Enterprise Income Tax Law of the PRC

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Chapter I — General Provisions

Article 1 — This Law is enacted for the purposes of regulating the collection and administration of enterprise income tax, safeguarding the lawful rights and interests of enterprises, promoting fair competition, and

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facilitating the sound development of the socialist market economy.

Article 2 — Enterprises are classified into resident enterprises and non-resident enterprises. For the purposes of this Law, "resident enterprise" means an enterprise that is established within the territory of China in accordance with the law, or an enterprise that is established in accordance with the law of a foreign country (region) but has its effective management institution located within the territory of China. For the purposes of this Law, "non-resident enterprise" means an enterprise that is established in accordance with the law of a foreign country (region) and has its effective management institution located outside the territory of China, but has an institution or establishment within the territory of China, or has no institution or establishment within the territory of China but derives income sourced within the territory of China.

Article 3 — A resident enterprise shall pay enterprise income tax on its income derived from sources both within and outside the territory of China. Where a non-resident enterprise has an institution or establishment within the territory of China, it shall pay enterprise income tax on the income derived by its institution or establishment from sources within the territory of China, as well as on the income derived from outside the territory of China but effectively connected with its institution or establishment. Where a non-resident enterprise has no institution or establishment within the territory of China, or its income derived within the territory of China is not effectively connected with its institution or establishment within the territory of China, it shall pay enterprise income tax on the income derived from sources within the territory of China.

Article 4 — The enterprise income tax rate shall be 25 percent. The applicable tax rate for the income of a non-resident enterprise as provided for in the third paragraph of Article 3 of this Law shall be 20 percent.

Chapter II — Taxable Income

Article 5 — The taxable income of an enterprise shall be the total amount of its income in each tax year, after deducting the non-taxable income, tax-exempt income, various deductions, and the permitted deductions for the losses of previous years.

Article 6 — The total amount of income of an enterprise shall be the monetary and non-monetary income derived from various sources, including: (1) income from the sale of goods; (2) income from the provision of labor services; (3) income from the transfer of property; (4) income from dividends, bonuses, and other equity investment proceeds; (5) interest income; (6) rental income; (7) royalty income; (8) income from the acceptance of donations; and (9) other income.

Article 7 — The following income in the total amount of income shall be non-taxable income: (1) fiscal appropriations; (2) administrative fees and government funds collected in accordance with the law and included in financial administration; and (3) other non-taxable income as prescribed by the State Council.

Article 8 — Reasonable expenses actually incurred by an enterprise in connection with the earning of income, including costs, expenses, taxes, and losses, may be deducted in the calculation of taxable income.

Article 9 — The portion of the expenditure incurred by an enterprise for public welfare donations that does not exceed 12 percent of the total annual profit may be deducted in the calculation of taxable income. The total annual profit as mentioned in this Article means the accounting profit calculated by the enterprise in accordance with the unified accounting system of the state.

Article 10 — The following expenses shall not be deducted in the calculation of taxable income: (1) dividends, bonuses, and other equity investment proceeds distributed to investors; (2) enterprise income tax payments; (3) tax late payment surcharges; (4) fines, penalties, and losses from confiscation of property; (5) public welfare donations other than those provided for in Article 9 of this Law; (6) sponsorship expenditures; (7) unaudited reserve expenditures; and (8) other expenses not connected with the earning of income.

Article 11 — When calculating taxable income, an enterprise may deduct the depreciation of fixed assets calculated in accordance with the provisions. The following fixed assets shall not be subject to depreciation

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deductions: (1) fixed assets other than houses and buildings that are unused and not in service; (2) fixed assets leased from other parties under operating leases; (3) fixed assets leased to other parties under finance leases; (4) fixed assets for which depreciation has been fully provided but that remain in use; (5) fixed assets unrelated to business operations; (6) land separately valued and recorded as fixed assets; and (7) other fixed assets for which depreciation shall not be deducted.

Article 12 — When calculating taxable income, an enterprise may deduct the amortization expenses of intangible assets calculated in accordance with the provisions. The following intangible assets shall not be subject to amortization deductions: (1) the portion of the costs of self-developed intangible assets that has been deducted in the calculation of taxable income; and (2) goodwill created by the enterprise itself.

Article 13 — The following expenses incurred by an enterprise shall be treated as long-term deferred expenses and amortized in accordance with the provisions, and may be deducted in the calculation of taxable income: (1) the expenses for the improvement of fixed assets for which depreciation has been fully provided; (2) the expenses for the improvement of fixed assets leased from other parties; (3) the expenses for the major repair of fixed assets; and (4) other expenses that shall be treated as long-term deferred expenses.

