
Answers

| | | Marks |
|----------|--|-----------|
| 1 | (a) Company H | |
| (i) | (1) In addition to the actual expense, a further deduction of 100% of the amount paid to disabled employees expenses is allowable. | 1·0 |
| | (2) Subject to the maximum amount of 0·5% of the sales/business income of the year, 60% of the entertaining expense is deductible. | 1·0 |
| | (3) Qualifying advertising and promotion expenses are deductible up to 15% of the sales/business income of the year. Any excess amount can be carried forward to the following years. | 1·0 |
| | (4) Charitable donations to the approved organisations are deductible up to 12% of the annual accounting profits. | 1·0 |
| | (5) In addition to the actual expense, a further deduction of 50% of the research and development expense is allowable. | 1·0 |
| | (6) Staff and worker benefits are deductible up to 14% of total salaries and wages. | 1·0 |
| | (7) Staff education expenses are deductible up to 2·5% of total salaries and wages. | 1·0 |
| | (8) Sponsorship of non-business activities is non-deductible. | 1·0 |
| | (9) The gross amount of the overseas dividend $85,000/(1 - 15\%) = \text{RMB } 100,000$ is taxable and the difference between the gross and net should be added back in the calculation of taxable income. Since the 25% PRC rate is greater than the foreign tax rate of 15%, the foreign tax credit can be set off in full against the income tax liability. | 1·0 |
| | (10) A gain on the disposal of listed shares is taxable. | 1·0 |
| | (11) Interest income from national debentures is exempt. | 1·0 |
| | (12) A gain on the disposal of a national debenture is taxable. | 1·0 |
| | (13) Only the tax written down value is allowable on the write off of a fixed asset. | 1·0 |
| | (14) Donation income is taxable at its fair value. | 1·0 |
| | | <u>15</u> |

(ii) Enterprise income tax computation for the year 2008:

| | RMB | RMB | |
|--|---------|-------------------|------------|
| Taxable profit before adjustment | | 65,175,000 | |
| <i>Add:</i> | | | |
| (2) Non-allowable entertainment (40% of RMB 1,500,000) | 600,000 | | 0·5 |
| (3) No adjustment | 0 | | 0·5 |
| (4) No adjustment | 0 | | 0·5 |
| (6) No adjustment | 0 | | 0·5 |
| (7) No adjustment | 0 | | 0·5 |
| (8) Non-allowable sponsorship | 100,000 | | 0·5 |
| (9) Tax withheld from overseas dividend (gross up) | 15,000 | | 0·5 |
| (10) No adjustment | 0 | | 0·5 |
| (12) No adjustment | 0 | | 0·5 |
| (13) Tax written down value over limit (300,000 – 200,000) | 100,000 | | 0·5 |
| (14) Donation income | 100,000 | 915,000 | 0·5 |
| <i>Less:</i> | | | |
| (1) Additional deduction for disabled employees | 200,000 | | 0·5 |
| (5) Additional deduction for research expense | 400,000 | | 0·5 |
| (11) National debenture interest is exempt | 20,000 | (620,000) | 0·5 |
| Adjusted taxable amount | | <u>65,470,000</u> | |
| Income tax at 25% | | 16,367,500 | 0·5 |
| <i>Less:</i> foreign tax credit | | (15,000) | 0·5 |
| Income tax payable | | <u>16,352,500</u> | |
| | | | <u>8·0</u> |

- (b) The sharing of administrative costs is generally non-tax deductible. 1·0
- However, where a specific benefit is received by the payer sharing the costs may be deductible. 1·0
- To qualify for the deduction, Company J must have supporting documents from the Chinese investor certifying the basis of the sharing and the scope of the expenses involved, together with a verification report issued by a certified public accountant. 2·0
- 4·0

