

China's Industrial Subsidies Study: High Technology

Trade Lawyers Advisory Group

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I. CHINESE GOVERNMENT SUPPORT TO THE HIGH-TECH INDUSTRY: AN OVERVIEW

Since 1995, when the Chinese government put forward the strategy of “revitalizing the country through science and education” (*Ke Jiao Xing Guo*), the enhancement of scientific and technological innovation capacity has been a priority on the national development agenda. The past decade has witnessed a rapid expansion of research and development (R&D) efforts and government spending on science and technology (S&T) activities in China. The ratio of R&D expenditure to GDP went up from 0.6% in 1996 to 1.4% in 2006, with the actual expenditure growing over six fold from RMB 40.45 billion yuan to RMB 300 billion yuan.¹ In terms of sources of funds, in 2005, 26.3% of the R&D expenditure came from government, 67% from businesses, and 0.9% from abroad.² The total government fiscal spending on S&T activities increased from RMB 30.3 billion yuan in 1996 to RMB 133.5 billion yuan in 2005, with an average annual growth of 14% and 20%, respectively, at the central and local level.³ See the charts on the following page.

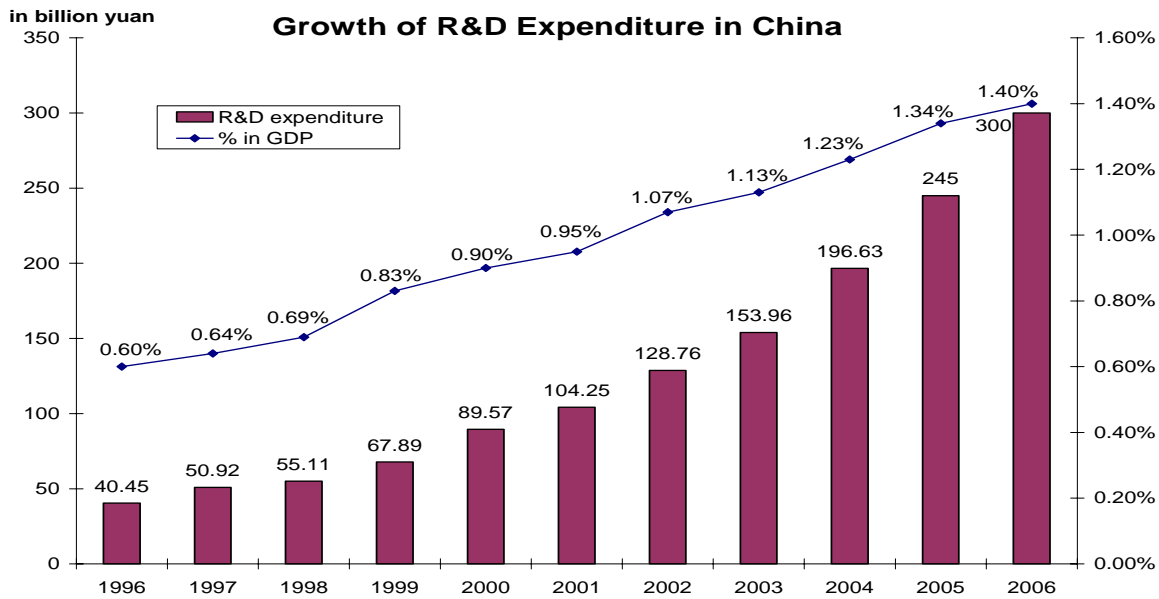
As the government and businesses devote considerable resources to the development of science and technology, China's high-tech industry has enjoyed vigorous growth. During the tenth five-year period (2001-2005), the total output value of the high-tech industry grew at an average rate of 27%, 3.3% higher than that of the manufacturing industry as a whole.⁴ The high-tech

¹ *China Science and Technology Statistics (2006): R&D Expenditure*, available at <http://www.sts.org.cn/sjkl/kjtjdt/data2006/2006-1.htm> (see Exhibit-53); *R&D Expenditure Reached 300 Billion Yuan in 2006*, Xinhua News (Jan 29, 2007), available at http://news.xinhuanet.com/fortune2007-01/29/content_5671044.htm (see Exhibit-54).

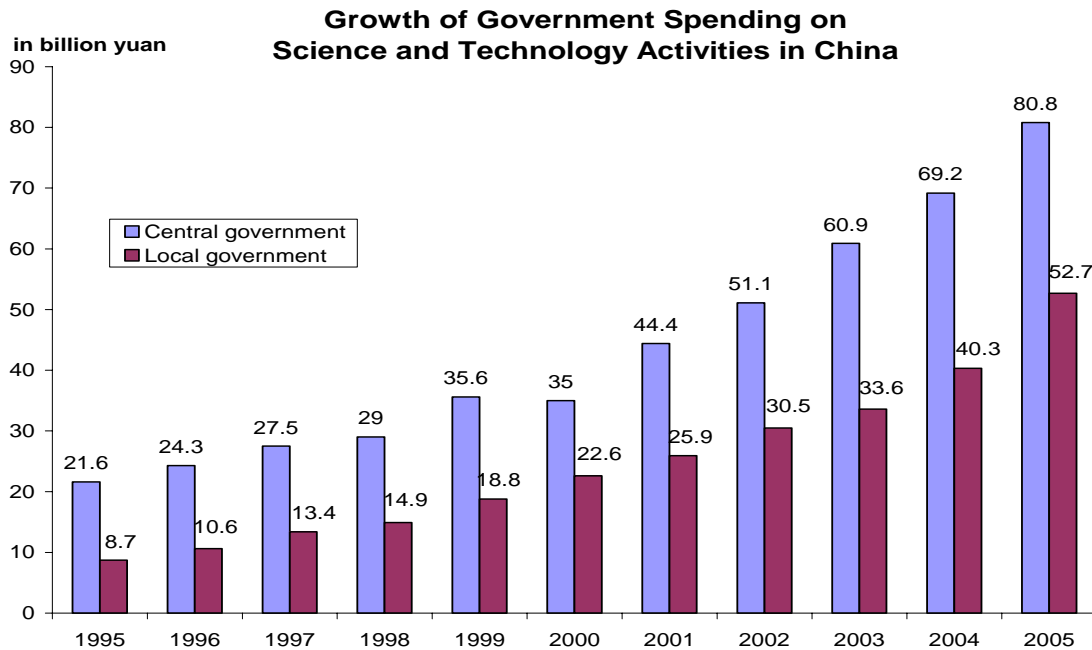
² Id.

³ *China Science and Technology Statistics (2006): Government S&T Appropriation*, available at <http://www.sts.org.cn/sjkl/kjtjdt/data2006/2006-2.htm> (see Exhibit-55).

⁴ *Analysis of 2005 Development of China's High-Tech Industry*, available at <http://www.sts.org.cn/tjbg/gjscopy/documents/2007/070125.htm> (see Exhibit-56).

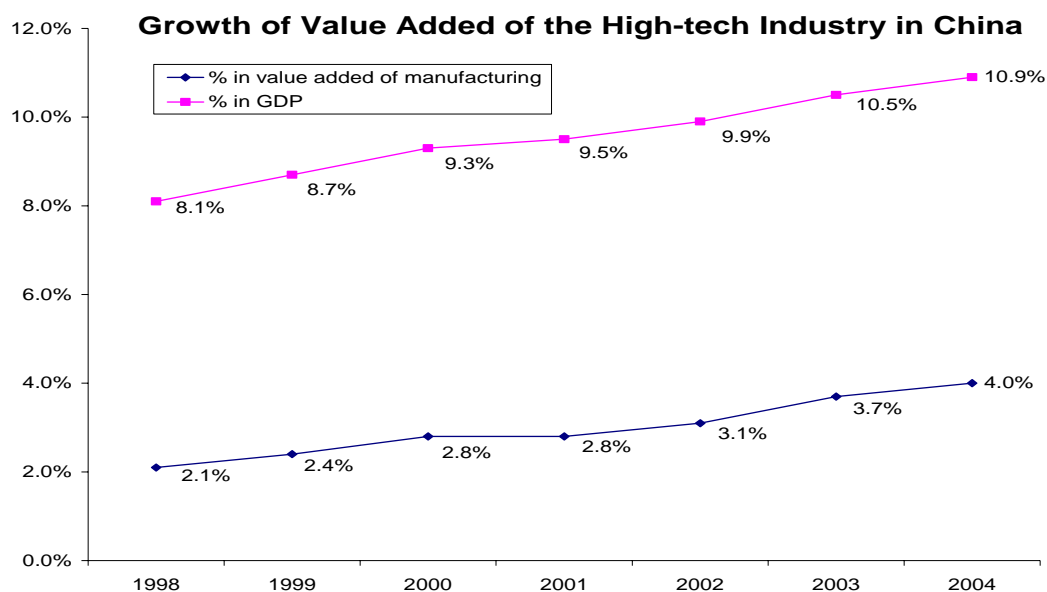


Source: *China Science and Technology Statistics (2006): R&D Expenditure*, available at <http://www.sts.org.cn/sjkl/kjtjdt/data2006/2006-1.htm>; *R&D Expenditure Reached 300 Billion Yuan in 2006*, Xinhua News (Jan 29, 2007), available at http://news.xinhuanet.com/fortune/2007-01/29/content_5671044.htm.



Source: *China Science and Technology Statistics (2006): Government S&T Appropriation* available at <http://www.sts.org.cn/sjkl/kjtjdt/data2006/2006-2.htm>.

output value reached RMB 3.44 trillion yuan in 2005, which ranked 3rd in the world, and is expected to exceed 10 trillion yuan in 2010.⁵ The value added by the high-tech industry to the manufacturing sector and GDP has increased steadily, rising from 8.1% of manufacturing and 2.1% of GDP in 1998 to 10.9% and 4% in 2004, respectively.⁶ China's exports of high-tech products also maintained a strong growth. In 2005, exports amounted to USD \$218.3 billion, or 28.6% of China's total exports; the 2001 figure was USD \$46.5 billion and 17.5%.⁷ In terms of product composition of the 2005 exports, computers and telecommunications equipment constituted the largest category, accounting for 81% of the total high-tech exports, followed by electronics (11%), opto-electronics (3%) and life science technologies (2%).⁸



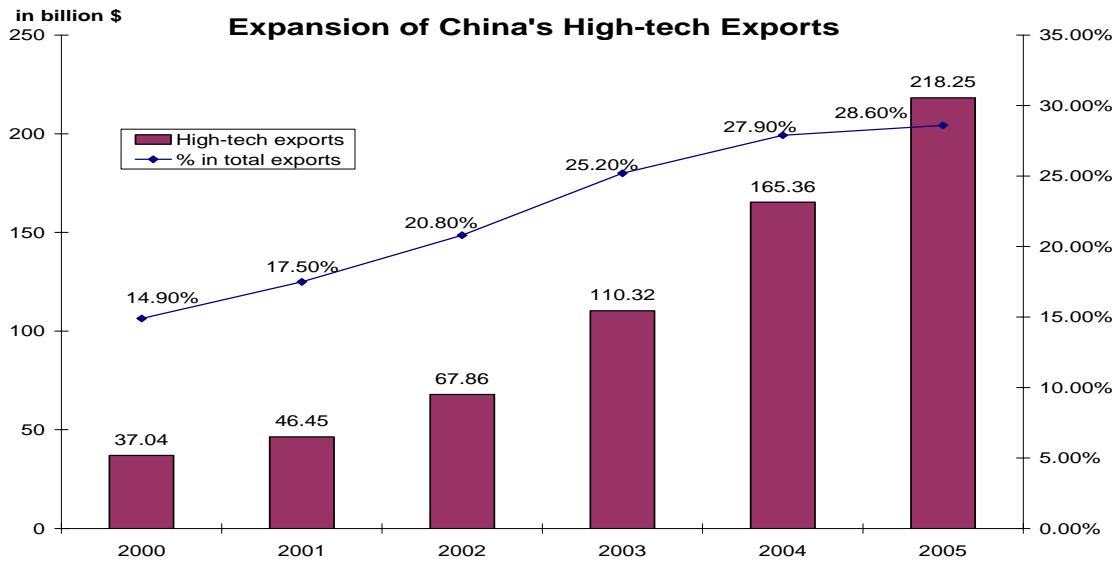
Source: *Analysis of 2005 Development of China's High-Tech Industry* available at <http://www.sts.org.cn/tjbg/gjscy/documents/2007/070125.htm>.

⁵ Id.

⁶ *China High-Tech Industry Statistics (2006): High-Tech Industry*, available at <http://www.sts.org.cn/sjkl/gjscy/data2006/2006-1.htm> (see Exhibit-57).

⁷ *China Science and Technology Statistics (2006): High Technology*, available at <http://www.sts.org.cn/sjkl/kjtjdt/data2006/2006-5.htm> (see Exhibit-58).

⁸ Id.



Source: *China Science and Technology Statistics (2006): High Technology* available at <http://www.sts.org.cn/sjkl/kjtjtdt/data2006/2006-5.htm>.

In the 11th five-year period (2006-2010) and over a longer time horizon, China will pursue the path of innovation, and, as emphasized by President Hu Jintao at China's Fourth National Conference on Science and Technology in 2006, government will play a leading role in this endeavor. Various government support programs put in place or under deliberation will reinforce the growth momentum in China's high-tech industry.

A. Central Government

1. Major programs and development focus

The 11th Five-Year (2006-2010) Guideline for National Economic and Social Development (see Exhibit-1) formulated by the central government set out the guiding principles of China's continued modernization drive, one of which is to "improve the capability of independent innovation" to pursue a balanced and sustainable social and economic development. Under this

principle, one of the development goals is to optimize the industrial structure, and more specifically, to strengthen the capacity of independent innovation, to increase the ratio of R&D expenditure to GDP to 2%, and to foster a group of globally-competitive companies with intellectual property (IP) ownership and well-known brands. In the high-tech sector, four industries are identified as the focus of development, namely, (1) electronics and information technology manufacturing, (2) biotechnology; (3) aviation and space; and (4) new materials. The blueprint also lays out major programs in the high-tech industry China is set to undertake as reviewed below:

- Integrated circuits and software: establishing integrated circuits research and development centers, industrializing the technology for 90-nanometer and smaller integrated circuits, and developing basic software, middleware, large key applied software and integrated systems.
- New-generation network: building next-generation Internet demonstration projects, a nationwide digital TV network and mobile communication demonstration networks with independent intellectual property rights.
- Advanced computing: making breakthrough in technology for petaflop computer systems, building grid-based advanced computing platforms, and commercializing the production of teraflop computers.
- Biomedicine: Building a number of demonstration projects for commercial production of vaccines for major diseases and gene-modified medicines, improving the modern traditional Chinese medicine system, and enhancing the capability for new medicine invention and production.
- Civil aircraft: developing planes for trunk and feeder lines, general-purpose planes and helicopters, as well as advanced engines.
- Satellite application: developing new meteorological, oceanographic, resource and telecommunication satellites, and poison- and pollution-free thrust augmented carrier rockets; building earth observation and navigation positioning satellite systems and facilities and application demonstration projects for civil satellite ground systems.
- New materials: building demonstration projects for commercial production of

high-performance new materials critically needed in information, biotechnology and aerospace industries.

The *Guideline for the National Medium- and Long-Term Science and Technology Development Plan (2006-2020)* (see Exhibit-2) issued by the State Council echoes the principles of the *11th Five-Year Guideline* and charts a course with more details for the national development of science and technology. It identifies innovation as a national priority strategy and sets the goal of advancing China into the rank of innovative countries by 2020. According to the Guideline, by 2020, China will invest more than 2.5% of its GDP in R&D, with the contribution of S&T to economic development exceeding 60% and with dependence on foreign technologies reduced to below 30%. Meanwhile, the annual number of indigenous patents granted and Science Citation Index papers are expected to rank among the top five in the world. The Guideline lists eleven priority sectors for technological development, such as information, manufacturing and agriculture, with a view to resolving pressing problems which are holding back the country's economic and social development. The Guideline also calls for the development of eight frontier technologies, *i.e.*, biotechnology, information technology, new materials technology, advanced manufacturing technology, advanced energy technology, marine technology, laser technology and aerospace technology.

