

Fundamentals Level – Skills Module

Taxation (China)

Thursday 9 June 2016



Time allowed

Reading and planning: 15 minutes

Writing: 3 hours

This question paper is divided into two sections:

Section A – ALL 15 questions are compulsory and **MUST** be attempted

Section B – ALL SIX questions are compulsory and **MUST** be attempted

Tax rates and allowances are on pages 2–3.

Do NOT open this question paper until instructed by the supervisor.

During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.

Do NOT record any of your answers on the question paper.

This question paper must not be removed from the examination hall.

Think Ahead

ACCA

Paper F6 (CHN)

The Association of
Chartered Certified
Accountants

SUPPLEMENTARY INSTRUCTIONS

1. Calculations and workings need only be made to the nearest RMB.
2. All apportionments should be made to the nearest month.
3. All workings should be shown in Section B.

TAX RATES AND ALLOWANCES

The following tax rates and allowances are to be used in answering the questions.

Enterprise income tax

	Rate
Income tax for resident enterprises and non-resident enterprises with an establishment in China	25%
Income tax for specific China sourced income of non-resident enterprises	10%

Deduction limits on certain expenses

Employment welfare expenses	14% of total wages
Labour union expenses	2% of total wages
Employee training expenses	2.5% of total wages*
Donations	12% of the accounting profits
Entertainment expenses	60% of the amount subject to a maximum of 0.5% of the sales/business income of the year.
Advertising and promotion expenses	15% of the sales/business income of the year*

*except for certain special industries

Individual income tax

Entrepreneurs who receive production or operations income derived from private industrial or commercial operations

Level	Annual taxable income (RMB)	Rate %	Quick deduction factor (RMB)
1	Up to and including 15,000	5	0
2	Over 15,000 to 30,000	10	750
3	Over 30,000 to 60,000	20	3,750
4	Over 60,000 to 100,000	30	9,750
5	Over 100,000	35	14,750

Allowance per annum RMB42,000

Employment income

Level	Taxable income on which employee bears the tax/employer bears the tax (RMB)	Rate %	Quick deduction factor (RMB)
1	Up to and including 1,500/1,455	3	0
2	Over 1,500 to 4,500/1,455 to 4,155	10	105
3	Over 4,500 to 9,000/4,155 to 7,755	20	555
4	Over 9,000 to 35,000/7,755 to 27,255	25	1,005
5	Over 35,000 to 55,000/27,255 to 41,255	30	2,755
6	Over 55,000 to 80,000/41,255 to 57,505	35	5,505
7	Over 80,000/57,505	45	13,505

Monthly personal allowance for a China local	RMB3,500
Additional allowance for expatriate employees	RMB1,300

Individual service income

Before tax income (RMB)	Rate %	Quick deduction factor (RMB)
Up to and including 20,000	20	0
Over 20,000 to 50,000	30	2,000
Over 50,000	40	7,000

Allowance each time for individual service income, income from manuscripts, royalties and rental of property

RMB4,000 and below	RMB800
Over RMB4,000	20%

Income from:

Manuscripts, royalties, interest, dividends, rental of property, transfer of property, incidental income and other income 20%

Donations of individuals

Limited to: 30% of the taxable income; or
100% if the donation is made to certain funds approved by the government

Value added tax (VAT)

	Rate
For importation of goods depending on the itemised goods	17%/13%
For small-scale taxpayers and simplified method	3%
For general taxpayers for the sale of itemised goods, processing, and repairing	17%
for the sale or import of itemised goods	13%
for the sale of certain agricultural products	exempt
input tax credit for agricultural products	13%

VAT pilot programme

Industries	Rate
Transportation, postal and certain telecom services	11%
R&D and technical services, IT services, cultural and innovation services, logistics auxiliary services, attestation and consulting services, and broadcasting, film and television and certain telecom services	6%
Tangible movable property leasing services	17%

Note: The above rates are based on the pilot rules published by 30 September 2015. The new rules issued from 1 October 2015 onwards are not examinable in the 2016 exams.

