



UPDATES: DEVELOPMENTS OF CHINESE TAX REGULATIONS

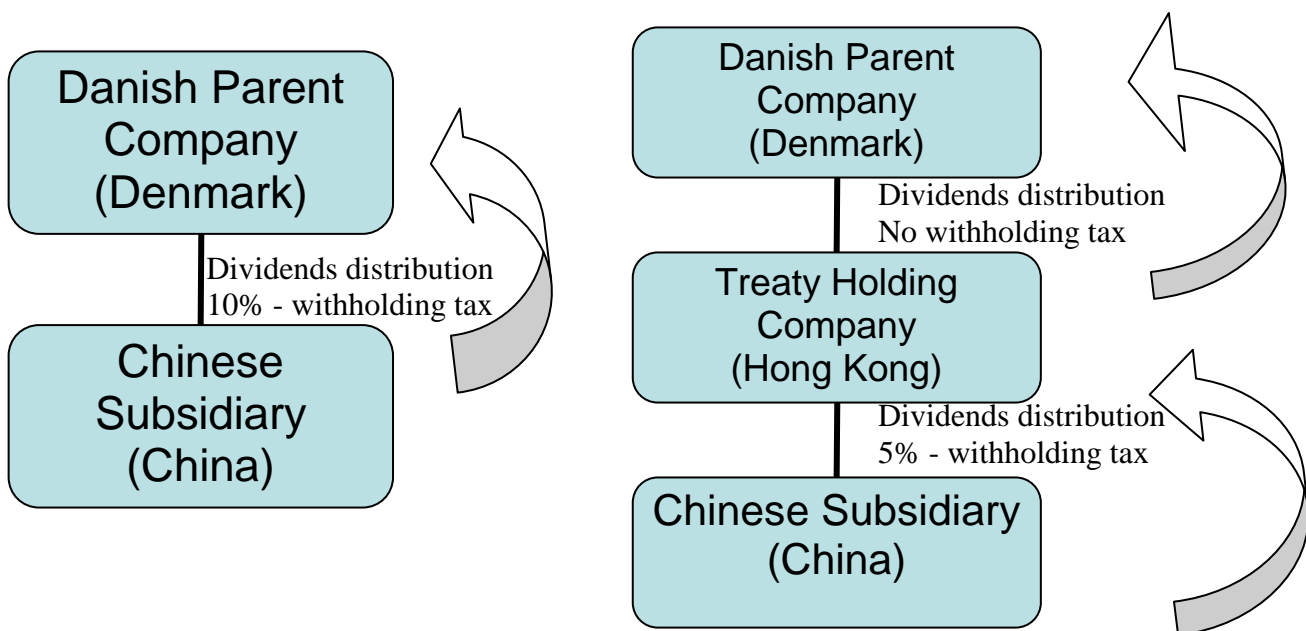
There are some important developments in the Chinese tax regulations which may have wide-spread impact on your current and potential investments in China.

Dividends Distribution from China

It is currently proposed that dividend distributed by Foreign Invested Enterprises ("FIEs") to their foreign investors will no longer enjoy tax exemption and will be subject to 10% withholding tax. The regulation is likely to correspond with the new Corporate Income Tax Law which will take effect on 1 January 2008.

Prior to the regulation above being approved by the China State Council, it is potentially possible for existing investments of multinational companies ('MNCs') in China to lower the China withholding tax through advanced planning.

Example: Potential Tax planning



Through insertion of an appropriate treaty holding company, for example, in Hong Kong, it may be possible to mitigate China withholding tax from 10% to 5%, following the conclusion of the comprehensive Double Tax Arrangement ("DTA") between the Mainland of China and Hong Kong in

August 2006. As for final distribution of dividends to foreign investors, there is currently no dividend withholding tax in Hong Kong.

Recommendation

Although the regulation on the distribution of dividends is currently in the proposal stage, it is, however, very likely that the China State Council will endorse the regulation in the next month or so. Therefore, proper planning needs to be in place to achieve the desirable structure and tax results. As for existing investments in China, in order to ensure the restructuring itself may enjoy tax free reorganisation treatment in China, the foreign investors must be able to complete all the restructuring steps properly within this year, i.e. 2007. Restructuring of this nature may take several months to complete and hence early attention is highly recommended.

Transfer Pricing in China - First Wave of Information Collection

With the issuance of Guo Shui Han [2007] No.363 by the SAT on 27 March 2007, Chinese tax authorities have been placing more significant emphasis on transfer pricing enforcement. Many companies in a number of provinces and municipalities such as Beijing and Tianjin have recently received inquiries from local tax authorities regarding transfer pricing.

Generally, the information request consists of an Enterprise Function and Risk Analysis Form and an Enterprise Related Party Transaction Financial Analysis Form, which are the same as the ones contained in Guo Shui Han [2007] No.363, as well as a number of other forms on the company's general, financial and related party transactions information. The specific information requests from these tax authorities may vary, but the forms are uniform within each of the local jurisdictions. In general, the Function and Risk Analysis Form is not straightforward, in fact, it is rather complicated and sometimes confusing.

We understand that the information requests are intended for the tax authorities to conduct desktop reviews in order to identify potential transfer pricing audit targets. For companies with significant amounts of intercompany transactions and having sustained low profitability or consecutive losses or dealing extensively with tax havens, their transfer pricing audit risk may be particularly high, so professional assistance is strongly recommended.

For further information please contact your usual contact person or: Jørgen Juul Andersen, telephone +45 3945 9434, email: jj@pwc.dk.

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