The *11th Five-Year Plan on Promoting Trade through Science and Technology* (see Exhibit-3), intended to bolster China's efforts to optimize its export structure and move up the value chain, is another manifestation of China's commitment to innovation. The Plan puts forward the following primary objectives to advance the implementation of the strategy of "promoting trade through science and technology" (*Ke Ji Xing Mao*) that was initiated in 1999 by the Ministry

of Foreign Trade and Economic Cooperation (now known as the Ministry of Commerce or MOFCOM):

- Expand exports of high-tech products: by 2010, high tech products to account for 35% in the total exports; software exports to exceed USD \$10 billion; pharmaceutical exports to exceed USD \$20 billion.
- Optimize the export system of high-tech products: by 2010, to foster 100 export innovation bases in high-tech industries such as information, pharmaceutical, software, new materials, aerospace and aviation; to foster 100 large global companies with annual high-tech exports of above USD \$1 billion; to foster 1000 large companies with annual high-tech exports of above USD \$100 million.
- Strengthen the capability of independent innovation: by 2010, exports of high-tech products with IP ownership and brand names to account for 15% of the total exports of high-tech products; to bring about 160 key export brand names in the high-tech industry.

2. Types of support

Under the framework of *the Guideline for the National Medium- and Long-Term Science and Technology Development Plan (2006-2020)*, the Chinese government will implement a series of preferential policies to stimulate innovation among businesses. Chief among them are:

- Tax policies: implement consumption-based VAT; further implement various preferential tax policies to promote innovation, accelerate the transformation of scientific and technological achievements, and upgrade equipment; intensify the magnitude of tax incentives such as tax deduction of R&D expenditure; provide tax relief to new- and high-tech companies; allow the acceleration of depreciation of R&D equipments; accord preferential tax treatment to the purchase of advanced scientific research equipment; facilitate the establishment of overseas R&D centers, giving support in foreign exchange and financing; formulate preferential tax policies to nurture technological innovation of small- and medium-sized companies.
- Government procurement: give preference to domestically-produced high-tech equipment and products with IP ownership.
- Banking and financing policies: extend preferential loans to key high-tech industrialization projects; encourage venture capital investment with government

funding, policy loans and commercial loans; create a favorable environment for companies to be listed overseas.

Pursuant to the 11th Five-Year Plan on Promoting Trade through Science and Technology, companies exporting high-tech products with IP ownership and brand names will enjoy preferential treatment related to tax, credit, insurance and international settlement, special government funding support in R&D, as well as expedited Customs clearance services. The Plan also calls for greater efforts to encourage foreign investors to establish R&D centers, industrialize their research achievements, and transfer technologies to Chinese state-owned and private companies.

In accordance with government development guidelines, high-tech companies benefit from numerous special funds and fiscal appropriation programs administered by different government agencies. For example, high-tech companies are eligible for government grants and loan interest subsidies if their projects are listed among the national high-tech development projects with the approval of the State Development and Reform Commission (SDRC). A company can receive up to RMB 200 million yuan in grants for a project. This practice is administered under the *Provisional Measures on the Management of Projects in the National High-Tech Industry* (see Exhibit-4).

The following table lists selected government funds and fiscal appropriation programs available to the high-tech industry:

No	Title	Agency in Charge	From	Types of Fund
1	National High-Tech Industry Development Program	State Development and Reform Commission	1999	Grants, loan interest subsidies
2	Program on Export Promotion through Science and Technology	Ministry of Science and Technology, Ministry of Commerce	1999	Grants, export guarantee, support in export insurance
3	Development Fund for the Electronics and Information Industry	Ministry of Finance, Ministry of Information Industry	1986	Grants, loan interest subsidies, capital investment
4	Special Fund for Research and Development of the Integrated Circuits Industry	Ministry of Finance, Ministry of Information Industry	2005	Grants, loan interest subsidies
5	Technological Innovation Fund for the Technological Small- and Medium-Sized Enterprises	Ministry of Science and Technology	1999	Grants, loan interest subsidies
6	Special Development Fund for Small- and Medium-Sized Enterprises	Ministry of Science and Technology	2005	Grants, loan interest subsidies
7	Special Fund for Foreign Economic and Technological Cooperation	Ministry of Finance, Ministry of Commerce	2005	Grants, loan interest subsidies
8	High-Tech Research and Development Program - 863 Plan	Ministry of Science and Technology	1986	Fiscal appropriation
9	National Science and Technology Breaking-through Program	Ministry of Science and Technology	1982	Fiscal appropriation
10	National Key New Products Program	Ministry of Science and Technology	1988	Fiscal appropriation

The Chinese government has also been providing myriad tax incentives to high-tech companies. Pursuant to the 1994 *Circular of the Ministry of Finance and the State Administration of Taxation on Several Preferential Corporate Income Tax Policies* (see Exhibit-6), Chinese domestic companies recognized as high- or new-technology companies established in the State high- or new-technology industrial development zones enjoy a reduced income tax rate of 15%, and are exempt from the income tax during the first two years of production.⁹ Likewise, the income tax of enterprises with foreign investment recognized as high-or new-technology

enterprises established in the State high- or new-technology industrial development zones shall be levied at a reduced rate of 15%, according to the 1991 *Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises* (see Exhibit-7). Under China's newly enacted *Enterprise Income Tax Law*¹⁰ (see Exhibit-8) that unifies the income tax system for domestic and foreign enterprises, the high-tech sector continues to enjoy favorable treatment. Article 28 of the law stipulates that "the income tax rate shall be reduced to 15% for the State-encouraged new and high technology enterprises." The government will draft an industry list to implement this article. The benefit provided will further encourage both domestic and foreign investment by high-tech companies.

High-tech companies can also take advantage of tax incentives intended to encourage technological innovation. Pursuant to the 2003 *Circular of the Ministry of Finance and the State Administration of Taxation on Expanding the Application of Tax Deduction for Technology Development Expenditure by Enterprises* (see Exhibit-9), industrial enterprises, regardless of ownership, are not only able to fully deduct the expenses incurred for research and development of new products, new technologies and new crafts from their income taxes, but are also allowed an additional 50% deduction of R&D expenses, if such expenses increase 10% or more from the previous year. The 2006 *Circular of the Ministry of Finance and the State Administration of Taxation on Preferential Corporate Income Tax Policies for Technological Innovation* (see Exhibit-10), which was formulated to implement *The Guideline for the National Medium- and Long-Term Science and Technology Development Plan (2006-2020)*, reaffirms the above practice.

⁹ Before January 1, 2008, the standard national corporate income tax rate is 30% plus a 3% local income tax.

¹⁰ The new *Corporate Income Tax Law* was approved at the recently-concluded Fifth Session of the Tenth National People's Congress on March 16, 2007. It is slated to take effect on January 1, 2008. The law equalizes the

In addition, the 2006 circular provided for an income tax deduction for employee educational expenses and the acceleration of R&D equipment depreciation.

There are also preferential tax policies designed to support specific high-tech sectors, such as the software and integrated circuits industry and the TFT-LCD¹¹ industry, which are discussed in Section II of the paper.

B. Local Government

Provincial and local governments, in the formulation of corresponding development plans, observe the fundamental guidelines set by the central government while tailoring development focus and targets to local situations. In the *11th Five-Year Plan of Beijing Municipality* (see Exhibit-5), for example, “to remarkably improve innovation capacity” is laid out as one of the primary development goals. More specifically, the plan targets the creation of an innovation system with the Zhongguancun Science and Technology Park at the core, an R&D spending that accounts for 6% of the GDP, a high-tech export value that amounts to 38% of the total exports, and the development of companies with ownership of intellectual property rights, famous brands and strong international competitiveness. On the development of the high-tech industry, the plan lays priorities on sectors such as software and integrated circuits, computers and networks, and modern biotechnology. Specific plans in these sectors include:

- Software: accelerate the construction of the second phase of Zhongguancun Software Park, Yongyou Software Park and other software bases; focus on key technologies such as embedded software, middleware, information security and digital content; rely on the national software export bases to expand outsourcing; continue to support domestically-developed software through measures such as

income tax for domestic and foreign-invested enterprises at 25%.

¹¹ TFT-LCD is short for Thin Film Transistor-Liquid Crystal Display.

government procurement.

- Integrated circuits: accelerate the construction of a national IC industrial park; integrate IC industrial resources focused on designing with the support of manufacturing and testing; improve the industrial chain of semiconductor materials and IC designing, manufacturing, encapsulation and testing.
- Computer and network: encourage the global operation of large computer companies; accelerate the industrialization of 3C products based on IGRS standards; support the R&D and industrialization of high-performance computers; consolidate the alliance of the next-generation Internet industry.
- Modern biotechnology industry: step up research efforts on biological engineering and new products, such as gene engineering, biological chip, and animal vaccine; promote the development of biomedicine, bio-agriculture and biological environmental protection.

These development goals and plans appear to be generally consistent with those spelled out by the central government.

With respect to specific support measures and preferential policies, while assisting the central government in implementing subsidy programs, provincial and local governments give additional local support to industries and companies. Tianjin Municipality provides an example. Besides providing supplementary grants to projects supported by some of the central government programs and funds listed in the previous section, Tianjin Municipality administers a *Special Fund for Science and Technology Innovation* designed for companies to introduce advanced technologies and industrialize key science and technology research achievements.¹² The Fund supports 10 projects every year with a grant of 10 million yuan for each project.¹³ In terms of measures to promote high-tech exports, Tianjin Municipality provides grants and loan interest subsidies through the municipal-level *Special Fund of Export Promotion through Science and*

¹² *Introduction of Science and Technology Programs (April 6, 2006)*, Tianjin Economic and Technological Development Area, available at <http://www.teda.ac.cn/tedaast/include/showfile.asp?id=1057>(see Exhibit-59).

Technology, awards software exports through a municipal fund dedicated to this purpose, and subsidizes the premium for export credit insurance using the municipal *Foreign Trade Development Fund*.¹⁴ All these additional supports reinforce the efforts of the central government support system.

¹³ Id.

¹⁴ *Ten New Measures of Tianjin Municipality to Promote High-Tech Exports*, News Release of Ministry of Commerce (June 29, 2004), available at <http://preview.kjs.mofcom.gov.cn/aarticle/d/200409/20040900272671.html> (see Exhibit-60).

II. CHINESE GOVERNMENT SUPPORT TO THE ELECTRONICS AND INFORMATION INDUSTRY

China's electronics and information industry registered impressive growth during the 10th five-year period (2001-2005). The value added in 2004 amounted to RMB 944.7 billion yuan, or 7.5% of GDP; sales revenue grew at an average annual rate of 30%, reaching RMB 2650 billion yuan in 2004.¹⁵ Meanwhile, exports of electronics and information products quadrupled from USD \$55.1 billion in 2000 to USD \$207.5 billion in 2004, accounting for over one third of the country's total exports.¹⁶ All these developments would not have been possible without vigorous government support. As demonstrated in the 11th Five-Year Guideline for National Economic and Social Development, going forward, China intends for the electronics and information industry to be placed high on the national development agenda.

A. Central Government

1. Major programs and development focus

Reviewed below are major development plans and policies in the electronics and information industry that have been put into effect or are under contemplation:

No	Programs	Issuing Agency	Issuing Date
1	The 11 th Five-Year Plan & 2020 Mid- to Long-Term Plan for the Science and Technological Development of the Information Industry	Ministry of Information Industry (MII)	August 2006
2	The 11 th Five-Year Plan of Foreign Trade in the Electronics and Information Industry	MII	2006
3	Opinions on Accelerating the 'Giant Company' Strategy in the Electronics and Information Industry	MII	2004
4	Development Policies on the National Electronics and	MII	August 2006

¹⁵ Speech of Mr. Wang Xudong, Minister of Information Industry, at the Opening Ceremony of the Exhibition of the Development Fund for the Electronics and Information Industry during the 10th Five-Year, available at <http://www.itfund.gov.cn/help/2005shwjchg.doc> (see Exhibit-61).

¹⁶ Id.

No	Programs	Issuing Agency	Issuing Date
	Information Industry Bases and Industrial Parks		
5	Provisional Measures for the Administration of the Development Fund for the Electronics and Information Industry	Ministry of Finance (MIF), MII	July 2001
6	Cooperation Agreement on Development Financing to Support the Development of Information Industry and Application of Information Technologies	MII, China Development Bank (CDB)	December 2005
7	Several Policies for Encouraging the Development of the Software and Integrated Circuits Industry	The State Council	June 2000
8	Tax Policies on Further Encouraging the Development of the Software and Integrated Circuits Industry	MII, State Administration of Taxation (SAT)	October 2002
9	Action Plans on Promoting the Software Industry (2002-2005)	The State Council	July 2002
10	Provisional Measures for the Administration of the Specific Project Funds for Research and Development of the Integrated Circuits Industry	MIF, MII, State Development and Reform Commission (SDRC)	March 2005
11	Special Policies to Support the Software and Integrated Circuits Industry (designed to supersede No.7)	The State Council	To be issued
12	Preferential Tax Policies to Support the Development of the TFT-LCD Industry	MIF, STA	February 2005

The development goals laid out in these plans/policies are summarized as follows:

- By 2010, to transform the R&D and production capacity of the software industry into compliance with the advanced international standard.¹⁷
- By 2010, to have domestically-produced software products satisfy the majority of the domestic demand while being exported in large quantities; to have domestically-produced IC products satisfy the majority of the domestic demand while also being exported.¹⁸
- To develop a group of competitive “giant companies”; by 2008, to have 4 companies listed in the Fortune 500.¹⁹

¹⁷ *Several Policies for Encouraging the Development of the Software and Integrated Circuits Industry* (see Exhibit-15).

¹⁸ Id.

¹⁹ *Opinions on Accelerating the ‘Giant Company’ Strategy in the Electronics and Information Industry* (see

- To increase exports 15% annually during the 11th five-year period, and to exceed USD \$400 billion in exports by 2010.²⁰
- By 2010, to foster 5 companies with exports over USD \$10 billion and 50 companies with exports over USD \$1 billion.²¹
- By 2010, to bring about 10 global brands; to have exports of brand name products account for over 20% in total exports.²²

As part of its efforts to transform China into a global player in the electronics and information industry, the central government has established 9 information industry bases, 34 information industry parks, and 11 software export bases across the nation; it also appraises the list of top 100 electronics and IT companies every year.²³ These industry bases/parks and major companies enjoy preferential policies in terms of government grants, financing, government procurement, and international cooperation projects, and represent the major focus of the government's efforts to drive industrial development.

2. Types of support

a. Government grants

Government grants, allocated through special funds earmarked from the government fiscal budget, constitute a major type of government support to the electronics and information industry. Most of the policies/plans listed above call for special funds to be arranged and used for the R&D and industrialization of core technologies and the global expansion of domestic companies.

Exhibit-13).

²⁰ *The 11th Five-Year Plan of Foreign Trade in the Electronics and Information Industry* (see Exhibit-18).

²¹ Id.

²² Id.

²³ For the 9 information industry bases, see http://www.mii.gov.cn/art/2005/12/30/art_56_4090.html (see Exhibit-62); for the 34 information industry parks, see http://www.mii.gov.cn/art/2005/12/30/art_56_4091.html and http://www.mii.gov.cn/art/2005/12/30/art_56_4092.html (see Exhibit-63); for the 11 software export bases, see <http://chinawto.mofcom.gov.cn/aarticle/g/ab/200612/20061203946229.html> and <http://fwmys.mofcom.gov>.

A major fund operated by the Chinese government in the information industry is the *Development Fund for the Electronics and Information Industry* (IT Fund). Set up in 1986, the IT fund is intended to aid the software and integrated circuits (IC) industry as well as the development and industrialization of core information technologies and products in the fields of computers, telecommunications, networks, digital audio and visual, and electronic components.²⁴ The fund is administered by the Ministry of Finance (MIF) and the Ministry of Information Industry (MII) who issue a project catalogue every year identifying priority fields and allocate grants through a combination of bidding and application by companies. The grants take the form of direct grants, loan interest subsidies, and capital investment.

From 1986 to 2004, the IT Fund supported a total of 1,859 projects with RMB 3.9 billion yuan.²⁵ The five-year period of 2000-2004 saw extraordinary growth of the Fund's scale, with total grants amounting to RMB 2.4 billion yuan and benefiting 1,345 projects.²⁶ The magnitude of the grants also increased on an annual basis as shown in the table below.²⁷ Across the major fields of the electronics and information industry, software and IC have been enjoying the strongest support, receiving 40.7% and 15.1%, respectively, of the total grants from 2000 to 2004.²⁸

cn/aarticle/zhongyzt/y/ab/200506/20050600134519.html (see Exhibit-64); for the list of the top 100 electronics and IT companies, see <http://www.ittop100.gov.cn/200605/188766.shtml> (see Exhibit-65).

