
Answers

		Marks
1	(a) Company C	
	(i) Correct treatment of items	
	(1) The bonus payable in January 2013 is not allowable until it is actually paid.	1
	(2) The interest on the loan borrowed to construct a canteen is of a capital nature and not allowable.	1
	(3) Subject to the maximum amount of 0.5% of the sales income of the year (i.e. 15,000,000 x 0.5% = 75,000), 60% of the entertainment expense (150,000 x 60% = 90,000) is deductible. Thus, RMB 75,000 is deductible and RMB 75,000 (150,000 – 75,000) is non-deductible.	1
	(4) Qualifying advertising and promotion expenses are deductible up to 15% of the sales income of the year (i.e. 15,000,000 x 15% = 2,250,000); thus the entire amount of RMB 60,000 is deductible.	1
	(5) In addition to the actual expense, an additional deduction of 50% of the research and development expense is allowable.	1
	(6) Staff and worker benefits cannot exceed 14% of the total salaries and wages, i.e. RMB 119,000.	1
	(7) Staff education expenses cannot exceed 2.5% of the total salaries and wages, i.e. RMB 21,250.	1
	(8) A direct donation to a non-approved entity is not allowable.	1
	(9) Sponsorship of non-business activities is not allowable.	1
	(10) A penalty for the late payment of tax is not allowable (but it is allowable for accounting purposes).	1
	(11) Interest income from a national debenture is exempt.	1
	(12) The gain on the disposal of an office is taxable.	1
	(13) Only the tax written down value of RMB 60,000 is allowable.	1
		<u>13</u>
	(ii) Enterprise income tax (EIT) for 2012	
		RMB
	Taxable profit before adjustment	1,700,000
	<i>Add:</i>	
	(1) Bonus payable	150,000
	(2) Capital nature interest	20,000
	(3) Non-allowable entertainment expense (150,000 – max. amount)	75,000
	(4) No adjustment	0
	(6) Over limit staff and worker benefits	81,000
	(7) Over limit staff education expense	78,750
	(8) Non-allowable donation	100,000
	(9) Non-allowable sponsorship	60,000
	(10) Tax penalty	20,000
	(12) No adjustment	0
	(13) Tax written down value over limit (80,000 – 60,000)	20,000
		<u>604,750</u>
	<i>Less:</i>	
	(5) Additional deduction for research and development expense	10,000
	(11) National debenture interest – exempt	30,000
		<u>(40,000)</u>
	Adjusted taxable profit	2,264,750
	Tax rate	25%
	Tax payable	566,188
		<u>7</u>
	(b) Company K	
	The sharing of administrative costs is generally not tax deductible.	1
	However, where a specific benefit is received by the payer sharing the costs, they may be tax deductible.	1

To qualify for a deduction, Company K must have:

- (i) supporting documents from the Chinese investor certifying the sharing basis and the scope of the expenses involved;
- (ii) the basis must be at 'arm's-length'; and
- (iii) a verification report must be issued by a certified public accountant.

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- (c) (i) The sale should be recognised according to the instalment date agreed in the sales contract.
- (ii) The sale should be recognised when the product is delivered to the customer.
- (iii) The sale should be recognised when the consignor receives the consignment sales list from the consignee.
- (iv) The sale should be recognised when the seller completes the bank procedures for collection of the payment.
- (v) The sale should be recognised when the buyer completes the acceptance check.

1 mark each 5

- (d) A small scale enterprise refers to an enterprise which operates in a non-restricted/prohibited industry and meets the following criteria:

- (i) For an industrial enterprise, the annual taxable profit does not exceed RMB300,000, the number of staff does not exceed 100 and the total assets do not exceed RMB30,000,000; and 2
- (ii) For any other enterprise, the annual taxable profit does not exceed RMB300,000, the number of staff does not exceed 80 and the total assets do not exceed RMB10,000,000. 2

From 1 January 2012 to 31 December 2015, for a small scale enterprise, the enterprise income tax rate is 20%, except for those enterprises whose taxable profit does not exceed RMB60,000, when the enterprise income tax rate is 10%.

