RMB is projected to be spent on other major infrastructure projects.³²² In 2008, Zhongwang obtained contracts for several state key projects, including the expansion of Beijing Capital International Airport, certain Beijing Olympic venues, and Expo 2010 Shanghai.³²³ In addition, China's stimulus calls for RMB 28 billion to be spent on affordable housing.³²⁴ China's construction sector is the largest consumer of aluminum extrusions.³²⁵ Public information indicates that Asia Aluminum also has been supplying aluminum extrusions for large state projects, such as the National Centre for the Performing Arts, and the National Aquatics Center, also known as the Water Cube.³²⁶

Xingfa Aluminum Holdings Ltd. also appears to have benefitted from government procurement contracts. The company's aluminum door and window frames have been used for the construction of several government buildings, such as the Guizhou provincial government building, and municipal government buildings in Hebei Province.³²⁷

³²² "China to Spend \$19 Bln in Second Stimulus Tranche," *Reuters* (Feb. 3, 2009), **Exhibit III-149**.

³²³ See MOFCOM, "China Zhong Wang Chairman Liu Zhongtian Accumulates 24 Billion Yuan Within 15 Years, Becomes Richest in China" (Sep. 22, 2009), **Exhibit III-147**.

³²⁴ "China to Spend \$19 Bln in Second Stimulus Tranche," *Reuters* (Feb. 3, 2009), **Exhibit III-149**.

³²⁵ Zhongwang Prospectus at 64-65, **Exhibit III-72**. The construction industry is still expected to remain the largest consuming sector of aluminum extrusion products with a dominant market share of more than 60 percent globally.

³²⁶ See "Zhaqing Will Have Largest Aluminum Industrial Base in Asia," *China Industry Newspaper* (May 17, 2005), **Exhibit III-150**; see also "World-Known Asia Aluminum Comes to Xi'an, Starts Competing in Northwest," *China Nonferrous Metals Net* (Sep. 29, 2009), **Exhibit III-151**.

³²⁷ See "Xinhua Net: Xingfa Aluminum Publishes Several Innovations, Resolve Difficulties in Aluminum Industry," *Xinhua Net* (Apr. 30, 2009), **Exhibit III-152**.

Government purchases of goods for more than adequate remuneration have been found by the Department to provide a countervailable subsidy in several prior proceedings. In *Low Enriched Uranium from France* ("Uranium from France"), for example, the Department found that Eurodif, the respondent in the investigation, received a countervailable benefit resulting from purchases of low enriched uranium by EdF, a wholly-owned subsidiary of the Government of France, for more than adequate remuneration. The Department found that this constituted a financial contribution provided by the Government of France under section 771(5)(D)(iv) of the Act.³²⁸

Similarly, in *Stainless Steel Sheet and Strip in Coils from the Republic of Korea*, the Department found that the purchase by POSCO (a company owned and controlled by the Government of Korea) of the specialty steel bar and pipe division of the respondent company, Sammi, was made for more than adequate remuneration. The Department found this to be a financial contribution to Sammi under section 771(5)(D) of the Act.³²⁹ The Department also found that the subsidy was specific in accordance with section 771(5A)(D)(i) of the Act.³³⁰

1. Financial contribution

Under section 771(5)(D)(iv) of the Act, a countervailable benefit may be provided through a government's purchase of a good for "more than adequate remuneration." In this instance, the entities purchasing goods are government entities making purchase for construction

³²⁸ *Notice of Final Affirmative Countervailing Duty Determination: Low Enriched Uranium From France*, 66 Fed. Reg. 65901 (Dec. 21, 2001) and accompanying Issues and Decision Memorandum ("*Uranium I&D Memo*") at Section "Purchase at Prices that Constitute 'More Than Adequate Remuneration'."

³²⁹ *Final Affirmative Countervailing Duty Determination: Stainless Steel Sheet and Strip in Coils From the Republic of Korea*, 64 Fed. Reg. 30636, 30643 (June 8, 1999).

³³⁰ *Id.*

and infrastructure improvements under China's stimulus spending plan and other projects. This would apply to all entities that are majority-owned by the Chinese government at any level, national, provincial, local, etc. Treating majority-government owned entities as the government for purposes of section 771(5)(D) of the Act is consistent with *Stainless Steel Sheet and Strip in Coils from the Republic of Korea*.³³¹ It is also consistent with the treatment of government entities for purposes of allegations regarding government provision of good for less than adequate remuneration in a host of recent countervailing duty investigations involving China.³³²

2. Benefit

Section 771(5)(E)(iv) of the Act states that a countervailable benefit may be provided through a government's purchase of a good for "more than adequate remuneration." Section 771(5)(E)(iv) of the Act goes on to provide that the adequacy of remuneration will be determined in relation to the prevailing market conditions for the goods being purchased in the country which is subject to investigation.

The law that covers government procurement in China is the *Government Procurement Law of the People's Republic of China* (the "*Government Procurement Law*"). Adopted in 2002, the *Government Procurement Law* permits government agencies in China to procure imported goods or services only when domestic goods or services are either unavailable or cannot be

³³¹ *Id.* "Based on the information on the record, we preliminarily determine that the actions of POSCO should be considered as an action of the GOK because POSCO is a government-controlled company. During the POI, the GOK was the largest shareholder of POSCO. We also note that POSCO is one of three companies designated as a "Public Company" by the GOK. One of the other "Public Companies" is the state-run utility company, KEPCO. This determination that POSCO should be treated as a government-owned provider of a good or service is consistent with other cases involving the provision of a good or service by government-owned companies. See, e.g., *Final Affirmative Countervailing Duty Determination: Steel Wire Rod from Venezuela*, 62 FR 55014 (Oct. 22, 1997)."

³³² See e.g., *China OCTG I&D Memo* at 70-71.

obtained under "reasonable commercial conditions."³³³ This law applies to all levels of government procurement -- national, provincial, and local.³³⁴

Article 10 of the *Government Procurement Law of the People's Republic of China* provides in relevant part:

The government shall procure domestic goods, construction and services, except in one of the following situations:

(1) where the goods, construction or services needed are not available within the territory of the People's Republic of China or, though available, cannot be acquired on reasonable commercial terms;

(2) where the items to be procured are for use abroad; and

(3) where otherwise provided for by other laws and administrative regulations.³³⁵

Moreover, the draft regulations implementing the *Government Procurement Law* guarantee that Chinese companies will benefit from significant pricing preferences. The PRC's draft *Implementation Regulations on the Government Procurement Law of the People's Republic of China* provides guidance regarding the implementation of China's *Government Procurement Law*. Specifically, the draft regulations state that "{t}he situation where reasonable commercial terms' are not available for procurement under Article 10 of the *Government Procurement Law*, refers to instances where the lowest offered price for domestic goods, construction or services, that meet the requirements of procurement documents, exceeds the lowest offered price for

³³³ *Government Procurement Law of the People's Republic of China*, Order of the President No.68 (Jun. 29, 2002), **Exhibit III-153**.

³³⁴ See the US-China Business Council, PRC Government Procurement Policy (Jul. 2009) at 3, **Exhibit III-154**.

³³⁵ *Government Procurement Law of the People's Republic of China*, Order of the President No.68 (Jun. 29, 2002), **Exhibit III-153**.

foreign goods, construction or services by more than 20 percent.³³⁶ Essentially, this means that goods procured from domestic sources have an automatic 20 percent price premium over any goods offered from foreign sources.

Beginning in 2006, the GOC took another important step to secure preferences for domestic Chinese companies in government procurement when the GOC adopted its policy of promoting "indigenous innovation."³³⁷ Under this policy, government agencies work cooperatively to develop measures that favor products that use indigenously-developed ideas and technology.³³⁸ In the wake of this policy pronouncement, government agencies at all levels have implemented preferential policies, product catalogues, financing schemes, and other tools aimed at furthering the indigenous innovation goals in government procurement.³³⁹ Subsequently, the GOC released the *Selected Supporting Policies for the 2006-2020 Medium and Long-Term Science and Technology Development Plan* issued in 2006.³⁴⁰ This plan developed preferences for indigenous innovation product in price-based bidding.³⁴¹ In 2007, the pricing preferences for indigenously-produced products were further strengthened when the GOC issued the *2007 Evaluation Measure on Indigenous Innovation Products for Government Procurement* (the

³³⁶ *Implementation Regulations on the Government Procurement Law of the People's Republic of China (Draft)* (Jan. 11, 2010), **Exhibit III-155**.

³³⁷ U.S.-China Business Council, *Issue Brief: New Developments in China's Domestic Innovation and Procurement Policies* (Jan. 2010) at 1, **Exhibit III-156**.

³³⁸ *Id.*

³³⁹ *Id.*

³⁴⁰ *Id.* at 3.

³⁴¹ *Id.*

"*Evaluation Measures*").³⁴² Article 13 of the *Evaluation Measures* provides that indigenous innovation products shall be given preferences at a margin of 5-10 percent in the event that price is the sole determining factor, while Article 14 states that indigenous innovation products shall enjoy an additional 4 to 8 percent technical and price evaluations if comprehensive evaluations methods are used.³⁴³

In November 2009, the GOC issued application procedures for gaining accreditation and inclusion in China's new indigenous innovation product catalog. Appendix 2 lists the products eligible for accreditation, which were taken from the 2006 National Catalogue of New and High-Technology Products.³⁴⁴ Many of the technologies focus on products promoting energy efficiency and alternative energy sources, many of which utilize extruded aluminum. For example, the list specifically mentions solar panel modules. Solar panels are a growing segment of the market for aluminum extrusions.³⁴⁵

Government procurement of goods at prices higher than those prevailing in the world market is considered by many as one of the problems in China's government procurement

³⁴² *Id.*

³⁴³ *Id.*

³⁴⁴ The U.S.-China Business Council, *Request for Company Input on PRC Domestic Innovation Policies* (Dec. 15, 2009) at 9, **Exhibit III-157**.

³⁴⁵ See Zhongwang Prospectus at 61, **Exhibit III-72**.

activities.³⁴⁶ Moreover, the GOC has a history of overpaying for purchases from the aluminum industry in connection with its efforts to support the sector.³⁴⁷

Petitioners have conducted an exhaustive search for information regarding the actual prices paid by GOC entities and by government-owned companies, but public sources do not reveal this information. However, Petitioners believe that the pricing preferences inherent in the various government procurement laws and regulations, as well as in the indigenous innovation program, information reasonably available to Petitioners, provides sufficient basis for the Department to initiate an investigation of whether GOC procurement of aluminum extrusions may result in a benefit to Chinese producers.

3. Specificity

Article 10 of the *Government Procurement Law* requires the GOC to source goods, construction, and other services from domestic companies. The only exception for this is when the goods, construction or services cannot be purchased on reasonable economic terms, when the procured items are services are for use abroad or where otherwise provided for by other laws or regulations -- *i.e.* only under very circumscribed situations.

The definitions for the domestic goods, construction or services mentioned in the preceding paragraph shall be applied in accordance with the relevant regulations of the State Council.³⁴⁸

³⁴⁶ See "Guangdong Legislation Attempts to Solve 'Chronic Problems' in Government Procurement," *Bid Winning Net* (Aug. 12, 2009), **Exhibit III-158**; see also "Problems in Supply by Agreement and Resolution Strategies," *Ningbo City Government Procurement Net* (Feb. 16, 2009), **Exhibit III-159**.

³⁴⁷ See the Aluminum Association, "China's State Reserve Agency Stockpile to Buoy Aluminum Sector" (Dec. 29, 2008) (indicating the GOC pays a ten percent premium when buying primary aluminum), **Exhibit III-140**.

³⁴⁸ *Government Procurement Law of the People's Republic of China*, Order of the President No.68 (Jun. 29, 2002), **Exhibit III-153**.

Consequently, as a matter of law, the GOC's government procurement program is contingent upon the use of domestic goods over imported goods, and is therefore specific under section 771(5A)(C) of the Act.

G. Currency Undervaluation

The GOC currently maintains an exchange rate regime in which the government ties the value of the Chinese currency, the RMB, to a basket of currencies heavily weighted by the U.S. dollar.³⁴⁹ For more than a decade, the GOC has ensured that the RMB exchange rate significantly understates the value of the RMB vis-à-vis the U.S. dollar -- by up to nearly 50 percent, according to some estimates.³⁵⁰ In fact, according to a recent article in the *Washington Post* “most economists agree that the yuan is generally undervalued by 25 to 40 percent against the dollar. The cheap yuan has allowed China to amass by far the largest trade surplus in the world and a war chest of more than \$1.7 trillion of foreign exchange.”³⁵¹ The same article states that President Obama “vowed to ‘get much tougher’ on China over the {currency} issue

³⁴⁹ See *United States Department of the Treasury, Report to Congress on International Economic and Exchange Rate Policies* (Apr. 15, 2009) (“2009 Treasury Report”) at 19, **Exhibit III-160**. For eight years prior to July 2005, the RMB was pegged exclusively to the dollar. See *id.* at 17.

³⁵⁰ See, e.g., *Assessing Progress on China's Exchange Rate Policies*, Testimony of Morris Goldstein, Senior Fellow, Peterson Institute for International Economics, before the Senate Finance Committee (Mar. 28, 2007) at 1, **Exhibit III-161**; *The Economist Big Mac Index*, which estimates that the RMB is undervalued by 48 percent, **Exhibit III-162**; *Currency Misalignments and the U.S. Economy*, Testimony of C. Fred Bergsten, Director, Peterson Institute for International Economics (May 9, 2007) (“*Currency Misalignments*”) at 3, **Exhibit III-163** (estimating that the RMB is currently overvalued by 36 percent); The China Currency Coalition, *Estimation of the Fundamental Misalignment of the Chinese Renminbi* (July 2008), **Exhibit III-164** (estimating that during the presumptive POI the RMB was undervalued by between 30 and 35 percent relative to the U.S. dollar).

³⁵¹ “U.S. officials hopeful China will make concessions on currency,” *Washington Post* (Feb. 5, 2010), **Exhibit III-165**.

'to make sure our goods are not artificially inflated in price and their goods are not artificially deflated in price'³⁵²

Between 1998 and the end of 2005, the value of RMB was pegged to the dollar and did not fluctuate by more than three percent relative to the dollar.³⁵³ In 2005, the GOC began to allow the RMB to appreciate, but only at an artificially low rate that does not reflect China's massive current account surpluses, which under normal market conditions would result in a significant appreciation.³⁵⁴

By maintaining the RMB at undervalued levels, the GOC promotes the export of Chinese manufactured goods.³⁵⁵ While this undervaluation may or may not run afoul of the relevant rules at the IMF -- a question that is beyond the scope this petition -- it is clear that that the undervaluation constitutes a subsidy under the countervailing duty law. The significant trade surplus that China maintains with the United States is a direct result of this undervaluation. China's exchange rate regime also results in a countervailable subsidy to Chinese manufacturers exporting to the United States, including aluminum extrusion producers. When these producers

³⁵² *Id.*

³⁵³ See *Currency Misalignments, Exhibit III-163; 2009 Treasury Report, Exhibit III-160.*

³⁵⁴ The United States Census Bureau reports that the trade deficit with China ballooned to \$268 billion by the end of 2008. See U.S. Census Bureau Statistics (2009), *Exhibit III-166.* As the Treasury Department reports: "China's continued large current account surplus and accumulation of foreign exchange reserves suggest the renminbi remains undervalued. To limit the pace of renminbi appreciation, the PBOC buys foreign currency in the foreign exchange market, adding to China's stock of foreign reserves." *2009 Treasury Report* at 19, *Exhibit III-160.*

³⁵⁵ While GOC officials do not generally discuss the role that China's undervalued currency plays in promoting exports, many observers have made this connection. See *e.g.*, Chu Ping Lo *et al.*, *Exchange Rate and International Outsourcing: Would Chinese Yuan Appreciate Against the Dollar?*, *Exhibit III-167.*

sell to the United States, they are paid in U.S. dollars. The producers are then required to sell those dollars to the official Chinese foreign exchange banks in return for RMB.³⁵⁶ Because the GOC manipulates the exchange rate to keep the RMB undervalued, the exporters receive more RMB per dollar than they otherwise would if the value of the RMB were determined through market mechanisms. The GOC's undervaluation of its currency constitutes an export subsidy, and meets all three criteria for countervailability: it involves a government financial contribution or income or price support, it provides a benefit, and it is specific.

I. Background on GOC's currency practices

Prior to 1994, China maintained an exchange system in which the government had strict control over the value of, as well as the supply of and demand for, foreign exchange. The government set exchange rates at levels that were either too high, in order to encourage imports of capital equipment, or too low, to discourage imports and to promote exports. Moreover, there were often large differences between the officially controlled exchange rate and market-based rates, including an officially authorized swap rate and illegal black market rates. The GOC worked to manage these divergences, but there was still significant volatility.

In order to maintain tighter control over exchange rates, in 1994 China fundamentally altered its foreign exchange system by abolishing the authorized swap market and establishing a single national market, with the exchange rate pegged at 8.70 RMB to the dollar.³⁵⁷ In addition,

³⁵⁶ China maintains strict capital controls. With limited exceptions, companies earning foreign exchange from transactions outside China must surrender these earnings which are then converted to RMB at the GOC-established exchange rates. See CRS Report for Congress, *China's Currency: Economic Issues and Options for U.S. Trade Policy*, RL32165 (May 22, 2008) ("CRS Report") at 14, **Exhibit III-168**; see also Robin Hang Luo *et al.*, "Currency Convertibility, Cost of Capital Control and Capital Account Liberalization in China," *Journal of Chinese Political Science* (Apr. 2005), **Exhibit III-169**.

³⁵⁷ See Jiawan Yang *et al.*, "The Chinese Currency: Background and the Current Debate," *George Washington University School of Business*, at 5, **Exhibit III-170**.