²⁴ *Introduction to the IT Fund*, available at <http://www.itfund.gov.cn/jianjie.php> (see Exhibit-66).

²⁵ *Speech of Mr. Wang Xudong, Minister of Information Industry, at the Opening Ceremony of the Exhibition of the Development Fund for the Electronics and Information Industry during the 10th Five-Year*, available at <http://www.itfund.gov.cn/help/2005shwjchg.doc> (see Exhibit-61).

²⁶ Id.

²⁷ *The IT Fund to Push Forward the Development of the Information Industry*, China Computer, available at http://www.media.ccidnet.com/art/2613/20050814/309883_1.html (see Exhibit-67).

²⁸ *Speech of Mr. Wang Xudong, Minister of Information Industry, at the Opening Ceremony of the Exhibition of the Development Fund for the Electronics and Information Industry during the 10th Five-Year*, available at <http://www.itfund.gov.cn/help/2005shwjchg.doc> (see Exhibit-61).

	2000	2001	2002	2003	2004	Total
Grants (in RMB million yuan)	265.3	387.85	459.8	561.1	754.45	2,428.5
Number of Projects	102	199	282	309	453	1,345

The IT Fund has created a ripple effect in which it influences the fiscal spending of local governments. From 2000 to 2004, local governments provided a total of RMB 15.6 billion yuan to projects supported by the IT Fund.²⁹ In the case of Shanghai, the municipal government allocated RMB 1.02 billion yuan to key projects, supplementing the grants of RMB 160 million yuan from the IT Fund.³⁰

The IT Fund has given a strong impetus to the development of the electronics and information industry. From 2000 to 2004, the IT Fund generated RMB 632.4 billion yuan in additional sales revenue and RMB 37.94 billion yuan in net profits; it also nurtured the development of 2,456 patents.³¹

With a view to giving priority support to the IC industry, the central government set up the *Special Fund for Research and Development of the Integrated Circuits Industry* (IC Fund) in 2005. The IC Fund is allocated in the form of direct grants, and a Chinese company may receive a grant up to 50% of the total R&D expenditures required in a project pursuant to the *Provisional Measures for the Administration of the Specific Project Funds for Research and Development of the Integrated Circuits Industry* (see Exhibit-11). As with the IT Fund, agencies in charge of the IC Fund, *i.e.*, the MIF, the MII, and the SDRC, issue a project catalogue every year identifying key fields that will receive grants and evaluate applications from individual companies. In 2005, the

²⁹ Id.

³⁰ Id.

³¹ Id.

IC Fund provided a total of RMB 150 million yuan to 27 companies for 29 projects.³²

Besides the IT Fund and the IC Fund, other sources of support available to the electronics and information industry include the "863 Plan," "National Science and Technology Breaking-through Program," and the *Technological Innovation Fund for the Technological Small- and Medium-Sized Enterprises*, which are the government fiscal appropriation programs and special funds for the high-tech industry in general that are administered by the Ministry of Science and Technology.³³ Under the *Action Plans on Promoting the Development of the Software Industry (2002-2005)* (see Exhibit-12) promulgated in 2002, these programs, together with the IT Fund, were intended to channel no less than RMB 3 billion yuan to the software industry from 2002 to 2005. In addition, the central government was to provide another RMB 1 billion yuan, bringing the total support goal to RMB 4 billion yuan.

In its endeavor to boost the competitiveness of the electronics and information industry, China is expected to set up more special-purpose funds and increase the magnitude of government grants. The *Opinions on Accelerating the 'Giant Company' Strategy in the Electronics and Information Industry* (see Exhibit-13), promulgated by the Ministry of Information Industry (MII) in 2005, calls on local governments to set up special-purpose funds for the development of "giant companies," especially companies whose R&D expenditures account for 6% of the sales revenue.

³² *Speech of Mr. Xiao Hua, Deputy Director of the Department of Products of Ministry of Information Industry (MII) at the 2006 Information Industry Meeting*, available at http://www.mii.gov.cn/art/2006/03/28/art_81_9281.html (see Exhibit-68).

³³ "863 Plan," also known as the High-Tech Research and Development Program, was launched in 1986. The program covers such areas as biotechnology, space technology, information technology, lasers, automation, advanced materials, energy technology, and marine technology. "National Science and Technology Breaking-through Program" launched in 1982 organizes the research and development of basic technologies related to the national economic and social development. *The Technological Innovation Fund for the Technological Small- and Medium-Sized Enterprises*, set up in 1999, provides direct grants and loan interest

Pursuant to *Development Policies on the National Electronics and Information Industry Bases and Industrial Parks* (see Exhibit-14), promulgated by the MII in 2006, every industry base is required to set up an annual special fund of no less than 50 million yuan to support key projects; for an industry park, the figure should be no less than 10 million yuan. According to the Chinese Semiconductor Industry Association, the new IC and software industry policies to be promulgated soon provide for an IC fund that will allocate USD \$12-25 million in grants for the first year followed by annual expansion in the scale of the grants.³⁴ Officials from the association also report that during the 11th five-year period (2006-2010), the Chinese government will spend a total of RMB 300 billion yuan on the IC industry.³⁵

b. Tax benefits

Pursuant to the government development plans and policies, there is an array of tax incentives available to electronics and IT companies in China. Major categories of tax benefits include income tax exemption and reduction, VAT rebate and exemption, and preferential tariff treatment.

Under the 2000 *Several Policies on Encouraging the Development of the Software and Integrated Circuits Industry* (see Exhibit-15), software companies registered in China are eligible for a full income tax exemption for the first two years after they start to make profits, followed by a 50% reduction for the next three years. This practice is known as the “two-free and three-half” treatment. Software companies that are recognized as key companies can enjoy a preferential 10%

subsidies to SMEs for technological innovation projects.

³⁴ *New Policies to Usher in New Vistas in the IC and Software Industry*, China Industry Information Network, available at <http://www.cinic.org.cn/HTML/2005/1799/20062160066.html> (see Exhibit-69).

³⁵ Id.

income tax rate during the time when these tax exemptions and reductions do not apply. The list of key software companies is jointly determined by the NDRC, MII, MOFCOM and SAT.³⁶ Under the same policy framework, IC companies with an investment of over RMB 8 billion yuan or that manufacture ICs with a width of less than 0.25 um are eligible to enjoy the preferential income tax rate that applies to foreign investors engaged in the energy and transportation sectors, which is full exemption for the first five years followed by a 50% reduction for the next five years, if the duration of operation is no less than 15 years.³⁷ In addition, the 2002 *Tax Policies on Further Encouraging the Development of the Software and Integrated Circuits Industry* (see Exhibit-16) accords the "two-free and three-half" preferential treatment to IC companies that manufacture ICs of 0.8 um or less in width.

The 2000 software and IC policies also stipulate that software companies are not subject to customs duties and import VAT for imports of equipment and technologies needed in their production, unless the commodities are listed in the *Catalogue of Imported Goods Not Eligible for Tariff Exemption for Foreign-Invested Projects* and the *Catalogue of Imported Goods Not Eligible for Tariff Exemption for Domestic-Funded Projects*. Imported IC technologies and whole sets of production equipment as well as separately imported special equipment and apparatus to produce ICs are also exempt from customs duties and import VAT. In addition, IC companies with an investment of over RMB 8 billion yuan or that manufacture ICs with a width of less than 0.25 um enjoy exemption from customs duties and import VAT for the imports of raw materials and consumption goods for their own production. The SDRC, together with other agencies,

³⁶ The 2005 list includes 157 software companies.

³⁷ See *Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises* and *Rules for the Implementation of the Income Tax Law of the People's Republic of China* for

administers a catalogue of tax-free IC products. Under the 2005 *Preferential Tax Policies to Support the Development of the TFT-LCD Industry* (see Exhibit-17), up until the end of 2008, TFT-LCD manufacturers are eligible to enjoy exemption from customs duties for imports of raw materials and consumption goods for their own production which cannot be produced domestically. In the meantime, they are not subject to customs duties and import VAT for imports of special construction materials for purification rooms, backup systems and equipment spare parts.

Pursuant to the 2000 software and IC policies, before 2010, general taxpayers must pay a 17% VAT for sales of software products that they have developed but are eligible to receive a refund of the portion above 3% after the collection. The VAT refund, used for the R&D of software products and production expansion, is not taxable as corporate income. In addition, the 2000 software and IC policies provide that chips designed by IC companies in China but manufactured overseas are eligible for a preferential tariff rate upon import into China.

c. Others: export promotion, financing support and government procurement

Under the 2000 software and IC policies, exports of software are incorporated into the business scope of the Export and Import Bank of China and enjoy credit support with a preferential interest rate. Under the same policy framework, export-oriented software companies enjoy support from the Central Foreign Trade Development Fund with respect to fees for the GB/T19000-ISO9000 and CMM System certification.

Pursuant to the 2005 *Opinions on Accelerating the 'Giant Company' Strategy in the*

Electronics and Information Industry and the *11th Five-Year Plan of the Foreign Trade in the Electronics and Information Industry* (see Exhibit-18), companies, especially "giant companies," receive governmental support when "going global" in terms of financing, insurance, foreign exchange, customs clearance, quality inspection, and staff entry and exit. The *Opinions* also encourage companies to participate in international cooperation projects to promote exports.

According to the *Cooperation Agreement on Development Financing to Support the Development of Information Industry and Application of Information Technologies*, signed by the Ministry of Information Industry and the China Development Bank (CDB) on December 21, 2005, within a timeframe of five years, CDB will arrange a credit of RMB 50 billion yuan to support the information industry.³⁸ As with other types of policy support, priorities will be given to "giant companies" and companies located in industrial bases and parks.³⁹

With respect to government procurement, the 2000 software and IC policies call for the use of domestic products in state-invested projects and major application systems under the same performance-to-price ratio. Pursuant to the 2005 *Opinions on Accelerating the 'Giant Company' Strategy in the Electronics and Information Industry*, priority consideration will be rendered to "giant companies" in government procurement. *The Action Plans on Accelerating the Development of the Software Industry* also encourages domestic companies to purchase domestically-developed software products and services.

³⁸ *Development Financing to Support the Innovation and Development of the Information Industry*, News Release of The Office of the Electronics Information System Promotion (December 21, 2005), available at http://www.qdb.gov.cn/pages/article_show.asp?articleID=126 (see Exhibit-70).

³⁹ See, e.g., *Development Policies on the National Electronics and Information Industry Bases and Industrial Parks* (see Exhibit-14).

B. Local Government

To implement the policies promulgated by the central government on promoting the electronics and information industry and to boost local competitiveness, local governments have formulated corresponding policies, reinforcing the spirit of the central government policies and providing additional support.

The following is a review of preferential policies in the software and IC industry adopted in four municipalities -- Shenzhen, Beijing, Shanghai and Suzhou -- which are among the 9 information industry bases in China:

Shenzhen: *Several Regulations on Accelerating the Development of Integrated Circuits Industry of Shenzhen City* (2001) (see Exhibit-19)

- To build an IC industrial park covering an area of 3-5 kilometers for the first phase; IC companies qualified to enter the park are exempt from the land use fee, municipal facilities fee, and the land development fee.
- To provide loan interest subsidies for up to three years to projects invested in prior to 2003.
- To subsidize IC companies' utility expenses.
- To provide preferential income tax treatment to IC companies located in Shenzhen; full exemption for the first five years followed by a 50% reduction for the next five years, provided the duration of operations is no less than 15 years.

Shanghai: *Several Policies on Encouraging the Development of Software and Integrated Circuits Industry of Shanghai Municipality* (2000) (see Exhibit-20)

- To arrange a special fund of RMB 500 million yuan for the software industry, rendering support to the infrastructure construction, key software projects, industrialization of technologies, and projects supported by the central government.
- To list the new chip production lines as key projects of the municipal government and provide 1% loan interest subsidies to the RMB portion of the loans for fixed assets.

- To exempt new chip production projects from transaction fees for the purchase of property for manufacturing purposes, property registration fees, water volume increase fees, gas volume increase fees, and additional power supply fees.

Beijing: Opinions of the Beijing Municipality on Implementing "Several Policies on Encouraging the Development of Software and IC Industry" of the State Council (2001) (see Exhibit-21)

- To provide 1.5% loan interest subsidies to approved IC projects during the construction period for up to three years; loan interest subsidies can be raised to 2% for projects constructed in areas guided by the government.
- To support the approved IC projects with a capital investment equal to 15% of the companies' registered capital; the municipal government has no voting power, nor does it share dividends, but it can transfer the ownership.
- To exempt IC investors from land use fee for 30 years.
- To set up a special fund for the software industry, supporting the innovation of software companies.

Suzhou: Trial Measures on Accelerating the Development of the Software Industry and the Integrated Circuits Design Industry of the Suzhou Industrial Park (2006) (see Exhibit-22)

- To subsidize the portion of the income tax above 7.5% during the tax reduction period for domestic-invested software companies recognized as provincial-level high-tech companies, using the technology development fund of the industrial park.
- To set up an investment fund of RMB 100 million yuan for the software and IC design industry, giving special support to the software and IC companies owning IP rights during the seed stage.
- To subsidize costs for Multi-Project Wafer samples and testing incurred by IC design companies when developing chips.
- To give preferential treatment in terms of land use fees and property rent to software and IC companies in the industrial park.
- To reward software companies with RMB 200,000 yuan to 500,000 yuan for obtaining CMM certifications (CMMI2, I3, I4, I5).
- To reward software companies (with an annual tax payment of RMB 500,000 yuan and above) respectively with RMB 500,000 yuan and 250,000 yuan for exporting over USD \$5 million and \$3 million for the first time.

- To reward software and IC companies with RMB 100,000 yuan when they go public.

In sum, additional local support is provided through many avenues, including grants from special funds, loan interest subsidies, preferential tax treatment, free land, preferential treatment in obtaining basic infrastructure services, and monetary awards.

C. Government Support to Chinese Companies in the Electronics and Information Industry

Many Chinese electronics and IT companies have sharpened their competitive edge and quite a few of them have started to catch global attention in recent years. Various government support programs at the central and local level have been playing a significant role in nurturing the development of these companies. The IT Fund, for example, has benefited over 70 out of the top 100 electronics and IT companies in China.⁴⁰ Many software and IC R&D projects have received grants from the IT Fund, including China's first digital media processing chip with IP ownership ("Hiview") developed by Hisense, Co., Ltd., the fifth-generation TFT-LCD developed by BOE Technology Group Co., Ltd, and the TD-SCDMA system related technology developed by Datang Telecom Technology Co. Ltd.⁴¹

The following is a review of subsidies as reported in the 2005 annual reports of six selected major Chinese players in the electronics and information industry. It demonstrates the breadth and diversity in the sources and types of subsidies enjoyed by these companies. Information on their sales revenue, stock listing, and ranking (of the companies or their parent companies) within the

⁴⁰ *Speech of Mr. Wang Xudong, Minister of Information Industry, at the Opening Ceremony of the Exhibition of the Development Fund for the Electronics and Information Industry during the 10th Five-Year*, available at <http://www.itfund.gov.cn/help/2005shwjchg.doc> (see Exhibit-61).

⁴¹ Id.

top 100 Chinese electronics and IT companies is also listed.⁴²

1. **Haier Electronics Group Co., Ltd.**⁴³ (part of the Haier Group): ranked 2nd; specializing in washing machines; listed on the Hong Kong Stock Exchange.

Subsidies (HK\$)	2,121,000
Sales Revenue (HK\$)	4,940,474,000

Source of subsidies:

- o Two of the group's subsidiaries in Mainland China received subsidies from the relevant authorities of Qingdao Municipality and Shunde Municipality as an encouragement for advanced research and development.
2. **BOE Technology Group Co., Ltd.**⁴⁴ ranked 3rd; specializing in TFT-LCD, color picture tube, monitor/flat panel TV, and small display devices; listed on the Shenzhen Stock Exchange.

Subsidies (yuan)	45,245,757
Sales Revenue (yuan)	13,461,793,093

Breakdown of subsidies:

- o 373,400 yuan in subsidies for the self-prepared generator from Shaoxing City Government.
 - o 43,772,357 yuan in loan interest subsidies for the TFT-LCD project received from the Economic Commission of Beijing Municipality.
 - o 1,100,000 yuan in loan interest subsidies for the fifth-generation TFT-LCD project received from the Ministry of Finance.
3. **Hisense Electric Co., Ltd.**⁴⁵ ranked 7th; specializing in televisions, refrigerators, mobile phones, air-conditioners, computers, and network devices; listed on the Shanghai Stock Exchange.