Business tax

Industries	Rate
Construction, culture and sports	3%
Finance and insurance services, transfer of intangible property, sale of immovable property	5%
Entertainment	5%~20%

Land appreciation tax

Level	The ratio of increased value against the value of deductible items	Rate	Quick deduction ratio
1	No more than 50%	30%	0
2	Over 50% to 100%	40%	5%
3	Over 100% to 200%	50%	15%
4	Over 200%	60%	35%

Exchange rate

USD1 = RMB6

Section B – ALL SIX questions are compulsory and MUST be attempted

Please write your answers to all parts of these questions on the lined pages within the Candidate Answer Booklet.

- 1 Taip Ltd is a foreign investment enterprise which has been a qualified software enterprise for enterprise income tax (EIT) since its inception in 2010. Taip Ltd produces software products in Mainland China and exports these products to associated companies in the Hong Kong Special Administrative Region for further sale to European customers. Taip Ltd's total costs, profits/(losses) and applicable tax rates are summarised below:

Year	2010 RMB '000	2011 RMB '000	2012 RMB '000	2013 RMB '000	2014 RMB '000
Total costs	7,100	9,300	12,000	15,000	21,000
Profit/(loss)	(1,530)	810	960	1,020	1,350
Tax rate	–	–	0%	0%	12.5%

In 2015 the tax authorities conducted a transfer pricing audit and concluded that Taip Ltd should adjust its profit based on a mark-up of 10% on total costs for all five years, 2010 to 2014.

Required:

- (a) List the four methods (other than cost plus) which the tax authorities can use for transfer pricing adjustments.

Note: No mark will be given for stating 'other method'. (4 marks)

- (b) Calculate the total amount of additional enterprise income tax (EIT) payable by Taip Ltd for the years 2010 to 2014 inclusive. (6 marks)

(10 marks)

- 2** Trinity Ltd is a production and trading company which sells cosmetics. In 2015 Trinity Ltd carried out the following transactions (except where stated otherwise, the amounts are exclusive of value added tax (VAT)):
- (1) Imported 10,000 cosmetic packs from France at a cost including freight and insurance (CIF) of USD100,000. The French supplier granted Trinity Ltd an early settlement discount of 2%. Trinity Ltd sold 8,000 of the imported cosmetic packs to a sole distribution agent, Beast Co, for RMB2,350,000. Trinity Ltd granted Beast Co an early settlement discount of RMB50,000.
 - (2) Purchased lipsticks from a manufacturer for RMB400,000. The manufacturer paid consumption tax on the production and sale of the lipsticks. The lipsticks were exported to a Vietnam customer for USD300,000.
 - (3) Purchased chemicals for RMB85,000 for use in the production of face powder. The total turnover from the sale of the face powder in 2015 was RMB250,000. The unsold inventory of face powder at 31 December 2015 had a cost of RMB150,000.
 - (4) Purchased 1,000 eyeliners for RMB10,000. All these eyeliners were given to customers as free gifts. The retail price of each eyeliner is RMB30 (VAT inclusive).

Required:

Calculate the following amounts payable by Trinity Ltd for 2015:

- (a) The customs duty and consumption tax on the importation of the cosmetic packs.**

Notes:

1. The customs duty rate on cosmetics is 6.5%.
2. The consumption tax rate on cosmetics is 30%. (2 marks)

- (b) The export value added tax (VAT) refundable on the lipsticks.**

Note: The VAT refund rate for lipsticks is 13%. (1 mark)

- (c) The consumption tax on the production and sale of the face powder.** (1 mark)

- (d) The total output VAT and total input/import VAT credit as a result of transactions (1) to (4). State zero (0) for any transaction(s) which do not have a VAT impact.** (6 marks)

(10 marks)

- 3 (a) **State ANY TWO major differences between a direct tax and an indirect tax.** (2 marks)
- (b) **State two direct taxes and two indirect taxes levied in China.** (2 marks)
- (c) In January 2014 Tee Ltd received approval from the local tax bureau on a tax exemption application. The amount of tax which was exempt for 2014 amounted to RMB5 million. In December 2015 the tax bureau found that it had made a wrong decision.