Article 14 — During the period of outward investment by an enterprise, the cost of the investment assets shall not be deducted in the calculation of taxable income when the enterprise calculates its taxable income.

Article 15 — When an enterprise uses or sells its inventory, the cost of the inventory calculated in accordance with the provisions may be deducted in the calculation of taxable income.

Article 16 — Where an enterprise transfers its assets, the net value of the assets may be deducted in the calculation of taxable income.

Article 17 — Where an enterprise aggregates its income, the losses of an overseas business institution shall not be used to offset the profits of a domestic business institution.

Article 18 — Losses incurred by an enterprise in a tax year may be carried forward and offset against the income of subsequent tax years. The maximum carry-forward period shall be five years; where the losses cannot be fully offset within five years, the unoffset portion may be carried forward for a maximum of ten years, provided that the enterprise is a high-tech enterprise or a technology-based small or medium-sized enterprise as recognized by the state.

Article 19 — Where a non-resident enterprise derives income as provided for in the third paragraph of Article 3 of this Law, its taxable income shall be calculated according to the following methods: (1) for income such as dividends, bonuses, and other equity investment proceeds, as well as interest, rentals, and royalties, the taxable income shall be the full amount of the income; (2) for income from the transfer of property, the taxable income shall be the balance of the full amount of the income less the net value of the property; and (3) for other income, the taxable income shall be calculated by reference to the methods provided for in the preceding two items.

Article 20 — The specific scope and standards for the determination of income and deductions as set out in this Chapter, and the specific measures for the tax treatment of assets shall be formulated by the finance and taxation departments under the State Council.

Article 21 — In the calculation of taxable income, where the financial accounting methods of an enterprise are inconsistent with the provisions of taxation laws or administrative regulations, the calculation shall be made in accordance with the provisions of taxation laws and administrative regulations.

Chapter III — Tax Payable

Article 22 — The tax payable by an enterprise shall be the taxable income multiplied by the applicable tax rate, less the amounts deducted or exempted in accordance with the provisions of this Law on tax incentives.

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Article 23 — The enterprise income tax paid abroad by an enterprise on the following income may be credited against the tax payable for the current period. The credit limit shall be the tax payable on such income calculated in accordance with the provisions of this Law. The portion exceeding the credit limit may be carried forward for credit in the subsequent five years using the balance of the annual credit limit after deducting the tax credited for the current year: (1) income derived by a resident enterprise from sources outside the territory of China; and (2) income derived by a non-resident enterprise with an institution or establishment within the territory of China from sources outside the territory of China but effectively connected with its institution or establishment within the territory of China.

Article 24 — Where a resident enterprise derives dividends, bonuses, and other equity investment income from an enterprise that it directly or indirectly controls and is established outside the territory of China, the portion of the enterprise income tax paid abroad by the foreign enterprise on such income may be credited against the foreign tax credit of the resident enterprise as provided for in Article 23 of this Law.

Chapter IV — Tax Incentives

Article 25 — The state shall provide enterprise income tax incentives for key industries and projects whose development is supported and encouraged by the state.

Article 26 — The following income of an enterprise shall be tax-exempt income: (1) interest on treasury bonds; (2) dividends, bonuses, and other equity investment income distributed among eligible resident enterprises; (3) dividends, bonuses, and other equity investment income received by a non-resident enterprise that has an institution or establishment within the territory of China from a resident enterprise that is effectively connected with its institution or establishment; and (4) income of eligible non-profit organizations.

Article 27 — The enterprise income tax on the following income of an enterprise may be exempted or reduced: (1) income from projects of agriculture, forestry, animal husbandry, and fishery; (2) income from the operation of public infrastructure projects supported by the state; (3) income from projects of environmental protection, energy conservation, and water conservation that meet the relevant conditions; (4) income from the transfer of technology that meets the relevant conditions; and (5) income as provided for in the third paragraph of Article 3 of this Law.

Article 28 — Eligible small and low-profit enterprises shall be subject to enterprise income tax at a reduced tax rate of 20 percent. High-tech enterprises that require key state support shall be subject to enterprise income tax at a reduced tax rate of 15 percent.

Article 29 — The state may, based on the needs of national economic and social development, or due to the impact of emergencies on enterprise production and business activities, formulate special preferential enterprise income tax policies and submit them to the Standing Committee of the National People's Congress for filing.