Chinese companies were no longer allowed to hold foreign exchange, but were required to surrender all of their export earnings to the Chinese government through official foreign exchange banks.³⁵⁸ The GOC strictly regulated the purchase of foreign exchange, which could only be transacted at the official rates set by the government.³⁵⁹

Between 1994 and 1998, the value of the RMB against the dollar appreciated slightly from the initial peg of 8.70 RMB to about 8.30 RMB to the dollar.³⁶⁰ Toward the end of 1998, the rate was set at 8.28 RMB to the dollar, and remained unchanged for *the next seven years*.³⁶¹ In July 2005, under international pressure to liberalize its exchange rate regime, the GOC announced a one-time revaluation of slightly more than two percent. The GOC also announced that it would henceforth peg the RMB to what it termed a basket of currencies and permit its currency to fluctuate within a daily trading band of +/- 0.3 percent.³⁶² These changes have not, however, eliminated the fundamental misalignment of the RMB and the dollar, and Chinese exporters continue to benefit from a windfall when exchanging their dollar-denominated export earnings for RMB.³⁶³

³⁵⁸ See Min Zhao, "External Liberalization and the Evolution of China's Exchange System: an Empirical Approach," (World Bank 2006), **Exhibit III-171**.

³⁵⁹ See *id.*

³⁶⁰ See Jiawan Yang *et al.*, "The Chinese Currency: Background and the Current Debate" at 6, **Exhibit III-170**.

³⁶¹ See *id.*

³⁶² See *Announcement of the People's Bank of China on Reforming the RMB Exchange Rate Regime* (July 21, 2005), **Exhibit III-172**.

³⁶³ Since China "liberalized" its exchange mechanism in July 2005, the RMB has only appreciated by about 17 percent, "How China Scores with A Managed Currency" (Jul. 21, 2009), *Commodity Online*, **Exhibit III-173**.

In order to maintain China's exchange rate at a fixed level, the GOC must intervene in several ways to control supply and demand imbalances. Among other things, the GOC maintains strict capital controls, restricting most companies in China from maintaining foreign exchange holdings.³⁶⁴ Most Chinese companies are required to repatriate their profits by exchanging the foreign currency for RMB at the mandated exchange rate.³⁶⁵ In addition, the GOC also places strict controls on the investment activities of both foreign and domestic companies, as evidenced by several of the catalogues of encouraged industries and projects identified in this Petition.

During most of the presumptive period of investigation, China's most basic law on foreign exchange control was the *Regulations of the People's Republic of China on Foreign Exchange Control* promulgated by the State Council on January 26, 1996, and amended on January 14, 1997.³⁶⁶ Article 7 of the law states that

Foreign currency is prohibited for circulation and shall not be quoted for pricing or settlement in the territory of the People's Republic of China.

Article 12 of the Regulation states that

The collection of export proceeds and the payments for imports in foreign exchange by domestic entities shall be processed in accordance with the relevant government regulations governing the verification procedures for export proceeds and import payments.

These regulations were revised in August 2008 but the new version does not appear to fundamentally alter these restrictions.³⁶⁷

³⁶⁴ See generally CRS Report at 14, **Exhibit III-168**.

³⁶⁵ See *id.*

³⁶⁶ See *1997 Regulations of the People's Republic of China on Foreign Exchange Control*, **Exhibit III-174**.

³⁶⁷ See *2008 Foreign Exchange Control Regulations of the People's Republic of China* at Arts. 8 and 12, **Exhibit III-175**.

In addition to strict currency controls, the GOC maintains the currency peg by intervening to purchase the excess foreign exchange accumulating in China on account of China's huge trade surpluses.³⁶⁸ It does this by means of printing RMB to pay for foreign exchange.³⁶⁹ By selling RMB and buying dollars, the GOC is able to artificially bid up the value of the dollar vis-à-vis the RMB.

2. China's undervaluation of its exchange rate

The Bretton Woods conference in 1944 established the IMF, which was founded to promote four primary objectives: a balanced expansion of world trade, maintaining stable exchange rates, avoiding competitive currency devaluations, and the orderly correction of balance-of-payments problems. Thus, one of the key elements of a healthy global economy is the minimization of situations where countries devalue their currencies in order to drive export-led growth. Article IV of the IMF Articles of Agreement states that members shall

avoid manipulating exchange rates or the international monetary system in order to prevent effective balance-of-payments adjustments or to gain unfair competitive advantage over other members.³⁷⁰

IMF member countries may select whatever exchange regime they want -- a fixed rate regime or a floating rate regime, or any type in between, known as intermediate exchange rate regimes, including conventional fixed pegs, crawling pegs, crawling bands, and tightly managed floats.³⁷¹ IMF members are also permitted to intervene intermittently in capital markets in order

³⁶⁸ See CRS Report at 13, **Exhibit III-168**.

³⁶⁹ See *id.* at 3.

³⁷⁰ See *IMF Articles of Agreement*, **Exhibit III-176**.

³⁷¹ It is interesting that China characterizes its own exchange rate as a managed float. Given the lack of fluctuation in the RMB exchange rate, the GOC obviously puts more emphasis

to maintain orderly exchange rates. What countries are *not* permitted to do is to intervene in financial and foreign exchange markets at a level that rises to "manipulation." In order to provide some guidance on what constitutes manipulation, the IMF adopted a standard in 1977 that discussed "protracted, large-scale intervention in one direction in the exchange market," as being indicative of manipulation and thus of concern to other members.

China's efforts to maintain its exchange rate at levels that undervalue the RMB rise to the level of "protracted," "large-scale," and "in one direction." It is typical that governments intervene in capital markets from time to time and on a temporary basis to influence the direction of their currency either up or down, in order to smooth out disjunctures.³⁷² China's intervention in the foreign exchange markets, however, has persisted at a significant level for years in order to benefit the export sector. The fact that the exchange rate remained essentially unchanged between 1995 and 2005 and appreciated only slightly over the next several years itself is

on the "managing" and not enough on the "floating." The IMF does not concur with China's characterization of its exchange rate regime, classifying it instead as a "conventional peg."

³⁷² As one commentator recently observed:

In most mature economies with floating exchange rates and open capital markets, intervention now occurs only infrequently... The European Central Bank and the U.S. Federal Reserve Board, for example, may let years go by without carrying out any intervention at all ...

Intervention among emerging market countries is most prevalent in those with exchange rate targets... {The} combination of sterilized intervention and barriers to capital mobility is thought to enable a country to maintain a relatively weak exchange rate without engendering domestic inflation. It is also exactly this combination of sterilized intervention and capital controls that so frustrates the trading partners of a few emerging market countries and provokes accusations of excessive currency manipulation.

Princeton Encyclopedia of the World Economy (2009) at 489-90, **Exhibit III-177.**

evidence that China's intervention has been protracted. The GOC's intervention has also been large in scale. In years past, the GOC intervened in the foreign currency market at a rate of \$15 to \$20 billion per month to suppress the value of the RMB, but more recent interventions are estimated to exceed \$45 billion per month.³⁷³ The GOC's accumulated foreign reserve holdings are also evidence that the GOC's intervention has been large in scale. China now holds more than \$1 trillion in foreign currency, with some reports indicating that the country has as much as \$2 trillion.³⁷⁴ The fact that the RMB-dollar exchange rate has remained relatively unchanged in the face of skyrocketing current account and trade surpluses is evidence that the GOC's intervention has been "in one direction."

The GOC effectively prevents the appreciation of the RMB against the dollar to a level that would reflect China's true balance of payments situation, resulting in a large and fundamental misalignment between the dollar and the RMB. Because of this GOC-maintained exchange rate, Chinese exporters earning dollars through export transactions receive an artificially inflated amount of RMB when they exchange those dollars at the People's Bank of China, a Chinese government entity. As a result, the GOC ensures that exporters who receive dollars from their export activities receive more RMB than they otherwise would if the value of the RMB were set through market mechanisms. This provides Chinese exporters with a considerable subsidy. As noted below, Petitioners believe that the GOC's program to maintain artificial exchange rates qualifies as a financial contribution or, alternatively, as a form of income or price support within the meaning of Article XVI of the GATT 1994, and provides Chinese

³⁷³ See *Currency Misalignments* at 3, **Exhibit III-163**.

³⁷⁴ See *id.* See also "China's Foreign Exchange Reserves Surge, Exceeding \$2 trillion," *Bloomberg News* (July 9, 2009), **Exhibit III-178**.

exporters of aluminum extrusions with a benefit. Because receipt of the subsidy is contingent upon export, the subsidy qualifies as a prohibited export subsidy.

3. Currency undervaluation has been a long-standing concern under the GATT and the WTO Agreements as well as U.S. law

The GATT and WTO Agreements, as well as U.S. law, have long recognized that government-managed exchange rates can confer countervailable subsidies on exports.

a) Currency undervaluation has been a long-standing concern under the GATT and the WTO Agreements

Article XV:4 of GATT 1994 is an overarching WTO provision addressing exchange rate issues. In particular, GATT Article XVI:4 provides that the “[c]ontracting parties shall not, by exchange action, frustrate* the intent of the provisions of this Agreement, nor, by trade action, the intent of the provisions of the Articles of Agreement of the International Monetary Fund.”

In his seminal book *World Trade Law and the Law of GATT*, Professor John Jackson explained the rationale of GATT Article XVI as follows:

It was well recognized at the time of drafting GATT that currency par value manipulation and exchange controls could be used to protect domestic markets against imports. In the 1945 legislative history of the act authorizing the United States participation in GATT, congressional complaints against foreign use of these devices were strong. (footnote omitted) The GATT draftsmen, particularly the American delegates, felt constrained to include some protection against them in the tariff agreement, even though the International Monetary Fund articles contained some similar provisions. (footnote omitted)

The use of exchange rates and exchange rate controls to inhibit imports can be illustrated by several examples. First, a nation can, by devaluing its currency, shift the terms of its international trade ... (footnote omitted) By making its currency cheaper with respect to foreign currencies, imports become more expensive relative to domestic products and are therefore discouraged ... Likewise, the same move makes exports cheaper relative to foreign goods ... ³⁷⁵

³⁷⁵ John H. Jackson, *World Trade and the Law of GATT*, The Bobbs-Merill Company, Inc, 1969, pp. 479-80.

Thus, GATT Article XVI:4 acknowledges that exchange rate measures can frustrate the intent of the provisions of GATT (for instance, by offsetting trade concessions under GATT Article II or undermining disciplines on subsidization under GATT Article XVI) and that, on account of these effects, such measures fall squarely within the purview of WTO rules, even if they are often considered exchange rate measures as opposed to trade measures.

For instance, currency manipulation in the form of sustained undervaluation can offset a trade concession by making imports artificially expensive in local currency. Multiple exchange rates can also offset the trade concessions relating to imports that are assigned an exchange rate that makes them artificially expensive in local currency. Finally, exchange rate controls can act as an import quota in respect of imports that are subject to exchange rate rationing.

Other WTO provisions expressly recognize that exchange rate measures can constitute export subsidies. For instance, multiple exchange rates can provide an export subsidy by enabling exporters of certain goods to earn more local currency for their export receipts than they would have earned absent this regime.

In particular, Note 2 to paragraphs 2 and 3 of GATT Article VI provides that "multiple currency practices" (*i.e.*, multiple exchange rates) can constitute either export subsidies or a form of dumping:

*GATT Ad Article VI
Paragraphs 2 and 3*

2. Multiple currency practices can in certain circumstances constitute a subsidy to exports which may be met by countervailing duties under paragraph 3 or can constitute a form of dumping by means of a partial depreciation of a country's currency which may be met by action under paragraph 2. By "multiple currency practices" is meant practices by governments or sanctioned by governments.

In 1957, the GATT Secretariat examined the application of antidumping and countervailing duties by the Contracting Parties. In reviewing the types of measures that involve subsidization, the Secretariat referenced the Ad Note to Article VI:

A special type of low price import may also be mentioned in this connection, namely those which are the consequence of currency measures taken in the exporting country. While in most such instances the price comparison will not permit the levy of an anti-dumping duty, GATT expressly permits the levy of countervailing duties in circumstances where the exportation of the product is facilitated by a multiple currency system (Note to Article VI). A case in which such a provision has been applied is the imposition of a countervailing duty by the United States on imports of wool tops from Uruguay.³⁷⁶

The study further noted: "Concerning countervailing duties, the United States has indicated that these are used to offset all types of export subsidization, including subsidization through differential exchange 'rates'."³⁷⁷

The Illustrative List of Export Subsidies in Annex I to the WTO SCM Agreement (as well as in the 1979 Subsidies Code) classifies as such both "currency retention schemes and any similar practices which involve a bonus on exports" (Item (b)), and the government provision of "exchange risk programmes, at premium rates which are inadequate to cover the long-term operating costs and losses of the programmes" (Item (j)). Clearly, if "currency retention schemes and any similar practices are in item (b), they must be presumed to qualify as a subsidies. A government's currency retention scheme would allow its exporters to retain foreign-exchange earnings rather than exchange them for local currency."³⁷⁸

³⁷⁶ GATT, *Anti-Dumping and Countervailing Duties* (1957) at 7, **Exhibit III-179**.

³⁷⁷ *Id.* at 13.

³⁷⁸ See Deborah E. Siegel, "Legal Aspects of the IMF/WTO Relationship: The Fund's Articles of Agreement and the WTO Agreements," 96 *Am. J. Int'l L.* 561, 596 (July 2002), **Exhibit III-180**.

While the GOC's managed exchange rate for U.S. dollars may not be identical to the "multiple currency practice," "currency retention scheme" or "exchange risk program" as referenced in the Ad Note 2 to GATT Article VI:2-3 or the SCM Agreement's Illustrative List of Export Subsidies, the GOC's exchange rate scheme is practically and functionally equivalent to those practices because it likewise favors or provides a "bonus" on exports by inflating the value of one currency (or basket of currencies). Accordingly, the GOC's managed exchange rate is a "similar practice" within the meaning of item (b).

b) Currency undervaluation has been a long-standing concern under U.S. law

Before the creation of GATT after World War II, as well as after the GATT was adopted, the United States has countervailed currency schemes where an incentive to export was created. For example, in the 1930s, Germany regulated and controlled its currency in such a manner that it maintained different categories of reichmarks with different conversion values. By regulation, Germany allowed the lower-valued reichmarks to be used for the purchase of German goods to be exported. The German exporter, however, could redeem the lower-valued marks at the rate of the higher-valued marks. This practice led the Treasury Department to issue Treasury Decision 48360 in June 1936, which stated:

Notice is hereby given that pursuant to the provisions of section 303 of the Tariff Act of 1930, countervailing duties equal to any bounty and/or grant found to have been paid and/or bestowed will be collected on articles of the kinds named below from Germany...

The courts upheld this decision in a number of proceedings:

- *F.W. Woolworth Co. v. United States:*

{T}o the {German} manufacturer one of the reichmarks paid from the registered reichmark account was worth the same as one of the marks paid from the free reichmark account.

* * *

It is not possible to escape the conclusion from the record that the German Government by various devices and through different authorized governmental agencies was seeking to aid its manufacturers in invading foreign markets with their goods to compete in such markets with domestic producers. . . . Among such was the control of the registered marks and the limitations placed upon their use.³⁷⁹

- *V. Mueller & Co., v. United States:*

We are of the opinion that the presumption of correctness attaches to this finding.³⁸⁰

- *Robert E. Miller & Co., Inc. v. United States:*

The imported goods were paid for on April 10, 1937, in Aski marks which were purchased at a lower price than the current value of free or gold reichmarks. Aski marks were of the class of currency which, under German regulation, could be used in payment for exported goods and subsequent to such use were redeemed by the German Government at the same value as free reichmarks thereby enabling the German manufacturer to dispose of his exported goods at a "dollar-equivalent" less than would otherwise be charged.³⁸¹

As noted in the above-referenced GATT study, in May 1953, as a result of a multiple exchange rate system maintained by Uruguay, the U.S. Treasury Department issued a notice of countervailing duties on imports of wool tops from Uruguay. T.D. 53257, 88 Treas. Dec. 105; 18 Fed. Reg. 2653 (May 7, 1953). On appeal, the Customs Court upheld T.D. 53257, stating:

Under this statute, it has been held that multiple exchange rate systems can result in a bounty or grant.

³⁷⁹ 28 C.C.P.A. 239 (1940) at 246 and 248, 115 F.2d 348.

³⁸⁰ 28 C.C.P.A. 249, 256 (1940), 115 F.2d 354.

³⁸¹ 34 CCPA 101, 102-103, 105 (1946).

It has also been recognized internationally that multiple currency practices can in certain circumstances constitute a subsidy to exports which may be met by countervailing duties. Interpretative Notes to the General Agreement on Tariffs and Trade, Ad Article VI....

* * *

In our opinion, the facts presented here support the Treasury Department's finding that, at the time of its decision, wool tops exported from Uruguay received bounties or grants within the meaning of section 303 of the Tariff Act of 1930.