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2 (a) Mr Chan – individual income tax (IIT) for 2012

- (1) The benefit to the shareholder, Mr Chan, is deemed to be a profits distribution and is taxed at 20%:
= 250,000 x 20% = RMB 50,000 1.5
 - (2) IIT on selling the copyright of his manuscript copy:
= 45,000 x (1 – 20%) x 20% = RMB 7,200 1
 - (3) IIT on selling a notable artist's scrolls painting:
= (300,000 – 200,000) x 20% = RMB 20,000 1
 - (4) IIT on the delivery of a three-day training course (individual service income):
= 24,000 x (1 – 20%) x 30% – 2,000 = RMB 3,760 1
 - (5) IIT in relation to the publication of the novel:
= (48,000 + 12,000) x (1 – 20%) x 20% x (1 – 30%) = RMB 6,720 1
- Tutorial note:** A further incentive 30% discount is given to arrive at the final tax liability.
- (6) IIT in relation to the income from the partnership:
= (80,000/2) x 20% – 3,750 = RMB 4,250 1
 - (7) The gain from the trading in listed shares is exempt. 0.5
 - (8) Additional IIT required on the overseas income from publishing a professional article in Country M:
IIT = (USD 600 x 7) x (1 – 20%) x 20% x (1 – 30%) = RMB 470 1
So, IIT of RMB 170 (470 – 300) needs be paid in China. 0.5
 - (9) IIT on property sale:
Taxable income (net of business tax) = (800,000 – 500,000) – (800,000 x 5%) = 260,000 1
IIT on the profit: 260,000 x 20% = RMB 52,000 0.5

	Marks
(10) The insurance compensation is exempt.	0.5
(11) IIT on lottery prize:	
RMB 6,000 (i.e. 30% of the prize) is deductible for the donation to the approved charity.	1
So, IIT for the lottery prize: $(20,000 - 6,000) \times 20\% = \text{RMB } 2,800$	0.5
	12

(b) Mr Christopher

(i) The following benefits will be exempt from individual income tax (IIT) for Mr Christopher:

- reimbursement for housing rental;
- meal allowance;
- laundry allowance;
- reimbursement for paid home leave (maximum two trips per year);
- language training;
- children's education fees;
- reasonable relocation expenses at the beginning and end of his assignment.

Note: Only THREE items required.

1 mark each, maximum 3

(ii) Individual income tax (IIT) is reported and paid on a withholding basis through withholding agents. In the case of employment income, the earner of the wages and salaries is the taxpayer and the paying unit or individual will normally be the withholding agent. However, in this case, since the payer is outside China, there is no withholding agent, so Mr Christopher himself has the obligation to report and pay the tax on a monthly basis.

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The tax withheld on a monthly basis must be paid to the State Treasury by the withholding agent within the first 15 days of the following month, together with the submitted tax returns.

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Note: *In some cases, local tax bureaus may have a different tax filing and payment date.*

As his annual income is over RMB 120,000 and it is earned from a source outside China, Mr Christopher must, as an individual taxpayer, file an annual return within 30 days after the end of the tax year, and pay any deficiency in the tax paid in advance on a monthly basis.

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3 (a) Company T – value added tax (VAT) refund for April 2012

Irrecoverable VAT = $(\text{USD}1,000,000 \times 7) \times (17\% - 13\%) = \text{RMB } 280,000$ 1

VAT payable = $1,500,000 \times 17\% - (1,300,000 - 280,000) = \text{RMB } (765,000)$ 1

Since the VAT payable is negative, the maximum refundable amount for the month needs to be calculated:

$(\text{USD}1,000,000 \times 7) \times 13\% = \text{RMB } 910,000$ 1

Since the absolute amount $765,000 < 910,000$, the refund amount is RMB 765,000 for the month of April 2012.

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(b) Company Y – value added tax (VAT) refund for May 2012

Irrecoverable VAT = $(4,000,000 - 2,000,000) \times (17\% - 13\%) = \text{RMB } 80,000$ 1

VAT payable = $8,000,000 \times 17\% - (2,600,000 - 80,000) = \text{RMB } (1,160,000)$ 1

Since the VAT payable is negative, the maximum refundable amount for the month needs to be calculated:

$(4,000,000 - 2,000,000) \times 13\% = \text{RMB } 260,000$ 1

Since the absolute amount $1,160,000 > 260,000$, the refund amount for the month of May 2012 is RMB 260,000 and the balance of RMB 900,000 ($1,160,000 - 260,000$) is carried forward for future offset.