Required:

State, with reason(s), whether the tax bureau can require Tee Ltd to pay back the amount of tax previously exempt. (2 marks)

- (d) **State whether the tax authorities can impose each of the following administrative actions on taxpayers:**
- (i) imprisonment;
 - (ii) stop a tax refund on exports;
 - (iii) stop providing VAT special invoices;
 - (iv) force the closure of the business of the taxpayer.

Note: You are not required to give any reasons. (2 marks)

- (e) **Briefly explain the method the tax bureau will normally use to impose enterprise income tax on a company which has lost all of its accounting records due to a fire.** (2 marks)

(10 marks)

4 (a) Design Ltd provides computer design services to overseas clients. The company's accountant has informed the chief executive officer that there are three alternative value added tax (VAT) policies which Design Ltd can choose to adopt:

- (1) Taxable
- (2) Zero rated
- (3) VAT exempt

The following items from Design Ltd's budget for 2016 are relevant to its VAT position:

	RMB
Amount expected to be collected from overseas clients in 2016	9,805,000
New computers to be purchased in January 2016 with an expected useful life of three years with no scrap value. This amount is VAT inclusive and the supplier is a VAT general taxpayer who can provide a VAT special invoice	3,500,000
Other service expenses in 2016. This amount is VAT inclusive and VAT special invoices at 6% can be obtained for all items	210,000

Required:

Assuming that there are no other transactions, costs or expenses in the year 2016, for each of the three alternative value added tax (VAT) policies available to Design Ltd:

- (i) Calculate the amount of VAT payable or refundable for the year 2016. (4 marks)
 - (ii) Calculate the gross profit for the year 2016. (5 marks)
- (b) State ONE major reason for the tax reform of merging business tax into value added tax. (1 mark)

(10 marks)

5 (a) Mrs Li had the following sources of income in the year 2015:

- (1) She won a prize of RMB876,000 from the Sports Lottery.
- (2) She received an insurance compensation of RMB60,000 from a medical and life policy. She had paid a premium of RMB40,000 for this policy.
- (3) She placed RMB150,000 on a time deposit account with a bank for six months and received interest at the rate of 6% per annum.
- (4) She received a villa from her husband as part of their divorce settlement. The villa had cost RMB5,000,000 and is currently valued at RMB9,500,000.
- (5) She had invested in SH Petro, an A-share listed company, in 2010 and in October 2015 received a dividend of RMB5,000 from this company.
- (6) She sold the shares in her personal company to a foreign investor and received RMB8,000,000 for agreeing not to compete in the same business for three years.

Required:

Calculate the individual income tax (IIT) payable by Mrs Li on each of her items of income (1) to (6) for 2015. Clearly identify any item(s) which are not taxable as either 'tax exempt' or 'not subject to IIT'.

Note: Ignore value added tax and business tax.

(5 marks)

(b) Ms Wu is an expatriate working and living in Guangzhou. Her remuneration package for 2015 is as follows:

	RMB	RMB
Housing allowance on a reimbursement basis	10,000	
Meal allowance on a reimbursement basis	5,000	
Tuition fees for her children studying in Hong Kong on a reimbursement basis	12,000	
Medical insurance on a reimbursement basis	500	
Salary	12,500	
Monthly total	<u>40,000</u>	
Total for a 12-month period (RMB40,000 x 12)		480,000
First half-year performance-related bonus payable in June		360,000
Second half-year performance-related bonus payable in December		360,000
Total for the year		<u>1,200,000</u>

Receipts/invoices can be obtained for all items received on a reimbursement basis.

Required:

Calculate the total individual income tax (IIT) payable by Ms Wu on her employment income for 2015 on the assumption that Ms Wu qualifies for all possible tax incentives allowable under the IIT rules. (6 marks)

- (c) Mr Huang is a China tax resident who has to file an annual individual income tax (IIT) return for 2015. His income and IIT withholding status for 2015 are as follows:

Type of income	Amount before taxation	Tax withheld
Salary from employers	Total salaries RMB11,400 per month for 12 months	IIT of RMB4,140 withheld and paid for the year 2015
Leasing out of unused residential property. The tenant is responsible for all the repairs and maintenance.	RMB20,000 per month for 12 months	0
Authorship fee from a European journal	USD2,500	European tax of USD200 withheld and paid

Required:

Calculate the individual income tax (IIT) which Mr Huang has to pay on filing his annual IIT return for 2015.