One of the purposes of Uruguay's multiple rate of exchange system was to aid industries which needed assistance in order to place products abroad. Under such a system, which assigns different exchange rates to different commodities, some exports are favored over others. In the instant case, the record shows that wool tops were favored over many other commodities and that the manufacturer was enabled to sell them to the United States profitably, which he could not otherwise have done. ... By means of the exchange rate granted to wool tops, an inducement was offered for the exportation of wool in the form of tops rather than in the form of unmanufactured wool. The result was to increase seriously the importation of wool tops into this country from Uruguay and to permit their sale at lower prices in competition with domestically produced wool tops.³⁸²

4. Currency undervaluation constitutes a countervailable subsidy because it is a financial contribution that provides a benefit to the recipient and is specific to exports

a) Financial contribution

The GOC's undervaluation of its currency to maintain an undervalued RMB represents a direct transfer of funds under Section 771(D)(i) of the Act. The GOC requires that foreign exchange earned from export activities be converted to RMB, at the government-prescribed rate,

³⁸² *Energetic Worsted Corp. v. United States*, 224 F. Supp. 606, 612-614 (Cust. Ct. 1963). Upon review by the Court of Customs and Patent Appeals, the decision of the Customs Court was reversed on other grounds. The CCPA did so because it found that Treasury's "procedure" in determining a weighted benchmark was not appropriate. *Energetic Worsted Corp. v. United States*, 53 CCPA 36, 45-46 (1968).

and only at government-owned banks or government-authorized exchange facilities. The rate at which exporters convert foreign exchange earnings exceeds what these exporters would otherwise obtain if the rate of exchange were market determined. This results in more RMB being provided to exporters for every dollar that they exchange than they otherwise would get absent government intervention. This represents a direct transfer of funds (RMB) from the GOC to exporters. The GOC's undervaluation of its currency to maintain an undervalued RMB could also be considered the provision of a good or service other than general infrastructure under Section 771(5)(D)(iii) of the Act.

b) Benefit

The GOC's undervaluation of its currency bestows a benefit to exporters because exporters receive more RMB per dollar than they otherwise would if the Chinese government were not manipulating the rate and markets were allowed to determine the equilibrium rate of exchange. If the financial contribution is deemed to take the form of the provision of a good or a service, a benefit would be conferred to the extent that such goods or services are provided for less than adequate remuneration, or in the case where goods are purchased, if such goods are purchased for more than adequate remuneration under Section 771(5)(E)(iv) of the Act. The benefit would be calculated as the difference between the RMB received by exports when they exchange dollars and the rate that they would receive absent the government's intervention in the foreign currency regime.³⁸³

c) Specificity

In the Preliminary Negative Countervailing Duty Determination: Certain Laminated Hardwood Trailer Flooring from Canada, 61 Fed. Reg. 59,079, 59,082 (Nov. 20, 1996)

³⁸³ See 19 C.F.R. § 351.501 and *Countervailing Duties; Final Rule*, 63 Fed. Reg. 65347 at 6539-60 (Nov. 25, 1998) describing the flexibility inherent in determining subsidy benefits.

("Laminated Hardwood Trailer Flooring from Canada"), the Department clarified its standard for finding a *de facto* export subsidy and provided an illustrative example of how currency restrictions constitute *de facto* export subsidies:

Article 3.1(a) and note 4 of the Agreement on Subsidies and Countervailing Measures clarifies that the "in fact" standard "is met when the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings...."

....

We recognize that the projects for which Leclerc sought financing were largely aimed at the U.S. market in the sense that the company expected to sell most of its increased production to the United States. However, there is no evidence to support a finding that Leclerc's receipt of the loans and guarantees was contingent upon or tied to actual or anticipated exportation to the United States. Although the granting authority was aware of the anticipated destination of the output, this fact alone does not render the program a *de facto* export subsidy. Specifically, we do not believe that the assistance awarded Leclerc was contingent upon the company exporting outside of Canada. Indeed, Leclerc could have qualified for assistance by "exporting" to another province in Canada. Therefore, we have preliminarily determined that the loans and guarantees given under the Export and Modernization and PREP programs are not export subsidies.

The situation we are addressing here can be contrasted with other situations that might give rise to possible *de facto* export subsidies. For example, a loan program might be structured to require repayment in U.S. dollars rather than local currency. If currency restrictions make it impossible to obtain U.S. dollars in that country except through exportation, then the requirement to repay the loan in U.S. dollars could lead to the finding of a *de facto* export subsidy.

In this case, as the Department contemplated in *Laminated Hardwood Trailer Flooring from Canada*, government restrictions make it impossible for Chinese producers to obtain U.S. dollars except through exportation. Moreover, in China, foreign-exchange earned from export

activities must largely be converted to RMB at government-owned banks or government-authorized exchange facilities.³⁸⁴ Therefore, a Chinese producer's ability to receive excess RMB is in fact tied to its ability to export, and thus receive dollars which then can and must be converted at the government-controlled rates provided by government-owned banks.³⁸⁵ The Chinese government's restriction on foreign exchange as a whole creates a *de facto* export subsidy, as envisioned by the Department in *Laminated Hardwood Trailer Flooring from Canada* by (1) making a Chinese producer's receipt of a subsidy (excess RMB) (2) contingent on its ability to export outside of China, and (3) thus receive foreign exchange that (4) the GOC strictly controls and largely requires the producer to surrender.

In the *Final Negative Countervailing Duty Determination; Pork Rind Pellets From Mexico*, 48 Fed. Reg. 39,105 (Aug. 29, 1983) ("*Pork Rind Pellets From Mexico*"), the Department did more than theorize that currency restrictions could constitute subsidies, it conducted an investigation of Mexico's "Dual Level Currency Exchange Rate System." Although the Department ultimately found that Mexico's system did not provide a subsidy to pork rind pellet producers, the points on which the Department based its reasoning require it to initiate an investigation of Chinese currency undervaluation in the instant proceeding.

³⁸⁴ See **Exhibit III-181**, Collis et al, *China's Policy of Substantially Undervaluing the Renminbi: A Challenge for the International Monetary and Trading System* at 52 (Sept. 15, 2008) (Research Paper prepared by the Trade Law Advisory Group under a grant funded by the U.S. Small Business Administration ("*TLAG Report on Undervaluing the RMB*"). Under the Administrative Rules of the People's Republic of China on Foreign Exchange Control in 1996 (1996 Forex Regulations), China-based organizations were required to remit any foreign exchange earnings back to China and deposit such earnings in authorized foreign exchange banks).

³⁸⁵ *Id.*

In *Pork Rind Pellets From Mexico*, the Department investigated Mexico's dual exchange rate system. At the time, the government of Mexico maintained two exchange rates, a controlled exchange rate (a less favorable rate applied to all export proceeds) and a free exchange rate (a more favorable rate available to purchase imports).³⁸⁶ Like the current Chinese system, when a Mexican company received dollars through export activities, the Department found that all export proceeds were required to be converted into pesos

at the controlled rate of exchange established by the Mexican government.... We also verified that the Mexican government will require Selectos (the respondent), upon receipt of any export proceeds, to exchange those proceeds, to pesos at the controlled rate, thus receiving fewer pesos per dollar than if they were converted at the free exchange rate.³⁸⁷

Therefore, even though the use of the controlled rate was contingent upon export, there was essentially no benefit, and thus no countervailable subsidy on this component of the exchange rate regime because an exporter actually received fewer pesos than otherwise would be provided on a free market. However, in this case, the Chinese controlled rate of exchange is a more favorable rate for those exchanging dollars than what a "free exchange rate" would be. See *Undervaluation Analysis Report at 5 et seq.* Therefore, if the Department applies the exact reasoning to Chinese currency undervaluation that it applied to Mexico's *controlled rate of exchange*, it must conclude that Chinese companies are receiving more RMB per dollar than if the GOC allowed a free exchange rate. Moreover, the Department also considered the effect of

³⁸⁶ The free exchange rate was effective for companies who needed to exchange pesos for foreign exchange in order to purchase imported production inputs. This component of Mexico's exchange rate was investigated but found not to constitute a subsidy. See *Final Negative Countervailing Duty Determination; Pork Rind Pellets From Mexico*, 48 Fed. Reg. 39,105 (Aug. 29, 1983).

³⁸⁷ *Id.*

Mexico's system on its exports and found "this system does not appear to stimulate export sales of pork rind pellets over domestic sales of pork rind pellets." However, virtually every economist agrees, and the GOC has acknowledged, that its foreign currency controls are designed to stimulate export sales.³⁸⁸ The *Undervaluation Analysis Report* at 3 also concludes that "{a}s the Chinese economy has become increasingly dependent upon exporting as a source of economic growth, so too has exporting become increasingly important as a means of expanding and sustaining employment in China."

Although the Department ultimately found that Mexico's dual exchange rate system did not constitute a countervailable subsidy, it did so largely on two points: (1) the controlled rate that applied to all export proceeds caused exporters to receive fewer pesos per dollar than if converted at the free exchange rate, and (2) the separate import purchase currency regime was not a specific domestic subsidy based on the facts of that case. However, in this instance, Petitioners are providing reasonably available information that (1) the Chinese government-controlled exchange rate provided more RMB per dollar than would be provided at a free exchange rate,³⁸⁹ and (2) allege that the government-controlled exchange rate is an export subsidy, and alternatively, is a specific domestic subsidy, which is demonstrated with reasonably available information provided below.

³⁸⁸ See "After 30 Years, Economic Peril on China's Path," *N.Y. Times* (Dec. 19, 2008), **Exhibit III-182**.

³⁸⁹ See Economic Consulting Services LLC, *Analysis of Evidence of the Undervaluation of the Chinese Currency and the Evidence of Specificity of the Subsidy Benefit Derived from Currency Undervaluation* (Jan. 13, 2010) ("*Undervaluation Analysis Report*") at 5 (stating that "The prevailing economic pressure has persistently been in a direction that should have strongly bid up the value of RMB vis-à-vis other currencies. However, as shown in Exhibit III-1, the strong economic pressure to bid up the price of the RMB has not been permitted to increase commensurately the value of the RMB."), **Exhibit III-183**.

Prior to *Pork Rind Pellets From Mexico*, the U.S. also investigated currency systems during the 1930s in Germany and during the 1950s in Uruguay, thus establishing that currency undervaluation can create a countervailable subsidy that should be investigated under the countervailing duty law. In *Energetic Worsteds Corp. v. United States*, the United States Customs Court specifically addressed whether countervailing duties were an appropriate remedy when other branches of the U.S. government had not denounced the particular currency practice:

Although the United States and other countries may have recognized or approved multiple exchange rate systems in general and although there may have been various causes for Uruguay's action, nevertheless, section 303 of our tariff act imposing countervailing duties in certain circumstances has not been repealed. It must be applied whenever it is shown that a bounty or grant has been bestowed. The fact that United States representatives on the International Monetary Fund and the National Advisory Council did not object to Uruguay's multiple exchange rate system in general is not relevant. Whether or not such a system is objected to, whenever the result is a bounty as to any particular article, the statute requires that countervailing duties be imposed. The facts here show that the preferential exchange rate did result in a bounty to the Uruguayan exporter.³⁹⁰

At issue in *Energetic Worsteds Corp. v. United States* was the Treasury Department's imposition of countervailing duties on imported wool tops from Uruguay. At the time, Uruguay had a multiple exchange rate system which was designed "to aid industries which needed assistance in order to place products abroad."³⁹¹ Like the current Chinese currency system that is used to encourage exports, the Uruguay system provided "an inducement" for exportation by

³⁹⁰ *Energetic Worsteds Corp. v. United States*, 51 Cust. Ct. 55, 65 (Cust. Ct. 1963) *rev'd* 53 C.C.P.A. 36 (1966) (Although the U.S. Customs Court upheld the Treasury Department's imposition of a countervailing duty under section 303 of the Tariff Act of 1930, the U.S. Court of Customs and Patent Appeals reversed this decision on the ground that the weighted benchmark used to calculate the subsidy benefit was not supported by substantial evidence).

³⁹¹ *Id.*

giving the Uruguayan exporter a favorable return on foreign exchange.³⁹² Similarly, as discussed in *Energetic Worsted Corp. v. United States* and cited in the *Petition* at 127 through 128, Germany's currency rate system was investigated under the Tariff Act of 1930 and countervailing duties were applied to merchandise subsidized by the German government's reliance upon multiple exchange rates and, in particular, upon a depreciated rate of exchange for German exports.³⁹³

As administering authorities did in prior cases where currency practices were alleged to create a countervailable subsidy, the Department should initiate an investigation of currency undervaluation in China. Given the United States' past investigations of currency practices, the information reasonably available to Petitioners indicates that current Chinese currency practices are more likely to bestow countervailable subsidies on Chinese producers of subject merchandise than did currency practices formerly investigated by the United States in Mexico, Uruguay and Germany. Furthermore, since the Department itself has acknowledged the particular difficulties inherent in specificity analysis, and has been deferred to by the Court of Appeals for the Federal Circuit, Petitioners submit that the following information as to the specificity of the subsidy created by Chinese currency undervaluation more than meets the threshold "information reasonably available" requirement for immediately initiating an investigation of this allegation.³⁹⁴

³⁹² *Id.*

³⁹³ See *F.W. Woolworth Co. v. United States*, 28 C.C.P.A. 239, 246, 115 F.2d 348 (1940); *V. Mueller & Co., v. United States*, 28 C.C.P.A. 249, 256, 115 F.2d 354 (1940); *Robert E. Miller & Co., Inc. v. United States*, 34 C.C.P.A. 101, 102-105 (1946).

³⁹⁴ See *Royal Thai Government v. United States*, 436 F.3d 1330 (Fed. Cir. 2006); see also *A.K. Steel v. United States*, 192 F.3d 1367, 1385 (Fed. Cir. 1999).

(i) **Chinese Currency Undervaluation Is A *De Jure* Export Subsidy**

Chinese currency undervaluation is a *de jure* export subsidy consistent with section 771(5A)(B) of the Act. As detailed in numerous studies,

China's basic regulation on the management of foreign exchange dates from 1996, has been amended twice since then (in January 1997 and, more recently, in August 2008), and is administered by the People's Bank of China and the State Administration of Foreign Exchange. These FOREX Rules are sweeping in their reach and lay down the framework and essential guidelines by which the Chinese government monitors and controls the flow of currency into, out of, and within China. In practice, this oversight means that the Chinese central government can insulate the renminbi to a great degree from the market's pressures and undervalue the renminbi relative to the values of the currencies of China's trading partners.³⁹⁵

Although the Chinese government has carefully worded its laws to avoid a forthright acknowledgment that its currency system is designed to promote exports and increase dollar holdings, this effect is widely acknowledged by economists and scholars: "China's government clearly is in a position to seal off foreign currencies - as much or as little as it chooses at any given time - from the Chinese domestic market. This segregation allows the Chinese government to intervene effectively in the foreign exchange markets to undervalue the renminbi."³⁹⁶ Similarly, the *Undervaluation Analysis Report* at 5 states that "It is evident that the reason that the "price" of the RMB against other currencies has not increased commensurately is the intervention by the People's Bank of China ("PBOC") which appears to have had as a policy goal the suppression of forces that would increase the value of the RMB.

³⁹⁵ See *TLAG Report on Undervaluing the RMB, Exhibit III-181*.

³⁹⁶ *Id.*

The PBOC achieves this goal by selling whatever volumes of RMB are necessary to keep the value of the RMB at the PBOC's desired level." Therefore, the GOC's policy as applied through the Chinese Foreign Exchange Rules, in particular Articles 7 - 9, 11, 12, 19, 20, 32, 33, when read together, demonstrate that the GOC has in place *de jure* restrictions that promote exports and reward exporters and FIEs with excess RMB.³⁹⁷

As discussed above, Chinese currency undervaluation is a *de facto* export subsidy, consistent with section 771(SA)(B) of the Act and the Department's prior cases. The Department's regulations state that "{t}he Secretary will consider a subsidy to be an export subsidy if the Secretary determines that eligibility for, approval of, or the amount of, a subsidy is contingent upon export performance."³⁹⁸ Essentially, the Chinese government can control the amount of excess RMB provided to its industries in two steps: first, by encouraging the development of an industry through specific government policies designed to launch the industry into the global market and second, by rewarding the successfully developed industry through the provision of excess RMB in exchange for foreign currency.

In this instance, the amount of excess RMB that Chinese producers of subject merchandise receive is contingent upon their export performance. Because the Chinese government has in place a *de jure* policy to support the Chinese aluminum extrusion industry, the Chinese aluminum extrusion industry is more likely than non-supported industries to successfully export its products, thus ultimately receiving more dollars, and therefore, more

³⁹⁷ See 2008 Foreign Exchange Control Regulations of the People's Republic of China, Exhibit III-175.

³⁹⁸ See 19 C.F.R. § 351.514. (emphasis added)

excess RMB than non-encouraged industries.³⁹⁹ Furthermore, the Chinese government's complete control over foreign exchange is a well-documented tool used in its efforts to keep the RMB undervalued vis-à-vis the dollar:

China's basic regulation on the management of foreign exchange dates from 1996, has been amended twice since then (in January 1997 and, more recently, in August 2008), and is administered by the People's Bank of China and the State Administration of Foreign Exchange. These FOREX Rules are sweeping in their reach and lay down the framework and essential guidelines by which the Chinese government monitors and controls the flow of currency into, out of, and within China. In practice, this oversight means that the Chinese central government can insulate the renminbi to a great degree from the market's pressures and undervalue the renminbi relative to the values of the currencies of China's trading partners. As the articles next highlighted illustrate, the current version of the FOREX Rules continues to vest extensive powers in the People's Bank of China and the State Administration of Foreign Exchange.⁴⁰⁰

Therefore, by both having a policy to support favored industries, such as the aluminum extrusion industry, and by maintaining total control over the foreign exchange system in order to reward favored industries with excess RMB, the Chinese government has created a *de facto* export subsidy to all industries who successfully respond to the government edict to go forward and export. Clearly, little if any doubt exists that the provision of excess RMB is linked to a Chinese producers' receipt of dollars upon exportation of subject merchandise.⁴⁰¹ Furthermore, as the *Undervaluation Analysis Report*, concludes,

³⁹⁹ See *Countervailing Duty Investigation of Coated Free Sheet from the People's Republic of China*, 72 Fed. Reg. 60,645 (Oct. 25, 2007) ("CFS") at Issues and Decision Memorandum, Comment 8, page 55.

