

Fundamentals Level – Skills Module

Taxation (China)

Thursday 10 December 2015



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.

The Association of Chartered Certified Accountants

Paper F6 (CHN)

ACCA

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

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%
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 2014. The new rules effective from 1 October 2014 are not examinable in the 2015 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 A – ALL 15 questions are compulsory and MUST be attempted

Please use the grid provided on page two of the Candidate Answer Booklet to record your answers to each multiple choice question. Do not write out the answers to the MCQs on the lined pages of the answer booklet. Each question is worth 2 marks.

1 Which government authorities promulgated the Enterprise Income Tax Law and the Consumption Tax Provisional Regulations?

- A The Standard Committee of the National People's Congress and the State Council
- B The State Council and the Ministry of Finance
- C The Ministry of Finance and the State Administration of Taxation
- D The State Administration of Taxation and the Standard Committee of the National People's Congress

2 Which of the following transactions is NOT subject to land appreciation tax (LAT)?

- A A state-owned enterprise contributed its land use right as capital to its subsidiary for the subsidiary to build a shopping mall
- B A local government transferred a land use right to a property developer
- C A property developer sold a standard residential property with a land appreciation value of 63%
- D An individual sold his self-used residence after owning it for one year

3 A yacht factory sold a yacht to an individual customer and received a total amount of RMB400,000. The consumption tax rate for yachts is 10%.

What are the amounts to be recorded in the factory's accounts for sales and consumption tax respectively?

- A RMB400,000 and RMB40,000
- B RMB310,800 and RMB31,080
- C RMB341,880 and RMB34,188
- D RMB376,068 and RMB37,607

4 The sales manager of a supermarket has proposed a marketing promotion of selling a pack of shampoo with a free bottle of hair-conditioner. This is termed as a 'buy-one-get-one-free' offer. The retail price (i.e. inclusive of value added tax (VAT)) of the items is as below:

Shampoo (on its own)	RMB50
Hair-conditioner (on its own)	RMB20
Offer pack of shampoo and hair-conditioner	RMB50

In January 2015, the supermarket sold 2,000 of the offer packs.

What is the amount of value added tax (VAT) charged on the sale of the 2,000 offer packs?

- A RMB14,530
- B RMB17,000
- C RMB20,342
- D RMB23,800

- 5 Mr Lee has licensed his new invention to a China company for a royalty of RMB200,000 per annum. Mr Lee is a not a China tax resident and he has not travelled to China in 2014.

What is the amount of individual income tax (IIT) payable by Mr Lee in 2014?

- A RMB0
- B RMB40,000
- C RMB22,400
- D RMB32,000

- 6 KINO Ltd is a company set up in China, which is subject to enterprise income tax (EIT) of 25%. KINO Ltd has a wholly (100%) owned subsidiary, Company A, set up in Country X.

In 2014, Company A had a profit of USD200,000 and paid enterprise income tax in Country X at the rate of 15% (USD30,000). Company A declared a dividend of USD170,000 and paid this to KINO Ltd after deduction of withholding income tax of 10% (USD17,000).

What is the additional enterprise income tax (EIT) which KINO Ltd will pay on the dividend income received from its subsidiary, Company A?

- A USD25,500
- B USD3,000
- C USD42,500
- D USD0

- 7 CA Ltd is a foreign-invested enterprise set up in Shanghai, China. CA Ltd declared a dividend of RMB500,000 to its investor, Hoo Ltd. Hoo Ltd is set up in the Cayman Islands, which does not have any tax treaty with China.

What are the amounts of enterprise income tax (EIT) and business tax respectively, which CA Ltd should withhold before remitting the dividend to Hoo Ltd?

- A RMB47,500 and RMB25,000
- B RMB50,000 and RMB25,000
- C RMB50,000 and RMB22,500
- D RMB50,000 and RMB0

- 8 A computer trading company took ten computers from its warehouse.

Which of the following uses of the computers will be classed as a deemed sale for BOTH value added tax (VAT) and enterprise income tax (EIT)?

- A To be used in the company's offices as fixed assets
- B To be given as souvenirs to the company's customers
- C To be sent to the company's branch office for sale
- D To be scrapped as they were no longer saleable

- 9 Xuno Ltd was set up in Shenzhen in 2007 and is subject to an enterprise income tax (EIT) rate of 25%. Xuno Ltd's taxable profits (losses) since its inception are summarised below:

	2007	2008	2009	2010	2011	2012	2013	In RMB 2014
Profit (loss)	(100,000)	(200,000)	(150,000)	(120,000)	25,000	34,000	138,000	510,000

What is the amount of enterprise income tax (EIT) payable by Xuno Ltd in 2014?