Note: Because the rental income is less than RMB30,000 per month it is exempt from value added tax/business tax. (4 marks)

(15 marks)

- 6 (a) GFH Ltd, a manufacturing company set up in Xi'an, produces and sells integrated circuits to an overseas associated company. It has not applied for the tax incentives for integrated circuits enterprises. GFH Ltd's statement of profit or loss for the year ended 31 December 2015 is as follows:

	RMB	RMB
Export sales		38,675,500
Cost of goods sold and expenses		<u>(36,508,700)</u>
		2,166,800
Government subsidy	210,500	
Royalties from an associated company in Vietnam	90,000	
Share of profit from an associated company in India	<u>123,100</u>	
		<u>423,600</u>
Profit for the year		<u>2,590,400</u>

The following information is relevant to the items charged/credited in the above statement of profit or loss:

- (1) The accountant has used the last in, first out (LIFO) method to value the inventories. If the first in, first out (FIFO) method were used, the cost of goods sold would have been reduced by RMB350,100.
- (2) The increase in the provision for obsolete inventory was RMB123,450.
- (3) A piece of equipment with a net book value of RMB80,000 was scrapped for nil proceeds.
- (4) RMB1,000,000 was paid to a senior production manager in lieu of notice for early dismissal.
- (5) In 2014, an antique vase was bought for RMB3,500,000 and put in the CEO's room for display. A ten-year economic life without scrap value has been used to calculate depreciation on this asset.
- (6) Research and development expenses of RMB123,000 were incurred for a project which qualifies for an additional tax deduction.
- (7) The salaries of the disabled employees hired by GFH Ltd in 2015 were RMB345,120. This cost qualified for the tax incentive.
- (8) A donation of RMB25,000 was made to some students of a remote school.
- (9) Interest at the rate of 25% per annum was paid on a loan of RMB8,000,000 from a finance institution in Xi'an. The interest rate of the People's Bank of China was 5%.
- (10) Entertainment expenses incurred were RMB5,210,200.
- (11) GFH Ltd acquired a new business in 2013 and paid RMB6,500,000 for the business' goodwill. This goodwill is being amortised over a period of ten years.
- (12) GFH Ltd acquired a patent from another company in 2014 and paid a fee of RMB3,200,000. This patent fee is being amortised over a period of ten years.
- (13) The dividend payable to the shareholder of GFH Ltd of RMB1,200,000 was treated as part of costs and expenses.
- (14) Newly acquired equipment costing RMB2,500,000 qualifies under the Safety Production Special Equipment Catalogue.
- (15) A warehouse was destroyed by a flood. The loss incurred of RMB150,000 was not covered by insurance.
- (16) Irrecoverable input value added tax (VAT) on an abnormal loss amounted to RMB119,000.
- (17) A subsidy of RMB3,000,000 was received from the Xi'an government for a specific project in 2013. The project was completed in 2015 and the amount spent on the project totalled RMB2,789,500. The balance of RMB210,500 was treated as income of 2015.
- (18) GFH Ltd has granted an associated company in Vietnam the right to use its technology. The royalty income received of RMB90,000 was after the deduction of 10% Vietnamese withholding tax.

(19) GFH Ltd invested in an associated company in India in 2010. The profit of RMB123,100 is the proportion of the associate company's profit attributable to GFH Ltd and is included in its consolidated accounts.

GFH Ltd pays enterprise income tax (EIT) at the standard rate.

Required:

Calculate the enterprise income tax (EIT) payable by GFH Ltd for the year 2015, assuming that GFH Ltd has made all the relevant applications.

Note: You should start your computation with the net profit figure of RMB2,590,400 and list all of the items referred to in notes (1) to (19) identifying any items which do not require adjustment by the use of zero (0).

(13 marks)

(b) The company's accountant has proposed that GFH Ltd should apply for the following enterprise income tax (EIT) incentives for the year 2015:

- (1) a qualified integrated circuit enterprise; and
- (2) an encouraged industry under the Central and Western catalogue.

Required:

State the preferential treatments available under each of these two enterprise income tax (EIT) incentives.

(2 marks)

(15 marks)

End of Question Paper