⁴⁰⁰ See *TLAG Report on Undervaluing the RMB, Exhibit III-181*.

⁴⁰¹ See *Can-Am Corp. v. United States*, 11 C.I.T. 424, 430 (Ct. Int'l Trade 1987) (upholding Commerce's interpretation of "contingent upon export" stating "Here Commerce asserts that in order to be an export bounty, grant or subsidy within the meaning of

70 % of China's foreign exchange earnings from Current Account transactions and from long-term Capital and Financial account transactions were derived from the export of goods...No other category of foreign exchange inflows comes close to matching the \$1.4 trillion foreign exchange earnings of Chinese exporters. Therefore, as exporters garner the overwhelming share of benefits from the undervaluation of the RMB, the subsidy benefit is *de facto* specific to exporters as a group.⁴⁰²

The Department's regulations also make clear that "the provision of the subsidy" can be "tied to actual or anticipated exportation or export earnings, alone or as one of two or more conditions."⁴⁰³ Therefore, the fact that the provision of excess RMB to producers of subject merchandise, can be tied to the export earnings that the Chinese government encourages through their policy to support the paper and forestry industries, is sufficient under the regulatory standard to find Chinese currency undervaluation a *de facto* export subsidy. Although the Department may hypothesize other conditions under which a particular company or individual may receive excess RMB upon converting dollars, hypothesis is irrelevant to this allegation and does not obviate the fact that exportation is one condition under which excess RMB are awarded to favored industries. Therefore, any non-exporting entity's use of this program is largely

the countervailing duty statutes the *benefit bestowed must be linked to the exportation of the goods*. The Court finds this interpretation of section 1677(5)(A) "export" subsidies to be consistent with the types of subsidies described in Annex A to the Agreement. The Court also finds the requirements that the alleged benefit be contingent upon export performance or that it stimulate export sales over domestic sales to be consistent with the other forms of export subsidies in Annex A, and holds that such requirements are reasonable criteria for determining whether the benefit bestowed is sufficiently tied to the exportation of the goods." (emphasis added).

⁴⁰² See *Undervaluation Analysis Report* at 8, Exhibit III-183.

⁴⁰³ See 19 C.F.R. § 351.514.

inconsequential to the Department's proper analysis of *de facto* export subsidies under its regulations.⁴⁰⁴

Finally, the Petitioners' treatment of *de facto* export subsidies also comports with the factors that the Department contemplated in *Laminated Hardwood Trailer Flooring from Canada* and that the WTO Appellate Body addressed in *Canada - Measures Affecting the Export of Civilian Aircraft*. ("*Canada - Aircraft*").⁴⁰⁵ According to the *Laminated Hardwood Trailer Flooring* factors contemplated by the Department the Chinese government's restriction on foreign exchange as a whole creates a *de facto* export subsidy by (1) making a Chinese producer's receipt of a subsidy (excess RMB) (2) contingent on its ability to export outside of China, and (3) thus receive foreign exchange that (4) the GOC strictly controls and largely requires the producer to surrender.

Similarly, the Appellate Body's discussion of *de facto* export subsidies in *Canada - Aircraft* also supports Petitioners' allegation of Chinese currency undervaluation as a *de facto* export subsidy. The Appellate Body upheld the panel's decision that the government of Canada provided a *de facto* export subsidy (through its Technology Partnerships Canada ("TPC") assistance) to its aircraft industry even though: (1) Brazil admitted TPC assistances was granted to non-aircraft industries with domestic sales; and (2) Canada asserted that "TPC provides

⁴⁰⁴ See *Coated Free Sheet Paper from the Republic of Korea: Notice of Final Affirmative Countervailing Duty Determination*, 72 Fed. Reg. 60,639, 60,642 (Oct. 25, 2007), stating "We find that the information regarding anticipated export effects included in the application Namhan filed with MOCIE is one of the conditions considered when issuing loans under the program and, thus, meets the specificity criteria under section 771(5A)(B) of the Act and 19 CFR 351.514. Indeed, the Preamble further clarifies that if exportation or anticipated exportation is the sole condition or one of several conditions, the subsidy is an export subsidy 'unless the firm in question can clearly demonstrate that it had been approved to receive the benefits solely under non-export-related criteria.'"

⁴⁰⁵ See Appellate Body Report, *Canada - Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, adopted 20 August 1999, DSR 1999:III, 1377 ("Appellate Body Report on Canadian Aircraft").

support to a broad base of sectors and technologies that touch on virtually all industrial sectors of Canada.”⁴⁰⁶ Ultimately, the underlying panel looked at numerous facts related to TPC assistance and found:

that TPC funding in the regional aircraft sector is expressly designed and structured to generate sales of particular products, and that the Canadian Government expressly takes into account, and attaches considerable importance to, the proportion of those sales that will be for export, when making TPC contributions in the regional aircraft sector. In this regard, we note again in particular that TPC contributions in the aerospace and defence sector, including the regional aircraft industry, are provided for “near-market projects with high export potential.” To us, therefore, these facts demonstrate that TPC assistance to the Canadian regional aircraft industry would not have been granted but for some expectation of exportation or export earnings. (Emphasis in original).⁴⁰⁷

In the instant case, the Chinese government has structured its economy to generate sales of particular products by instituting industrial plans. Like the Canadian government did in granting TPC assistance, the Chinese government “attaches considerable importance” to the fact that its championed industries will export merchandise.⁴⁰⁸ As a result, the totality of the facts surrounding Chinese currency undervaluation demonstrates that it functions as a *de facto* export subsidy to the manufacturers of subject merchandise, whose exports are considerably important to the GOC.

⁴⁰⁶ *Id.*

⁴⁰⁷ See Panel Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/R, adopted 20 August 1999 at para. 9.341, as upheld by Appellate Body Report WT/DS70/AB/R, DSR 1999:IV, 1443.

⁴⁰⁸ See *TLAG Report on Undervaluing the RMB, Exhibit III-181*; see also “After 30 Years, Economic Peril on China’s Path,” *N.Y. Times* (Dec. 19, 2008), *Exhibit III-182*.

The Appellate Body upheld the panel's decision that TPC assistance was a *de facto* export subsidy for the regional Canadian aircraft industry and acknowledged the difficulty in analyzing *de facto* export subsidies:

Proving *de facto* export contingency is a much more difficult task. There is no single legal document which will demonstrate, on its face, that a subsidy is "contingent ... in fact ... upon export performance". Instead, the existence of this relationship of contingency, between the subsidy and export performance, must be *inferred* from the total configuration of the facts constituting and surrounding the granting of the subsidy, none of which on its own is likely to be decisive in any given case.⁴⁰⁹

Therefore, Petitioners allege that based on the totality of the facts surrounding Chinese currency undervaluation which are reasonably available to Petitioners, the Department should initiate an investigation of Chinese currency undervaluation as a *de facto* export subsidy.

(ii) Chinese Currency Undervaluation Is A Specific Domestic Subsidy Which The GOC Bestows On Foreign-Invested Enterprises ("FIEs")

The Department's regulations state that {i)n determining whether a subsidy is being provided to a "group" of enterprises or industries within the meaning of section 751(5A)(D) of the Act, the Secretary is not required to determine whether there are shared characteristics among the enterprises or industries that are eligible for, or actually receive, a subsidy. See 19 C.F.R. § 351.502(b).⁴¹⁰ In *Dynamic Random Access Memory Semiconductors from the Republic of*

⁴⁰⁹ See Appellate Body Report on Canadian Aircraft at para. 167.

⁴¹⁰ See *British Steel PLC v. United States*, 20 C.I.T. 394, 443 (Ct. Int'l Trade 1996) citing to *PPG Indus., Inc. v. United States*, 9 Fed. Cir. (T) 71, 80, 928 F.2d 1568, 1577 (1991) and stating that "The CVD statute provides that for Commerce to countervail a bounty or grant, the agency must determine whether the bounty, grant, or subsidy in law or in fact is provided to a specific enterprise or industry, or group of enterprises or industries." 19 U.S.C. § 1677(5)(B) (1988). A finding of *de facto* specificity "requires a case by case analysis to determine whether there has been a bestowal upon a specific class."

Korea: Final Results of Countervailing Duty Administrative Review, 73 Fed. Reg. 14,218 (Mar. 17, 2008) the Department found that Hynix was a member of a “group of enterprises” and reiterated that (1) “the Department is not required to determine whether or not there are shared characteristics among enterprises for purposes of its specificity analysis” and (2) “the Department has discretion in evaluating the shared characteristics among enterprises or industries in determining whether they constitute a ‘group’ for purposes of specificity analysis.”

Chinese FIEs are a “group of enterprises” consistent with the Department’s legal standards and past practice. In prior cases, the Department has determined that Chinese FIEs are “groups of enterprises” in the context of specificity analysis and should continue to do so in this case.

Our finding is that FIEs constitute a group of enterprises for specificity purposes. We note that section 771(5A)(D) of the Act defines “enterprise or industry” to include a group of such enterprises or industries. Much of Yixing Union’s argument is misplaced because it focuses on the industries containing FIEs, not on whether FIEs can be classified as a “group.”

.....
Moreover, while we acknowledge that the language in the CVD Preamble discussing *PPG Industries v. United States* refers to numerous and diverse industries, and that FIEs may in fact operate in numerous and diverse industries in the PRC, the preambular language cannot be read to mean that where the law limits a subsidy to a specific group of recipients, the subsidy is not specific because the limited recipients operate in many industries. Also, in our view, the *Roses* decision cited by Yixing Union supports our finding because FIEs are a discrete class of enterprises that benefit from a variety of subsidy programs.⁴¹¹

⁴¹¹ See *Citric Acid and Certain Citrate Salts From the People’s Republic of China: Final Affirmative Countervailing Duty Determination*, 74 Fed. Reg. 16,836, 16,838 (Apr. 13, 2009); see also *Certain Kitchen Shelving and Racks from the People’s Republic of China: Final Affirmative Countervailing Duty Determination*, 74 Fed. Reg. 37,012 (July 27, 2009); *Polyethylene Retail Carrier Bags from the Socialist Republic of Vietnam: Preliminary Affirmative Countervailing Duty Determination and Alignment of Final Countervailing Duty*

Alternatively, under the same reasoning applied to FIEs, Petitioners allege that exporters, as a discrete class of enterprises, are a "group of enterprises" consistent with section 771(5A)(D)(iii) of the Act for the purpose of analyzing Chinese currency undervaluation as a domestic subsidy.

As demonstrated above, FIEs are a group of enterprises according to section 771(5A)(D) of the Act and 19 C.F.R. § 351.502.⁴¹² Because FIEs exported 55 percent of total Chinese exports during the period of investigation (2008), they were the predominant recipient of excess RMB according to section 771(5A)(D)(iii)(II) of the Act. *See Undervaluation Analysis Report* at 10. Moreover, from 2005 through April 2009 (a period of time which included the entire period of investigation), FIEs alone accounted for over half of Chinese exports. Specifically, as detailed in Exhibit 11 of the *Undervaluation Analysis Report*, FIEs accounted for 56.1% of total exports from China between January and November 2009. Their exports amounted to 55.3%, 57.1%, 58.2% and 58.3% of China's total exports in 2008, 2007, 2006, and 2005 respectively.⁴¹³

Petitioners' analysis is consistent with the Department's specificity practice regarding "predominant use." Moreover, although there is no bright-line for determining predominant use,

Determination with Final Antidumping Duty Determination, 74 Fed. Reg. 45,811 (Sept. 4, 2009)(discussion of Corporate Income Tax Exemptions received by Fotai and Chin Sheng).

⁴¹² *See Saudi Iron & Steel Co. (Hadeed) v. United States*, 11 C.I.T. 880 (Ct. Int'l Trade 1987)(*"Saudi Steel v. U.S."*)(upholding Commerce's determination regarding a "group of enterprises" and stating "{D}ecisions of this Court require Commerce to conduct a *de facto* case by case analysis to determine whether a program provides a subsidy, or a bounty or grant, to 'a specific enterprise or industry or group of enterprises or industries...').

⁴¹³ *See Undervaluation Analysis Report*, data at Exhibit III-11, **Exhibit III-183**.

the FIEs' receipt of excess RMB has consistently been over 50 percent for three-years prior to the period of investigation.⁴¹⁴

As discussed above, the GOC's stringent control over foreign exchange requires FIEs to exchange the dollars earned through exportation at the controlled rate of exchange, thus receiving more RMB than they would in the absence of the government-controlled currency regime. As a result, because FIEs earn, and are required to exchange, a predominate amount of foreign currency, they are the predominate recipients of excess RMB consistent with the Department's practice.⁴¹⁵

(iii) Exporters, as a Group of Enterprises, are Predominant Users of Chinese currency undervaluation

For the reasons discussed above, exporters are a "group of enterprises" according to section 771(5A)(D) of the Act and 19 C.F.R. § 351.502.⁴¹⁶ Petitioners submit that although exporters' preponderant share of China's total foreign exchange inflows constitutes reasonably available information evidence that Chinese currency undervaluation is a *de facto* export subsidy, as alleged above, this fact is also evidence that Chinese exporters, as a group of enterprises, are predominant users of the subsidy under section 771(5A)(D)(iii)(II) of the Act. If the Department does not find that Chinese currency undervaluation is a *de jure* or *de facto* export

⁴¹⁴ See, e.g., *Final Affirmative Countervailing Duty Determination: Stainless Steel Plate in Coils from South Africa*, 64 Fed. Reg. 15,553, 15,564 (Mar. 31, 1999) (finding predominate use when a group of industries received more than fifty percent of a subsidy over a several year period).

⁴¹⁵ See *Certain New Pneumatic Off-the-Road Tires From the People's Republic of China: Final Affirmative Countervailing Duty Determination and Final Negative Determination of Critical Circumstances*, 73 Fed. Reg. 40,480 (July 15, 2008) (discussing that consuming "over half of the total rubber consumed in the country during the POI, indicat{es} that this program may also be *de facto* specific under the predominant and disproportionate analyses.")

⁴¹⁶ See *Saudi v. U.S.*, *supra* note 57.

subsidy, then the Petitioners alternatively allege that Chinese exporters, as a group of enterprises, are predominant users of excess RMB resulting from Chinese currency undervaluation according to section 771(5A)(D)(iii)(II) of the Act. As the *Undervaluation Analysis Report* demonstrates,

70 % of China's foreign exchange earnings from Current Account transactions and from long-term Capital and Financial account transactions were derived from the export of goods... No other category of foreign exchange inflows come close to matching the \$1.4 trillion foreign exchange earnings of Chinese exporters. Therefore, as exporters garner the overwhelming share of benefits from the undervaluation of the RMB, the subsidy benefit is *de facto* specific to exporters as a group.⁴¹⁷

Petitioners allege that FIEs receive a disproportionately large amount of excess RMB according to section 771(5A)(D)(iii)(III) of the Act. As the Department acknowledged in the *Preamble* to its regulations, and as discussed above, detailed distribution data for domestic subsidies is frequently not reasonably available to petitioners. Therefore, in order to analyze whether FIEs receive a disproportionately large amount of excess RMB, Petitioners relied on the *Undervaluation Analysis Report*, which compares FIEs share of exports, and therefore, their receipt of excess RMB, to the overall contribution to Chinese Gross Domestic Product ("GDP") made by FIEs.

After adjusting for FIEs' role in the overall manufacturing sector, the *Undervaluation Analysis Report* concludes that: "FIEs as a group appear likely to account for no more than about 20% of GDP, but they do account for 55% of total Chinese exports."⁴¹⁸ Petitioners note that this approach is consistent with the Department's analysis of whether disproportionately large

⁴¹⁷ See *Undervaluation Analysis Report* at 8, Exhibit III-183.

⁴¹⁸ See *Undervaluation Analysis Report* at 10, Exhibit III-183.

amounts of subsidies were granted in prior cases where distribution data were unavailable.⁴¹⁹

Based on information reasonably available, the amount of excess RMB received by FIEs, as a percentage of total Chinese exports, is disproportionate to FIEs' contribution to manufacturing or total Chinese GDP.

(iv) Exporters, as a Group of Enterprises, receive a disproportionately large amount of excess RMB resulting from Chinese currency undervaluation

Alternatively, Petitioners allege that exporters, as a group of enterprises, receive a disproportionately large amount of excess RMB according to section 771(5A)(D)(iii)(III) of the Act. As the Department acknowledged in the *Preamble* to its regulations, and as discussed above, detailed distribution data for domestic subsidies is frequently not reasonably available to petitioners. Therefore, in order to analyze whether exporters receive a disproportionately large amount of excess RMB, Petitioners relied on the *Undervaluation Analysis Report*. As documented in the *Undervaluation Analysis Report* at 3, China's exports as a percent of total GDP were 33 percent in 2008. However, exporters received 70 percent of China's foreign exchange earnings from Current Account transactions and from long-term Capital and Financial Account transactions. See *Undervaluation Analysis Report* at 8. Therefore, based on information reasonably available, the amount of excess RMB received by exporters is disproportionate to exporters' contribution total Chinese GDP.

Finally, Petitioners assert that, as it has done in prior cases where domestic subsidies were at issue, the Department should initiate an investigation of Chinese currency undervaluation and review detailed distribution data that can only be fully developed over the course of an

⁴¹⁹ See, e.g., *Coated Free Sheet Paper from the Republic of Korea: Notice of Final Affirmative Countervailing Duty Determination*, 72 Fed. Reg. 60,639 (Oct. 25, 2007) (dividing the pulp, paper, and wood sectors' share of KDB lending to the manufacturing sector by the sectors' share of manufacturing GDP).

investigation. Even where distribution data has been forthcoming and relatively transparent (unlike the instant case), the complexity of specificity analysis often requires multiples layers of analysis and changes from preliminary to final determinations. For example, in *Alloy Magnesium from Canada: Final Results of Countervailing Duty New Shipper Review*, 68 Fed. Reg. 22,359 (April 28, 2003), the Department changed its specificity analysis in the final determination and analyzed the program on a company-specific basis instead of an industry-specific basis. The Department also made several types of comparisons before finding that the respondent company had received a disproportionately large amount of the subsidy.⁴²⁰ Petitioners submit that such detailed analysis is appropriate in an ongoing investigation, but inappropriate when used as a threshold requirement to decide whether to initiate an investigation.

