



# Examiner's report

## P6 Advanced Taxation (CHN)

### June 2009

#### General Comments

The examination was divided into two sections. Section A consisted of two compulsory questions worth a total of 64 marks. In section B candidates were required to answer two of the three questions worth 18 marks each.

The questions in this paper were practically set and case-oriented, with the requirements of the questions broken up as specific as possible. Section A covered a very broad scope of the syllabus including Question 1 on enterprise income tax (EIT) and tax avoidance; and Question 2 on value added tax (VAT) and customs duty (CD). Very few marks were awarded to computations, and candidates were expected to demonstrate their abilities in analysing the questions and presenting their answers with logics and principles rather than detailed calculations. Candidates should also note that marks were available for professional skills in questions 1 and 2. In order to earn these marks candidates had to satisfy the requirement in relation to the format of the document requested (a report in question 1 and a letter in question 2); and to provide clear answers with logical conclusions.

Performance of this paper was fair. Most candidates attempted all four questions. However, many candidates presented their answers in a messy way. Candidates are advised to make use of the pre-exam 15 minutes reading and planning time to finish reading all questions, get a full picture of the facts in Questions 1 and 2, understand what exactly the requirements are, identify which two optional questions to be attempted, decide on the priority of the questions to be attempted, and finally, plan the layout and organisation of their answers and roughly allocate the time to each question.

#### Specific Comments

##### Question One

The question examined candidates' knowledge of the tax treatment of associated enterprises, transfer pricing adjustments and tax avoidance. Most candidates were able to demonstrate a good understanding of the tax treatment of associated enterprises and transfer pricing adjustments. However, they were rather weak at tax avoidance. Common mistakes include:

- misunderstood that to be associated, one entity needs to own more than 50% of the share capital of the other enterprise;
- did not address whether the enterprises were associated;
- could not define 'arm's length principle';
- not able to analyse and advise how the company can defend that it is not avoiding tax;
- did not answer in the required format, i.e. not using report format; and
- a lot of answers with report format were found to have no ending or conclusion.

##### Question Two

The question focused on VAT and CD implications and planning. In general, performance was poor. Most candidates could not calculate the different VAT and CD costs under the alternative modes of operation; and did not know how the bonded logistic park could be used to lower the VAT cost. Candidates' poor performance was mainly due to the failure to appreciate and address the following issues:

- under non-bonded export trade, if the VAT refund rate is lower than 17% part of the VAT incurred on local purchases of raw materials cannot be refunded and will become part of the cost of sales;
- under contract processing, raw materials can be imported under bonded treatment such that CD and import VAT need not be paid; processing fee can also be exempted from output VAT but input VAT on local purchases of raw materials cannot be refunded and will become part of the cost of sales;

- under import processing, the company can apply for bonded treatment; export sale of finished goods will be exempt from output VAT but if the VAT refund rate is lower than 17%, part of the VAT incurred on local purchases of raw materials cannot be refunded and will become part of the costs of sales;
- recommend contract processing as the best alternative;
- VAT implications under the use of bonded logistic park; and
- As in Question 1, did not answer in the required format, i.e. not using letter format; and did not give ending to the letter.

### **Question Three**

The question was on individual income tax (IIT) and tax administration. Part (a) examined candidates' understanding of the tax reliefs provided for temporary visitors to China under IIT. It was found that most candidates were familiar with the tax relief and were able to discuss whether the relief is applicable to the taxpayer. Part (b) and (c) examined candidates' understanding of the late payment surcharges and fines and taxpayer's rights. Most candidates were quite familiar with the law and gave rather satisfactory answers. Part (d) asked candidates to prepare a list of actions that the taxpayer should take to ensure proper compliance with the tax requirements. Most candidates were rather weak at giving advice and some did not give any answer to this part.

### **Question Four**

The question was set to examine candidates' knowledge of the stamp duty (SD) and turnover tax implications of given transactions. In part (a), candidates were able to explain the tax implications but their answers were not comprehensive; and some of them did not give calculations to support their answers. In part (b), some candidates could not explain their answers clearly, and were weak at identifying possible tax planning ideas.

### **Question Five**

The question examined candidates' knowledge of the taxability of employment benefits and income – compensation payment, discretionary bonus, housing benefits and stock options provided to expatriates; and to identify possible tax planning ideas. As in question 3, most candidates were quite familiar with the IIT treatments of employment benefits; but some of them could not explain their answers clearly, and were very weak at identifying possible tax planning ideas.