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# Answers

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		<i>Marks</i>
<b>1</b>	<b>(a) Company A</b>	
<b>(i)</b>	(1) Donation income is taxable at its fair value. Omission of the donation receipt will have resulted in the under-recording of income for both accounting and tax purposes of RMB 170,000 (150,000 + 20,000).	1·5
	(2) The salaries and bonuses, including the long service award are for business purposes and fully tax allowable.	1·5
	(3) Subject to the maximum amount of 0·5% of the sales/business income of the year, 60% of the entertaining expense is deductible, i.e. the lesser of RMB 1,000,000 (0·5% of 200,000,000) and RMB 900,000 (60% of 1,500,000).	1·5
	(4) Qualifying advertising and promotion expenses are deductible up to 15% of the sales/business income of the year, i.e RMB 30,000,000 (15% of 200,000,000).	1
	(5) Charitable donations to approved organisations are deductible up to 12% of the annual accounting profits, i.e. RMB 5,436,000 (12% of (45,130,000 + 170,000)).	1·5
	(6) Staff and worker benefits are deductible up to 14% of total salaries and wages, i.e. RMB 1,400,000 (14% of 10,000,000).	1
	(7) Amortisation of approved self-developed intangible assets enjoys an additional deduction of 50% of the expense for tax purposes, i.e. RMB 30,000.	1
	(8) A penalty imposed by the government is not allowable.	1
	(9) A general provision is not allowable.	1
	(10) A gain on the disposal of listed shares is taxable.	1
	(11) Interest income from a national debenture is tax exempt.	1
	(12) A gain on the disposal of a national debenture is taxable.	1
	(13) On the writing off of a fixed asset, only the tax written down value is an allowable deduction.	1
		<u>15</u>
<b>(ii)</b>	<b>Enterprise income tax (EIT) for 2009</b>	
		RMB
	Taxable profit before adjustment	45,130,000
<i>Add:</i>	(1) Unrecorded donation	170,000
	(2) No adjustment	0
	(3) Non-allowable entertainment (1,500,000 – 900,000)	600,000
	(4) No adjustment	0
	(5) No adjustment	0
	(6) No adjustment	0
	(8) Penalty for late filing	100,000
	(9) Stock provision	400,000
	(10) No adjustment	0
	(12) No adjustment	0
	(13) Adjustment to tax written down value (200,000 – 150,000)	50,000
		<u>1,320,000</u>
<i>Less:</i>	(7) Additional deduction for research expense	30,000
	(11) National debenture interest (exempt)	30,000
		<u>(60,000)</u>
	Adjusted taxable amount	46,390,000
	Tax rate	25%
	Tax payable	11,597,500
		<u>7</u>
<b>(b)</b>	<b>(i)</b> Tax law stipulates that the losses suffered by a taxpayer during a tax year may be carried forward and set off against the taxable income of the next five consecutive tax years. It is irrelevant whether or not profits are earned or losses are suffered in any one or more of those five consecutive years following the year when the loss was suffered.	1·5

	<b>Marks</b>
The carry forward period may not exceed five years, so any loss that has not been offset within five years will be wasted.	0.5
	<u>2</u>
<b>(ii)</b> The loss suffered by Company B in 2002 can only be carried forward and offset against the taxable profits in the years from 2003 to 2007, even if the enterprise is not sufficiently profitable in those years to actually offset the loss.	1
There is a loss in 2008 so the tax payable in that year is zero.	1
The losses suffered by Company B in the years 2004 and 2008 will be carried forward and offset against the taxable profits in 2009. Therefore, in 2009, the adjusted taxable profit will be RMB 450,000 (850,000 – 300,000 – 100,000) and the tax payable in 2009 will be RMB 112,500 (450,000 x 25%).	2
	<u>4</u>
<b>(c)</b> A resident enterprise is an enterprise that is incorporated in the PRC in accordance with the PRC's laws and administrative regulations; or an enterprise that is incorporated under the laws of other countries or regions but whose place of effective management is located in the PRC.	1.5
Place of effective management refers to an establishment that exercises, in substance, overall management and control over the production and business, personnel, accounting, properties, etc of the enterprise.	1
A resident enterprise is liable to pay enterprise income tax (EIT) on its income sourced BOTH from within and outside of the PRC.	1
A non-resident enterprise is an enterprise that is incorporated under the laws of other countries or regions and the place of effective management is located outside of the PRC.	0.5
A non-resident enterprise with an establishment or place of business in the PRC is liable to pay EIT on its PRC-sourced income derived by such an establishment or place of business AND on its foreign sourced income that is effectively connected with such an establishment or place of business.	1
A non-resident enterprise that does not have an establishment or place of business in the PRC, or that has an establishment or place of business in the PRC but whose income is not effectively connected with such an establishment or place of business, is liable to pay EIT only on its PRC-sourced income.	1
'Effectively connected' refers to situations whereby the establishment or place of business of a non-resident enterprise in the PRC owns the shareholdings, creditor's rights which give rise to the income; or owns, manages and has control over the properties, etc, which give rise to the income.	1
	<u>7</u>
	<b><u>35</u></b>