5. In the alternative, currency undervaluation constitutes a subsidy because it qualifies as “income or price support within the meaning of Article XVI of the GATT 1994” under Section 771(S)(B)(ii) of the Act that provides a benefit to the recipient and that is specific to exports

a) “Income or price support that operates directly to increase exports”

Article XVI:1 of GATT 1994 characterizes any form of income or price support which operates directly or indirectly to increase exports, or reduce imports, as a subsidy. In particular, GATT Article XVI:1 provides, in relevant part:

Subsidies

Section A - Subsidies in General

1. If any contracting party grants or maintains any subsidy, including any form of income or price support, which operates directly or indirectly to increase exports of any product from, or to reduce imports of any product into, its territory, it shall notify the CONTRACTING PARTIES in writing of the extent and nature of

⁴²⁰ See *Alloy Magnesium from Canada: Final Results of Countervailing Duty New Shipper Review*, 68 Fed. Reg. 22,359 (Apr. 28, 2003)(discussion of Magnola’s MTM benefits)(the Department’s methodology was upheld by a Binational NAFTA Panel, *In Re Alloy Magnesium from Canada*, USA-CDA-2003-1904-02 (Sept. 9, 2005).

the subsidization, of the estimated effect of the subsidization on the quantity of the affected product or products imported into or exported from its territory and of the circumstances making the subsidization necessary.

The WTO SCM Agreement reflects this characterization of certain income or price support in defining the term "subsidy." In particular, according to Article 1.1 of the SCM Agreement, a subsidy is deemed to exist where there is either a "financial contribution" or "any form of income or price support in the sense of Article XVI of GATT 1994" that provides a benefit to the recipient. This standard has been implemented under Section 771 of the Act, which provides in relevant part:

5) Countervailable subsidy.

- (A) In general. Except as provided in paragraph (5B), a countervailable subsidy is a subsidy described in this paragraph which is specific as described in paragraph (5A).
- (B) Subsidy described. A subsidy is described in this paragraph in the case in which an authority
 - (i) provides a financial contribution,
 - (ii) provides any form of income or price support within the meaning of Article XVI of the GATT 1994, or
 - (iii) makes a payment to a funding mechanism to provide a financial contribution, or entrusts or directs a private entity to make a financial contribution, if providing the contribution would normally be vested in the government and the practice does not differ in substance from practices normally followed by governments

The Act does not define the term "income or price support" and the Department has not adopted a definition for this term in its countervailing duty practice. Neither the SCM Agreement nor GATT provide a definition for this term, and its meaning has not been clarified either in GATT or WTO dispute settlement. The *Shorter Oxford English Dictionary* defines the noun "support" as "{t}he action of holding up, keep from falling, or bearing the weight of

something.”⁴²¹ In turn, dictionaries of economic terms and textbooks on the theory of international economics characterize the term “exchange rate” as “the price of one currency in terms of another.”⁴²²

Accordingly, by constantly intervening in the foreign market to prevent the price of dollars in terms of RMB from falling (that is, to prevent the dollar from depreciating vis-à-vis the RMB), the GOC provides “price support” to Chinese producers of aluminum extrusions. In turn, such “price support” operates directly to increase exports of this product, on account that the price support concerned (*i.e.* the support of the exchange rate) allows the dollar price of Chinese imports of aluminum extrusions into the United States to remain at artificially low levels.⁴²³

⁴²¹ See *Shorter Oxford English Dictionary*, Oxford University Press, Sixth Edition, 2007.

⁴²² See, for example, *Oxford Dictionary of Economics*, Oxford University Press, Third Edition, 2009, p. 151 (“exchange rate: The price of one currency in terms of another”); Alan V. Deardorff *Terms of Trade: Glossary of International Economics*, World Scientific Publishing Co.: Singapore, 2006, p. 94 (“Exchange rate: The price at which one country’s currency trades for another”); and Dennis R. Appleyard, Alfred J. Field and Steven L. Cobb, *International Economics*, McGraw-Hill, Sixth Edition, 2008, p. 479 (“the foreign exchange rate is simply the price of one currency in terms of another”).

⁴²³ Notably, in its final countervailing duty determination in Rice from Thailand, Commerce found that price support programs in respect of the subject merchandise itself provide benefits in the nature of a grant and thus do not constitute “the provision of goods at preferential rates” under section 771(5)(B)(ii). See *Final Affirmative Countervailing Duty Determination and Countervailing Duty Order, Rice From Thailand*, 51 Fed. Reg. 12356 (April 10, 1986). Because grants are a type of financial contribution under section 771(5)(D)(i) of the Act, it follows that price support programs in respect of the subject merchandise itself do not constitute “income or price support within the meaning of Article XVI of the GATT 1994”.

This finding is consistent with economic analysis. “Price support within the meaning of Article XVI of the GATT 1994” stands for price support that operates directly or indirectly to increase exports of the merchandise at issue. However, price support in respect of the subject merchandise itself would lead to reducing exports rather than increasing exports, because the purchases that the government would make to raise the domestic price of the subject merchandise, by boosting domestic demand, would reduce the exportable surplus.

Hence, China's currency manipulation constitutes "a form of income or price support within the meaning of Article XVI of GATT 1994" under Section 771(5)(B)(ii) of the Act.

b) Benefit

The GOC's manipulation of its currency bestows a benefit to exporters because, on account of the GOC's intervention in the foreign exchange market to prevent the dollar from depreciating vis-à-vis the RMB, exporters receive more RMB per dollar than what they would receive if the Chinese government were not manipulating the exchange rate and markets were allowed to determine the equilibrium rate. Pursuant to 19 C.F.R. § 351.503(a), the benefit would be calculated as the difference between the RMB actually received and the RMB they would receive absent the government's intervention in the foreign exchange market.⁴²⁴

c) Specificity

The GOC's maintenance of an undervalued currency is a prohibited subsidy because it is contingent upon export performance. As an export subsidy, it is deemed specific pursuant to Section 771(5A)(B) of the Act. This subsidy is *de facto* contingent upon export performance because it directly linked with the act of exporting and export earnings. Moreover, the more a Chinese company exports, the more subsidy it receives. This direct and positive correlation between the export activity/export earnings and the amount of subsidy received means that the subsidy is "in fact, contingent on export performance."

VI. CONCLUSION

Based on the foregoing information reasonably available to Petitioners, the Department should initiate an investigation into countervailable subsidies provided to China's aluminum

⁴²⁴ See also 19 C.F.R. § 351.501 and *Countervailing Duties; Final Rule*, 63 Fed. Reg. 65347 at 6539-60 (Nov. 25, 1998) describing the flexibility inherent in determining subsidy benefits.

extrusion industry and impose duties through a countervailing duty order in an amount that would offset these unfair and injurious subsidy practices.

China-Singapore Suzhou Industrial Park Development Co., Ltd.

Start-up Procedure

Investors who wish to set up their operations in Suzhou Industrial Park may select from the following options:

- 1) Buy land to build their own factories;
- 2) Rent ready-built factories of different types, such as: Terrace Factory, Workshops, Freestanding Factory and Multi-storey Factory.

If the enterprise is export oriented, we recommend you consider to locate in Export Processing Zone (EPZ), where the above options are also available.

Tax Incentives

The preferential tax incentives available to foreign manufacturing enterprises and infrastructure developers in the park are shown in the table below.

Corporate Income Tax	Tax Rate	Reduction/Exemption Policy
Foreign Invested Enterprises of manufacturing Nature		
General	15%	Exempted from 3% Local Corporate Income Tax.
Period of operation exceeds 10 years	15%	As above. In addition, 2 years exemption plus 3 years half tax at the rate of 7.5% from the first profit-making year.
Exporting enterprises	15%	As above. After first 5 years of enjoying the additional tax incentive, if export value in any year exceeds 70% of output value, tax rate is reduced to 10%.
Technologically advanced enterprises	15%	As above. After first 5 years of enjoying the additional tax incentive, further 3 years of Corporate Income Tax rate at 10%.
Others		
Enterprises developing harbors, wharves & other infrastructure	15%	If intended period of operation exceeds 15 years, exemption for 5 years from the first profit-making year and reduced tax rate of 7.5% for another 5 years.
Financial Institutions with more than US\$10 million capital investment	15%	Must exceed 10 years period of operation. Exemption for 1st profit-making year and reduced tax rate of 7.5% for another 2 years.
Tax Rebates for re-investments		
Re-investments in the same enterprise, or a new FIE	40% Rebate	New FIE must have an operation period of more than 5 years; Rebate amount is 40% of corporate income tax that has been paid on sum re-invested.
Re-investment in export-oriented or advanced technology enterprises	100% Rebate	New FIE must have an operation period of more than 5 years; 100% rebate on corporate income tax that has been paid on sum re-invested.
Withholding Tax		

Dividends remitted to foreign shareholders	0%	Complete Exemption
Interests, rental, leasing payment, capital gains, or franchise fees	10%	May be further reduced depending on Double Taxation Agreements signed between China and other countries after payment of 5% business tax

Legal Services

There are tens of partnership law firms in Suzhou, which are recognized by China's Ministry of Law. They are specialized in corporate law, finance (bank, securities) law, foreign investment law, property law, and intellectual property law, etc.



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I topped the 2010 list of the provincial key service enterprises

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People's Government of Henan Province in 2010 focused on the issuance of the List of service enterprises

People's Government under provincial jurisdiction, provincial government departments:

To promote the province's Industrial economic restructuring and development patterns, fostering the growth of strategic industries and strategic support for new industries, speed up the industrialization process, the government decided to focus on services each year to determine a number of provincial enterprises. Now decided that the 2010 provincial key service enterprises (one hundred and one hundred-scale enterprises with high growth companies) list to be issued.

All levels of government, the provincial departments to increase the focus on service enterprises of services, support enterprise development to develop specific policy measures and timely solutions to business projects, production and management process the difficulties and problems. Provincial key service enterprises to effectively play on the province's industrial transformation and upgrading of the role model to lead the drive to accelerate the pace of project construction, strengthening of technological innovation, product updates, energy conservation, business management and other work. Activities of provincial offices to lead the business services co-ordination of work to do to establish target assessment and dynamic management mechanisms to strengthen routine monitoring scheduling system to promote the rapid development of key service enterprises.

February 26, 2010

1. Henan Coal Chemical Industry Group Co., Ltd.
2. Zhengzhou Coal Industry (Group) Co., Ltd.
3. Zhengzhou Yutong Group Co., Ltd.
4. Henan Yulan Energy Group Co., Ltd.
5. Zhengzhou Nissan Automobile Co., Ltd.
6. White Elephant Food Group Company
7. Henan Sunshine Oil Group Co., Ltd.
8. Zhengzhou Coal Mine Machinery Group Co., Ltd.
9. Food Co., Ltd. Henan miss
10. Henan Ming Tai Aluminum Co., Ltd.
11. Henan Branch of China Aluminum Industry Group
12. Zhengzhou three full-Food Company Limited
13. Henan Jinding Beer Group Corporation
14. Henan Shaolin Auto Co., Ltd.
15. Zhengzhou Textile Machinery Co., Ltd.
16. Henan Investment Group Co., Ltd.
17. Henan Branch of China Delang Corporation
18. China Power Investment Corporation Henan Branch
19. China Petroleum & Chemical Corporation Henan Petroleum Company
20. Henan, China National Petroleum Marketing Company Limited
21. Zhongyuan Publishing & Media Group
22. Henan Tobacco Industry Co., Ltd.
23. China National Tobacco cigarette sales branch in Henan Province
24. Henan, China Mobile Communications Group Co., Ltd.
25. China Unicom Henan Branch Company
26. China Telecom subsidiary Henan Telecom
27. Henan Communications Investment Group Co., Ltd.
28. Henan Post
29. Henan Material Group Corporation
30. Tai Wang Construction and Development Co., Ltd.
31. Kaifeng, Henan Province, Shanxi Investment Holding Group Co., Ltd. Open
32. Luoyang Branch of China Petroleum & Chemical Corporation
33. Luoyang Xin'an Power Group Co., Ltd.
34. Yichuan Power Group Corporation
35. China First Tractor Group Co., Ltd.
36. CITIC Heavy Machinery Co., Ltd.

37. Luoyang Molybdenum Industry Group Co., Ltd.
38. China's Luoyang Copper Co., Ltd.
39. China Shipbuilding Industry Corporation Institute for the seventh twenty-five
40. Luoyang Hong Jiang Wanji Aluminum Co., Ltd.
41. Pingdingshan Shanma China Chemical Industry Group Co., Ltd. Energy
42. Henan Tianrui Group
43. Wuyang Iron and Steel, Hebei Iron and Steel Group Co., Ltd.
44. Ping Gao Group Co., Ltd.
45. Pingdingshan Coal Mining Machinery Co., Ltd.
46. Anyang Iron & Steel Group Co., Ltd.
47. Anyang Germany million Axle Co., Ltd.
48. Linzhou Heavy Machinery Group Co., Ltd.
49. Henan Dayong Group Co., Ltd.
50. Golden Dragon Precise Copper Tube Group Co., Ltd.
51. Xinxiang Liuzhuang farming Yonhap
52. Henan Electric Group fly
53. Xinxiang New Asia Paper Group Ltd.
54. Xinxiang Aviation Industry (Group) Co., Ltd.
55. Henan Weihua Group Co., Ltd.
56. Xinxiang Chemical Fiber Group Co., Ltd. egret
57. Henan Fertilizer Co., Ltd. Heart to Heart
58. Henan Huanyu Group Co., Ltd.
59. Henan floating Security Group
60. Aobus Tyre Co., Ltd.
61. Jaozuo Wanfeng Aluminum Co., Ltd.
62. Haohua Yuhang Chemical Co., Ltd.
63. Henan Zhongyuan Co., Ltd. equipped
64. Zhongyuan Oilfield
65. XJ Group Corporation
66. Henan Zhongpin Food Industry Co., Ltd.
67. Henan Qingshan Jinhui Stainless Steel Industry Co., Ltd.
68. Henan Huanghe Industrial Group Co., Ltd.
69. Henan Sen Source Group Co., Ltd.
70. Henan Rebecca Holding Co., Ltd.
71. Shinyway Group
72. Luohe Nanjie Group
73. Lotte Lee O Beverage Co., Ltd.
74. Silver Pigeon Group
75. Henan Zhongyuan Gold Smelter Co., Ltd.
76. Lingbao Jinyuan Mining Co., Ltd.
77. Yima Coal Industry Group Co., Ltd.
78. Cayman (Sanmenxia) Aluminum Products Co., Ltd.
79. East Hope Sanmenxia Aluminum Co., Ltd.
80. Sinopec Henan Oilfield Company
81. Henan Long Cheng Group Co., Ltd.
82. Henan Tianguan Enterprise Group Co., Ltd.
83. Henan Textile Co., Ltd. Wild
84. Henan MCC Material Group Co., Ltd. Paul West
85. Nanyang Explosion Protection Group Co., Ltd.
86. Henan Shanhuo Group Co., Ltd.
87. Henan Kedi Food Group Co., Ltd.
88. Huaying Poultry Industry Group Co., Ltd. Henan
89. Henan Fu Jen Pharmaceutical Group Co., Ltd.
90. Henan Caixen Group Co., Ltd.
91. Henan Chi Yuan Food Co., Ltd.
92. Yi Hai (Zhoukou) Oils & Grains Industries Co., Ltd.
93. Henan Lianhua Gourmet Powder Co., Ltd.
94. Zhoukou Golden Monkey Food Co., Ltd.
95. Zhumadian Haohua Chemical Co., Horse Group
96. Zhumadian CIMC Huajun Vehicle Co., Ltd.
97. Henan Topfond Pharmaceutical Co., Ltd.

I topped the 2010 list of the provincial...