Subsidies (yuan)	9,844,309
Sales Revenue (yuan)	10,163,432,298

⁴² The 2006 top 100 electronics and IT companies list is available at <http://www.ittop100.gov.cn/200605/188766.shtml> (see Exhibit-65).

⁴³ Company website <http://www.haier.com>; see Exhibit-23 for its 2005 annual report.

⁴⁴ Company website <http://www.boe.com.cn>; see Exhibit-24 for its 2005 annual report.

⁴⁵ Company website <http://www.hisense.com>; see Exhibit-25 for its 2005 annual report.

Breakdown of subsidies:

- 1,000,000 yuan in grants from the central government's IT Fund for their flat screen TV products project.
- 384,309 yuan in VAT refunds received by Zibo Hisense Electronics Co., Ltd. as part of the preferential tax policy for Zibo Hisense.
- 250,000 yuan in VAT refunds received by Qingdao Sales Company of Beijing Hisense Electric Co., Ltd.
- 8,210,000 yuan in grants received by Guiyang Hisense Electronics Co., Ltd. from the Finance Bureau of Guiyang City Government.

4. **Langchao Electronic Information Industry Co., Ltd.**:⁴⁶ ranked 17th; specializing in computers, software, electronics, and telecommunications equipment; listed on the Shenzhen Stock Exchange.

Subsidies (yuan)	24,319,380
Sales Revenue (yuan)	1,305,936,889

Breakdown of subsidies:

- 23,296,380 yuan in VAT refunds for software products.
- 1,000,000 yuan in grants from the central government's IT Fund.
- 23,000 yuan in grants from the Fund for Enterprises in Potential Tapping and Upgrading from Taishan City Government.

5. **Tsinghua Tongfang**:⁴⁷ ranked 23rd; specializing in computers, laser disk player and chip components; listed on the Shanghai Stock Exchange.

Subsidies (yuan)	28,161,973
Sales Revenue (yuan)	9,775,186,870

Breakdown of subsidies:

- 23,788,555 yuan in VAT refunds for software products.
- 4,152,500 yuan in fiscal subsidies.
- 220,917 yuan in loan interest subsidies for export credit and other items.

6. **Shanghai Belling Corp., Ltd.**:⁴⁸ (part of the Huahong Group); ranked 44th; specializing in integrated circuits; listed on the Shanghai Stock Exchange.

⁴⁶ Company website <http://www.langchao.com>; see Exhibit-26 for its 2005 annual report.

⁴⁷ Company website <http://www.thtf.com.cn>; see Exhibit-27 for its 2005 annual report.

⁴⁸ Company website <http://www.belling.com.cn>; see Exhibit-28 for its 2005 annual report.

Subsidies (yuan)	13,296,180
Sales Revenue (yuan)	638,135,413

Breakdown of subsidies:

- 12,484,607 yuan in VAT refunds for IC products.
- 283,305 yuan in fiscal subsidies from the Finance Bureau of Shanghai Pudong New District Government based on value added.
- 420,000 yuan in grants from the IC development fund of the Finance Bureau of Hangzhou City Government.
- 81,090 yuan in fiscal subsidies from the Finance Bureau of Shanghai Pudong New District Government based on total profit.
- 27,178 yuan from other sources.

As demonstrated above, subsidies received by these companies are sourced from both central and local governments through a broad range of support programs, including the IT Fund, the IC Fund, loan interest subsidies, VAT refunds, fiscal subsidies based on total profit, fiscal subsidies based on value added, subsidies to encourage advanced research and development, the fund for enterprise potential tapping and upgrading, and others.

It is worth noting that these companies may receive some other government subsidies that are not booked as subsidies but rather as non-operating revenue in their annual reports. For example, BOE Technology Group announced on March 6, 2007 that it just received a grant of RMB 53.27 million yuan from the *Special Fund for Foreign Economic and Technological Cooperation*⁴⁹ approved by the Ministry of Finance and the Ministry of Commerce. According to BOE, the grant, which will be used as working capital and booked as non-operating revenue for the first quarter of 2007, will have a positive impact on the company's profit.⁵⁰

⁴⁹ The fund is administered under the *Administrative Measures on the Special Fund for Foreign Economic and Technological Cooperation* issued by the Ministry of Finance and the Ministry of Commerce on December 9, 2005 with a view to implementing the national strategy of "going global."

⁵⁰ *BOE Technology Group Received Government Subsidies of RMB 53.27 Million Yuan*, Sina News Release (March 7, 2007), available at <http://finance.sina.com.cn/stock/t/20070307/06511247445.shtml> (see Exhibit-71).

As shown in their annual reports, these companies also enjoy income tax benefits that are not reflected as subsidies *per se*. In their 2005 annual reports, BOE Technology Group (as a high-tech company established in the Beijing New Technology Development Experimental Zone), Shanghai Belling Corp (as a high-tech company established in the Shanghai Caohejing New Technology Development Zone), Tsinghua Tongfang (as a high-tech company recognized by the Beijing Science and Technology Commission), and Langchao Electronic Information Industry Co., Ltd. (as a high-tech company established in the Jinan New and High Technology Development Zone), are all eligible for a reduced income tax rate of 15%. This preferential treatment is accorded pursuant to relevant provisions on high-tech companies in the 1994 *Several Preferential Corporate Income Tax Policies* (see Exhibit-6). One of the subsidiaries of Langchao Electronic Information Industry Co. Ltd., namely, Langchao Cheeloosoft, enjoys a reduced rate of 10% as a key software company recognized by the central government, a treatment granted under the 2000 *Several Policies on Encouraging the Development of the Software and Integrated Circuits Industry* (see Exhibit-15). In the case of Haier Electronics Group, among its seven subsidiaries established in China, four are Sino-foreign equity joint ventures, two are wholly-foreign-owned enterprises and the remaining one is a limited liability company. Except for the limited liability company and one Sino-foreign equity joint venture, all subsidiaries are entitled to preferential tax treatment including reduction of corporate income tax and full income tax exemption for two years starting from their first profit-making year followed by a 50% reduction for the next three years. This two-free and three-half treatment is granted under the 1991 *Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises* (see Exhibit-7).

Another major source of government support for these companies and other major players in the electronics and information industry is the easy access to preferential policy loans. Two of the three policy banks in China, the China Development Bank and the Export and Import Bank of China, have been rendering strong credit support to companies in their technological innovation and global expansion. The following are examples of such support received by major Chinese electronics and IT companies:

- On February 13, 2004, the Export and Import Bank of China agreed to provide USD \$600 million in export credit to Huawei Technology, a telecoms-network equipment maker.⁵¹
- On September 7, 2004, the Export and Import Bank of China agreed to provide a credit line of USD \$1.5 billion to Haier Group for its exports and overseas investment in the next five years.⁵²
- On December 27, 2004, the China Development Bank agreed to offer a credit line of USD \$10 billion to Huawei Technology for its global market expansion in the next five years.⁵³
- On March 12, 2005, the Export and Import Bank of China agreed to provide RMB 6 billion yuan in export credit to TCL, now the world's largest TV maker, who acquired the TV business of Thompson and the mobile phone business of Alcatel in 2004.⁵⁴
- In June 2005, the China Development Bank agreed to offer a credit line of RMB 3.8 billion yuan to Tsinghua Tongfang in its efforts to go global.⁵⁵
- On August 5, 2005, the China Development Bank agreed to offer a credit line of

⁵¹ *Huawei Has Obtained USD \$600 Million In Export Financing*, News Release of Huawei Technology, available at <http://www.huawei.com/cn/news/view.do?id=619&cid=86> (see Exhibit-72).

⁵² *The Export and Import Bank of China and Haier Group Signed a Cooperation Agreement of USD \$1.5 Billion of Export Credit*, News Release of the Export and Import Bank of China (September 8, 2004), available at http://www.eximbank.gov.cn/info/Article.jsp?a_no=493&col_no=79 (see Exhibit-73)

⁵³ *Development Financing Facilitating the Strategy of "Going Global,"* News Release of Huawei Technology, available at <http://www.huawei.com/cn/news/view.do?id=515&cid=86> (see Exhibit-74)

⁵⁴ *Chinese Companies Going Global*, China International E-Commerce Network (January 9, 2006), available at http://zsq.ec.com.cn/pubnews/2006_01_19/100300/1127775.jsp (see Exhibit-75)

⁵⁵ Id.

RMB 8 billion yuan to TCL in its efforts to go global in the next five years.⁵⁶

- By November 2006, the China Development Bank extended loans of USD \$440 million to BOE Technology Group, including a soft loan of RMB 1.12 billion yuan extended recently to support the fifth-generation TFT-LCD project.⁵⁷

⁵⁶ Id.

⁵⁷ *Governor of the China Development Bank Mr. Chen Yuan Visited BOE for the Fifth-Generation TFT-LCD Project*, News Release of BOE Technology Group, available at <http://www.boe.com.cn/0821/cn/news/ViewArticle.aspx?articleid=212> (see Exhibit-76)

III. CHINA'S SUBSIDIES RELEVANT TO THE HIGH-TECH INDUSTRY NOTIFIED BY CHINA TO THE WTO

China undertook various commitments on subsidies in joining the WTO in 2001. Specifically, China committed to eliminate all subsidy programs prohibited under Article 3 of the Agreement on Subsidies and Countervailing Measures (SCM) (*i.e.*, subsidies contingent on export performance (export subsidies) and subsidies contingent on the use of domestic over imported goods (import substitution subsidies)). In addition, China committed to phasing out three subsidy programs: (1) subsidies provided to certain state-owned enterprises which are running at a loss (to be terminated by the end of 2000); (2) priority in obtaining loans and foreign currencies based on export performance (to be terminated by the end of 2000); and (3) preferential tariff rates based on localization rate of automotive production. China also assumed the other general obligations of the SCM Agreement, including the annual subsidies notification required under Article 25.1.

On April 13, 2006, China filed its long-overdue subsidies notification to the WTO.⁵⁸ The notification contains information on 78 subsidy programs granted or maintained at the central government level in China. As noted by USTR, “although the notification is lengthy, with over 70 subsidy programs reported, it is also notably incomplete, as it failed to notify any subsidies provided by China’s state-owned banks or by provincial and local government authorities. In addition, while China notified several subsidies that appear to be prohibited, it did so without making any commitment to withdraw them, and it failed to notify other subsidies that appear to be prohibited.”⁵⁹

⁵⁸ *New and Full Notification Pursuant to Article XVI:1 of the GATT 1994 and Article 25 of the SCM Agreement – People’s Republic of China*, G/SCM/N/123/CHN (13 April 2006).

⁵⁹ See USTR, *2006 Report to Congress on China’s WTO Compliance*, at page 42.

Among the 78 notified programs, three programs are designed to encourage high- and new-technology industrial development specifically (*see programs VIII, IX, LVII*), with one program intended to aid the development of the integrated circuits industry (*see program LVII*). Fourteen other programs, which are not of an industry-specific nature, also apply to certain companies in the high-tech industry, or can benefit the high-tech industry through encouraging foreign investment (*see programs I, II, VI, X, XI, XIII, LVIII, LX*), domestic investment (*see programs LIX, LX*), regional development (*see programs X, XI, XIII, XIV*), research and development (*see programs XXVI, XXVII*), transfer of technology (*see program XXVIII*), purchase of domestically-produced equipment (*see programs LVIII, LIX*), technological innovation (*See program XXXI*) and technological upgrading (*see program LIX*). Preferential tax treatment, direct grants and loan interest discounts constitute the major forms of the subsidies. The following table reviews the 17 programs relevant to the high-tech industry:

I. Preferential tax policies for foreign-invested enterprises (FIEs).

Legislation:

Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises(*see Exhibit-7*); *Rules for the Implementation of the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises*(*see Exhibit-29*)

Benefits:

- (1) Two years of income tax exemption and three years of 50% reduction for production-oriented FIEs scheduled to operate for not less than ten years from the first profit-making year.
- (2) Refund of 40% of income tax paid on reinvestment for increasing the registered capital of the existing enterprise or establishing other enterprises, to operate for not less than five years.
- (3) Full refund of the income tax paid on the reinvestment in China for the organization and expansion of export-oriented enterprises or advanced-technology enterprises.
- (4) Reduced income tax rate of 10% for the royalty received for the supply of technical know-how in scientific research and the development of important technologies.

II. Preferential tax policies for foreign-invested export enterprises.

Legislation:

Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises(see Exhibit-7); *Rules for the Implementation of the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises*(see Exhibit-29)

Benefits:

After the expiration of the normal income tax exemption and reduction, foreign-invested export-oriented companies can pay income tax at a rate reduced by one half, if 70% of their products are exported. Such companies located in special economic zones and economic and technological development zones and other such companies subject to a 15% income tax rate that comply with the foregoing conditions, shall pay income tax at 10%.

VI. Preferential tax policies for enterprises with foreign investment which are technology-intensive and knowledge-intensive.

Legislation:

Circular on the Preferential Tax Treatment to Foreign Invested Companies That Are Technology and Knowledge Intensive (Guoshuifa No.139 of 1995) (see Exhibit-30); *Circular on the Preferential Tax Treatment to Foreign Invested Companies That Are Technology and Knowledge Intensive* (Guoshuifa No.135 of 2003) (see Exhibit-31)

Benefits:

A reduced income tax rate of 15% for FIEs that are technology-intensive and knowledge-intensive and whose major products are listed in the "Catalogue of High and New Technology Products of China" promulgated by MOST provided that the sales revenue of these products accounts for over 15% of the total annual sales revenue.

VIII. Preferential tax policies for (1) enterprises with foreign investment recognized as high or new technology enterprises established in the State high or new technology industrial development zones, and for (2) advanced technology enterprises invested in and operated by foreign businesses.

Legislation:

Rules for the Implementation of the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises (see Exhibit-29)

Benefits:

- (1) Reduced income tax rate of 15%, and income tax exemption for the first two years since profit-making.
- (2) Extension of an income tax rate reduced by half for an additional three years after the expiration of tax exemption and reduction.

IX. Preferential tax policies for enterprises recognized as high or new technology enterprises established in the State high or new technology industrial development zones.

Legislation:

Circular on Several Preferential Corporate Income Tax Policies (Caishuizi No.1 of 1994) (see Exhibit-6)

Benefits:

Reduced income tax rate of 15%, and income tax exemption for the first two years of production.

X. Preferential tax policies for enterprises with foreign investment established in special economic zones (excluding Shanghai Pudong area).

Legislation:

Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises (see Exhibit-7); Rules for the Implementation of the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises (see Exhibit-29)

Benefits:

- (1) Reduced income tax rate of 15% for FIEs established in Shenzhen, Zhuhai, Shantou, Xiamen and Hainan special economic zones.
- (2) Reduced income tax rate of 24% for FIEs established in the old urban districts of cities where the above special economic zones are located.
- (3) Reduced income tax rate of 15% for FIEs defined under (2) that are engaged in (a) technology-intensive or knowledge-intensive projects, (b) projects with foreign investments of over USD \$30 million which have long periods for return on investment, and (c) energy resource, transportation and port construction projects.

XI. Preferential tax policies for enterprises with foreign investment established in the coastal economic open areas and in the economic and technological development zones.

Legislation:

Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises (see Exhibit-7); Rules for the Implementation of the Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises (see Exhibit-29)

Benefits:

- (1) Reduced income tax rate of 15% for production-oriented FIEs established in the economic and technological development zones.
- (2) Reduced income tax rate of 24% for production-oriented FIEs established in the coastal economic open areas and in the old urban districts of cities where the economic and technological development zones are located.
- (3) Reduced income tax rate of 15% for FIEs defined under (2) that are engaged in (a) technology-intensive or knowledge-intensive projects, (b) projects with foreign investments of over USD \$30 million which have long periods for return on investment, and (c) energy resource, transportation and port construction projects.

XIII. Preferential tax policies for enterprises with foreign investment established in the Three Gorges of Yangtze River Economic Zone.

Legislation:

Circular on the Tax Policy for Relocation of Residents in the Three Gorges Area and Regional

Development (Caishuizi No.034 of 1995) (*see* Exhibit-32)

Benefits:

- (1) Reduced income tax rate of 24% for production-oriented FIEs established in the Three Gorges Economic Zone.
- (2) Reduced income tax rate of 15% for the above FIEs engaged in energy resources, transportation, harbor and wharf projects or other projects encouraged by the State.
- (3) Reduced income tax rate of 24% for FIEs established in the old urban districts of the open cities along the Yangtze River.
- (4) Reduced income tax rate of 15% for FIEs defined under (3) that are engaged in (a) technology-intensive or knowledge-intensive projects, (b) projects with foreign investments of over USD \$30 million which have long periods for return on investment, and (c) energy resource, transportation and port construction projects.