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	Marks
(c) Requirements for an export refund	
The export of goods must be subject to value added tax or consumption tax.	1
The export must be recorded as an export sale in the book of the registered export enterprise.	1
A monthly declaration form needs to be submitted for the tax refund supported by the relevant documents, such as the export invoice, foreign exchange verification and the cancellation certificate.	1
	<u>3</u>
(d) Withholding agent for business tax	
(i) The main contractor is the withholding agent.	
(ii) The overseas entity's agent or the assignee or the purchaser of the service is the withholding agent.	
(iii) The agent selling the tickets is the withholding agent.	
(iv) The principal insurer is the withholding agent.	
(v) The assignee is the withholding agent.	
	1 mark each
	<u>5</u>
(e) Company F – business tax for January 2012	
(1) Income from the nursing home is exempt from business tax.	1
(2) Service category: $(120,000 + 100,000) \times 5\% = \text{RMB } 11,000$	1
(3) Karaoke category: $(7,000 + 15,000 + 40,000) \times 20\% = \text{RMB } 12,400$	1
	<u>3</u>
	<u>20</u>
4 (a) Non-resident enterprise	
A non-resident enterprise is an enterprise which is incorporated under the laws of other countries or regions and whose place of effective management is located outside China.	1
Place of effective management refers to an establishment which exercises, in substance, overall management and control over the production and business, personnel, accounting, properties, etc of the enterprise.	1
Effectively connected	
Effectively connected refers to the situation whereby the establishment or place of business of a non-resident enterprise in China owns the share rights or creditor's rights which give rise to the income; or which owns, manages, or controls properties, etc, which give rise to the income.	2
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(b) A non-resident enterprise with an establishment or place of business in China pays enterprise income tax (EIT) on its China-sourced income derived by such an establishment or place of business AND on its foreign-sourced income which is effectively connected with such an establishment or place of business.	2
(c) (i) A non-resident enterprise which does not have an establishment or place of business in China, or which has an establishment or place of business in China but whose income is not effectively connected with such an establishment or place of business, pays enterprise income tax only on its China-sourced income.	2
The enterprise income tax payable on such income will be collected on a withholding basis by the payer of the income on the behalf of a non-resident enterprise.	1
	<u>3</u>
(ii) Sources of income	
(1) Source is determined in accordance with the location of the enterprise making the distribution (the payer).	
(2) Source is determined in accordance with the location of the enterprise paying the royalty (the payer).	

- (3) Source is determined in accordance with the place where the transferred immovable property is located.
- (4) Source is determined in accordance with the location of the transferor of the movable property.
- (5) Source is determined in accordance with the place where the invested enterprise is located.
- (6) Source is determined by the relevant government authority.

1 mark each

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- 5 (a) (1) The tax laws issued by the Standing Committee and the National People's Congress. A typical tax law consists of a set of general principles setting forth the scope of the tax, the tax rate, the tax administration, the computation and the penalty provisions, e.g. 'Individual income tax law', 'Law of the PRC concerning tax administration and tax collection', etc.
- (2) The tax regulations issued by the State Council. These generally contain detailed provisions, which elaborate on the principles set forth in the tax laws, e.g. 'Rules for the implementation of the law of the PRC concerning tax administration and tax collection'. Also some provincial governments, e.g. Hainan, have the same legal status and its tax rules are only applied at the local level under the scope of the authority granted by the National People's Congress.
- (3) The administrative rules issued by the bureaus of the State Council, i.e. The State Administration of Taxation (SAT), the Ministry of Finance (MOF) and the Customs General Administration. For some taxes, such as value added tax and business tax, these are usually supplemented by 'detailed implementation rules' promulgated by the Ministry of Finance after obtaining approval from the State Council. The detailed rules are to clarify the application of the provisional regulations.
- (4) The tax notices and rulings issued periodically by the SAT and MOF. These notices are sent to the various finance and tax bureaus all over China to explain how tax laws and regulations should be interpreted and applied in different situations (e.g. GuoShuifa, GuoShuihan, etc).

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- (b) (i) The state tax bureau – value added tax, consumption tax, enterprise income tax.
- (ii) The local tax bureau – individual income tax, business tax, land appreciation tax, enterprise income tax paid by local state-owned enterprises.

Note: Only TWO examples required.

½ mark each, maximum

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