98. Henan Yuguang Gold & Lead Group Co., Ltd.
99. Henan Jiyuan Iron & Steel (Group) Co., Ltd.
100. Zhongyuan Special Steel Co., Ltd.
- One hundred enterprises of scale advantages
1. Zhengzhou Aircraft Equipment Co., Ltd.
2. Zhong'an Technology Group Co., Ltd.
3. Zhengzhou Sunrise Optoelectronics Technology Co., Ltd.
4. Hippocampus (Zhengzhou) Automobile Co., Ltd.
5. Henan star Technology Co., Ltd.
6. Jing Cheng (Zhengzhou) Co., Ltd.
7. Henan Hanwei Electronics Co., Ltd.
8. Optoelectronics Technology Co., Ltd. Henan Health Mao
9. VCOM Technology Co., Ltd.
10. Fangqiao Liang Machinery Co., Ltd. Zhengzhou
11. UNPROFOR Crop Science and Technology Co., Ltd.
12. China Railway Tunnel Equipment Manufacturing Co., Ltd.
13. Zhengzhou Show Clothing Co., Ltd. Link
14. Henan, China Crystal Superhard Materials Co., Ltd.
15. Henan Science and Technology Co., Ltd. brilliant
16. Zhengzhou new Yihua Medical Technology Co., Ltd.
17. Henan Qingan Chemical technology Co., Ltd.
18. Zhangzhou Yalida Garments Co., Ltd.
19. Zhengzhou Top Rolling Technology Co., Ltd.
20. Henan Trading Group Co., Ltd.
21. Zhengzhou Dennis Department Store Co., Ltd.
22. Zhengzhou Grain Wholesale Market Co., Ltd.
23. Henan Tourism Group Co., Ltd.
24. Henan Province Coalbed Methane Development and Utilization Co., Ltd.
25. Henan Yuxin Logistics Co., Ltd.
26. Henan Cultural Industry Investment Co., Ltd.
27. Daxin Materials Co., Ltd. Henan
28. Kaifeng Lanxiang Vehicle Industry Group Co., Ltd.
29. Lankao Ring Industrial Group, Westlands
30. Fluid Equipment Co., Ltd. Henan, the sea
31. Optoelectronics Technology Co., Ltd. In the Air
32. Luoyang Suntech Power Co., Ltd.
33. CNAC lithium (Luoyang) Co., Ltd.
34. Artes photovoltaic power (Luoyang) Co., Ltd.
35. Shanghai Super Day (Luoyang) Solar Energy Co., Ltd.
36. Luoyang Locomotive Co., Ltd. CSR
37. Luoyang Sino-silicon High-Tech Co., Ltd.
38. Luoyang Pulai Ke Biotechnology Co., Ltd.
39. Luoyang North Glass Technology Co., Ltd.
40. Pingdingshan City Light Medical Products Co., Ltd.
41. Henan Jie Shi Industrial Group
42. Pingdingshan Electronic Scale Co., Ltd.
43. Anyang Xingsheng Machine Tool Co., Ltd.
44. Henan Kerry Digital Co., Ltd.
45. Anyang Jianfeng Foods Co., Ltd.
46. Anyang Forging Machinery Industry Co., Ltd.
47. New Feng Technology Co., Ltd. of Henan Province
48. Henan Tianhai Electric Co., Ltd.
49. Veenker Hebi magnesium-based materials Co., Ltd.
50. Yongda Food Industry Co., Ltd. Henan
51. Henan Kono Electronics Development Co., Ltd.
52. Henan Communication Technology Co., Ltd. Shi Jia
53. Hebi to grace New Material Technology Co., Ltd. to
54. Yu Fei Industry Group
55. Hualan Biological Engineering Co., Ltd.
56. Henan Heavy Crane Group Limited
57. Henan Vientiane Communication Co., Ltd.

I topped the 2010 list of the provincial...

58. Xinxiang Extension New Biochemical Technology Co., Ltd.
59. Henan Province Yi Pharmaceutical Co., Ltd.
60. Henan Cologne Group
61. Xinxiang Super Power Co., Ltd.
62. Jiaozuo City Fluoride Chemical Co., Ltd.
63. Henan Ads Group Limited
64. Henan thinking up new energy materials Co., Ltd.
65. Jiaozuo health yuan Biological Products Co., Ltd.
66. Zhongyuan Petrochemical Co., Ltd.
67. Henan Hongye Biochemical Co., Ltd.
68. Puyang Pu high-temperature materials (Group) Co., Ltd.
69. Xuchang Drive Shaft Co., Ltd. Far East
70. Xuchang U.S. special Bridge Co., Ltd.
71. Light Optical Cable Co., Ltd. Henan Xuchang
72. Xu Changchang Heng Technology Co., Ltd.
73. Henan Jinlong Industry Co., Ltd. Surface
74. Henan Dawn Jenkins Medical Devices Group Ltd.
75. Luohe Guanghua Electronic Technology Co., Ltd.
76. Henan View source fruit industry Co., Ltd.
77. Sanmenxia Day Card Wheel Manufacturing Co., Ltd.
78. Sanmenxia City, Hang Song and Biochemical Technology Co., Ltd.
79. South Diamond Co., Ltd.
80. Henan Wanxi Pharmaceutical Co., Ltd.
81. Nanyang Golden Crown Electric Co., Ltd.
82. Fussen Pharmaceutical Co., Ltd. Henan
83. RG Petroleum Equipment (Group) Co., Ltd.
84. Lucky Group Second Film Factory
85. Henan Costar Group Co., Ltd.
86. Yucheng County Venture Tape Material Co., Ltd.
87. Shangqiu City Furun Food Group Co., Ltd.
88. Shangqiu Galaxy Cotton Ltd
89. Shanghai Modern Hassan (Shangqiu) Pharmaceutical Co., Ltd.
90. Xiayi Huaihai Casting Co., Ltd.
91. Lingrui Pharmaceutical Co., Ltd. Henan
92. Xinyang Wheel Co., Ltd. with co-
93. Henan Victoria Snow Beer Group Co., Ltd.

94. Saver lactate Technology Co., Ltd. Henan
95. Yinfeng Plastic Co., Ltd. of Henan Province
96. Wood Industry Co., Ltd. Henan people
97. Henan Hsu Fu Chi Food Co., Ltd.
98. Henan Cereals, Oils Group Co., Ltd. Tai Cheng
99. Zhumadian Huazhong Chia Tai Co., Ltd.
100. Henan Water Technology Co., Ltd. Qing

One hundred high-growth enterprises

Henan Province on the establishment of hotlines and enterprise business services network platform announcement

To push forward the province's business service activities in depth, easy and efficient government and enterprises to build a bridge of communication to effectively solve production and operation enterprises in difficulties and problems encountered in promoting sound and rapid economic development of the province, the provincial business service activities office (located in the province of Industry and Information Technology Department) has set up special telephone lines in Henan enterprises and business services network platform. The announcement is as follows:

First, telephone and network services platform settings

(A) Hotline: number is 400-63-71580 (homonym: Enterprise I help you), 24-hour manned business calls, for business services.

(B) The enterprise service network platform: at the provincial Office of Industry and Information Technology website (<http://www.litba.gov.cn>) on the establishment of "Enterprise Service column in Henan Province", as the province of business services to the private network platform services real-time dynamic enterprises in the province, national and provincial business services laws, regulations and policy measures; Sheng business service activities of important documents issued by the office, and reflected in accepting the enterprise line, the problem will be handling the situation in the online Yu Yi announced.

(C) opening time: at 8:00 on March 15, 2010.

I topped the 2010 list of the provincial...

PUBLIC FILE 27

Second, clients

Various enterprises within the jurisdiction of Henan Province.

Third, the main services

(A) enterprises in the production and project construction process requires government departments to coordinate and solve problems;

(B) combined with their own development, the proposed policy support recommendations;

(C) of the departments at all levels to do the work of business service views and suggestions.

Fourth, pledge

Firmly establish a sense of public service, adhere to the purpose of dedication to business services, enterprise network platform through the hot line and reflect the problems, so that "everything has an echo, parts of these suits."

Notice is hereby given.

Achilles of Henan Province, the Office of Enterprise Services

March 10, 2010

Category: News respective topics:

Editor: Sanmenxia Day Card Wheel Manufacturing Co., Ltd.

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Bill Davidson <bill.davidson@roh.com.au>

FW: CHINA, NINGBO FOREIGN TRADE AND ECONOMIC COOPERATION BUREAU

Toby Forwood <issint@ozemail.com.au>
To: Bill Davidson <bill.davidson@roh.com.au>

Fri, Jul 2, 2010 at 4:22 PM

Dear Bill,

As I mentioned , Shirley's initial answer to our detailed enquiry was to say that all her bosses are in Germany at the moment , and ,anyway , why did we want their info seeing we have contacted Jishigang Industrial Park, etc , etc , etc.

She did add - item 5 in her letter - that Ningbo Government does provide some additional benefits , so I asked her to at least tell us about those.

Her reply to my request is below .

Bad news is the lack of detail , better news is the formidable list of topics which confirms the extent to which Provincial governments are prepared to go.

Best , Toby .

From: chengsy [mailto:chengsy@nbfet.gov.cn]
Sent: Thursday, 1 July 2010 6:29 PM
To: toby forwood
Subject: Re: CHINA, NINGBO FOREIGN TRADE AND ECONOMIC COOPERATION BUREAU
Importance: High

Dear Toby,

Here are some information for item 5:

8/11/2010

ROH Automotive Mail - FW: CHINA, N...

PUBLIC FILE 25

From 2008, the high and new zone finance arranges special fund of RMB 10,000,000 Yuan to use for introducing the study abroad talented person to work in Ningbo every year.

Financial support.

Discount loans and grants.

Financing guarantee.

Intellectual Property shares

Tax rebates, subsidies

Office business space rental subsidy.

Housing subsidy

Other premium services

I would say, it all depends on the final location of your company, for example - Yinzhou districts may have better incentives for you.

Regards

Shirley



Economic and Commercial Counsellor's Office of
the Embassy of the People's Republic of China
in the Republic of Singapore

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P+21 and 93

**Notification of the State Council on Providing Transitional Preferential Tax
Treatments to High-tech Enterprises Newly Set up in Special Economic Zones
and in Pudong New District of Shanghai**

Monday, January 28, 2008 Posted: 10:27 BJT(02:27 GMT)
From:fdi.gov.cn Article type:Reproduced

Guo Fa [2007] No. 40

The people's governments of all provinces, autonomous regions, municipalities directly under the Central Government, all ministries and commissions of the State Council, and all organs directly under the State Council,

According to Article 57 of the Enterprise Income Tax Law of the People's Republic of China, the State Council determines to provide transitional preferential tax treatments to the high-tech enterprises under the powerful support of the state, which were set up in the special zones set up by law for advancing foreign economic cooperation and technological communication and in the area where the State Council has offered to carry out the abovementioned special policy. The following issues are notified:

1. The expression "special zones set up by law for advancing foreign economic cooperation and technological communication" means Shenzhen, Zhuhai, Shanou, Xiamen and Hainan Special Economic Zones. The expression "the area where the State Council has provided for the implementation of the abovementioned special policy" means Pudong New District of Shanghai.

2. For a high-tech enterprise under the key support of the state in a special economic zone or in Pudong New District of Shanghai that completes the registration on or after January 1, 2008 (hereinafter referred to as the high-tech enterprise), the incomes acquired by it in the special economic zone and in Pudong New District of Shanghai shall be relieved from the enterprise income tax (hereinafter referred to as the EIT) for the first 2 years as of the tax year to which the first revenue coming from production or operation contributes, and shall be levied at half of the statutory tax rate of 25% for the third to the fifth years. The expression "high-tech enterprises under the powerful support of the State" means the high-tech enterprises which have their own kernel independent intellectual property rights and meanwhile meet the conditions as referred to, in Article 93 of the Regulation on Carrying out of the Enterprise Income Tax Law of the People's Republic of China and have been realized in pursuance of the Measures for the Determination of High-tech Enterprises.

3. In case a high-tech enterprise newly set up in a special economic zone or in Pudong New District of Shanghai embarks upon production and operation in other areas aside from the special economic zone or Pudong New District of Shanghai at the same time, it shall separately calculate the incomes it acquires in the special economic zone or Pudong New District of Shanghai and rationally divide the expenses incurred during the corresponding period. In case it cannot calculate independently, it shall not enjoy the preferential treatments regarding enterprise income tax.

4. In case a high-tech enterprise newly set up in a special economic zone or in Pudong New District of Shanghai no longer has the high-tech enterprise qualification because of review or because of its failure to pass a spot-check during the period when it enjoys the transitional preferential tax treatments stated in this Notification, once it does not have the high-tech enterprise qualification, it shall have no chance to enjoy the transitional preferential tax treatments from the tax year. Where it is once again approved as a high-tech enterprise later, it shall not continue to enjoy the transitional preferential tax treatments.

25/03/2011

Notification of the State Council on Pr...
shall not continue to enjoy the transitional preferential tax treatments.

PUBLIC FILE 23

5. This Notification shall enter into force as of January 1, 2008.

The State Council December 26, 2007

[Big medium-sized small] [Print] [Transmit]

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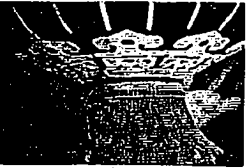
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PRICEWATERHOUSECOOPERS

China Tax / Business News Flash

2008 Issue 1

Jan 2008



Grandfathering Treatments Available to Old Foreign Investment Enterprises and High/New Tech Enterprises Newly Established in Specific Regions

The State Council released two important tax circulars dated 26 December 2007 but only publicised on 29 December 2007, just before the end of 2007, addressing the grandfathering treatments available to old foreign investment enterprises ("Old FIEs") (referring to FIEs whose business registration have been completed on or before 16 March 2007) and high/new tech enterprises ("HNTEs") newly established in certain specific regions under Article 57 of the Corporate Income Tax Law ("CIT Law").

Guofa [2007] No.39 ("Circular 39") ✓

The first circular is Circular 39 which mainly addresses the grandfathering treatments available to Old FIEs. It provides the detailed rules on the phasing-in of the CIT rate of Old FIEs which are currently enjoying an income tax rate of lower than 25% under the Foreign Enterprise Income Tax ("FEIT") regime to the statutory rate of 25% within the five-year period as stipulated in Article 57 of the CIT Law. The following table summarizes the transitional arrangement:

FEIT regime	CIT regime	Phasing-in of CIT rate
24%	25%	Change will take place on 1 Jan 2008
15%	25%	The rates will gradually increase in the following manner: 2008 18% 2009 20% 2010 22% 2011 24% 2012 25%

For those FIEs which were subject to 33% FEIT tax, the new applicable CIT rate will be 25% starting from 1 January 2008.

It also addresses the grandfathering treatments of unutilized tax holiday of Old FIEs. For those Old FIEs which have already commenced their tax holidays before 2008, they can continue to enjoy the remaining unutilized tax holidays until expiry. For those Old FIEs which have not commenced their tax holidays before 2008 due to losses, their tax holidays will be deemed to commence in 2008 and can be utilized until expiry.

For sake of clarity, Circular 39 has an appendix showing the types of tax incentives under the FEIT regime which qualify for the grandfathering treatments.

Circular 39 also states that the existing preferential tax policy available to enterprises established in the Western Region as stipulated in Caishui [2001] No.202 will continue to apply. This means those enterprises currently enjoying an income tax rate of 15% under that policy can continue to enjoy the same until its expiry in 2010 and those enterprises currently eligible for a "2+3" tax holiday under that circular can continue to enjoy the tax holiday until expiry.

It also clarifies that for an enterprise which qualifies for the grandfathering treatments and also new tax incentives under the CIT Law which cross over the above treatments, it is allowed to choose the one which is more preferential. This implies that there should be no duplication of benefits to be enjoyed. In addition, once the choice is made, it cannot be changed. Based on the literal reading of Circular 39, an example of this could be an FIE engaging in primary industries, e.g., the raising of livestock. Such FIE should qualify as "Production Enterprise" under the FEIT regime and be eligible for the grandfathering treatment if it has unutilized tax holiday. At the same time, income from such project is exempt from CIT under the new Law. In that respect, the FIE can choose between the grandfathering treatment of using such unutilized tax holiday and the exemption available under the CIT Law, and obviously the FIE would choose the latter one.

Guofa [2007] No.40 ("Circular 40")

The second circular is Circular 40 which addresses the tax incentive available to HNTEs newly established within certain specified regions as stipulated in Article 57 of the CIT Law. Circular 40 clarifies that the specific regions refer to the five special economic zones (namely, Shenzhen, Zhuhai, Shantou, Xiamen and Hainan) and the New Area of Pudong ("5+1 Zones") and the tax incentive applies to HTNEs established in the 5+1 Zones on or after 1 January 2008.

The tax incentive is in the form of a tax holiday of two-year exemption and three-year 50% tax rate reduction, with the holiday commencing from the first-income generating year (instead of "first-profit making year" which was generally applied under the FEIT regime). In addition, the 50% tax rate reduction is based on the statutory rate of 25% rather than the preferential income tax rate of 15% available to HTNEs under the CIT Law. This implies that the income tax rate for these new HTNEs will be as follows: 0% for the first two years, 12.5% for the next three years, and 15% thereafter.

The qualifying criteria for these new HTNEs are the same as those provided for under Article 93 of the CIT Detailed Implementation Regulations ("DIR"), namely core proprietary IP right and other prescribed criteria. To avoid the old problem of "registration within the zone but operating outside the zone", the tax holiday is only applicable to profits derived within the 5+1 Zones. Any profits derived outside the 5+1 Zones will not be eligible for the tax holiday. If the new HTNE has operations both within and outside the 5+1 Zones, it has to segregate its income and expenses between the two operations on a reasonable basis; if it fails to do so, then it will not be allowed to enjoy the tax holiday at all.

Further, if such HTNE is re-assessed on its qualifying criteria during the tax holiday period and fails the re-assessment, it will not be allowed to enjoy the tax holiday commencing from the year in which it fails the re-assessment. Even if it subsequently qualifies again as an HTNE, it cannot resume the remaining tax holiday or re-run a new round of the tax holiday.

PwC Observation

The two circulars have provided clarity on the criteria, scope and tax incentives addressed under Article 57 of the CIT Law. Most of them confirm our previous understanding. This will be helpful to most FIEs in assessing the tax profiles under the new CIT regime. For instance, the announcement of the detailed rules on the phasing-in of the CIT rate for Old FIEs which are currently enjoying an income tax rate of lower than 25% under the FEIT regime to the statutory rate of 25% over the five year period will now provide statutory support to these FIEs for booking their deferred taxes. However, there are still some issues relating to grandfathering treatments which are still unclear. To name a few here:

- the phasing-in of the income tax rate for non-productive Old FIEs established in the New Area of Pudong under the FEIT regime. The preferential income tax rate of 15% for non-production enterprise established in the New Area of Pudong does not appear in the appendix to Circular 39 of the types of tax incentives under the FEIT regime which qualify for the grandfathering treatment. In that respect, it is doubtful whether such non-productive FIEs will qualify for the phasing-in of the income tax rate from 15% to 25% as stated in the above table or immediately subject to 25% starting from 2008.