XIV. Preferential tax policies in the western regions.

Legislation:

Circular on Several Policies on the Development of Western Region (Guofa No.33 of 2000) (*see* Exhibit-33); *Circular on the Implementation of New Policies for the Development of Western Region* (Guobanfa No.73 of 2001) (*see* Exhibit-34); *Circular on Preferential Tax Treatment for Western Regions Development Program* (Caishui No.202 of 2001) (*see* Exhibit-35); *Circular on Extending 15% Preferential Income Tax Rate for Three Years to Foreign Invested Companies in Central and Western Regions* (Guoshuifa No.172 of 1999) (*see* Exhibit-36)

Benefits:

- (1) Reduced income tax rate of 15% for domestic and foreign-invested enterprises established in the western regions which are engaged in industries encouraged by the State from 2001 to 2010. For domestic enterprises, industries encouraged by the State refer to those listed in the "Catalogue of the Industries, Products and Technologies Particularly Encouraged by the States." For these enterprises, the items included in the Catalogue must be its major business and must account for over 70% of total revenue. For FIEs, industries encouraged by the State refer to those listed as encouraged in the "Catalogue for the Guidance of the Foreign Investment Industries" and listed in the "Catalogue for the Guidance of the Advantageous Industries in Central and Western Regions for Foreign Investment." For these enterprises, the items listed in the two Catalogues must be its major business and must account for over 70% of total revenue.
- (2) Tariff and import VAT exemption for equipment imported by domestic and foreign-invested enterprises, as defined in (1), for self use that is within the total amount of the investment, excluding such equipment listed in the "Catalogue for the Imported Products Not Subject to Tax Exemption in Foreign Investment Projects" and the "Catalogue for the Imported Products Not Subject to Tax Exemption in Domestic Investment Projects."
- (3) Since 2000, reduced income tax rate of 15% for an additional three years following the expiration of the two years of tax exemption and three years of 50% tax reduction for FIEs established in 19 provinces, autonomous regions and municipalities in central and western regions which are engaged in industries encouraged by the State as listed in the "Catalogue for the Guidance of Foreign Investment Industries" as well as in the advantageous industries and projects approved by the State Council.

XXVI. Preferential tax policies for the research and development of enterprises.

Legislation:

Circular on Expanding the Application of Tax Deduction for Technology Development Expenditure by Enterprises (Caishui No.244 of 2003) (see Exhibit-9)

Benefits:

Domestic industrial enterprises, regardless of ownership, may deduct from their taxable income 150% of the actual expenses incurred on research and development of new products, new technologies and new crafts, provided such expenses have increased 10% or more from the previous year.

XXVII. Preferential tax policies for the research and development of foreign-invested enterprises.

Legislation:

Circular on Granting Income Tax Deduction to Foreign-invested Enterprises for Technology Development Expenditure (Guoshuifa No.173 of 1999) (see Exhibit-37)

Benefits:

Foreign-invested enterprises may deduct from their taxable income 150% of the actual expenses incurred on research and development conducted in China, provided such expenses have increased 10% or more from the previous year.

XXVIII. Preferential tax policies for enterprises transferring technology.

Legislation: *Circular on Several Preferential Corporate Income Tax Policies* (Caishuizi No.1 of 1994) (see Exhibit-6)

Benefits:

Income tax exemption for enterprises profiting from technology transfers as well as from technology consultation, technology services and technology training provided as part of the transfer, where the annual net income is less than RMB 300,000; net income above RMB 300,000 is subject to the regular tax rate.

XXXI. Funds for supporting technological innovation for the technological small and medium-sized enterprises.

Legislation:

Circular on the Interim Administrative Rules of the Technological Innovation Fund for the Technological Small- and Medium-Sized Enterprises (Guobanfa No.47 of 1999) (see Exhibit-38)

Benefits:

Science- and technology-oriented SMEs are eligible to receive two types of support – grants and loan interest discounts. Support is provided in two stages. Initially, SMEs receive 70% of the grant and 80% of the interest discount. The remaining portions of the grant and interest discount are paid after the project is completed, checked, and accepted. Each project can receive no more than RMB 1 million and, in particular cases, no more than RMB 2 million.

The total and annual amount budgeted for the subsidy: in million RMB

2001	2002	2003	2004	Total
800	500	500	500	2300

LVII. Preferential tax policies for integrated circuit industry.

Legislation:

Certain Tax Policies Promoting the Development of the Software and Integrated Circuits Industry (Caishui No.25 of 2000) (see Exhibit-39); *Circular on Tax Policies Further Promoting the Development of the Software and Integrated Circuits Industry* (Caishui No.70 of 2002) (see Exhibit-16); *Circular on Tax Policies on Raw Materials Imported by Integrated Circuits Manufacturers for Self-use* (Caishui No.136 of 2002) (see Exhibit-40); *Circular on Tax Policy on Imports of Domestically Designed Integrated Circuits Products Produced Overseas* (Caishui No.140 of 2002) (see Exhibit-41); *Circular on Termination of VAT Rebate for Integrated Circuits* (Caishui No.174 of 2004) (see Exhibit-42); *Circular on Strictly Enforcing Individual Income Tax Deduction and Exemption Standards* (Caishui No.40 of 2004) (see Exhibit-43)

Benefits:

- (1) Refund of 40% of the income tax paid on reinvestment by IC enterprises by increasing the registered capital of the existing enterprises or establishing other IC enterprises, provided these enterprises will operate for a period of not less than five years.
- (2) Refund of 80% of the income tax paid on reinvestment by domestic or foreign economic organizations from shares of profits obtained inside China into IC enterprises located in the western regions, provided these enterprises will operate for a period of not less than five years.
- (3) IC enterprises investing more than RMB 8 billion or producing ICs with a width less than 0.25 um enjoy the same preferential tax treatment that applies to foreign investors engaged in the energy and transportation sectors.
- (4) IC enterprises producing ICs with a width of 0.8 micron or less enjoy two years of income tax exemption followed by three years of 50% reduction from the first profit-making year.
- (5) Refund of VAT portion over 6% for enterprises selling independently-designed IC products from June 2000 to the end of 2001; refund of VAT portion over 3% for such enterprises starting from 2002. This policy ceased on April 1, 2005.
- (6) Refund of import VAT portion over 6% for domestically-designed ICs with self-owned intellectual property rights when processed overseas from July 1, 2000 to October 1, 2004.
- (7) Tariff and import VAT exemption for raw materials for self-production and consumption goods imported by IC enterprises investing more than RMB 8 billion or producing ICs with a width less than 0.25 um.
- (8) Tariff and import VAT exemption for IC technologies and whole sets of production equipment, as well as separately imported special equipment and apparatus to produce ICs, imported by IC companies.

LVIII. Preferential tax policies for foreign-invested enterprises and foreign enterprises which have establishments or place in China and are engaged in production or business operations purchasing domestically-produced equipment.

Legislation:

Circular Concerning the Issue of Tax Credit for Business Income Tax for Homemade Equipment Purchased by Enterprises with Foreign Investment and Foreign Enterprises (Caishui No.49 of 2000) (see Exhibit-45); *Circular on Printing and Distributing the Measures Concerning Business Income Tax Credit on the Investment of Enterprises with Foreign Investment and Foreign Enterprises by Way of Purchasing Homemade Equipment* (Guoshuifa No.90 of 2000) (see Exhibit-46)

Benefits:

40% of the expenses incurred to purchase domestically-produced equipment that is within the total investment of the project, or beyond the total investment of the project but for the purpose of upgrading existing equipment, may be deducted from the increment in income tax in the year the equipment is purchased compared to the previous year. The deductible amount in a given year should not exceed the increment in income tax. If the deductible amount exceeds the income tax increment, the amount in excess may be deducted from the next year's increment in income tax. Such postponement of deductibility shall not last more than five years.

LIX. Preferential tax policies for domestic enterprises purchasing domestically-produced equipment for technology upgrading purpose.

Legislation:

Circular on Distribution of Interim Measures Concerning Reduction and Exemption of Enterprise Income Tax for Investment in Domestically Made Equipment for Technological Renovation (Caishui No.290 of 1999) (see Exhibit-47)

Benefits:

For technology renovation projects consistent with national industrial policies, 40% of the expenses incurred to purchase domestically-produced equipment required in the projects may be deducted from the increment in income tax in the year the equipment is purchased compared to the previous year. The deductible amount in a given year should not exceed the increment in income tax. If the deductible amount exceeds the income tax increment, the amount in excess may be deducted from the next year's increment in income tax. Such postponement of deductibility shall not last more than five years.

LX. Exemption of tariff and import VAT for imported technologies and equipment.

Legislation:

Circular of the State Council Concerning the Adjustment in the Taxation Policy of Imported Equipment (GuoFa [1997] No.37) (see Exhibit-48)

Benefits:

Tariff and import VAT exemption for equipment purchased for self-use that is within the total investment of the project, excluding such equipment listed in the "Catalogue for the Imported Products Not Subject to Tax Exemption in Foreign Investment Projects" and the "Catalogue for the Imported Products Not Subject to Tax Exemption in Domestic Investment Projects."

IV. CONCERNS OF WTO MEMBERS ON CHINA'S SUBSIDIES TO THE HIGH-TECH INDUSTRY

China's subsidies practice has been one of the priority issues for China's trading partners. At the WTO, Members have been employing various platforms to voice their concerns, including the annual transitional review mechanism (TRM), submission of requests for information prior to China's subsidies notification, submission of follow-up questions in response to China's subsidies notification, and dispute settlement consultations. In these platforms, WTO Members have identified substantial subsidies relevant to the high-tech industry, many of which were not included in China's subsidies notification.

A. Subsidies Raised at the Transitional Review of China's WTO Compliance

In the context of the annual transitional review of China's implementation of its WTO commitments by the Committee on Subsidies and Countervailing Measures (2002-2006), several Members, such as the United States, the EU, and Japan, identified a wide range of subsidies granted at the central and local level that they believed conflict with China's commitments not to provide subsidies contingent upon export performance or the use of domestic over imported goods, as well as other disciplines of the SCM Agreement. So as to ensure China's compliance, they also sought clarification on many programs about which they had learned certain information. Concerns/questions raised by Members in their written submissions include subsidies specific to the high-tech industry as well as cross-industry subsidies applicable to the high-tech industry, as summarized below.

1. Subsidies Specific to the High-Tech Industry

1. An MII program for the integrated circuit industry reported by the Chinese press that includes 40% VAT rebate contingent upon export performance, reduction in VAT charged to producers, preferential treatment in the purchase of raw materials and other types of financial support from the central government.⁶⁰ --- *U.S., 2002 TRM; WTO consistency is questioned*
2. A program reported by the Chinese press that provides subsidized government support for the export of various high-tech products in the electronics, bio-medicine, and new materials sectors.⁶¹ --- *U.S., 2002 TRM; WTO consistency is questioned*
3. Changes announced by NDRC on September 21, 2004 to the 2000 IC and software support policies – full VAT rebates on semiconductor exports, support in R&D and training.⁶² --- *U.S. and Japan, 2004 TRM*
4. A plan of Wuhan city reported by *International Herald Tribune* (May 2006) to spend \$1.5-\$3.0 billion to build a semiconductor plant that will make 12-inch wafers; the Semiconductor Manufacturing International Corp. will design, build and manage the plant.⁶³ --- *U.S., 2006 TRM*
5. A new NDRC aid policy reported by *China Daily* (July 2006) for semiconductors – income tax deductions and exemptions; research loans and using research expenditures to offset taxes (in addition to the RMB 500 million fund previously established to help semiconductor companies' research); tax reductions on imported equipment and a special fund for IC design.⁶⁴ --- *U.S., 2006 TRM*

2. Cross-industry Subsidies Applicable to the High-Tech Industry: Export-related

1. As reported from the website of Shanghai Foreign Investment Center, export-oriented enterprises enjoy various preferential policies in the use of land, water, electricity, transportation, telecommunication, short-term funds and necessary loans, as well as local income tax exemption after expiration of normal income tax exemption if more than 70% of the production is exported.⁶⁵ --- *EU, 2003 TRM; WTO consistency is questioned*
2. Income tax reduction by one half enjoyed by export-oriented foreign-invested companies if they export 70% of their production after expiration of normal income tax exemption and reduction; additional reduction for export-oriented companies located in special economic zones and economic

⁶⁰ *Subsidies – Questions Posed by the United States to the People's Republic of China*, G/SCM/Q2/CHN/2 (18 October 2002).

⁶¹ *Id.*

⁶² *Questions from the United States to China Concerning Subsidies and Price Controls*, G/SCM/Q2/CHN/8 (6 October 2004); *Request from Japan to China Pursuant to Article 25.8 of the Agreement on Subsidies and Countervailing Measures*, G/SCM/Q2/CHN/10 (15 October 2004).

⁶³ *Questions from the United States to China*, G/SCM/Q2/CHN/23 (16 October 2006).

⁶⁴ *Id.*

⁶⁵ *Questions Posed by the European Communities to the People's Republic of China*, G/SCM/Q2/CHN/5 (2 October 2003).

and technological development zones and other companies subject to the 15% tax rate that qualify under the above conditions. ⁶⁶ --- <i>Mexico, 2002 TRM; EU, 2005 TRM; WTO consistency is questioned</i>
3. As reported by www.tdctrade.com and <i>China Daily</i> , the Shenzhen WTO affairs office sponsors a fund of more than 10 million yuan in order to reimburse up to 30% of legal fees incurred by local export companies facing anti-dumping lawsuits. ⁶⁷ --- <i>EU, 2004, 2005 and 2006 TRM; WTO consistency is questioned</i>
4. As reported by www.tdctrade.com, the Guangdong provincial government supports private enterprises to “expand outward,” and eligible private enterprises may apply for special funds conceived for developing foreign trade activities. These funds include market exploration, export credit insurance, offshore processing trade project loan interest subsidy, export research and development fund, antidumping proceedings fund, export rebate account loan interest subsidy fund and outward-looking enterprises development fund. ⁶⁸ --- <i>EU, 2004, 2005 and 2006 TRM; WTO consistency is questioned</i>
5. As reported by www.tdctrade.com, the Export Interest Subsidy for Shenzhen Enterprises has been raised from 20% to 40%. The policy of subsidizing USD \$0.03 for every USD \$1 export of general merchandise is only applicable to merchandise procured in Shenzhen. SMEs with exports below USD \$15 million are eligible to apply. Fund allocation is on a first-come-first-serve basis. The fund would provide RMB 800 million in 2004. ⁶⁹ --- <i>EU, 2004, 2005 and 2006 TRM; WTO consistency is questioned</i>
6. As reported from Zhejiang province, an Export Subsidy Fund based on a federal program enables regional authorities to provide all exporting companies exporting more than USD \$3 million with a subsidy of 0.01 RMB per each USD \$ exceeding this threshold. ⁷⁰ --- <i>EU, 2004, 2005 and 2006 TRM; WTO consistency is questioned</i>
7. As reported by MOFCOM, Dalian Branch of the Export-Import Bank would provide RMB 5 billion of export credits to companies to enter global markets, and, since November 2003, “low-cost credit provided by the bank has saved the enterprises RMB 150 million interest.” ⁷¹ --- <i>U.S., 2005 TRM</i>
8. Low-interest loans offered by China Exim Bank to finance manufacturing projects that are able to

⁶⁶ *Subsidies – Questions Posed by Mexico to the People’s Republic of China under its Protocol of Accession and Article 25.8 of the SCM Agreement*, G/SCM/Q2/CHN/4 (4 November 2002); *Questions from the European Communities to China with regards to China’s Transitional Review Mechanism on Subsidy Practices*, G/SCM/Q2/CHN/12 (22 September 2005).

⁶⁷ *Questions from the European Communities to China with regards to China’s Transitional Review Mechanism on Subsidy Practices*, G/SCM/Q2/CHN/7 (23 September 2004); *Questions from the European Communities to China with regards to China’s Transitional Review Mechanism on Subsidy Practices*, G/SCM/Q2/CHN/12 (22 September 2005); *Questions from the European Communities to China with regards to China’s Transitional Review Mechanism on Subsidy Practices*, G/SCM/Q2/CHN/24 (20 October 2006).