Article 30 — The following expenses of an enterprise may be additionally deducted in the calculation of taxable income: (1) research and development expenses incurred for the development of new technologies, new products, and new processes; (2) wages paid for the employment of disabled persons and other persons encouraged by the state for employment; and (3) other expenses as prescribed by the State Council.

Article 31 — Venture capital enterprises engaged in venture capital investment supported by the state may deduct a certain percentage of the amount of their investment from their taxable income.

Article 32 — Where an enterprise's fixed assets really need to be depreciated on an accelerated basis due to technological progress or any other reason, the number of years of depreciation may be shortened, or accelerated depreciation methods may be adopted.

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Article 33 — The income derived by an enterprise from comprehensive utilization of resources and the production of products that comply with the state's industrial policies may be deducted in the calculation of taxable income.

Article 34 — A certain percentage of the amount invested by an enterprise in the purchase of special equipment for environmental protection, energy conservation, water conservation, safe production, and other purposes may be credited against the tax payable.

Article 35 — The specific measures for the tax incentives provided for in this Law shall be formulated by the State Council.

Article 36 — Where, based on the needs of national economic and social development, or due to the impact of emergencies and other circumstances on the production and business activities of enterprises, it is necessary to formulate special preferential enterprise income tax policies, the State Council may formulate such policies and submit them to the Standing Committee of the National People's Congress for filing.

Chapter V — Withholding at Source

Article 37 — The enterprise income tax payable on the income derived by a non-resident enterprise as provided for in the third paragraph of Article 3 of this Law shall be withheld at source, and the payer shall be the withholding agent. The withholding agent shall withhold the tax from each payment or the payment due at the time of each payment or the time when the payment is due.

Article 38 — The withholding agent for the enterprise income tax payable on the income derived by a non-resident enterprise from engineering operations or labor services within the territory of China may be designated by the taxation authority. The taxation authority shall designate the payer of the project price or the labor service fee as the withholding agent.

Article 39 — Where a withholding agent fails to withhold in accordance with the law, or is unable to perform the withholding obligation, the taxpayer shall pay the tax at the place where the income is derived. Where the taxpayer fails to pay the tax in accordance with the law, the taxation authority may recover the tax payable from the taxpayer from other income items payable by other payers within the territory of China to the taxpayer.

Article 40 — A withholding agent shall, within seven days from the date on which the withholding obligation arises, turn over the tax withheld to the state treasury, and shall submit the enterprise income tax withholding return and relevant materials to the local taxation authority.

Chapter VI — Special Tax Adjustments

Article 41 — Where a transaction between an enterprise and its related parties does not comply with the arm's length principle and results in a reduction of the taxable income of the enterprise or its related parties, the taxation authority shall have the right to make adjustments using reasonable methods. Where the costs of an enterprise and its related parties in jointly developing or transferring intangible assets, or in jointly providing or accepting labor services, are required to be shared in the calculation of taxable income, the costs shall be shared in accordance with the arm's length principle.

Article 42 — An enterprise may propose to the taxation authority the pricing principles and calculation methods for transactions with its related parties, and the taxation authority shall, after negotiation and confirmation with the enterprise, enter into an advance pricing arrangement.

Article 43 — When an enterprise submits its annual enterprise income tax return to the taxation authority, it shall attach an annual report on its related party transactions. When the taxation authority conducts an investigation on related party transactions, the enterprise and its related parties, as well as other enterprises related to the investigation, shall provide relevant information in accordance with the provisions.

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Article 44 — Where an enterprise fails to provide information on its related party transactions, or provides false or incomplete information that fails to truthfully reflect the related party transactions, the taxation authority shall have the right to determine its taxable income in accordance with the law.

Article 45 — Where an enterprise established by a resident enterprise, or a resident enterprise and a Chinese resident individual, in a country (region) where the actual tax burden is significantly lower than the tax rate provided for in Article 4 of this Law, does not distribute its profits or distributes profits in a reduced amount, and the profits are not for reasonable business needs, the portion of the profits that belong to the resident enterprise shall be included in the current income of the resident enterprise.

Article 46 — Where the ratio of debt investment to equity investment accepted by an enterprise from its related parties exceeds the prescribed standard, the interest expenses incurred on the excess portion shall not be deducted in the calculation of taxable income.

Article 47 — Where an enterprise enters into any other arrangement without reasonable business purposes and thereby reduces its taxable income or its tax payable, the taxation authority shall have the right to make adjustments using reasonable methods.