- The preferential income tax rate of 15% for Old Enterprises which have qualified as HNTEs ("Old HNTEs") under the FEIT regime is not in the list of tax incentives provided in the appendix to Circular 39, while the tax holiday for such Old HNTEs is. This would indicate that there is no grandfathering treatment on the 15% preferential income tax rate. An Old HNTE may enjoy the 15% income tax rate for HNTE under the CIT regime only if it satisfies the new HNTE criteria. Otherwise, it should be subject to the standard CIT rate of 25% from 2008. As to the grandfathering of tax holiday, an Old HNTE which also qualifies as an HNTE under the CIT regime would appear to be eligible for the unutilized tax holiday, if any. However, it is unclear whether those Old HNTEs which could not qualify as HNTEs under the CIT regime would be eligible for the grandfathering treatment. A literal reading of the appendix to Circular 39 seems suggesting that it would, but this is contrary to our understanding from previous discussion with some Chinese tax officials.
- Both circulars do not mention the grandfathering treatments in respect of other tax incentives provided under the FEIT regime, e.g. the 3-year extended tax holiday for the Technologically Advanced Enterprises, Reinvestment Refund out of the pre-2008 profits, Export-oriented Enterprises, tax credit for purchase of domestically made equipment, etc. On one hand, these types of tax incentives will not survive under the new CIT regime. On the other hand, it appears that these original tax incentives would not be grandfathered, unless the Chinese authorities provide further concessions under separate circulars later on.

These two State Council circulars are just two of the many circulars and guidelines which are expected to be issued by the Chinese authorities in the near future to further clarify the CIT Law and its DIR. We will share with you timely any important updates on these circulars and guidelines in future issues of PwC News Flash.

NEW ENTERPRISE INCOME TAX LAW IN CHINA

2007 was an important year for China's enterprise income tax reform. This Newsletter aims at providing you with background information of the recent development of the new enterprise income tax law during 2007, and highlighting key elements

Key Issues Affecting Foreign Investors

If you plan to invest in China, you need to know how the NEITL and the EITLR will affect your investment, and the degree of impact. In this section we highlight the key areas contained in the NEITL and EITLR that you should be aware of when formulating your China investment plan.

1. Enterprise income tax ("EIT") rate

EIT rates effective 1 January 2008 are as follows:

Unified EIT rate effective 1 January 2008	25%
Small scale / low profit enterprises	20%
High / new technology enterprises	15%

IMPORTANT

As mentioned above, qualifying high / new technology enterprises may enjoy a reduced EIT rate at 15%. According to the EITLR, in order to obtain the high / new technology enterprises' qualification, an enterprise is required to possess several characteristics (e.g. R&D personnel should be more than a prescribed percentage of total number of employees) which details will be promulgated later.

2. Tax resident enterprise and non-tax resident enterprise

The NEITL segregates enterprises into two categories: tax resident enterprises and non-tax resident enterprises. Tax resident enterprises will be subject to EIT on worldwide basis, while non-tax resident enterprises will only be subject to EIT on China sourced income.

The NEITL defines the meaning of tax resident enterprises to include enterprises incorporated outside China (e.g. a company incorporated under the laws of Hong Kong) with their place of effective management situated in China.

The "place of effective management" is elaborated in the EITLR. Instead of merely looking at where the board of directors meetings of an enterprise are held, the EITLR adopts a more comprehensive (but at the same time quite vague) approach to define the place of effective management as "the place where a substantive overall management and control of the production and business operation, personnel accounting, properties and sets of an overseas enterprise is situated." No universal rules are available to ascertain the tax residency of overseas enterprises, and each case will be assessed by reviewing its own facts.

IMPORTANT

Foreign investors should pay attention when formulating their investment plan to determine whether they are qualified to obtain the high / new technology enterprises' qualification. As mentioned above, a company is required to possess several characteristics (e.g. R&D personnel should be more than a prescribed percentage of total number of employees) which details will be promulgated later.

3. Withholding tax

Prior to 1 January 2008, dividends remitted to foreign investors from FIEs in China are exempt from withholding tax.

The NEITL indicates that with effect from 1 January 2008, outbound China sourced passive income (including dividends, royalties, interest etc.) will be subject to withholding tax at 20%. The EITLR reduces the withholding tax rate to 10%.

IMPORTANT

As mentioned above, dividends remitted to foreign investors from FIEs in China are exempt from withholding tax. However, with effect from 1 January 2008, outbound China sourced passive income (including dividends, royalties, interest etc.) will be subject to withholding tax at 10%.

4. Tax incentives

The NEITL provides a number of tax incentives including exemption or reduction in EIT rates, reduction in taxable income or tax payable, and extra deduction on certain types of expenses. The EITLR further elaborates the details of these tax incentives. However, many details still pending further clarification.

New tax incentives:

- High / new technology enterprises
- Venture capital enterprises
- Encouraged projects
- Extra deduction on R&D costs and disabled employees' salary
- Tax credit for the acquisition of equipments enhancing environment protection, energy or water saving, and production safety

Some of the tax incentives are discussed in detail below.

High / New Technology Enterprises

As mentioned above, qualifying high / new technology enterprises may enjoy a reduced EIT rate at 15%. According to the EITLR, in order to obtain the high / new technology enterprises' qualification, an enterprise is required to possess several characteristics (e.g. R&D personnel should be more than a prescribed percentage of total number of employees) which details will be promulgated later.

One of the characteristics is that a qualifying high / new technology enterprise should own a core proprietary intellectual property, which foreign investors usually are reluctant to hold in China given their inherent challenges with protecting intellectual property in China. Currently, it is uncommon for multinational corporations to transfer the ownership of their core proprietary intellectual properties to their Chinese subsidiaries due to various reasons, including intellectual properties protection concerns.

IMPORTANT

As mentioned above, a company is required to possess several characteristics (e.g. R&D personnel should be more than a prescribed percentage of total number of employees) which details will be promulgated later.

Venture Capital Enterprises

A venture capital enterprise investing in the equity of a non-listed small or medium high / new technology enterprise for more than two years can credit 70% of its investment amount against its taxable income with an indefinite carry-forward period.

Tax Exemption / Reduction on Income from Encouraged Projects

Some general preferential tax treatments granted under the old tax laws are no longer available under the NEITL. Instead preferential tax treatments are granted depending on the types of projects invested by investors.

Income derived from eligible encouraged projects can either be exempted from EIT or enjoy a reduced EIT rate.

Encouraged projects include the following:

Type of projects	Tax incentives available
<ul style="list-style-type: none"> ▪ Agricultural, forestry, animal husbandry and fishery projects 	Exemption from EIT or 50% tax reduction
<ul style="list-style-type: none"> ▪ Infrastructure projects 	3 years exemption from EIT plus 3 years half tax reduction period
<ul style="list-style-type: none"> ▪ Environmental protection, energy and water conservation projects 	

Detailed requirements regarding the qualification of these projects have not yet been promulgated.

5. Grandfather rules

The State Council has passed and issued two notices, *GuoFa (2007) no.39* and *GuoFa (2007) no.40* on 26 December 2007 regarding the transitional and grandfathering treatments in respect of tax incentives offered under the old tax laws.

GuoFa (2007) no.39

This notice provides the grandfathering treatment for enterprises (both DEs and FIEs) that have obtained business licenses before 16 March 2007 and are entitled to preferential tax treatments under the old tax laws.

This notice confirms the followings:

- a. Enterprises subject to a reduced tax rate of 15% before 2008: the EIT rate will increase gradually over 5 years according to the following table:

Year	EIT rate
2007	15%
2008	18%
2009	20%
2010	22%
2011	24%
2012	25%

- b. Enterprises subject to a reduced tax rate of 24% before 2008: the EIT rate will increase to 25% in 2008.

- c. Various tax holidays under old tax laws (most of the tax holidays were only available to FIEs, while some were also available to DEs):

- For those enterprises which have already started their tax holidays before 2008, they are able to enjoy the remaining tax holidays until expiry
- For those enterprises which have not yet started their tax holidays before 2008, the tax holidays will be deemed to start from 1 January 2008 and they are able to enjoy the remaining tax holidays until expiry

GuoFa (2007) no.40

This notice mainly addresses the tax incentives available to high / new technology enterprises newly established (i.e. established after 1 January 2008) in certain locations as stipulated under Article 57 of the NEITL. Details as follows:

- There are 6 zones, including the 5 economic zones (Shenzhen, Zhuhai, Shantou, Xiamen and Hainan) and Shanghai Pudong New Area
- These newly established high / new technology enterprises should comply with the requirements stipulated by the NEITL and EITLIR (discussed in Section 4 above)
- Tax incentive available to these enterprises is "2 years exemption followed by 3 years half tax reduction". The tax holiday will commence in the year when the enterprise starts generating income

6. Anti-avoidance provisions

The NEITL introduces a number of anti-avoidance provisions, and the EITLR further elaborates the same.

Anti-avoidance rules include:

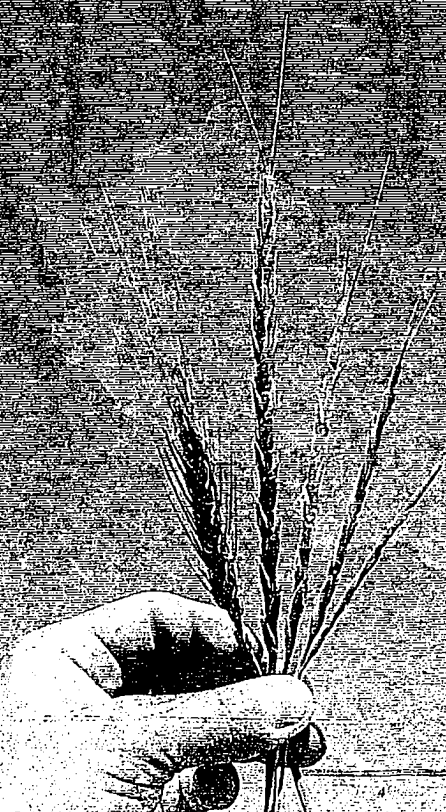
- Compulsory transfer pricing ("TP") documentation requirement
- Thin capitalization provision
- Controlled foreign corporation ("CFC") provision
- General anti-avoidance provision

EITLR does not provide very detailed elaboration of the above rules, and further guidance will likely be issued subsequently.

Of the above anti-avoidance provisions, TP may pose the biggest challenges to foreign investors. After the issuance of the NEITL and EITLR, it is expected that the Chinese tax authorities will turn their focus to TP regulations and enforcement.

IMPORTANT

When formulating the investment plan in China, foreign investors should consider the tax and calculation method of inter-company trading of goods and services with related companies. In addition, foreign investors need to be well-informed that related party transactions are properly supported by documents. Consulting with professional tax advisory firm is recommended.

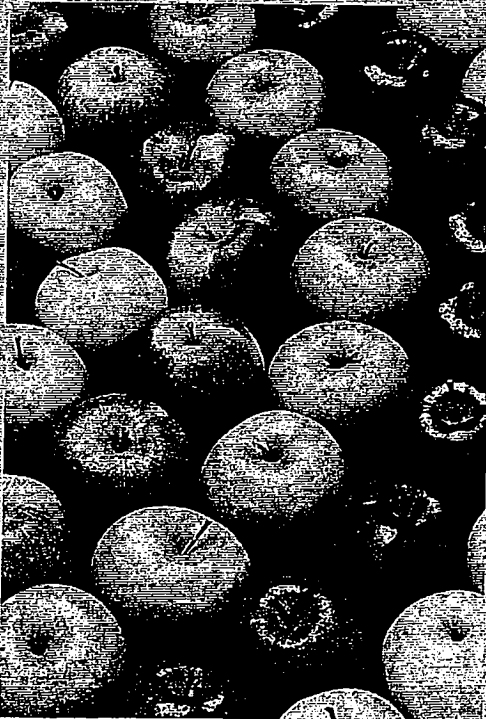


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IN CHINA**

7. Deductions

According to the NEITL and EITLIR, deductibility of some expenses are limited to certain levels or restricted to certain conditions.

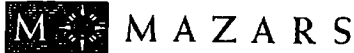
Type of expense	Treatment
<ul style="list-style-type: none"> ▪ Entertainment expenses 	60% of expenses are tax deductible, subject to a cap of 0.5% of annual turnover
<ul style="list-style-type: none"> ▪ Goodwill acquired 	Not deductible until disposal or liquidation
<ul style="list-style-type: none"> ▪ Advertising and promotion expenses 	Capped at 15% of annual turnover and remained portion can be carried forward for future deduction
<ul style="list-style-type: none"> ▪ Employee welfare expenses 	Deductible up to 14% of total salaries
<ul style="list-style-type: none"> ▪ Employee education expenses 	Deductible up to 2.5% of total salaries
<ul style="list-style-type: none"> ▪ Charitable donations 	Deductible up to 12% of accounting profit



Closing Comment

The issuance of the NEITL and EITLIR marks the launch of China's enterprise income tax reform, but there is still a long way to go. There are still a lot of uncertainties surrounding the NEITL and further explanations from the Chinese tax authorities will be announced from time to time. During this transitional period, we expect that foreign investors investing in China will no doubt face uncertainties on various tax positions over many important areas.

We will follow closely on future developments of the China enterprise income tax reform and update you in future issues of our Newsletter. No doubt that questions will arise after reading this Newsletter. Further professional opinion may be required.



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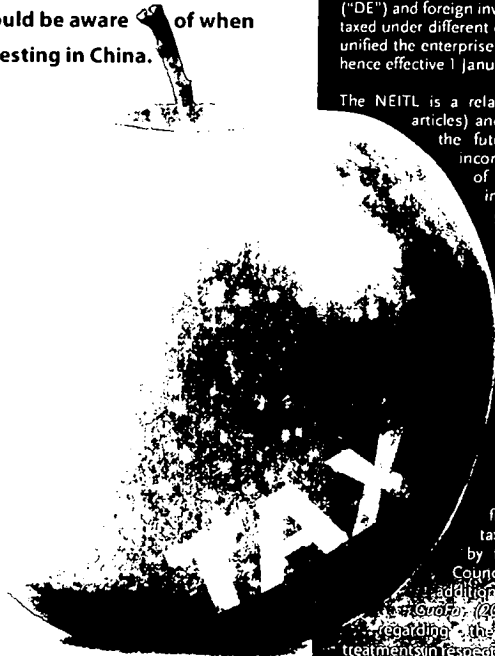
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2007 was an important year for China's enterprise income tax reform. This Newsletter aims at providing you with background information of the recent development of the new enterprise income tax law during 2007, and highlighting key elements that you should be aware of when consider investing in China.



Background

On 16 March 2007, the National Peoples' Congress in China passed the New Enterprise Income Tax Law ("NEITL"), effective 1 January 2008.

The issuance of the NEITL viewed as a milestone for China's enterprise income tax reform and brought China's corporate tax regime in line with other developed countries.

Prior to the issuance of the NEITL, domestic enterprises ("DE") and foreign invested enterprises ("FIE") in China were taxed under different enterprise income tax laws. The NEITL unified the enterprise tax law applicable to both DE and FIE, hence effective 1 January 2008.

The NEITL is a relatively short notice (only contains 60 articles) and mainly sets out a framework guiding the future evolvement of China enterprise income tax regime. It introduces a number of significant rules (e.g. types of tax incentives available, anti-avoidance provisions etc) without providing much detail.

On 6 December 2007, the State Council approved the detailed Enterprise Income Tax Law Implementation Rules ("EITLIR") and it was publicly released on 11 December 2007. The EITLIR contains 133 articles and further elaborates some of the terms and rules mentioned in the NEITL.

As yet, the EITLIR is far from complete and further notices will be issued by various Chinese authorities from time to time addressing specific tax areas that have not yet been covered by the EITLIR. As of today, the State Council has issued and issued two additional notices (Circular (2007) No. 30 under the Order (2007) No. 40 on 26 December 2007) regarding the transitional and grandfathering treatments in respect of tax incentives offered under the old tax laws.

3. Withholding tax

Prior to 1 January 2008, dividends remitted to foreign investors from FIEs in China are exempt from withholding tax.

The NEITL indicates that with effect from 1 January 2008, outbound China sourced passive income (including dividends, royalties, interest etc) will be subject to withholding tax at 20%. The EITLIR reduces the withholding tax rate to 10%.

THE EITLIR
The EITLIR provides a more detailed description of the tax incentives available to high / new technology enterprises. The EITLIR also provides a more detailed description of the tax incentives available to high / new technology enterprises.

If you plan to invest in China, you need to know how the NEITL and the EITLIR will affect your investment, and the degree of impact. In this section we highlight the key areas contained in the NEITL and EITLIR that you should be aware of when formulating your China investment plan.

1. Enterprise income tax ("EIT") rate

EIT rates effective 1 January 2008 are as follows:

Unified EIT rate effective 1 January 2008	25%
Small scale / low profit enterprises	20%
High / new technology enterprises	15%

THE EITLIR
The EITLIR provides a more detailed description of the tax incentives available to high / new technology enterprises. The EITLIR also provides a more detailed description of the tax incentives available to high / new technology enterprises.

2. "Tax resident enterprise" and "non-tax resident enterprise"

The NEITL segregates enterprises into two categories: tax resident enterprises and non-tax resident enterprises. Tax resident enterprises will be subject to EIT on worldwide basis, while non-tax resident enterprises will only be subject to EIT on China sourced income.

The NEITL defines the meaning of "tax resident enterprises" to include enterprises incorporated outside China (e.g. a company incorporated under the laws of Hong Kong) with their place of effective management situated in China.