- A RMB34,250
 B RMB90,000
 C RMB127,500
 D RMB60,000
- 10 **Which of the following imports to China from overseas can be exempt or temporarily exempt from China customs duty?**
- (1) The importation of goods into a China free trade zone
 (2) The importation of equipment under an operating lease
 (3) The importation of raw materials under a processing trade
 (4) The importation of raw materials under a general trade
- A 1, 2, 3 and 4
 B 1, 2 and 3 only
 C 1 and 3 only
 D 2 and 4 only
- 11 Carti Ltd is a Beijing company which trades in light bulbs. In December 2014, Carti Ltd purchased light bulbs for RMB100,000 (excluding value added tax (VAT)) and a VAT special invoice was obtained. Carti Ltd exported the light bulbs to Europe for RMB150,000. The export VAT refund rate for light bulbs is 16%.

What is the amount of the value added tax (VAT) refund which Carti Ltd can receive?

- A RMB16,000
 B RMB24,000
 C RMB8,000
 D RMB500

- 12 Ms Wang won a smart phone with a market value of RMB3,000 in a lucky draw at a supermarket. The supermarket agreed to bear all of the taxes for the winners of the lucky draw.

What is the individual income tax (IIT) payable on Ms Wang's lucky draw prize and who will be responsible for paying it to the tax bureau?

	Amount of IIT (RMB)	Tax payable/withheld by
A	750	Ms Wang
B	600	Ms Wang
C	750	Supermarket
D	600	Supermarket

- 13** SHL Ltd, a property developer, developed a shopping mall. SHL Ltd acquired the land use right for RMB10 million and incurred construction costs of RMB12 million. The shopping mall was sold for RMB32 million.

What is the amount of business tax payable on the sale of the shopping mall?

- A** RMB1.6 million
- B** RMB1.1 million
- C** RMB0.5 million
- D** RMB1 million

- 14** The accountant of Zeta Ltd altered the amount charged on an invoice for purchases from RMB50 to RMB50,000 so as to increase the deduction for enterprise income tax (EIT).

What is the type of offence Zeta Ltd has committed under the Tax Collection and Administrative Law?

- A** Transfer pricing
- B** Tax avoidance
- C** Tax evasion
- D** Fraudulence in the issuance of an invoice

- 15** Alpha Trading Ltd (Alpha) is a value added tax (VAT) general taxpayer. On 1 January 2014, Alpha lent RMB200,000 to Beta Ltd at an interest rate of 10% per annum.

What is the type and amount of turnover tax which Alpha Trading Ltd will pay on the interest income received for the year 2014?

- A** Business tax of RMB1,053
- B** Business tax of RMB1,000
- C** Value added tax of RMB3,400
- D** Value added tax of RMB1,200

(30 marks)

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 Lambda Ltd was set up in Guangzhou 12 years ago. The company has been continually loss making in recent years, and the shareholders decided to liquidate it in December 2014. The following assets were sold before the start of the liquidation process.

	Net book value per the accounts before disposal RMB	Selling price (tax inclusive amount) RMB	Notes
Factory building	1,600,000	6,000,000	(1)
Inventory of finished goods	460,000	460,000	(2)
Inventory of raw materials	230,000	200,000	(3)

Notes

- (1) The factory building was acquired 12 years ago for RMB4,000,000. The replacement cost of the same factory building in 2014 was RMB5,000,000.
- (2) The inventory of finished goods comprised self-produced cosmetics packs. Cosmetics packs with a cost of RMB20,000 were expired and needed to be destroyed. The remaining (unexpired) packs with a cost of RMB440,000 were sold on to another trader.
- (3) The inventory of raw materials comprised chemicals.

After carrying out all of the above transactions, Lambda Ltd had input value added tax (VAT) not yet credited of RMB135,600.

Required:

- (a) Calculate the amount of business tax and land appreciation tax (LAT) payable on the sale of the factory building.**

Notes:

1. City maintenance and construction tax and education levy should be calculated at 12% of business tax.
2. Ignore stamp duty. (4 marks)

- (b) Calculate the consumption tax payable on the sale of the cosmetics packs.**

Note: The consumption tax rate for cosmetics is 30%. (1 mark)

- (c) State, giving reasons, if the expired cosmetic packs would be treated as a value added tax (VAT) abnormal loss.** (2 marks)

- (d) Calculate the output VAT on the sale of the inventories (finished goods and raw materials).** (2 marks)

- (e) State whether Lambda Ltd can obtain a VAT refund on the liquidation of the company.** (1 mark)

(10 marks)

2 Mr Lin, a China tax resident, had the following incomes in February 2014.

(1) The payroll information relating to his employment with DSR Ltd for the month of February 2014 is as summarised below:

	RMB
Basic salary	4,500
Monthly meal allowance	3,000
Reimbursement of expenses on business trips	850
Air tickets and hotel charges for a vacation outside China	8,200
Employer's social security contributions	3,250
Employee's social security contributions	1,250

- (2) He is a part-time lecturer at the Shanghai Design Institute. He gave three lectures in February 2014 and he received a lecturing fee of RMB1,000 for each lecture.
- (3) He received an insurance compensation of RMB2,000 because of a delayed flight.
- (4) During the Spring Festival, his parents gave him RMB10,000 red-packet money.
- (5) He won USD1,000 in a lottery when he was on vacation outside China. He paid foreign tax of USD150 on this income.
- (6) He had an article published in the January 2014 edition of a journal. The authorship fee of RMB1,000 was paid to him in February 2014.
- (7) He is a non-executive director of a listed company. In February 2014, he received a director's fee of RMB60,000.
- (8) He was the only shareholder of Little Ltd. He sold all of his shares in this company for RMB1,000,000 on 28 February 2014, when the net asset value of Little Ltd was RMB800,000. The purchase cost of the shares was RMB400,000.

Required:

Calculate the individual income tax (IIT) payable by Mr Lin on each of his items of income ((1) to (8)) for February 2014. State clearly if any item is tax exempt or not taxable.

Note: Ignore value added tax and business tax.

(10 marks)

- 3 (a)** Phi Ltd is a company set up in Guangzhou. In 2014 Phi Ltd incurred the following expenses:
- (1) A consultancy fee of RMB3,500 for services provided in China paid to Mr Xie, who is a China tax resident.
 - (2) A consultancy fee of RMB70,000 for services provided in China paid to Ms Ma, who is not a China tax resident.
 - (3) A royalty of RMB80,000 paid to Deji Ltd, which is a China tax resident enterprise.
 - (4) A royalty of RMB90,000 paid to Backa Ltd, which is not a China tax resident enterprise.

Required:

For each of the four payments, state whether Phi Ltd will be a withholding agent for income tax, and where Phi Ltd is the withholding agent, calculate the amount of income tax to be withheld.

Note: Ignore value added tax and business tax, and any tax incentives available under tax treaties.

(7 marks)

- (b)** Jack has set up an e-shop selling goods via an internet platform. His total sales in 2014 were RMB400,000. He did not register with the tax authorities or pay any taxes in 2014. This was discovered by the tax bureaus in 2015.

Required:

State the possible consequences Jack may be exposed to under the Tax Collection and Administrative Law, as a result of his failure to comply with the tax registration and tax payment requirements.

(3 marks)

(10 marks)

- 4 (a)** Chris and Wendy graduated from high school in 2012 and set up a hair-dressing shop in the form of a limited company, Hair Ltd. The total amounts received from the customers of Hair Ltd in each of the last three years has been as follows. The income is evenly spread over the 12 months.

Year	RMB
2012	200,000
2013	300,000
2014	300,000

In order to encourage small enterprises, the State Council has granted the following tax reliefs:

- Before 1 August 2014, an entity with a turnover of less than RMB20,000 per month was exempt from business tax (BT).
- For the period from 1 August 2014 to 31 December 2018, the exemption threshold was increased to RMB30,000 per month.

Hair Ltd files business tax on a monthly basis.

Required:

- (i) Calculate the business tax payable by Hair Ltd in each of the three years, 2012, 2013 and 2014.** (4 marks)
- (ii) Calculate the enterprise income tax (EIT) of Hair Ltd of 2014.** (2 marks)

- (b) With respect to the three turnover taxes in China, namely, value added tax (VAT), business tax (BT) and consumption tax (CT):**

- (i) State which two of the turnover taxes are mutually exclusive.** (1 mark)
- (ii) Briefly explain the purpose and effect of levying consumption tax.** (3 marks)

(10 marks)

5 (a) Mr Xu, a domestic Chinese, is a designer. He is considering the following four options:

Option A: Joining Delta Ltd as a manager with a monthly salary of RMB40,000 and an annual bonus of RMB100,000 payable in December each year.

Option B: Providing services to Delta Ltd as a consultant for a consultancy fee of RMB50,000 per month.

Option C: Setting up his own sole proprietorship. He will pay himself a monthly salary of RMB20,000 from this sole proprietorship. For 2014 the net profit of the sole proprietorship after charging Mr Xu's salary is expected to be RMB420,000.

Option D: Setting up a limited company, Xupa Ltd. He will pay himself a monthly salary of RMB20,000 from Xupa Ltd. For 2014 the net profit of the company after charging Mr Xu's salary is expected to be RMB420,000. Xupa Ltd will pay enterprise income tax at the rate of 25% and distribute all of its profit after tax to its shareholder, Mr Xu, as a dividend.