Article 48 — Where the taxation authority makes an adjustment to taxable income in accordance with the provisions of this Chapter and it is necessary to recover the tax that has been underpaid, it shall recover the tax and impose interest on the underpaid tax in accordance with the provisions of the State Council.

Chapter VII — Collection and Administration

Article 49 — The collection and administration of enterprise income tax shall be governed by the Law of the People's Republic of China on the Administration of Tax Collection as well as the provisions of this Law.

Article 50 — Unless otherwise provided for by taxation laws or administrative regulations, a resident enterprise shall pay enterprise income tax at the place where it is registered; where the place of registration is outside the territory of China, it shall pay the tax at the place where its effective management institution is located. Where a resident enterprise establishes a business institution that does not have the status of a legal person within the territory of China, it shall consolidate the calculation and payment of its enterprise income tax.

Article 51 — Where a non-resident enterprise derives income as provided for in the second paragraph of Article 3 of this Law, it shall pay the tax at the place where its institution or establishment is located. Where a non-resident enterprise has two or more institutions or establishments within the territory of China, it may, with the approval of the taxation authority, choose to have its principal institution or establishment consolidate the calculation and payment of enterprise income tax. Where a non-resident enterprise derives income as provided for in the third paragraph of Article 3 of this Law, it shall pay the tax at the place where the withholding agent is located.

Article 52 — Enterprises shall not consolidate the payment of enterprise income tax, except as otherwise provided for by the State Council.

Article 53 — Enterprise income tax shall be calculated on the basis of a tax year. The tax year shall commence on January 1 and end on December 31 of the Gregorian calendar year. Where an enterprise commences or terminates its business operations in the middle of a tax year, thereby making its actual business period in the tax year shorter than 12 months, the actual business period shall be treated as a tax year. Where an enterprise undergoes liquidation in accordance with the law, the liquidation period shall be treated as a tax year.

Article 54 — Enterprise income tax shall be prepaid on a monthly or quarterly basis. An enterprise shall, within 15 days after the end of a month or quarter, submit its prepaid enterprise income tax return to the taxation authority and prepay the tax. An enterprise shall, within five months after the end of each year,

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submit its annual enterprise income tax return to the taxation authority, make the final settlement of the tax, and pay the balance of tax payable or claim a refund for the overpaid tax. When submitting the enterprise income tax return, the enterprise shall attach the financial and accounting reports and other relevant materials in accordance with the provisions.

Article 55 — Where an enterprise terminates its business operations in the middle of a year, it shall, within 60 days from the date of actual termination of business operations, make the final settlement of the enterprise income tax with the taxation authority. Where an enterprise is deregistered in accordance with the law, a liquidation income tax return shall be filed before the deregistration.

Article 56 — Enterprise income tax payable shall be calculated in Renminbi. Where income is denominated in a currency other than Renminbi, the tax shall be calculated after the income is converted into Renminbi in accordance with the provisions.

Chapter VIII — Supplementary Provisions

Article 57 — Enterprises that were established before the promulgation of this Law and that were previously entitled to enterprise income tax at a reduced tax rate may, within five years after the implementation of this Law, gradually transition to the tax rate provided for in this Law in accordance with the provisions of the State Council. Enterprises that were entitled to regular tax exemption or reduction may continue to enjoy such treatment until the expiration of the period in accordance with the provisions of the State Council after the implementation of this Law. However, if they have not yet started to enjoy the benefits due to failure to make profits, the period for the benefits shall be calculated from the year in which this Law is implemented. High-tech enterprises that require key state support and that are established in special economic zones or in the new area of Pudong in Shanghai, and enterprises in encouraged industries established in the western region, shall be entitled to transitional preferential tax treatment. Other enterprises in encouraged industries that were already entitled to tax incentives shall be entitled to the transitional preferential tax treatment within five years in accordance with the provisions of the State Council.

Article 58 — Where the provisions of a tax treaty concluded between the government of the People's Republic of China and the government of a foreign country are different from the provisions of this Law, the provisions of the tax treaty shall prevail.

Article 59 — The State Council shall formulate implementation regulations for this Law.

Article 60 — This Law shall come into force as of January 1, 2008. The Enterprise Income Tax Law of the People's Republic of China on Foreign-Invested Enterprises and Foreign Enterprises, adopted at the Fourth Session of the Seventh National People's Congress on April 9, 1991, and the Interim Regulations of the People's Republic of China on Enterprise Income Tax, promulgated by the State Council on December 13, 1993, shall be repealed simultaneously.

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