The "place of effective management" is elaborated in the EITLIR. Instead of merely looking at where the board of directors meetings of an enterprise are held, the EITLIR adopts a more comprehensive (but at the same time quite vague) approach to define the place of effective management as "the place where a substantive overall management and control of the production and business operation, personnel, accounting, properties and etc of an overseas enterprise is situated". No universal rules are available to ascertain the tax residency of overseas enterprises, and each case will be assessed by reviewing its own facts.

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The NEITL provides a number of tax incentives including exemption or reduction in EIT rates, reduction in taxable income or tax payable, and extra deduction on certain types of expenses. The EITLIR further elaborates the details of these tax incentives. However, many details still pending further clarification.

- New tax incentives:**
- 1. High / new technology enterprises
 - 2. Venture capital enterprises
 - 3. Encouraged projects
 - 4. Extra-deduction on R&D costs and disabled employees' salary
 - 5. Tax credit for the acquisition of equipments enhancing environment protection, energy or water saving, and production safety

Some of the tax incentives are discussed in detail below:

High / New Technology Enterprises

As mentioned above, qualifying high / new technology enterprises may enjoy a reduced EIT rate at 15%. According to the EITLIR, in order to obtain the "high / new technology enterprises" qualification, an enterprise is required to possess several characteristics (e.g. R&D personnel should be more than a prescribed percentage of total number of employees) which details will be promulgated later.

One of the characteristics is that a qualifying high / new technology enterprise should own a core proprietary intellectual property, which foreign investors usually are reluctant to hold in China given the inherent challenges with protecting intellectual property in China. Currently it is uncommon for multinational corporations to transfer the ownership of their core proprietary intellectual properties to their Chinese subsidiaries due to various reasons, including intellectual properties protection concerns.

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The NEITL introduces a number of anti-avoidance provisions, and the EITLIR further elaborates the same.

Anti-avoidance rules include:

- Compulsory transfer pricing ("TP") documentation requirement
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EITLIR does not provide very detailed elaboration of the above rules, and further guidance will likely be issued subsequently.

Of the above anti-avoidance provisions, TP may pose the biggest challenges to foreign investors. After the issuance of the NEITL and EITLIR, it is expected that the Chinese tax authorities will turn their focus to TP regulations and enforcement.

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**NEW ENTERPRISE
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IN CHINA**

7. Deductions

According to the NEITL and EITLIR, deductibility of some expenses are limited to certain levels or restricted to certain conditions.

Item	Condition
Entertainment expenses	60% of expenses are tax deductible, subject to a cap of 0.5% of annual turnover
Goodwill acquired	Not deductible until disposal or liquidation
Advertising and promotion expenses	Capped at 15% of annual turnover and remained portion can be carried forward for future deduction
Employee welfare expenses	Deductible up to 14% of total salaries
Employee education expenses	Deductible up to 2.5% of total salaries
Charitable donations	Deductible up to 12% of accounting profit



Closing Comments

The issuance of the NEITL and EITLIR marks the launch of China's enterprise income tax reform, but there is still a long way to go. There are still a lot of uncertainties surrounding the NEITL and further explanations from the Chinese tax authorities will be announced from time to time. During this transitional period we expect that foreign investors investing in China will no doubt facing uncertainties on varies tax positions over many important areas.

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Tax 稅務

Issue M11/2008 – 12 March 2008

PRC Tax

China Enterprise Tax Reform Series

Tax Incentive Developments

Guidance in this Chinese post-tax reform period has been coming in fits and starts. While some of the developments have represented unexpectedly good news for many investors, many would have appreciated earlier announcement of these developments.

So what's new?

- Exemption from 10% dividend withholding tax when pre-2008 earnings are distributed
- Refunds for reinvestment of profits
- Prior incentives allowed "grandfathering" transition benefits
- Final phase-in "grandfathered" tax rates and adjusted phase-in tax rates for companies qualified for "grandfathering" of both a "2+3-type" incentive and the prior 15% incentive rate
- 2008 tax rate to be used by companies that held high and new-tech status in 2007
- 2007 Tax Returns and Settlement Arrangements
- Continued application of certain interest and royalty withholding exemptions
- Effect of post-2007 disqualification on certain pre-2008 tax incentives
- New location-specific incentive for companies holding high and new-tech status
- New software and integrated circuit ("IC") design incentives
- New IC production industry incentives
- New security investment fund incentives

In connection with the 1 January 2008 implementation of China's new Unified Enterprise Income Tax Law (the "New Law"), the State Council, both directly and through the State Administration of Taxation ("SAT") and Ministry of Finance ("MOF"), has been issuing guidance on issues of immediate importance. This Tax Analysis covers the more important of these issues.

Those interested in China should expect continued guidance and some surprises as the government slowly deals with each open issue and publishes its decisions.

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Dividend Withholding Tax Exemption

Caishui [2008] No. 1 announced at the end of February the much anticipated confirmation that China's new 10% withholding tax on dividends would not be imposed in certain situations. In brief, where a foreign invested enterprise ("FIE") pays a dividend from pre-2008 earnings to any non-resident shareholder, that dividend is exempt from Chinese withholding tax.

This circular does not provide any guidance regarding how the year(s) of the earnings from which the dividend is paid will be determined. Dividends declared during 2008, as a practical matter, will only be out of 2007 and prior years' earnings. As such, for such dividends, this will not be an issue. (While not common in China, it is of course possible that a company could declare in 2008 an interim dividend out of the current year's earnings. Such a dividend would be subject to withholding tax.)

From 2009, designating the years' retained earnings from which a dividend is paid will become a significant issue. In the absence of any "ordering rules" or other guidance that might be issued by the authorities in the future, we suggest that each FIE (or former FIE if that status has been lost) that plans to declare a dividend initiate from 2009 a procedure to identify within the resolution that declares the dividend the years' earnings out of which the dividend will be paid.

From solely a Chinese perspective it will always be best to choose the pre-2008 retained earnings first, which we believe should be acceptable, since that would defer the payment of withholding tax. However, it is possible that an investor's home country foreign tax credit rules might sometimes suggest otherwise. As such, some home country analysis should be conducted before dividends are actually declared.

Refunds for Reinvestment of Profits

An important feature of the pre-tax reform tax incentives system was the ability of foreign investors to receive refunds of taxes paid by the companies in which they invested by reinvesting the profits either in those companies paying the dividends or in other companies.

Although the New Law has eliminated this tax refund procedure for the future, Guoshuifa [2008] No. 23 issued on 27 February 2008 provides transition rules for claiming refunds related to 2007 reinvestments. (See below under the heading "New IC Production Incentives" for a limited continuing reinvestment refund procedure.)

In brief, foreign investors that have completed their reinvestment transactions and relevant registration procedures with the State Administration for Industry and Commerce (or its local branches) prior to the end of 2007 may apply for their tax refund in accordance with the old tax law. Interestingly, this circular makes clear that no tax refund will be granted for any reinvestment that is made from a 2007 interim dividend.

While there is no stated time limit in the circular for making the tax refund application, we suggest that investors initiate their applications soon.

Prior Incentives Allowed "Grandfathering" Transition Benefits

Guofa [2007] No.39 ("Circular 39"), issued at the end of December 2007, listed 30 incentives available under the old tax regime that would receive transition benefits. What is interesting is not what was included, but rather what was missing from this list that arguably should have been included, given the broad mandate for transition relief found in the New Law.

These missing items included, for example, certain foreign banks, Sino-foreign joint banks and other financial institutions established in Special Economic Zones or other districts approved by the State Council and FIEs qualifying as high and new-tech companies located in high-tech parks. Caishui [2008] No. 1 eliminates any hope that these types of missing items will receive any transition benefit. As a result, they will pay enterprise income tax ("EIT") from 1 January 2008 at a 25% rate and will not be allowed the transition phase-in rates.

Also not expressly included in the transition benefits listing were certain old law holidays and benefits

granted to software and IC companies. Because of technical legal drafting considerations, it is not perfectly clear that either or both of these had to be "expressly" included in the listing to arguably be covered by Circular 39. As a result, there has been considerable controversy.

Interestingly, as covered in more detail below, Caishui [2008] No. 1 announced very favorable incentives for these two industries. This circular, though, was silent on this controversial issue of whether these two industries would receive transition benefits. This therefore remains an open issue.

Certain preferences allowed by Caishui [2001] No. 202 focused on development of China's Western Region will continue to be implemented.

It may happen that a company qualifying for transition benefits under Circular 39 also qualifies for some new benefit granted under the New Law and implementation rules. For example, say that a company involved in harvesting forestry products sees that it will be exempt from tax from 2008 under the New Law. It is also listed in Circular 39 as qualifying for transition benefits.

Circular 39 provides that if any transitional benefit overlaps with New Law/implementation rule incentives, a company may choose the more favorable policy, but cannot enjoy both. Further, once a decision is made, the chosen policy cannot be changed. In the example of the forestry company, it would logically choose the new exemption rather than the less beneficial transition relief.

Final Phase-In Tax Rates and Adjusted Phase-In Tax Rates

After considerable internal governmental discussion, Circular 39 finalized the transition phase-in tax rates for qualifying companies previously paying tax at a 15% rate as follows:

2008	18%
2009	20%
2010	22%
2011	24%
2012 & thereafter	25%

For those that had paid tax at a 24% rate, they move immediately to a 25% tax rate in 2008.

An issue of some controversy was what tax rates would apply to companies qualified for "grandfathering" of both a tax holiday/50% reduction-in-rate incentive (e.g. the "2+3" incentive) and the prior 15% incentive rate. This issue was recently resolved by Caishui [2008] No. 21.

Under this new circular, the tax rate within the half-rate reduction period shall be calculated as 50% of the transition phase-in rates stipulated in Circular 39. This means that the following rates will apply if the indicated year is a half-rate year for a particular company.

2008	9%
2009	10%
2010	11%
2011	12%
2012	12.5%

For companies previously eligible for both the 24% tax rate and a half-rate reduction, the tax rate for each half-rate year is 12.5%, calculated as 50% of 25%.

Former High and New-Tech Status Companies

The New Law provides that companies qualifying for high-new technology status from 2008 will pay tax at a beneficial 15% rate.

In Guoshuifa [2008] No. 17, the SAT clarified that companies holding this high-new technology status prior to 1 January 2008 must use the normal 25% tax rate in their quarterly tax filing in 2008. They may not use the beneficial 15% until they have received a new 2008 qualification.

Due to the considerably higher 2008 requirements for this status, it is expected that many companies

Tax Incentive Developments - 12 March 2008

qualifying in prior years will be unable to continue this status in 2008 and beyond. For many FIEs that only license technology from abroad and that do not either legally or economically own their own technology, qualification will be very unlikely due to the 2008 requirement of ownership of "core intellectual property".

2007 Tax Returns and Settlement Arrangements

Under Guoshuihan [2008] No. 85, the SAT requires that old tax laws and regulations apply for both domestic companies and FIEs regarding their final settlement of EIT and the filing of their 2007 tax returns. However, the tax return filing deadline will be as set under the New Law at five months after the end of the tax year. This represents a one-month later filing deadline.

Certain Interest and Royalty Withholding Tax Exemptions

Guoshuifa [2008] No. 23 provides transition guidance for certain royalties and interest that had exemptions from withholding tax under the old tax law. In brief, any applicable tax exemption shall continue to apply during the contract period as long as the contract was signed prior to the end of 2007. For any period of extension of the original contract, the exemption will be lost.

Post-2007 Disqualification on Pre-2008 Tax Incentives

Under Guoshuifa [2008] No. 23, if an FIE enjoying an exemption/reduction (e.g. "2+3" tax holiday incentive) under the old tax law is disqualified for the incentives due to changes occurring in 2008 or later (say, due to changes in its business nature or operational period), the FIE must repay to the government the amount of tax that would have been paid previously had the incentive not been granted. The refund will include any benefits realized during the transition period.

Location-Specific Incentive for Companies Holding High and New-Tech Status

Although termed a "transition tax incentive", in Guofa [2007] No. 40, the State Council has unexpectedly continued to a limited extent the prior geographic focus of tax incentives. Applicable only to Pudong and five Special Economic Zones ("SEZs" and including Shenzhen, Zhuhai, Shantou, Xiamen and Hainan), this new incentive applies only to companies newly established from 1 January 2008. Where such companies also hold high and new-tech status, they are granted a "2+3" tax holiday. As a result, they will pay tax at the following rates from their first year of revenue:

Year 1	0.0%
Year 2	0.0%
Year 3	12.5%
Year 4	12.5%
Year 5	12.5%
Year 6	15.0%

To achieve and continue these tax rates, a company will have to re-qualify each year as being high and new-tech status.

New Software and IC-Design Incentives

Consistent with the innovation/high-tech goals of the government generally and its long-term 15-year innovation-focused plan (2006-2020), Caishui [2008] No. 1 provides a comprehensive approach to strongly encouraging the software production industry in China. Under this circular, this approach is also applied to IC-design companies.

In particular, this circular includes:

- "2+3" incentive for newly established approved software production companies ("SPCs") beginning from the first profit-making year (i.e., two years of tax holiday followed by three years of 50% reduction-in-rate)

It should be noted that the initiation of this tax holiday (as well as that below for IC production companies) in the first profit-making year is more favorable than the general rule as found for other tax holidays included in the New Law's implementation rules issued in December 2007. There, the holiday period begins in the first year of revenue, even if net taxable losses are being incurred.

- 10% tax rate for key SPCs listed in government plans in any taxable year not otherwise eligible for tax exemption
- Certain value added tax refunds received by SPCs exempt from EIT
- Full deduction for employee training expenses (in contrast to the 2.5% of total employees' salary and remuneration limitation that otherwise would apply)
- Two year depreciable life for approved capitalized purchased software (this benefits the SPCs' customers)
- Western region 80% reinvestment incentive for investment in SPCs (see under "New IC Production Incentives" below)

New IC Production Incentives

Caishui [2008] No. 1 provides a comprehensive approach to strongly encouraging the IC production industry in China.

In particular, this circular includes:

- "2+3" incentive for approved IC production companies beginning from the first profit-making year when ICs have a width of less than 0.8 μ m (i.e., two years of tax holiday followed by three years of 50% reduction-in-rate)

This incentive is not applicable for any company that has previously used a "2+3" tax holiday. In contrast to the above described software production and IC-design incentive that requires a newly formed company, this indicates that an existing IC production company that has not previously benefited from a "2+3" tax holiday under old law can qualify under the New Law.

An approved IC production company could potentially qualify as a high and new tech status company, thereby having a 15% tax rate. It is as yet not clear if, in such a case, the three 50% reduction-in-rate years will be taxed at 7.5% or 12.5%.

- "5+5" incentive for IC production companies with a 15-year or more operation period beginning from the first profit-making year when total investment exceeds RMB 8 billion or where produced ICs have a width of less than 0.25 μ m (i.e., five years of tax holiday followed by five years of 50% reduction-in-rate)

Interestingly, the circular does not include for this "5+5" incentive a similar prohibition against benefiting from two or more series of tax holidays as is mentioned above for the "2+3" incentive. As such, it is perhaps possible that an existing IC production company that qualified for, and benefited from, a tax holiday previously could again benefit from this new "5+5" incentive under the New Law.

Where such a company does not qualify for the special "5+5" holiday (say due to a less than 15 year operation period) or in years not covered by a holiday, a 15% rate will apply. This 15% rate raises the issue of whether a 7.5% rate or a 12.5% rate will apply in the five 50% reduction-in-rate years. At present, there is no guidance on this issue.

- For the three calendar years from 2008 through 2010, refund of 40% of the tax paid by an IC production or assembly company that relates to any profit distributions (i.e. dividends) paid to an investor in that company that reinvests its after-tax share of profits (i) directly back into that company by increasing registered capital or (ii) as capital investment into a newly established IC production or assembly company. A five year operating period is a requirement for both alternatives.

This and the following reinvestment benefits apply to both domestic and foreign investors. The

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former receive dividends from other resident companies free of any EIT. The latter, though, are subject to the 10% dividend withholding tax to the extent the profits distributed were earned in 2008 or later years. As covered earlier in this Tax Analysis, any dividends paid out of earlier years' earnings are paid free of this 10% withholding tax. Interestingly, the circular does not include for foreign investors for this reinvestment benefit or for the following one any exemption from this 10% withholding tax. That presumably is still payable.

Note also that if an investor sells all or a portion of its investment or withdraws all or a portion of its reinvested amounts prior to the end of five years for this or the following reinvestment incentive, any tax benefits relating to the sold or withdrawn portion must be repaid to the government. This treatment is based on old law that we do not expect will change.

- For the three calendar years from 2008 through 2010, refund of 80% of the tax paid by any Chinese company that relates to any profit distributions (i.e. dividends) paid to an investor in that company that reinvests its after-tax share of profits as capital investment into a newly established company in China's western region that will operate for five years or more and that is engaged in IC production or assembly or that qualifies as an SPC
- Appropriately reduced depreciation periods as short as three years for approved IC production equipment

Security Investment Fund Incentives

In addition to the above new "hi-tech" focused incentives, the government has chosen to encourage the continued growth of Chinese security investment funds. As a result, Caishui [2008] No. 1 includes "temporary" exemptions from EIT for security investment funds and their investors.

In China, in addition to pure domestic security investment funds, there are also several special categories. These include:

- Qualified foreign institutional investors ("QFIIs")—Mechanism for foreign investors to invest in the Chinese domestic markets
- Qualified domestic institutional investors ("QDIIs")—Mechanism for Chinese investors to access foreign securities markets

To date, there have been no clear tax rules for the taxation of foreign investors investing through QFIIs or Chinese investors investing through QDIIs. Due to the general language of Caishui [2008] No. 1, it is unknown whether its temporary exemptions cover QFIIs, QDIIs and their investors.

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