| | Marks |
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| (c) (i) Company L would have been enjoying a 15% preferential tax rate before the implementation of the new EIT. In such cases the tax rate will be increased step by step to 25% in the following manner: 2008 –18% /2009 – 20% /2010 – 22% /2011 – 24% /2012 – 25%. | <u>3·0</u> |
| (ii) Company M is currently enjoying a tax holiday (two years exempt and following three years half exempt) therefore, it will continue to enjoy the tax holiday until its expiration. | <u>2·0</u> |
| (iii) Company N has not yet started enjoying the tax holiday due to its losses, so the tax holiday period will be deemed to commence from 1 January 2008. In other words, even if Company N continues to make losses and does not have a chance to enjoy the tax holiday, Company N will be subject to the full tax rate of 25% of its taxable profits after offsetting any accumulated losses from the end of the five year transition period, i.e. from 1 January 2013. | <u>3·0</u> |
| | <u>35</u> |
| 2 (a) Mr C – Individual income tax (IIT) for the month of January 2008 | |
| (1) The IIT for monthly employment income = $(10,000 + 3,000 - 1,600) \times 20\% - 375 = \text{RMB } 1,905$. The IIT for the yearly bonus is calculated as follows: Divide the bonus by 12 $10,000/12 = 833.33$ to find the applicable tax rate of 10% and the fast deduction factor of RMB 25 Apply to the bonus amount: $10,000 * 10\% - 25 = \text{RMB } 975$. | <u>2·0</u> |
| (2) The gain from trading in listed shares is exempt. | <u>1·0</u> |
| (3) The bank deposit interest is subject to tax at 5%: $1,000 \times 5\% = \text{RMB } 50$ | <u>1·0</u> |
| (4) The interest income from the national debenture is exempt. The net gain on the national debenture is taxable at 20%: $20,000 \times 20\% = \text{RMB } 4,000$. | <u>1·0</u> |
| (5) The insurance compensation is exempt. | <u>1·0</u> |
| | <u>9·0</u> |
| (b) (i) The benefit to the shareholder Mr D is deemed to be a profits distribution. It is taxed at 20%: $200,000 \times 20\% = \text{RMB } 40,000$. | <u>2·0</u> |
| (ii) The loan to the shareholder Mr E is deemed to be a profits distribution. It is taxed at 20%: $200,000 \times 20\% = \text{RMB } 40,000$. | <u>2·0</u> |
| (iii) The benefit to the sole owner Mr F is deemed to be income received by an entrepreneur from a private enterprise. It is taxed under the schedule with the fast deduction factor: $200,000 \times 35\% - 6,750 = \text{RMB } 63,250$ | <u>2·0</u> |
| (c) 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. 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. (Note: in some cases, local tax bureaus may have different tax filing and payment dates). Where annual income is over RMB 120,000, the taxpayer must file an annual return within 3 months after the end of the taxable year. Where there is earned income from a source outside China, the taxpayer must file an annual return within 30 days after the end of the taxable year. | <u>2·0</u> |
| | <u>1·0</u> |
| | <u>2·0</u> |
| | <u>5·0</u> |
| | <u>20</u> |

