

Fundamentals Level – Skills Module

Taxation (China)

Tuesday 6 December 2011

Time allowed

Reading and planning: 15 minutes

Writing: 3 hours

ALL FIVE questions are compulsory and MUST be attempted.
Tax rates and allowances are on pages 2–3.

Do NOT open this 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.

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

The Association of Chartered Certified Accountants

Paper F6 (CHN)

The ACCA logo consists of the letters 'ACCA' in a bold, white, sans-serif font, centered within a solid black square.

SUPPLEMENTARY INSTRUCTIONS

1. Calculations and workings need only be made to the nearest RMB.
2. Apportionments should be made to the nearest month.
3. All workings should be shown.

TAX RATES AND ALLOWANCES

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

Enterprise income tax

Income tax for domestic and foreign enterprises	Rate 25%
Entrepreneurs who receive production or operation income derived from private industrial or commercial enterprises	

Level	Annual taxable income (RMB)	Rate	Quick deduction factor (RMB)
1	5,000 or below	5%	0
2	5,001– 10,000	10%	250
3	10,001 – 30,000	20%	1,250
4	30,001 – 50,000	30%	4,250
5	Over 50,000	35%	6,750

Individual income tax

Employment income

Grade	Taxable income on which employee bears the tax/employer bears the tax (RMB)	Rate %	Quick deduction factor (RMB)
1	500/475 or below	5	0
2	501 – 2,000/476 – 1,825	10	25
3	2,001 – 5,000/1,826 – 4,375	15	125
4	5,001 – 20,000/4,376 – 16,375	20	375
5	20,001 – 40,000/16,376 – 31,375	25	1,375
6	40,001 – 60,000/31,376 – 45,375	30	3,375
7	60,001 – 80,000/45,376 – 58,375	35	6,375
8	80,001 – 100,000/58,376 – 70,375	40	10,375
9	Over 100,000/70,376	45	15,375

For other income

each time below RMB 800	Rate 0%
each time from RMB 801 to RMB 4,000	20%
each time above RMB 4,000 (with 20% allowance)	20%

Income from services provided

for the part RMB 20,000 to RMB 50,000	30%
for the part above RMB 50,000	40%

Individual service income

Net of tax income (RMB)	Before tax income (RMB)	Rate %	Quick deduction factor (RMB)
1 – 16,000	1 – 20,000	20	0
16,001 – 37,000	20,001 – 50,000	30	2,000
37,001 and above	50,001 or above	40	7,000

Business tax

		Rate
Group A	transportation, construction, communication, culture and sports	3%
Group B	hotels, restaurants, tourism, warehousing, advertising, transfer of intangible property, sale of real estate	5%
Group C	finance	5%
Group D	recreation	5~20%

Land appreciation tax

	The ratio of increased value against the value of deductible items	Rate
For the part	50% or below	30%
For the part	above 50% to 100%	40%
For the part	above 100% to 200%	50%
For the part	above 200%	60%

Value added tax (VAT)

		Rate
For small-scale taxpayers		3%
For ordinary taxpayers	for the sale or import of itemised goods, processing, and repairing	17%
	for the sale or import of itemised goods	13%
	for transportation charges	7%

Allowances

Funds for enterprises

Trade union fund	2% of total basic wages
Employee welfare fund	14% of total basic wages
Employee training fund	2.5% of total basic wages

Donations

Enterprises	up to 12% of the accounting profits
Individuals	up to 30% of the taxable income 100% if donation made to certain funds approved by the government

Entertainment expenses

For domestic and foreign enterprises	60% of the amount subject to a maximum of 0.5% of the sales/business income of the year.
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ALL FIVE questions are compulsory and MUST be attempted

- 1 (a) The following is the statement of enterprise income tax (EIT) payable prepared by the accountant of Company P for the year 2010:

	RMB	RMB
Turnover		45,000,000
Cost of services (including salaries and bonuses paid to workers RMB 3,000,000)		<u>(30,000,000)</u>
Gross profit		15,000,000
Management expenses		(5,250,000)
The following amounts were included within the management expenses:		
Salaries and bonuses paid to staff	1,500,000	
* Refurbishing expense of the office	75,000	
* Business tax and late payment penalty (225,000 + 2,250)	227,250	
* Entertaining expense	300,000	
* Donation to an unrelated scientific research centre	22,500	
* Staff and workers benefits	750,000	
* Union expenses (note 1)	150,000	
* Staff and workers education expenses	75,000	
Investment income:		
* Overseas dividend (net of foreign income tax at 10%)		40,500
Financial expenses:		
* Interest expense for a loan borrowed by the investor for the fulfillment of his capital contribution obligation		(300,000)
Other loss:		
* Writing off of fixed asset (note 2)		(45,000)
Other income:		
* Writing off of a liability due to a creditor (note 3)		300,000
* Write back of debtors provision (note 4)		<u>150,000</u>
		<u>9,895,500</u>
Tax rate		25%
Tax payable		2,473,875

Notes:

- (1) The union has not yet been set up and the expense is a general provision.
- (2) The original cost of the fixed asset was RMB 150,000 and the accumulated depreciation was RMB 105,000, while the accumulated tax allowances claimed were RMB 120,000.
- (3) The creditor had been liquidated three years ago.
- (4) Last year (2009) was the first year a debtors provision was made. A general provision of RMB 500,000 was made but the whole amount was disallowed by the tax bureau. This year the management decided to write back part of provision amounting to RMB 150,000.

Required:

- (i) **Briefly comment on the correctness of the accountant's treatment of the 12 items marked with an asterisk (*) in the income tax calculation sheet;** (17 marks)
 - (ii) **Calculate the correct amount of enterprise income tax (EIT) payable by Company P for the year 2010.** (6 marks)
- (b) **Briefly explain the term 'arm's length principle' in the context of transactions between associated enterprises pursuant to the enterprise income tax law, together with the adjustment methods that may be used by the tax bureau in cases where this principle is not complied with.** (6 marks)

- (c) Company C, a limited company with equity of RMB 1,000,000, borrowed two loans from related companies:
- RMB 1,000,000 at a 7% annual interest rate from Company A; and
 - RMB 2,000,000 at an 8% annual interest rate from Company B.

The market interest rate for the equivalent loans is a 6% annual interest rate.

In 2010, the interest paid to Company A and Company B was RMB 70,000 and RMB 160,000 respectively. The total amount of interest of RMB 230,000 was allocated RMB 140,000 to interest expense and RMB 90,000 to construction in progress in Company C's accounts.

Required:

Calculate the amount of interest that will be disallowed for enterprise income tax under each of the account headings: interest expense and construction in progress. (6 marks)

(35 marks)

- 2 (a)** Mr Y, a local Chinese national, a professional writer and artist, had the following income during 2010:
- (1) Received income of RMB 45,000 for publishing the first edition of a book, and of RMB 15,000 for the second edition of the same book. The book was also published in a newspaper and he was paid RMB 5,250 for this.
 - (2) Sold one of his paintings for RMB 5,400.
 - (3) Gave a speech and was paid RMB 28,500.
 - (4) Acted as a translator for a movie and was paid RMB 60,000.
 - (5) Gave a speech in overseas country M and was paid the gross equivalent of RMB 27,000, from which the equivalent of RMB 6,750 in overseas tax was deducted at source.
 - (6) Sold one of his paintings in overseas country H, and was paid the gross equivalent of RMB 15,000, from which the equivalent of RMB 2,250 in overseas tax was deducted at source.
 - (7) Received interest of RMB 7,500 on a loan he had made to a domestic enterprise.

Required:

- (i) **Calculate the individual income tax (IIT) payable by Mr Y in respect of each of the items (1) to (7);** (12 marks)
 - (ii) **State how and when any IIT due on Mr Y's overseas income will be reported and paid.** (3 marks)
- (b)**
- (i) **State when a withholding agent must report and pay the individual income tax (IIT) deducted on a monthly basis from employment income;** (1 mark)
 - (ii) **List ANY FOUR situations in which an individual taxpayer needs to do self-reporting for IIT purposes.** (4 marks)
- (20 marks)**

- 3 (a)** Enterprise G, a general value added tax payer incorporated in Shenzhen for more than 20 years, had the following transactions in the month of May 2010. Some of the enterprises sales are subject to the standard value added tax (VAT) rate, while others are exempt (VAT) activities. All figures are stated including any applicable VAT:
- (1) Sold product A (a standard VAT rate item) for RMB 400,000 and product B (a VAT exempt item) for RMB 350,000.
 - (2) In addition to the sales in (1) above, distributed product A with a market value of RMB 20,000 for staff welfare benefit.
 - (3) Purchased RMB 500,000 production materials, of which RMB 50,000 was used for a self-constructed building.
 - (4) Purchased RMB 200,000 agriculture product, of which RMB 20,000 was used for staff welfare benefit.
 - (5) Purchased a production machine for RMB 100,000 and sold a used machine for RMB 10,000. The used machine had been bought in May 2009 and used by the enterprise ever since then.