⁶⁸ Id.

⁶⁹ Id.

⁷⁰ Id.

⁷¹ *Questions from the United States to China Concerning Subsidies and Price Controls*, G/SCM/Q2/CHN/14 (29 September 2005).

generate favorable economic returns with secured repayment capacity, that are tied to Chinese exports of mechanical and electronics products and complete sets of equipment, and that may be considered as official development assistance; companies implementing these projects should be medium-sized and large SOEs.⁷² --- U.S., 2006 TRM; **WTO consistency is questioned**

9. Preferential loans offered by China Exim Bank to selected SOEs in certain selected sectors, including construction, electronics, mechanical, high and new technology products/capital goods, and telecommunications and power equipment to support their international strategies – these preferences include preferential interest rates, longer than standard repayment terms, and waiver of certain fees.⁷³ --- U.S., 2006 TRM; **WTO consistency is questioned**

10. Export credits offered by China Development Bank to support sectors considered to be essential to China's long-term competitiveness and specifically for companies engaging in R&D, Chinese brand name companies and certain companies in overseas expansion.⁷⁴ --- U.S., 2006 TRM; **WTO consistency is questioned**

3. Cross-industry Subsidies Applicable to the High-Tech Industry: SOEs and Regional Development

1. Whether subsidies to state-owned enterprises operating at a loss have been ended and what decrees or government documents ended them.⁷⁵ --- U.S., 2002, 2003, 2004 and 2005 TRM; **WTO consistency is questioned**

2. Continued use of state-owned banks to keep non-viable SOEs afloat by writing off non-performing loans of SOEs as part of the Northeast revitalization program; one example is that Heilongjiang Province agreed to write off RMB 36 billion worth of non-performing loans of SOEs.⁷⁶ --- U.S. 2004 TRM; **WTO consistency is questioned**

3. Direct government intervention in manufacturing sectors in Northeast China – China's State Property Commission reported China was carrying out "strategic restructuring and technical transformation of key enterprises in the areas of oil, petrochemical, iron and steel, automotive, shipbuilding and aircraft products manufacturing sectors in Northeast China in a bid to establish production bases of advantage industries."⁷⁷ --- U.S., 2005 TRM

⁷² *Questions from the United States to China*, G/SCM/Q2/CHN/23 (16 October 2006).

⁷³ *Id.*

⁷⁴ *Id.*

⁷⁵ *Subsidies – Questions Posed by the United States to the People's Republic of China*, G/SCM/Q2/CHN/2 (18 October 2002); *Subsidies – Questions Posed by the United States to the People's Republic of China*, G/SCM/Q2/CHN/6 (27 October 2003); *Questions from the United States to China Concerning Subsidies and Price Controls*, G/SCM/Q2/CHN/8 (6 October 2004); *Questions from the United States to China Concerning Subsidies and Price Controls*, G/SCM/Q2/CHN/14 (29 September 2005).

⁷⁶ *Questions from the United States to China Concerning Subsidies and Price Controls*, G/SCM/Q2/CHN/8 (6 October 2004).

⁷⁷ *Questions from the United States to China Concerning Subsidies and Price Controls*, G/SCM/Q2/CHN/14 (29

At the SCM Committee's annual transitional reviews over the past five years, China addressed orally concerns/questions raised in Members' written submissions. Members often expressed disappointment that some questions were left unanswered and that some responses provided by China were limited and unsatisfactory.⁷⁸

On the concerns related to subsidized government support for high-tech exports raised by the United States in 2002, China said it encouraged high-tech exports as a general policy but that no specific measure had been applied up to October 2002.⁷⁹ With regard to the MII program on the IC industry, also raised by the United States in 2002, China held the opinion that the preferential tax policies were not based upon export performance and were adopted for a product or an industry regardless of the ownership of companies.⁸⁰ On the reported changes to the aid policy for the IC industry, raised in later TRMs by the United States and Japan, China said that new policies were still under consideration and would be in accordance with WTO rules and the common practice of other countries.⁸¹ On the U.S. question regarding Wuhan city's plan to build a semiconductor plant, China noted its failure to gather detailed information due to time constraints, but believed there was no subsidy involved in this project according to preliminary information.⁸²

September 2005).

⁷⁸ See, e.g., *Chairman's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/115 (22 November 2004), at paras 60-61.

⁷⁹ *Chairman's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/M/49 (18 November 2002).

⁸⁰ Id.

⁸¹ *Chairman's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/115 (22 November 2004); *Chairman's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/119 (16 November 2006).

⁸² *Chairman's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/119 (16 November 2006).

In response to questions from Mexico and EU on the income tax reduction enjoyed by export-oriented foreign-invested enterprises, China noted that consistency of some provisions with the SCM Agreement was currently being reviewed and were also being examined in the context of China's tax reform under preparation.⁸³ According to China, a major step to be taken in the reform is to unify the income tax system for domestic enterprises and enterprises with foreign investment, following the principles of fair competition and national treatment.⁸⁴

With respect to several export subsidy programs raised by the EU based on information from certain Chinese websites, China initially held the view that it had no obligation to verify information on non-official websites and that such information should not be used as a basis to make accusations against China's policies.⁸⁵ The EU found the answer disappointing and brought up the same questions in later TRMs. China only responded to one question related to the special funds provided by the Guangdong provincial government to support private enterprises in foreign trade activities, claiming that the program, which was aimed at promoting the participation of SMEs in the international market, did not constitute an export subsidy.⁸⁶

On the U.S. concern regarding subsidies provided to SOEs running at a loss, a concern raised at several TRMs, China insisted that such subsidies had already been eliminated since 2001, regardless of a 2003 press report noted by the United States that indicated China was still working

⁸³ *Chairperson's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/118 (9 November 2005); *Chairperson's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/111 (18 November 2003).

⁸⁴ *Chairperson's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/118 (9 November 2005).

⁸⁵ *Chairman's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/115 (22 November 2004).

⁸⁶ *Chairman's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/119 (16 November 2006).

to eliminate the subsidies.⁸⁷ With regard to the U.S. concern on the continued use of state-owned banks to keep non-viable SOEs afloat, citing the example that Heilongjiang Province agreed to write off RMB 36 billion worth of non-performing loans to SOEs, China pointed out that the non-performing loans involved in the Heilongjiang example were only RMB 18 billion. China also noted that to restructure non-performing loans, creditor banks and debtor enterprises had negotiated a resolution themselves; creditor banks followed commercial principles and the government would neither assume the losses nor provide subsidies to the creditor banks.⁸⁸ With regard to the direct government intervention of the State Property Commission raised by the United States, China stated that the policy on the strategic restructuring and technical transformation of key enterprises was just a guideline focusing on the reform and reconstruction and was not mandatory.⁸⁹

With regard to several U.S. questions related to export credit provided by state-owned banks to certain companies and sectors on preferential terms, China stated that the export credit business of the China Export and Import Bank was consistent with the provisions of the SCM Agreement, and the export credit adopted by the China Development Bank was a market-oriented business.⁹⁰

⁸⁷ *Chairperson's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/111 (18 November 2003).

⁸⁸ *Chairman's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/115 (22 November 2004).

⁸⁹ *Chairperson's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/118 (9 November 2005).

⁹⁰ *Chairman's Report to the Council for Trade in Goods on Transitional Review of China*, G/SCM/119 (16 November 2006).

B. Subsidies Raised in the Request for Information Prior to China's Subsidies Notification

Prior to China's first subsidies notification, China's failure to fulfill this obligation in a timely manner had been a chronic complaint of China's trading partners. Given China's lack of transparency in reporting its subsidies, on October 5, 2004, pursuant to Article 25.8 of the SCM Agreement, the United States submitted a written request⁹¹ to China for information on the nature and extent of certain subsidies granted or maintained by China. In the submission, the United States identified an array of subsidies contingent upon export performance and the use of domestic over imported goods as well as other types of subsidies across industries. From the U.S. submission, the following are subsidies applicable or specific to the high-tech industry.

1. Subsidies Contingent upon Export Performance Prohibited under Art. 3.1(a) of the SCM Agreement

1) Honorable Enterprises

Article 3 of the *Detailed Rules for Reward and Punishment for the Trial Implementation Measures for Appraising Foreign Exchange Receipts for Exports*, describes the criteria that an enterprise must meet to be considered an "honorable enterprise for foreign exchange receipts." One criterion is an annual export volume of over USD \$200 million. Articles 5 and 6 of this measure describe benefits that honorable enterprises enjoy, including preferential access to foreign trade funds. Commercial bank lending rates for honorable enterprises can also be lowered up to 10% based on the lending rates fixed by the People's Bank of China.

2) Export-Contingent Tax Reduction for FIEs in Special Zones

Foreign-invested enterprises (FIEs) located within Special Economic Zones, Economic Technological Development Zones, Open Coastal Economic Zones and Old Urban Areas that export at least 70% of their production are assessed the lowest rate of the national income tax, *i.e.*, 10%. FIEs which do not meet the 70% export requirement are taxed at rates of 12%, 15% or 24%. The relevant measure is the *Detailed Implementation Rules of the Income Tax Law of China of Foreign Investment Enterprises and Foreign Enterprises* (issued on June 30, 1991).

3) Income Tax Refund for Foreign Investors Investing in Export-Oriented Businesses

Foreign investors in FIEs that reinvest their profits in export-oriented businesses for at least five

⁹¹ Request from the United States to China Pursuant to Article 25.8 of the Agreement on Subsidies and Countervailing Measures, G/SCM/Q2/CHN/9 (6 October 2004).

consecutive years qualify for a 100% refund of the income tax paid on the amount of reinvestment. On the other hand, foreign investors that reinvest in non-export-oriented businesses in China for at least five years qualify for only a 40% refund of income tax paid on the amount of reinvestment. This program is described in the *Detailed Implementation Rules of the Income Tax Law of China of Foreign Investment Enterprises and Foreign Enterprises*.

4) Export Subsidies for High-Technology Products

MOFCOM, MOST and MII administer a program designed to increase exports of high-tech products and offer subsidies to export-oriented firms in the electronics, bio-medical, new materials and other high-technology sectors.

5) Customs Duty and VAT Refund on Imported Capital Equipment Used for Production of Products for Export

Enterprises that import capital equipment used exclusively to produce export products are eligible to receive a full refund of customs duties and VAT on the imported capital equipment. Enterprises receive 20% of the tax refund each year the equipment is used exclusively for export production, resulting in a full tax refund at the end of a five-year period. Enterprises that wish to receive this tax refund are investigated every year for five consecutive years to verify that the equipment is used only for export.

6) Guangdong Grants Provided for Export Performance

The Guangdong provincial government has introduced a program to provide RMB 25 million in grants over five years to export-oriented companies meeting specific export targets.

**2. Subsidies Contingent upon the Use of Domestic over Imported Goods
Prohibited under Art. 3.1(b) of the SCM Agreement**

1) VAT Rebate on Purchases of Domestic Equipment by Foreign-invested Companies

Pursuant to the *Notice of the Trial-Implementation Measures for the Administration of Tax Refund on Domestic Equipment Purchased by Enterprises with Foreign Investment* (issued on August 20, 1999), a full VAT rebate is provided to manufacturers that purchase domestically-made machinery and equipment through the end of 2010.

2) Enterprise Income Tax Reduction for Purchase of Domestically-Made Machinery and Equipment by Foreign-invested Companies

According to paragraph 1 of the *Notice Concerning Some Issues on the Deduction of the Investment Made by Enterprises with Foreign Investment and Foreign Enterprises in Purchasing Domestic Equipment from Enterprise Income Tax* (issued on 14 January 2000), 40% of the cost of purchasing domestic equipment in a given year may be deducted from the increment of enterprise income tax in the year the equipment is purchased compared to the previous year

3. Other Programs That Provide Subsidies as Defined in Art.1 of the SCM Agreement and Are Specific Within the Meaning of Art.2 of the SCM Agreement

1) Assumption of Interest on Loans for Technology Upgrades

Chinese government pays interest expenses on bank loans for the technology upgrades of state-owned enterprises. Recipients include the textile, petrochemical and paper industries, but may include other industries as well.

2) Chengdu Assistance to the Semiconductor Industry

The Semiconductor Manufacturing International Corporation and the city government of Chengdu signed an agreement on July 16, 2004 to invest USD \$175 million in building a chip assembly and testing plant. The Chengdu city government is the majority shareholder in this project, and is slated to purchase the land if the investment reaches a certain amount and will subsidize the investor's bank loan for fixed assets.

Article 25.9 of the SCM Agreement provides that members receiving requests shall “provide such information as quickly as possible and in a comprehensive manner.” So far, China has not responded in writing to the U.S. request. The United States noted that, while some of the programs identified in the request were included in China’s subsidies notification, many of them were not.⁹²

C. Subsidies Raised in the Submissions of Follow-Up Questions in Response to China’s Subsidies Notification

Following China’s subsidies notification in April 2006, concerns have been raised among WTO Members that there are a large number of subsidy programs being used which have not been properly notified. For example, China did not notify subsidies provided at the provincial and local government levels nor subsidies provided through state-owned banks. The United States, the EU, Japan, Canada, Australia, Mexico and Turkey have filed submissions in response to China’s notification, seeking further information on the notified subsidies, and raising additional subsidy

⁹² *Questions from the United States Regarding the New and Full Notification of China*, G/SCM/Q2/CHN/19 (26 July 2006).

programs omitted in China's notification, including many that appear to be prohibited under WTO rules. Additional subsidy programs that are specific and applicable to the high-tech industry include the following.⁹³

1. Subsidies Specific to the High-Tech Industry	
1. Export Contingent Support to the Software and IC Industries	Article 12 of the <i>Policies For Encouraging the Development of Software and Integrated Circuit Industries</i> (issued on July 14, 2000), provides credits at favorable interest rates to exports of software will be incorporated into the import and export banking business in China. --- U.S.; WTO consistency is questioned
2. Provisional Measures for the Administration of the Specific Project Funds for R&D of the IC Industry	According to the Provisional Measures for the Administration of the Specific Project Funds for Research and Development of the Integrated Circuits Industry (issued on March 23, 2005), Chinese firms in the integrated circuit industry may receive grants equal to 50% of their research and development expenditures. --- U.S.
3. Hynix Large Scale Integrated Circuit Project in Wuxi, China	Information available to the United States indicates that Hynix, the Korean semiconductor manufacturer, received approval in 2004 to build a semiconductor manufacturing plant in the Wuxi Export Processing Zone in Jiangsu Province, China. Chinese banks will finance USD \$1 billion or half of the investment through debt and long-term leasehold. --- U.S.
4. "Five-Plus-Five" Income Tax Incentive for Integrated Circuit Companies in Certain Locations	Information available to the United States indicates that integrated circuit manufacturing companies located in Hainan Island, Shanghai Pudong New District and Western China, with operational terms not less than fifteen years, are eligible for a full income tax exemption for their first five years of operation, followed by a 50% income tax reduction for the next five years. The exemptions and reductions begin in the company's first profitable year. --- U.S.
5. Beijing Economic Technological Investment Development Corp.	Information available to the United States indicates that the government-owned Beijing Economic Technological Investment Development Corp. has provided an estimated USD \$3 million interest-free, dollar-denominated, short-term loan to Semiconductor Manufacturing International Corporation (SMIC), a Chinese semiconductor manufacturer. --- U.S.

⁹³ For subsidies raised by the United States, see *Questions from the United States Regarding the New and Full Notification of China*, G/SCM/Q2/CHN/19 (26 July 2006); for subsidies raised by the EU, see *Subsidies – Questions from the European Communities Regarding the New and Full Notification of China*, G/SCM/Q2/CHN/16 (25 July 2006); for subsidies raised by Canada, see *Subsidies – Questions from Canada Regarding the New and Full Notification of China*, G/SCM/Q2/CHN/18 (26 July 2006).

6. Opinions Concerning Promoting Export of Pharmaceutical Products

Information available to the United States indicates that this program, announced in early December 2005 by the Ministry of Commerce and seven others ministries, provides the following benefits: assistance in establishing international pharmaceutical export bases, creating famous export brands that hold certain market share in the international market, encouraging risk funds to invest in pharmaceutical R&D, and promoting intellectual property rights protection. --- U.S.; *WTO consistency is questioned*

7. Wuxi Aid to Exporters

Information available to the United States indicates that under this program the Wuxi government will provide grants up to RMB 100,000 to high-tech companies with an export value of over USD \$5 million. --- U.S.; *WTO consistency is questioned*

8. Provisional Measures for the Administration of State High Technology Development Projects

Information available to the United States indicates that under the *Provisional Measures for the Administration of State High Technology Development Projects* (issued on March 2, 2006) investment and interest loan subsidies will be provided to high-tech industries in the form of grants. --- U.S.