Required:

Calculate the individual income tax (IIT) payable by Mr Xu for 2014 under each of the four options.

Note: Ignore value added tax and business tax.

(10 marks)

(b) **State, giving reasons, whether the following persons will be subject to individual income tax in China on their worldwide income in 2014:**

(1) **Ms Wang has her household in Xiamen and holds a China identity card. She has been studying in Australia since 2010 and has not returned to China for the last six years, including in 2014.**

(2) **Mr Beth is a US citizen, who has lived in China working for a non-government organisation since 2010. He has not travelled outside China for the last six years, including in 2014.**

(3) **Ms Ruth is an Australian citizen. She travelled to China and stayed in China for a total of 250 days in 2014.**

(5 marks)

(15 marks)

- 6 Sware Ltd is a software company set up in the Xinjiang Autonomous Region. Sware Ltd's enterprise income tax (EIT) rate is 25%. The company's accountant has prepared the following statement of profit or loss for the year end 31 December 2014.

Notes	RMB	RMB
(1) Sales		29,345,000
(2) Wages, salaries and staff welfare	9,393,600	
(3) Entertainment	967,000	
(4) Bad debt written off	65,000	
(5) Provision for specific doubtful debts	78,000	
(6) Research and development costs	2,140,000	
(7) Compensation paid to customers	97,600	
(8) Penalty paid to the State Administration for Industry and Commerce	120,000	
(9) Expenditure on Project Pibeta	680,000	
(10) Loss of assets destroyed in a fire	216,000	
(11) Interim dividend	5,000,000	
12) Donation to China Red-Cross	80,000	
(13) Donation to a school	50,000	
(14) Goodwill written off	6,260,000	
Other costs and expenses	10,550,050	
		(35,697,250)
Other income		
(15) Interest income from a subsidiary	360,000	
(16) Profit on sale of government bonds	215,000	
(17) Dividend income from A-shares	92,100	
(18) Specific government subsidy for Project Pibeta	2,300,000	
		2,967,100
Loss for the year		(3,385,150)

Notes:

- Customers who settle their bills within 30 days receive an early payment discount of 2%. Discounts totalling RMB55,000 were deducted directly from sales.
- Staff welfare is calculated and provided for in the accounts at 14% of the wages and salaries paid of RMB8,240,000. The actual amount of staff welfare expenses incurred was RMB1,026,350.
- Entertainment expenses incurred in the year 2014 were as charged in the profit or loss account, i.e. RMB967,000. Entertainment expenses incurred in 2013 in excess of the deduction threshold were RMB68,000.
- The bad debt related to a debtor who went bankrupt in 2013. The accountant has submitted a report to the tax bureau in relation to this bad debt.
- The specific provision for doubtful debts relates to an amount which was difficult to recover. The accountant has submitted a report to the tax bureau in relation to this specific provision.
- These research and development costs qualified for an additional deduction.
- The compensation was due to the late delivery of software to the customers.
- Sware Ltd was penalised by the State Administration for Industry and Commerce because of misstatements on its website.
- Project Pibeta relates to the piloting of software encouraged by the government. The project was started in 2013 and is expected to be completed in 2016. The project is subsidised by the government (see (18) below).
- A fire destroyed a warehouse with a net book value of RMB2,500,000. Sware Ltd received insurance compensation of RMB2,284,000. The accountant has submitted a report to the tax bureau in relation to this loss.

- (11) Sware Ltd declared an interim dividend of RMB5,000,000 in 2014. Individual income tax was withheld from this interim dividend before distribution to the company's shareholders.
- (12) A donation receipt was obtained for the donation to China Red-Cross.
- (13) A donation receipt was obtained for the donation to the school.
- (14) Sware Ltd acquired a new subsidiary in 2014 and wrote off the goodwill incurred on this acquisition.
- (15) Sware Ltd lent some of its surplus funds to its Shanghai subsidiary at an interest rate of 36% per annum. The market interest rate was 8% per annum.
- (16) Sware Ltd has invested some of its surplus funds in the capital market. The profit on the sale of government bonds included interest of RMB15,000.
- (17) The A-shares were acquired in 2012.
- (18) The government granted Sware Ltd a specific financial subsidy to cover all of the expenditure on Project Pibeta.

Required:

- (a) Calculate the enterprise income tax (EIT) payable by Sware Ltd for the year 2014.**

Note: You should start your computation with the net loss figure of RMB3,385,150 and list all of the items referred to in notes (1) to (18) identifying any items which do not require adjustment by the use of zero (0).

(11 marks)

- (b) Identify and briefly describe ANY TWO enterprise income tax (EIT) preferential policies which Sware Ltd could consider applying, in addition to the qualified research and development additional deduction.**

(4 marks)

(15 marks)

End of Question Paper