**2 (a) Mr Zhang – Individual income tax (IIT) for the month of January 2009**

(1) IIT for monthly employment income: $(18,000 - 2,000) \times 20\% - 375 = \text{RMB } 2,825$ .	1
IIT for the yearly bonus: $12,000 \times 10\% - 25 = \text{RMB } 1,175$	1.5
The applicable tax rate and the fast deduction factor for the bonus are determined by dividing the bonus by 12 ( $12,000/12 = 1,000$ ).	
(2) IIT on authorship (book): $18,000 \times (1 - 20\%) \times 20\% \times (1 - 30\%) = \text{RMB } 2,016$	1
IIT on authorship (magazine): $(1,000 \times 4 - 800) \times 20\% \times (1 - 30\%) = \text{RMB } 448$	1
(3) The gain from trading in listed shares is exempt.	0.5
(4) IIT on four seminars for Enterprise X: The total income for four seminars is RMB 4,800, which is an average of RMB 1,200 per seminar. The IIT payable each time is thus, $(1,200 - 800) \times 20\% = \text{RMB } 80$ and in total, RMB 320 ( $80 \times 4$ )	1.5
(5) IIT on the translation income: $5,200 \times (1 - 20\%) \times 20\% = \text{RMB } 832$	1
(6) The gain from selling a small size house that has been owned and lived in for at least five years is exempt.	1
(7) The bank deposit interest is exempt.	0.5
(8) The insurance compensation is exempt.	1
	<u>10</u>

	<b>Marks</b>
<b>(b) (i)</b> Mr Smith will be regarded as a resident taxpayer as his stay in the PRC is for one year or more but not more than five years.	1
He will therefore be liable to individual income tax (IIT) on his PRC-sourced income and any non-PRC-sourced income which is borne by a PRC individual or entity.	1
	<u>2</u>
<b>(ii)</b> As an expatriate living in the PRC for less than five years, Mr Smith will be exempt from individual income tax (IIT) on the following benefits:	
– reimbursement for housing rental;	
– meal allowance;	
– laundry allowance;	
– reimbursement for paid home leave;	
– language training;	
– children’s education fees;	
– reasonable relocation expenses at the beginning and end of his assignment.	
<b>Note: only THREE items required.</b>	
1 mark each, maximum	<u>3</u>
<b>(iii)</b> 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 be the withholding agent.	2
The tax withheld on a monthly basis must be paid to the State Treasury within the first seven days of the following month together with the submitted tax returns.	1
<b>Note: in some cases, local tax bureaus may have a different tax filing and payment date.</b>	
Whereas in Mr Smith’s case, annual income is over RMB 120,000 or where there is earned income from a source outside China, the individual taxpayer must 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.	2
	<u>5</u>
	<b><u>20</u></b>
<b>3 (a) Company C: consumption tax (CT) and value added tax (VAT) for the month of February 2009</b>	
(1) Input VAT on imported engines: $(2,000,000 + (2,000,000 \times 25\%)) \times 17\% = \text{RMB } 425,000$	1
Input VAT on transport fee: $10,000 \times 7\% = \text{RMB } 700$	1
There is no consumption tax on either the import or the transportation fee.	1
(2) Input VAT on raw materials (the discount for early payment is ignored): $(800,000 \times 17\%) = \text{RMB } 136,000$ .	1
Input VAT on transport fee: $8,000 \times 7\% = \text{RMB } 560$	0.5
There is no input VAT or CT on the insurance fee.	0.5
(3) Sale of Model A motor vehicles:	
CT = $(200 \times 150,000 / (1 + 17\%) \times 10\%) = \text{RMB } 2,564,103$	1
Output VAT = $(200 \times 150,000 / (1 + 17\%) \times 17\%) = \text{RMB } 4,358,974$	1
(4) The Model A motor vehicles sold to the company’s own staff are deemed sales (with an open market value):	
CT = $(10 \times 150,000 / (1 + 17\%) \times 10\%) = \text{RMB } 128,205$	1
Output VAT = $(10 \times 150,000 / (1 + 17\%) \times 17\%) = \text{RMB } 217,949$	1
(5) Model B motor vehicles self-used for testing purpose are a deemed sale (without an open market value):	
Composite value = $(5 \times 130,000 \times (1 + 8\%) / (1 - 10\%)) = \text{RMB } 780,000$	1
CT = composite value $\times 10\% = \text{RMB } 78,000$	0.5
Output VAT = composite value $\times 17\% = \text{RMB } 132,600$	0.5
	<u>11</u>

(b) The VAT treatment of assets sold on or after 1 January 2009 (i.e. following the changes made by 2008 Circular 170 2009 circular 9) is as follows:

Type of assets	Date of acquisition of the item	VAT treatment	Marks
(i) Used fixed assets	On or after 1 January 2009	For General VAT taxpayers: Output VAT = sales proceeds*/(1 + 17%) x 17%	0.5
		For Small-scale VAT taxpayers: VAT payable = sales proceeds*/(1 + 3%) x 2%	0.5
Used fixed assets	On or before 31 December 2008	For General VAT taxpayers: Output VAT = Sales proceeds*/(1 + 4%) x 4% x 50%	0.5
		For Small-scale VAT taxpayers: VAT payable = Sales proceeds*/(1 + 3%) x 2%	0.5
			<u>2</u>
(ii) Used articles (other than item used as fixed assets)		For General VAT taxpayers: Output VAT = Sales proceeds*/(1 + 17%) x 17%	0.5
		For Small-scale VAT taxpayers: VAT payable=sales proceeds*/(1 + 3%) x 3%	0.5
Used cars		For General VAT taxpayers: Output VAT = sales proceeds*/(1 + 4%) x 4% x 50%	0.5
		For Small-scale VAT taxpayers: VAT payable = sales proceeds*/(1 + 3%) x 2%	0.5
			<u>2</u>
Note: * refers to cum-VAT sales proceeds			
(iii)	(1) Company D: 250,000/(1 + 4%) x 4% x 50% = RMB 4,808		1
	(2) Company E: 180,000/(1 + 3%) x 2% = RMB 3,495		1
	(3) Company F: 150,000/(1 + 17%) x 17% = RMB 21,795		1
	(4) Company G: 150,000/(1 + 3%) x 2% = RMB 2,913		1
	(5) Company H: 150,000/(1 + 4%) x 4% x 50% = RMB 2,885		1
			<u>5</u>
			<b><u>20</u></b>

4 (a)	A mixed sale activity is a single sales activity that involves both the provision of taxable services, which are subject to business tax (BT), and a sale of goods, which is subject to value added tax (VAT).	1
	Mixed sales activities are regarded as a sale of goods not subject to BT tax if they are conducted by operators who are engaged in the production, wholesale or retail of goods.	1
	Mixed sales activities conducted by other entities or individuals are regarded as the provision of taxable services and are subject to BT (not VAT).	1
	Operators who are engaged in the production, wholesale or retail of goods include enterprises, entities of an enterprise nature or individual business operators who engage mainly in the production, wholesale or retail of goods and concurrently provide taxable services.	1
	The phrase 'engage mainly in the production, wholesale or retail of goods and concurrently provide taxable services' refers to situations in which the total (combined) turnover of the taxpayer comprises annual sales revenue from goods and the taxable services which are subject to VAT in excess of 50% of the total (combined) turnover, while the business revenue applicable to taxable services subject to business tax, is less than 50% of the total (combined) turnover.	1
		<u>5</u>

(b) Company J: business tax (BT) for the month of October 2009

(1)	Remuneration paid to artists cannot be deducted, but the television centre broadcast fee can be deducted. BT = ((3,000,000 – 800,000) x 5%) = RMB 110,000	1
(2)	Where income is considered to be too low and without proper justification by the tax bureau it has the right to re-determine the taxable income. Fees paid to the media for broadcasting/publishing can be deducted from the taxable income. Taxable income = (870,000 x (1 + 18%)/(1 – 5%)) = RMB 1,080,632 BT = ((1,080,632 – 200,000 – 150,000) x 5%) = RMB 36,532	2 1

	<i>Marks</i>
(3) Advertising banner: BT = (1,200,000 x 5%) = RMB 60,000	1
(4) Investment is not within the taxable scope of business tax, therefore no BT levied.	1
(5) Holding a fashion show is classified as 'Cultural activities and sports'. BT = (200,000 x 3%) = RMB 6,000	1
(6) Transfer of intangible assets: BT = (500,000 x 5%) = RMB 25,000	1
	8
 (c) Under all the amended Provisional Business Tax Regulations, taxpayers with either a monthly or a quarterly BT filing period, should make their respective tax return filing and payment within 15 days after the end of each filing period.	1
Tax paid late will incur an overdue tax surcharge of 0.05% per day for every day the tax payment is in default.	1
	2
	<b>15</b>
 <b>5 (a)</b> Enterprises are allowed to deduct eligible donations of up to 12% of the total amount of their annual accounting profits.	1
Where an enterprise donates its products, property or labour (as opposed to cash), it is deemed to have sold the goods, transferred the property or provided labour services.	1
The deductible donation must be made through a charitable social organisation or government body at or above county level.	1
Charitable social organisations include the Red Cross Society of China, China Charity Federation and China Youth Development Foundation, etc.	0.5
The donating enterprise must obtain a special official charitable donation receipt and the charitable social organisation is required to issue the special receipt to the donors to support their claim for relief.	1.5
	5
 (b) An individual can claim a deduction of up to 30% of taxable income for the making of charitable donations to domestic social organisations and government agencies for the relief of education, public welfare and disaster/poverty.	2
For donations made to certain designated charitable organisations such as the Red Cross Society of China and China Charity Federation, etc, no limit is imposed.	1
The individual making the charitable donation must obtain an official receipt from the charitable social organisation as a supporting document in order to claim an individual income tax (IIT) deduction.	1
	4
 (c) The monetary charitable donations made by a representative office (RO) for domestic charitable and relief purposes are allowed to be excluded from the operating expenses of the RO in determining the deemed income amount.	1
	<b>10</b>