2. Cross-Industry Subsidies Applicable to the High-Tech Industry

1. Export Contingent Support for Famous Name Brand Products*

On January 26, 2005, MOFCOM identified 190 Chinese famous brands in six industrial fields eligible for export promotion for years 2005-2006. In order to increase Chinese name brand exports and limit its reliance on foreign name brand exports, the Chinese Government is offering the following incentives:

- An Export Brands Development Fund to develop and promote designated exports.
- Preferential funding for research and development products.
- Support for technology to strengthen the competitiveness of famous brand exports.
- Special assistance for domestic brand name enterprises to establish state-level R&D centers.
- Simplified loan application procedures and easy access to export credit insurance.

Similar or implementing programs offered at the central or sub-central government levels include:

- According to a circular issued on March 24, 2005 by the State Administration for Quality Supervision, Inspection and Quarantine (AQSIQ), AQSIQ requested that local bureaus provide benefits to firms that apply for designation as a Chinese-made world famous brand such as "honorific titles," financial support and export credit guarantees. Designated firms must be the top producer and exporter within their industry, export to multiple foreign markets and have annual exports of over USD \$50 million.
- Information available to the United States indicates that in early December 2005, MOFCOM announced a program called "Six Initiatives to Promote Domestic Name Brand Exports." Some aspects of the initiatives include: choosing specific domestic name brands to support; creating policies to support those firms; helping those firms expand abroad; and working with the Ministry of Finance to appropriate RMB 700 million to support these firms' research and

development activities.

- A program was announced on February 3, 2005 by the Jiangsu Province Famous Brand Strategy Promotion Committee which selected 515 products as “Jiangsu Province Famous Brand Products.”
- The Wuxi government allows enterprises obtaining the “Famous Export Brands to be Nurtured and Supported” to receive incentives from Wuxi city.
- The government of Shishi County in Fujian province announced an initiative including a one-time prize to any Shishi company accorded the central government’s “famous export brand” designation.

--- U.S.; *WTO consistency is questioned*

2. Certain local export-related awards

Information available to the United States indicates that various Chinese government entities at the sub-central levels provide awards and direct payments for exports by a wide-range of industries. There are regional programs that tie monetary awards solely to the amount exported or to a percentage growth above the previous year’s export totals. Examples include:

- (a) *Awards Tied to Amount Exported or Export Growth.* The Xiamen City government awards a one-time monetary award to all companies with Chinese brand name exports over USD \$100 million as well as year-on-year percentage growth of at least 5%.
- (b) *Direct Benefits to Processing Trade Exporters.* A Changxing County government program in Zhejiang in which the province provides monetary awards to all processing trade export enterprises for trade of over USD \$3 million per year.
- (c) *Award for High Year-on-Year Export Growth.* A program in Zibo City’s Zhoucun District provides awards based on the percentage of export growth over the previous year.
- (d) *Awards to Year’s Top 10 Exporters.* A program in Yueqing City in Zhejiang Province awards the city’s top 10 exporters (exports of over USD \$10 million) prizes of RMB 100,000.
- (e) *Reward for Each Dollar Exported.* An export program detailed on the website of Lishui City in Zhejiang Province establishes a monetary award for each dollar exported.

--- U.S.; *WTO consistency is questioned*

3. Income Tax Reduction for Certain Encouraged Enterprises

According to Article 73.6 of the *Rules for the Implementation of the Income Tax Law*, an income tax reduction is available to foreign enterprises with foreign investment engaged in projects “encouraged” by the State. One “encouraged” category is “Permitted foreign-funded projects whose products are to be wholly exported directly.” --- U.S.; *WTO consistency is questioned*

4. Free Land Given as Part of Foreign Investment Projects

The Yinchuan government grants foreign investors, which meet certain investment conditions, land valued at twice the amount of an investor’s original investment. --- U.S.

5. Ningbo City Key Industry Technological Development Fund

According to the MOFCOM website, Ningbo city has set up a RMB one billion special fund to support four fast-growing key industries, namely, electronic information, new materials, auto/auto parts and machinery production industries. The purpose of the fund is to assist key industries in their technological upgrading projects, expand their sales and assist companies in applying to be considered a national famous brand. The maximum subsidy for a qualified enterprise or project is RMB five million. --- U.S.

6. Incentives to Pillar Industries in Tianjin

Information available to the United States indicates that Tianjin city plans to allocate RMB 160 billion (USD \$19.2 billion) of investment to 560 projects related to six pillar industries in 2005, including the IT industry, the chemical and metallurgical sector, the automotive industry, biotechnology and modern pharmaceutical industry, and the energy and environmental protection sector. --- *U.S.*

7. Preferential Loans Provided by the Chinese Government

According to a document posted by the Jiangsu Province Tax Bureau in September 2004 entitled "Tax Reimbursement Regime on Exported Goods in China," exported goods that are "manufactured by using preferential loans of the Chinese government" will be "given approval to reimburse or exempt VAT or consumption tax due to some special features such as . . . turnover linkages and settlement methods, etc." --- *U.S.*

8. VAT refunds on domestic equipment purchases for foreign-invested enterprises

This is provided for in Art. 4 of the *Interim Measure for the Administration of Tax Refund to Enterprises with Foreign Investment for their Domestic Equipment Purchases*. --- *EU, Canada; WTO consistency is questioned*

9. Exemption from mandatory worker benefit contribution

Foreign-invested enterprises that export more than 50% of their products, or utilize foreign advanced technology to produce products for export, are exempt from mandatory contributions that help the Chinese government pay for worker/staff benefits, according to Art. 3 of the *Provisions of the State Council on the Encouragement of Foreign Investment*. --- *EU, Canada; WTO consistency is questioned*

10. Income tax exemption on profits made by certain FIEs

Profits distributed to foreign investors by foreign-invested enterprises that export more than 50% of their products, or that utilize foreign advanced technology to produce products for export, are exempt from income tax, according to Art. 7 of the *Provisions of the State Council on the Encouragement of Foreign Investment*. --- *EU, Canada; WTO consistency is questioned*

11. Consolidated and commercial tax exemption on products exported by FIEs

Export products of enterprises with foreign investment, except crude oil, oil products and other products subject to special State provisions, shall be exempt from the consolidated and commercial tax, according to Art. 11 of the *Provisions of the State Council on the Encouragement of Foreign Investment*. --- *Canada; WTO consistency is questioned*

12. Import licensing exemption on products imported by FIEs to produce goods for export

This subsidy is provided for in Art. 13 of the *Provisions of the State Council on the Encouragement of Foreign Investment*. --- *Canada; WTO consistency is questioned*

13. Discounted lending rates for FIEs meeting certain export criteria

Foreign-invested enterprises that meet certain export criteria receive a 10% discount on lending rates from the People's Bank of China, according to Art. 6 of the *Detailed Rules on Rewarding and Punishment Concerning Provisional Regulations over Examination of Export Collections of*

Foreign Exchange. --- EU, Canada; WTO consistency is questioned

14. Repayment tax exemption on certain products generated by FIEs

By-products, substandard products and leftover industrial surplus generated by FIEs while producing goods for export, are exempt from repayment tax when sold domestically. Such products, if generated while producing goods for domestic consumption, are not exempt. This subsidy is provided for in Art. 20 of the *Measures of the Customs of China on the Control over and the Levy and Exemption of Tax for Import and Export Goods of Enterprises with Foreign Investment* [Decree 1992 No. 29 of the General Administration of Customs]. --- *EU, Canada; WTO consistency is questioned*

15. VAT expenses exemption and deduction

Based on the EU's experience in anti-dumping cases, it seems that certain levels of production are exempt from paying VAT and that traders were able to deduct VAT expenses even though their suppliers did not charge and pay VAT.--- *EU; WTO consistency is questioned*

16. The Central Foreign Trade Development Fund

Information available to Canada shows that the Central Foreign Trade Development Fund, established in 1996, is managed by the provinces under the direction of MOFCOM and that a Chinese bank, the ICBC, is responsible for managing the transactions under this Fund. The alleged purpose of the Fund is: to regulate and promote foreign trade; to encourage the development and export of new electronic, deep-processing, high-tech and high value-added products; and to increase Chinese export capacity and competitiveness. --- *Canada*

To date, China has not responded to the follow-up questions and additional subsidies raised by WTO Members.

D. The U.S. Request for Dispute Settlement Consultation with China over Prohibited Subsidies

On February 2, 2007, the United States filed a formal request at the WTO for consultation with China with regard to certain prohibited subsidies.⁹⁴ In the request, the United States identified nine measures granting refunds, reductions, or exemptions from taxes or other payments, which are designed to subsidize exports of manufactured goods and encourage the purchase of domestic over imported equipment and manufacturing inputs. According to the United States,

⁹⁴ *China – Certain Measures Granting Refunds, Reductions or Exemptions from Taxes and Other Payments – Request for Consultations by the United States*, WT/DS358/1 (7 February 2007).

these measures are inconsistent with the WTO rules, including Article 3 of the SCM Agreement which prohibits subsidies contingent upon export performance and the purchase of domestic over imported goods. The USTR noted in its news release on the WTO action that these subsidies tilt the playing field in China's favor and unfairly impact American manufacturers and workers, especially small- and medium-sized companies.⁹⁵

The subsidies at issue are not specifically designed for the high-tech industry, but are applicable across industries including high-tech. The following table is a summary of benefits offered under each of the nine measures:

1.	<u>Legislation:</u> <i>Circular of the State Administration of Taxation Concerning Transmitting the Interim Measure for the Administration of Tax Refunds to Enterprises with Foreign Investment for Their Domestic Equipment Purchases (see Exhibit-44)</i>	<u>Benefit:</u> Full VAT refund available to foreign-invested companies for the purchase of Chinese-produced equipment.
2.	<u>Legislation:</u> <i>Circular of the Ministry of Finance and the State Administration of Taxation Concerning the Issue of Tax Credit for Business Income Tax for Homemade Equipment Purchased by Enterprises with Foreign Investment and Foreign Enterprises (see Exhibit-45), read in conjunction with Circular of the State Administration of Taxation on Printing and Distributing the Measures Concerning Business Income Tax Credit on the Investment of Enterprises with Foreign Investment and Foreign Enterprises by Way of Purchasing Homemade Equipment (see Exhibit-46)</i>	<u>Benefit:</u> Income tax reduction available to foreign-invested companies for the purchase of Chinese-produced equipment. Foreign-invested companies may deduct 40% of the cost of purchasing domestically-produced equipment that is within the total investment of the project, or beyond the total investment of the project but for the purpose of upgrading the existing equipment, from the increment in income tax in the year the equipment is purchased compared to the previous year. The deductible amount in a given year should not exceed the increment in income tax. If the deductible amount exceeds the income tax increment, the amount in excess may be deducted from the next year's increment in income tax. Such postponement of deductibility shall not last more than five years.

⁹⁵ *United States Files WTO Case Against China Over Prohibited Subsidies*, USTR news release (February 2, 2007), available at http://www.ustr.gov/Document_Library/Press_Releases/2007/January/United_States_Files_WTO_Case_Against_China_Over_Prohibited_Subsidies.html.

3.	<p><u>Legislation:</u> <i>Circular on Distribution of Interim Measures Concerning Reduction and Exemption of Enterprise Income Tax for Investment in Domestically Made Equipment for Technological Renovation</i> (see Exhibit-47)</p>	<p>Benefit: Income tax reduction available to Chinese companies for the purchase of Chinese-produced equipment.</p> <p>For technology renovation projects consistent with the national industrial policies, 40% of the cost to purchase domestically-produced equipment required in the projects can be deducted from the increment in income tax in the year the equipment is purchased compared to the previous year. The deductible amount in a given year should not exceed the increment in income tax. If the deductible amount exceeds the income tax increment, the amount in excess may be deducted from the next year's increment in income tax. Such postponement of deductibility shall not last more than five years.</p>
4.	<p><u>Legislation:</u> Articles 75(7) and 75(8) of the <i>Rules for Implementation of the Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises</i> (see Exhibit-29), read in conjunction with Articles 8 and 9 of the <i>Provisions of the State Council on the Encouragement of Foreign Investment</i> (see Exhibit-49) and Articles 6 and 8 of the <i>Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises</i> (see Exhibit-7)</p>	<p>Benefit: Income tax reduction available to foreign-invested companies that satisfy certain export performance requirements.</p> <p>After the expiration of the normal reduction or exemption of income tax (<i>i.e.</i>, two-free and three-half) for production-oriented FIEs, foreign-invested exporting companies can pay income tax at one-half of the present rate, provided 70% of their products are exported. Companies located in special economic zones and economic and technological development zones and other companies subject to the 15% income tax rate that comply with the foregoing conditions, shall pay income tax at 10%. After the normal reduction or exemption of income tax (<i>i.e.</i>, two-free and three-half) expires, technologically-advanced companies may enjoy for an additional three years the rate reduced by one-half.</p>
5.	<p><u>Legislation:</u> Article 73(6) of the <i>Rules for Implementation of the Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises</i> (see Exhibit-29), read in conjunction with Articles 6 and 7 of the <i>Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises</i> (see Exhibit-7) and Section XIII of the <i>Catalogue for the Guidance of Foreign Investment</i></p>	<p>Benefit: Income tax reduction available to foreign-invested companies that satisfy certain export performance requirements.</p> <p>Foreign-invested companies engaged in industries allowed by the State that export all of their products may pay a reduced income tax of 15%.</p>

	<i>Industries (see Exhibit-50)</i>	
6.	<u>Legislation:</u> Article 81 of the <i>Rules for Implementation of the Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises</i> (see Exhibit-29), read in conjunction with Articles 6 and 10 of the <i>Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises</i> (see Exhibit-7) and Article 10 of the <i>Provisions of the State Council on the Encouragement of Foreign Investment</i> (see Exhibit-49)	<p>Benefit: Income tax refund available to foreign-invested companies that satisfy certain export performance requirements.</p> <p>Foreign investors who reinvest their profits to establish or expand exporting companies or technologically-advanced companies for a period of operation of not less than five years shall be refunded the total amount of income tax already paid on the reinvested portion.</p>
7.	<u>Legislation:</u> Article 3 of the <i>Provisions of the State Council on the Encouragement of Foreign Investment</i> (see Exhibit-49)	<p>Benefit: Exemptions from mandatory worker benefit contributions available to foreign-invested companies that satisfy certain export performance requirements.</p> <p>Foreign-invested "product export enterprises" and technologically-advanced enterprises shall be exempt from payment to the State of all subsidies to staff and workers, except for the payment or allocation of funds for labor insurance, welfare expenses and housing subsidies for Chinese staff and workers in accordance with the provisions of the State. "Product Export Enterprises" are defined as enterprises "whose products are mainly export" that also have a foreign exchange surplus.</p>
8.	<u>Legislation:</u> Articles 3 and 6 of the <i>Circular of the People's Bank of China, the State Administration of Foreign Exchange, the Ministry of Foreign Trade and Economic Cooperation and the State Administration of Taxation Concerning Printing and Distribution Detailed Rules on Rewarding and Punishment Concerning Provisional Regulations over Examination of Export Collections of Foreign Exchange</i> (see Exhibit-51)	<p>Benefit: Discounted lending rates available to companies that satisfy certain export performance requirements.</p> <p>"Honorable Enterprises for Collection of Export Receipts of Foreign Exchange" may receive up to a 10% reduction in lending rates of RMB loans extended by commercial banks based on the lending rates fixed by the People's Bank of China. "Honorable Enterprises" are defined as enterprises with annual exports exceeding \$200 million in value and that meet certain other conditions related to foreign exchange and export receipt verification forms.</p>
9.	<u>Legislation:</u> <i>Circular of the State Council Concerning the Adjustment in the Taxation Policy of Imported Equipment</i> (see	Benefit: VAT and tariff exemption available to foreign-invested companies that satisfy certain

Exhibit-48), read in conjunction with Section XIII of the <i>Catalogue for the Guidance of Foreign Investment Industries</i> (see Exhibit-50)	export performance requirements. For foreign-invested companies engaged in industries allowed by the State that export all of their products, equipment purchased for self-use shall be exempt from tariff and import VAT.
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According to a February 28, 2007 notice issued by the People's Bank of China, the State Administration of Foreign Exchange, the Ministry of Commerce and the State Administration of Taxation, measure 8 in the above table, *i.e.*, the *Circular of the People's Bank of China, the State Administration of Foreign Exchange, the Ministry of Foreign Trade and Economic Cooperation and the State Administration of Taxation Concerning Printing and Distribution Detailed Rules on Rewarding and Punishment Concerning Provisional Regulations over Examination of Export Collections of Foreign Exchange*, which grants discounted lending rates to companies contingent upon export performance, was to be abolished as of March 8, 2007.⁹⁶

On March 16, 2007, the Fifth Session of the Tenth National People's Congress approved China's new *Enterprise Income Tax Law* (see Exhibit-8). The new law will come into effect as of January 1, 2008; in the meantime, the 1991 *Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises* as referenced in measures 4, 5 and 6, as well as the 1993 *Provisional Regulations on Income Tax Law for Enterprises* has been annulled. Under the existing system, Chinese domestic enterprises pay a 33% income tax while foreign-invested enterprises (FIEs) on average enjoy a preferential tax rate of about 15%. The new law equalizes the income tax rate for foreign and domestic enterprises at 25% to create a level playing field. FIEs will no longer be able to enjoy the broadly-granted tax holidays, and will be

⁹⁶ Notice [2007] No.7 of the People's Bank of China, the State Administration of Foreign Exchange, the Ministry of

subject to the same tax incentives as domestic enterprises, such as tax breaks for companies in the State-encouraged sectors. The new system provides for a five-year phase-in period under which FIEs in existence before the new law takes effect are allowed a gradual transition from the existing preferential tax rate to the new rate. In addition, FIEs that are currently enjoying preferential treatment in the form of tax reduction or exemption may continue to enjoy such treatment until the end of the preferential treatment period. Implementing rules will be developed to further define the new policy.