| | | Marks |
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| 3 | (a) | |
| | (1) | Self-built and self-used buildings are exempt from business tax (BT). 1·0 |
| | (2) | When sold, the two floors are subject to BT at 3%. The composite value of the two floors is $20,000,000 \times (2/5) \times (1 + 30\%)/(1 - 3\%) = 10,721,650$ BT for the construction activity is $10,721,650 \times 3\% = \text{RMB } 321,650$ 2·0 |
| | (3) | BT is also chargeable on the sale of immovable property at 5%: $15,000,000 \times 5\% = \text{RMB } 750,000$ 1·0 |
| | | Total BT = $750,000 + 321,650 = 1,071,650$. <hr/> 4·0 |
| | (b) | Company A: customs tariff, consumption tax (CT) and value added tax (VAT) for the month of May 2008 |
| | (1) | For importation: Composite value for tariff = $100 \times 30,000 \times (1 \cdot 02) \times (1 \cdot 003) = \text{RMB } 3,069,180$ 1·0 Customs tariff = $3,069,180 \times 20\% = \text{RMB } 613,836$ 0·5 Composite value for CT and VAT = $(3,069,180 + 613,836)/(1 - 10\%) = \text{RMB } 4,092,240$ 1·0 CT = $4,092,240 \times 10\% = \text{RMB } 409,224$ 0·5 VAT = $4,092,240 \times 17\% = \text{RMB } 695,681$ 0·5 |
| | (2) | For subcontracting goods: Composite value for subcontracting goods = $20,000 + 5,000 = \text{RMB } 25,000$ 1·0 Customs tariff = $25,000 \times 20\% = \text{RMB } 5,000$ 0·5 Composite value for VAT = $(25,000 + 5,000) = \text{RMB } 30,000$ 1·0 VAT = $30,000 \times 17\% = \text{RMB } 5,100$ 0·5 |
| | (3) | For used machine: Taxable period = five years – three years = two years 1·0 Customs tariff = $500,000 \times (2/5) \times 20\% = \text{RMB } 40,000$ 1·0 |
| | (4) | For the sales activity: Output VAT = $60,000/(1 + 17\%) \times 17\% \times 50 = \text{RMB } 435,897$ 1·0 Input VAT for 100 motor cycles = $695,681 + 7\% \text{ of } 20,000 = \text{RMB } 697,081$ 1·0 Input VAT for the self-used motor cycle to be transferred out = $697,081/100 = \text{RMB } 6,970$ 1·0 Total input VAT = $697,081 - 6,970 + 5,100 = \text{RMB } 695,211$ 0·5 VAT payable for the month is Nil because $435,897 - 695,211 = \text{RMB } (259,314)$ 0·5 The excess input tax of RMB (259,314) is carried forward. 0·5 <hr/> 13 |
| | (c) | Taxpayers with a one month assessable period must report and pay the VAT due within ten days following the end of the month (period). 1·0 |
| | | For assessable periods of less than a month (one day, three days, five days, ten days and fifteen days), the VAT due must be prepaid within five days following the end of the period and a monthly return filed within ten days from the first day of the following month together with the balance of tax due (if any). 2·0 <hr/> 20 |
| 4 | (a) | Company Z – value added tax (VAT) for the month of April 2008 |
| | (1) | Output VAT for used machinery: $(80,000/1 \cdot 04) \times 4\% \times 50\% = \text{RMB } 1,538$ 2·0 |
| | (2) | Sales proceeds for the used car are less than the original cost, therefore, exempt 1·0 |
| | (3) | Output VAT for scrap: $10,000/1 \cdot 17 \times 17\% = \text{RMB } 1,453$ 1·0 |
| | (4) | Output VAT for TV: $1,200 \times 100 \times 17\% = \text{RMB } 20,400$ 1·0 Input VAT for TV: $1,000 \times 100 \times 17\% = \text{RMB } 17,000$ 1·0 |
| | (5) | Input VAT for used materials: $10,000 \times 10\% = \text{RMB } 1,000$ 2·0 |
| | (6) | Input VAT for electricity: $5,000 \times 17\% = \text{RMB } 850$ 1·0 |
| | | VAT payable for the month: $(1,538 + 1,453 + 20,400 - 17,000 - 1,000 - 850) = \text{RMB } 4,541$ 1·0 <hr/> 10 |
| | (b) | (1) The general provision is not tax allowable and RMB 30,000 should be added back to the accounting profit of year one. 1·0 |

| | Marks |
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| (2) A specific stock write off will be allowable if the write off is incurred in the course of business with the tax bureau's approval. | 2·0 |
| (3) Given that the provision of RMB 30,000 was added back in calculating the taxable profit in year one, the write back RMB 5,000 should not be treated as taxable income in year two. | <u>2·0</u> |
| | <u>5·0</u> |
| | <u>15</u> |
| | |
| 5 (a) The tax authority will impose a period for the taxpayer to remedy the situation and, if no remedy is made within the period, may impose a fine up to RMB 2,000. If the case is serious, the tax authority may impose a fine greater than RMB 2,000 but not more than RMB 10,000. | 2 |
| (b) If a withholding agent does not perform its statutory duty to withhold tax under the relevant tax laws, the tax authority will pursue the tax from the taxpayer and impose a fine of over 50% but no more than three times the tax on the agent. | 2 |
| (c) Where a tax payer or tax withholding agent fails to make a tax filing within the prescribed time limit, the tax authority will order the failure to be rectified within a prescribed time limit and impose a fine up to RMB 2,000. If the taxpayer or withholding agent still fails to comply, the tax authority may impose a fine greater than RMB 2,000 but not more than RMB 10,000. | 2 |
| (d) Where a tax payer fraudulently gains an export tax refund by deceptive means such as fraudulently declaring the export, the tax authority will pursue the repayment of the tax refund and impose a fine of over one time but not more than five times the tax refund. | |
| Criminal liability may also be pursued when a term of imprisonment ranging from below five years to a life sentence may be imposed depending on the seriousness of the offence. | <u>4</u> |
| | <u>10</u> |