Required:

Calculate the value added tax (VAT) payable by Enterprise G for the month of May 2010. (7 marks)

- (b)** Enterprise H, a small-scale value added tax payer, had the following transactions in the month of May 2010. All figures are stated including VAT:
- (1) Sold product for RMB 20,000.
 - (2) Purchased RMB 500,000 of production materials.
 - (3) Purchased a production machine for RMB 100,000 and sold a used machine for RMB 10,000. The used machine had been bought in May 2009 and used by the enterprise ever since then.

Required:

Calculate the value added tax (VAT) payable by Enterprise H on each of the above transactions, giving brief explanations of their treatment. (4 marks)

- (c)** Company X, a property developer, had the following transactions in 2010:
- (1) Donated a new building to a high school. The cost of construction of the building was RMB 500,000 and the deemed profit rate is 10%.
 - (2) Contributed an office building as part of a capital contribution. The cost of the building was RMB 600,000 and the market value RMB 800,000.
 - (3) Sold an equity holding of unlisted stock for RMB 900,000. The equity holding had been obtained by the contribution of a factory building by Company X which had cost RMB 300,000.
 - (4) Obtained a six-month bank loan of RMB 2,000,000 from 1 July 2010 with the pledge of a shop owned by the company. During the loan period, the bank did not charge any interest, but instead the bank had the right to use the shop rent free. The market interest rate for a similar loan is 6% per year. At the end of the loan period, Company X sold the shop for a price which gave it RMB 1,000,000 more than the amount needed to repay the bank loan.

Required:

Calculate the business tax (BT) payable by Company X as a result of each of the above transactions (1) to (4), giving brief explanations of their treatment. (6 marks)

- (d)** State the THREE conditions that must be met for a transportation fee paid by the seller to be excluded from the sale consideration for the purposes of value added tax (VAT). (3 marks)

(20 marks)

- 4 (a) Company K carried out the following transactions:
- (1) Imported a vehicle costing RMB 300,000 and paid transportation costs of USD 10,000 for the journey from the overseas supplier to the port in China.
 - (2) Shipped a machine with a value of RMB 500,000 overseas for repair and paid for materials of USD 10,000 and a repairing fee of USD 30,000. The machine was shipped back to China in the same month.
 - (3) Subcontracted some domestic raw materials valued at RMB 200,000 to an overseas company. The related fee and transportation costs were USD 100,000 and USD 20,000 respectively.
 - (4) Imported raw materials costing RMB 30,000,000 and paid transportation costs of USD 50,000 for the journey from the overseas supplier to the port in China. After the arrival of the materials, Company K discovered that 20% of the materials had a quality problem. The supplier agreed to ship a further 20% replacement materials at no cost to Company K in the same month. Both parties agreed that the quality problem goods should be kept in China.

Required:

Calculate the customs tariff, consumption tax (CT) and value added tax (VAT) payable by Company K as a result of each of the above transactions.

Note: for the purposes of your calculations you should assume that:

- (1) The customs tariff for all kinds of imported goods is 20%.
- (2) The rate of consumption tax (CT) is 10%.
- (3) The USD:RMB exchange rate is 1:6.6 (12 marks)

- (b) **Briefly explain the procedures, including any time limits, for the declaration and payment of the customs tariff due on importation.** (3 marks)

(15 marks)

- 5 **Briefly explain the consequences of the following actions, including any fines or other penalty that may be imposed:**

- (a) **Failure to keep or maintain proper accounting records/vouchers.** (2 marks)
- (b) **Failure to file a return within the prescribed time limit.** (2 marks)
- (c) **Failure to file a return and hence not paying or paying less tax than is duly payable.** (1 mark)
- (d) **Failure to pay tax by concealment of property.** (3 marks)
- (e) **Refusal to pay tax by violence or menace.** (2 marks)

(10 marks)

End of Question Paper