To date, China has not released official plans to abolish other legislation granting the prohibited subsidies in question.

V. VIEWPOINTS OF INTERNATIONAL ORGANIZATIONS, INDUSTRIAL ASSOCIATIONS AND OTHER INTERESTED PARTIES ON CHINA'S SUBSIDIES TO THE HIGH-TECH INDUSTRY

In addition to monitoring by WTO Members countries, international organizations and industrial associations, as well as other interested parties, also have a strong interest in monitoring China's subsidies practice in general and specific measures to support the high-tech industry in particular.

The OECD, in its study of science and technology policy developments in non-member economies, described China's policy efforts to enhance the country's innovation capacity as follows:

China's plan to become a major innovation economy by 2020 is probably the most significant as it will launch a series of reforms and strategic projects to make research and innovation the motor of its new economic development strategy.⁹⁷

With respect to specific measures to support research and innovation, the OECD noted subsidized loans, tax incentives and funding for venture capital, as discussed below:

The China Development Bank for example provides subsidized loans for firms in high-tech export industries.... China's new tax incentive policy will allow firms to use 150% of its spending on R&D to offset income taxes. The part that is not offset in any current year can be carried forward for the next five years. The new policy also encourages companies to accelerate depreciation of research-related facilities. Moreover, local governments in the national high-tech industrial development zones are authorized to offer two-year exemptions of income tax to newly founded high-tech enterprises, which could also apply for the favorable income tax rate at 15% in the following two years.

China encourages relevant central government departments and local governments to create seed funding for venture capital and to

⁹⁷ *OECD, Science, Technology and Industry Outlook 2006*, at page 88.

facilitate the flow of funds available to venture capital funds. It now also allows insurance and investment companies to invest in venture capital funds and it provides tax incentives for venture capital enterprises that focus on supporting start-ups in high and new technology industries.⁹⁸

U.S. industry associations in the high-tech sector have voiced many concerns that China's subsidies have disadvantaged their members. For example, the National Electrical Manufacturers Association (NEMA) has had a long-term complaint over subsidized purchases of raw materials that give Chinese electrical exports an unfair competitive edge. In its 2006 comments on China's WTO compliance, NEMA reiterated the concern as follows:

Potentially "subsidized" product coming into the US: some of our members have noted competition from extremely low-priced Chinese electrical imports. Since the goods in question are frequently not labor-intensively produced, these member companies are concerned that the Chinese government may be subsidizing the purchase of raw materials and/or providing them below cost via state-owned enterprises. China has made WTO accession commitment regarding state-trading enterprises and subsidies; we trust the USG will join us in encouraging China to meet and keep those commitments...⁹⁹

The U.S. Semiconductor Industry Association (SIA) has also been closely monitoring Chinese government subsidies. In its submission for the 2005 National Trade Estimate Report on Foreign Trade Barriers, while welcoming China's repeal of its VAT rebate to semiconductors manufactured in China as a result of the U.S.-China WTO consultation, SIA expressed concerns over new industry-targeted measures under contemplation:

The proposed semiconductor-specific policy reportedly consists of four key elements: 1) establish a special development fund of RMB

⁹⁸ Id. at pages 88-89.

⁹⁹ *NEMA Comments on China's WTO Compliance* (July 2006), available at <http://www.nema.org/gov/trade/positions/upload/6july25chinatrm.pdf>.

0.5-1 billion (approx. \$60.4-120.8 million) allocated from the Ministry of Finance to the chip industry every year; 2) create a personnel training fund of RMB 10-100 billion (approx. \$1.2-12.08 billion) annually for the industry; 3) relax income taxes from two years of tax-free followed by three years of half tax to five years of tax free followed by five years of half tax (or possibly ten years of tax-free); and 4) provide 1% discount on loans for new investments.

Since details on these policies are still emerging, SIA urges USTR to closely monitor any potential new Chinese government measures designed to encourage the development of the semiconductor industry. Any promotional measures should be developed and implemented in a transparent manner and be fully consistent with China's WTO obligations.

In particular, the development fund must be implemented with full transparency to ensure that it does not amount to a pass-back of the VAT that otherwise would have been rebated to domestic firms. The Chinese government must establish a clear and public notice procedure for disbursement from the fund, and a list of recipients, amounts, and purposes should be publicly available. Further, this fund should not have the effect of distorting trade or investment by directly supporting product development or equipment purchase. If such a fund is established, it should instead focus on pre-competitive R&D activities and be open to participation of foreign firms.¹⁰⁰

In testimony before the US-China Economic and Security Review Commission on China's WTO Compliance and Industrial Subsidies, Dr. Usha C.V. Haley, Director of the Global Business Center at the University of New Haven, noted that subsidies in China exist in all industries considered economically or militarily strategic, including resource extraction, steel, computing, software, R&D, environmental services and conservation, and autos.¹⁰¹ According to Dr. Haley,

¹⁰⁰ *Comments of the Semiconductor Industry Association for the 2005 National Trade Estimate Report on Foreign Trade Barriers – China* (December 21, 2004), available at http://www.sia-online.org/downloads/2005_NTE_China_Comments.pdf.

¹⁰¹ *Statement of Dr. Usha C.V. Haley, Director of Global Business Center of University of New Haven, before the US-China Economic and Security Review Commission during the Hearing on China's WTO Compliance: Industrial Subsidies and the Impact on U.S. and World Markets* (April 4, 2006), available at http://www.uscc.gov/hearings/2006hearings/written_testimonies/06_04_04wrts/06_04_04_haley.php.

the subsidies take such forms as free or low-cost loans, asset injections, no break-even,¹⁰² subsidized purchases of components and raw materials, international bargaining power,¹⁰³ labor controls, tax breaks, energy and land subsidies, sectoral credit allocation, stock listings,¹⁰⁴ cheap technology and control over distribution channels. He also highlighted in his statement China's use of subsidies to build national champions:

Specifically, the Chinese government wants its own global stars. The SASAC, which oversees SOEs, has the mandate to transform 30-50 SOEs into globally competitive national champions by 2010. These include PetroChina, ChinaMobile, Sinopec, CNOOC, Baosteel, China Aluminum, Shanghai Auto, Lenovo, TCL, and Qingdao Haier. Korea's chaebol, rather than Japan's keiretsu provide the guiding model for China's policy on industrial subsidies: through subsidies, the state helps the national champions to diversify their range of businesses and to link more closely to the state.

Among the 10 selected companies listed above, three of them, namely Lenovo, TCL and Qingdao Haier, are from the high-tech sector.

¹⁰² In Dr. Haley's statement, "no break-even" is explained as "poor bookkeeping practices, and lax bottom-line considerations, grant SOEs freedom from the need to make profits, or to break even."

¹⁰³ In Dr. Haley's statement, "international bargaining power" is explained as "Beijing has used its enormous buying power to intercede for its SOEs with foreign suppliers and to reduce acquisition costs for raw materials..."

¹⁰⁴ In Dr. Haley's statement, "stock listings" is explained as "SOEs and collectives form over 93 percent of the listing of approximately 1300 companies on China's Shanghai and Shenzhen Stock Exchanges. Provincial governments pressure government regulators to discriminate against private companies and give the precious slots to their ailing state dinosaurs..."

VI. OPTIONS AVAILABLE TO THE U.S. HIGH-TECH SECTOR TO ADDRESS SUBSIDIES BEING PROVIDED IN CHINA

Industry policy support or subsidies provided by the Chinese government to domestic companies can disadvantage U.S. high-tech businesses either by displacing U.S. exports to foreign markets or causing a loss of U.S. domestic market sales. When that happens, there are several options available to the U.S. high-tech sector to eliminate distortions.

One option would be to file a WTO dispute settlement case. An example of this course of action involving the high-tech sector occurred on March 18, 2004, when the United States filed the first WTO case against China with respect to China's value-added tax rebate policy that discriminated against imported integrated circuits (ICs) (*i.e.*, semiconductors).¹⁰⁵ China's VAT regime provided for a rebate of 14% of a 17% VAT to enterprises in China on ICs manufactured in China but subjected imported ICs to the full 17% VAT with no refunds where the product was used domestically. In addition, China allowed for a refund of 11% of the 17% VAT to domestically-designed ICs that, because of technological limitations, are manufactured abroad, a practice that accorded more favorable treatment to imports from one country than another. The United States and China were able to resolve the issues during the consultation phase, with China eliminating VAT rebates for domestic IC production, effective April 1, 2005, and revoking the rebate policy on imported chips designed in China, effective October 1, 2004.

The IC case was filed on the ground of national treatment obligations that China undertook as part of the WTO accession requiring that foreign goods and services be treated as favorably as domestic goods and services. The U.S. high-tech sector could also address subsidies under the

¹⁰⁵ *China – Value-Added Tax on Integrated Circuits – Request for Consultations by the United States*, WT/DS309/1

WTO dispute settlement mechanism pursuant to the *Agreement on Subsidies and Countervailing Duties* when the subsidies at issue fall under the category of prohibited subsidies under the SCM agreement. Article 4.1 of the agreement provides that:

Whenever a Member has reason to believe that a prohibited subsidy is being granted or maintained by another Member, such Member may request consultations with such other member.

The U.S. government exercised this option on February 2, 2007 by requesting consultations with China over certain prohibited subsidies, including export subsidies and import substitution subsidies as defined under Article 3 of the SCM Agreement. With respect to actionable subsidies as defined in Article 5, which are subsidies that cause adverse effects to the interests of other WTO Members, Article 7 provides that:

Except as provided in Article 13 of the Agreement on Agriculture, whenever a Member has reason to believe that any subsidy referred to in Article 1, granted or maintained by another Member, results in injury to its domestic industry, nullification or impairment or serious prejudice, such Member may request consultations with such other Member.

Besides making use of the existing WTO dispute settlement system, the U.S. high-tech industry and the U.S. government could attempt to reform the system by improving the subsidy disciplines under the SCM Agreement which would help to address subsidy issues more effectively. Such attempts have already been made by the U.S. government in the ongoing Doha Round rules negotiations. One of the proposals tabled by the United States is to expand the existing category of prohibited subsidies to include instances of government intervention that have the same distortive effect on trade or competitiveness as export and import substitution

subsidies.¹⁰⁶ Candidates for inclusion are some of the practices listed in the dark amber provision of Article 6.1 of the SCM Agreement such as large domestic subsidies, subsidies to cover operating losses by a company and direct forgiveness of debt.¹⁰⁷

When the problem faced by the U.S. high-tech sector is market-distorting imports, the industry could, of course, pursue trade remedies under U.S. law where the statutory elements are present. The U.S. high-tech industry could petition for the imposition of countervailing duties when it is injured by reason of Chinese high-tech imports benefiting from Chinese government subsidies. Where prices are believed to be discriminatory, U.S. high-tech companies could pursue anti-dumping actions if the imported products at issue are sold at less-than-normal-value in the United States and injure the U.S. domestic industry. U.S. companies could also resort to the China-specific safeguard mechanism, which China agreed to be subject to during a transitional period of its WTO membership, if an import surge of the products at issue results in market disruption.

¹⁰⁶ *Subsidies Disciplines Requiring Clarification and Improvement – Communication from the United States*, TN/RL/W/78 (19 March 2003), at page 2.

¹⁰⁷ *Id.*

VII. REVIEW OF HIGH-TECH TRADE FLOWS BETWEEN THE U.S. AND CHINA

Trade in high-tech products cuts across many categories under the Harmonized Tariff Schedule (HTS). Subsidy programs in the high-tech industry discussed in the present paper involve some of the product subsets in the HTS categories related to high-tech sectors. With a view to presenting a comprehensive picture of the dynamics of the high-tech trade flows between the United States and China, trade data covering the full range of advanced or high-tech sectors is analyzed and presented in Exhibit-77, Exhibit-78 and Exhibit-79.

Exhibit-77 is provided by MBG Information Services based on the data sourced from the U.S. Bureau of the Census. It covers U.S. trade with China in advanced technology products (ATP), more specifically, (1) export, import and balance totals from 1990-2006, (2) exports, imports and balances from 1997-2006 for each 2-digit HS chapter included in the detailed ATP data, and (3) exports, imports and balances from 2000 to 2006 for ATP at the detailed 10-digit HS level (altogether 821 products). As demonstrated by the data, the U.S. ATP trade balance with China has been worsening since 1994, with the United States running a rapidly widening trade deficit with China especially in the past seven years. In 2000, the U.S. ATP trade deficit with China was USD \$6.95 billion; the figure climbed to USD \$55.08 billion in 2006. From 1990 to 2006, China's share in the U.S. ATP trade with the world expanded in terms of both import and export; however, the growth of U.S. imports from China as a percentage of total U.S. imports was more three times the growth of U.S. exports to China as a percentage of total U.S. exports. For the 2-digit HS chapters included in the ATP data, a worsening U.S. trade balance with China is shown in Organic Chemicals (HS 29), Mechanical/Computers (HS 84), Electrical Machinery (HS 85), and Arms and Ammunition (HS 93).

Exhibit-78 covers the U.S. ATP trade with China and all other sources from 2002 to 2006 grouped in ten product categories as defined by the U.S. Bureau of the Census, which include (1) biotechnology, (2) life science, (3) opto-electronics, (4) information & communications, (5) electronics, (6) flexible manufacturing, (7) advanced materials, (8) aerospace, (9) weapons, and (10) nuclear technology. The detailed ATP concordance is also included in the exhibit. The data show that the United States ran an annual trade deficit for the entire time period of 2002-2006 in six out of the ten categories, with a worsening trade deficit in four categories, *i.e.*, biotechnology, opto-electronics, information & communications, and weapons. In addition, U.S. imports from China outpaced U.S. imports from all other sources in all of these categories except opto-electronics and nuclear technology.

Exhibit-79 reviews U.S. trade in high technology products with China and all other sources from 2000 to 2006 based on ITC product groups from Shifts in Merchandise Trade reports. The 28 groups included are related to the electronic products sector and the machinery sector. The data show that the United States had a deteriorating trade deficit with China in the following 17 product groups:

<ul style="list-style-type: none">▪ Office machines▪ Telephone and telegraph apparatus▪ Consumer electronics (except televisions)▪ Blank media▪ Navigational instruments and remote control apparatus▪ Television receivers and video monitors▪ Radio and television broadcasting equipment▪ Electric sound and visual signaling apparatus	<ul style="list-style-type: none">▪ Printed circuits▪ Circuit apparatus not exceeding 1000V▪ Circuit apparatus assemblies▪ Parts of circuit apparatus▪ Optical goods, including ophthalmic goods▪ Photographic cameras and equipment▪ Medical goods▪ Drawing, drafting, and calculating instruments▪ Non-metalworking machine tools
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