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# Answers

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Section A

Marks

1 C

2 D

Per Article 86 of the Tax Collection and Administrative Law, the statute of limitation for an administrative penalty on non-compliances is five years.

3 C

4 A

5 A

6 D

Delivery of finished goods to a branch in another city for sale is a deemed sale for VAT purposes but delivery to a branch for storage is not a deemed sale.

7 D

$$(20,000 + 180,000) = \text{RMB}200,000$$

8 B

$$(250,000 - 100,000) \times 5\% = \text{RMB}7,500$$

9 A

$$\text{USD}500,000 \times 12\% \times 10\% = \text{USD}6,000$$

10 C

$$20,000 \times (1 - 20\%) \times 20\% \times 70\% + (3,000 - 800) \times 20\% \times 70\% = \text{RMB}2,548$$

11 B

$$500,000 \times 20\% \times 25\% = \text{RMB}25,000$$

12 A

13 B

14 C

$$(1,000,000 + 44,000 + 66,000) \times 10\% = \text{RMB}111,000$$

15 B

$$[200,000 - (10,000 + 60,000 - 13,000)] \times 30\% = \text{RMB}42,900$$

2 marks each

30

## Section B

Marks

## 1 (a) Prop Ltd – Land appreciation tax (LAT)

- (i) Ordinary standard residential property sold by a property developer will be exempt from land appreciation tax (LAT) if the land appreciation value is no more than 20% of the total deduction. 1

## (ii) LAT on Project K

	RMB (in millions)	RMB (in millions)	
Sale proceeds		600	
Cost of land use right	110		0.5
Deed tax	3.3		0.5
Cost of constructions	170		0.5
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Total land costs and construction costs		283.3	
Interest on bank loan		50	0.5
Management and administrative expenses (capped at 5% x 283.3)		14.165	1
Sales taxes (business tax + city maintenance and construction tax [(600 x 5%) + (600 x 5% x 12%)])		33.6	1
Additional deduction for property developer (283.3 x 20%)		56.66	1
		<hr/>	
Total deduction		437.725	
Land appreciation value		162.275	
% appreciation (162.275/437.725)		37%	0.5
LAT rate		30%	0.5
LAT liability		<hr/> <hr/>	<hr/>
			<u>6</u>

## (b) Manu Ltd – Land appreciation tax (LAT) on the sale of factory premises

	RMB (in millions)	RMB (in millions)	
Sale proceeds		200	
Cost of building	90		0.5
Additional deduction for used property (90 x 5% x 18 years)	81		1
Sales taxes (business tax + city maintenance and construction tax = [(200 – 90) x 5% + (200 – 90) x 5% x 12%])	6.16		0.5
	<hr/>		
Total deductions		177.16	
Land appreciation value		<hr/>	
		22.84	
% appreciation (22.84/177.16)		12.9%	0.5
LAT rate		30%	0.5
LAT		<hr/> <hr/>	<hr/>
			<u>3</u>
			<u>10</u>

- 2 (a) (i) Under the Enterprise Income Tax law [Article 47], if an enterprise carries out any business arrangements without a reasonable commercial purpose, which result in the lowering of its taxable income, the tax authorities will be authorised to make adjustments using all reasonable methods. 2

- (ii) An appeal against the tax imposed by the local tax authority can only be made if the tax requested has been paid and the application is made within 60 days of the tax payment. 2

Therefore, as BVI Co-XX has not made payment of the tax due, it cannot appeal against the decision. 1

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- (b) (i) The interest payable by the Shanghai company to the Guangxi company should be determined on an arm's length basis. Where this is not the case, the tax authority can disallow a deduction of interest to the Shanghai company in excess of the market interest rate of 8% per annum, while the Guangxi company will still have to pay enterprise income tax on the total interest income received at 30% per annum. 3

(ii) The other taxes which the STP group will pay are:

- Business tax
- City maintenance and construction tax
- Education levy
- Stamp duty

*Any TWO required, 1 mark each*

2  
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**3 Make-it Ltd – Value added tax (VAT)**

(a) A VAT input credit will be allowed in respect of the purchase of equipment because equipment comes within the definition of a fixed asset. 1

No input credit will be allowed in the case of the purchase of concrete and building materials or the cost of the construction of the factory premises because it is an immovable property and the construction company paid business tax. 1

2

(b) An abnormal loss is a loss due to theft, spoilage or deterioration or resulting from poor or improper management. 2

Items (3) and (4) are not abnormal losses. 1  
Item (5) is an abnormal loss. 1

4

(c) Total input VAT creditable for 2014

	<b>RMB</b>	
Production materials (400,000 x 17%)	68,000	0·5
Electricity (80,000 x 17%)	13,600	0·5
Irrecoverable input VAT on abnormal loss: materials stolen (800 kg x 10 x 17%)	(1,360)	1
	<u>80,240</u>	
Irrecoverable input VAT on sales of Exo [80,240 x 200,000/(300,000 + 200,000)]	(32,096)	1·5
Equipment (350,000 x 17%)	59,500	0·5
	<u>107,644</u>	

4  
**10**

**4 (a) Chops Ltd – Consumption tax (CT) payable for 2015**

	<b>RMB</b>	
CT under the existing model (730,000 x 5%)	36,500	1
CT under proposal A (650,000 x 5%)	32,500	1
CT under proposal B [(520,000 x (1 + 7%))/(1 – 5%) x 5%]	29,284	2
		<u>4</u>

(b) Const Ltd – Business tax (BT) on self construction

(i) BT on the self construction will be payable in 2014 (on the sale of the building). 1

(ii) BT payable in 2014

	<b>RMB</b>	
BT on self construction (4,300,000 x (1 + 5%))/(1 – 3%) x 3%	139,639	2
BT on sale of the building (8,000,000 x 5%)	400,000	1

3

**(c) Karaoke – Business tax (BT) on bill**

	RMB	
Tax base for business tax	2,150	1
Business tax at 15%	323	1
		<u>2</u>
		<b>10</b>

**5 Hit Ltd****(a) Taxable profit for 2014**

	RMB	
Net profit for the year	2,952,110	
<i>Add:</i>		
(3) (a) Normal wastage	0	0.5
(3) (b) Provision for obsolete inventory	405,140	0.5
(4) (b) Non-deductible entertainment expenses (125,800 – 56,400) [Deductible amount of 60% of actual incurred, i.e. RMB75,480 but limited to 0.5% of sales, i.e. RMB56,400]	69,400	1.5
(4) (c) Compensation to customers	0	0.5
(4) (d) Penalty paid to government authority	18,500	0.5
(5) Compensation paid on dismissal of senior manager	0	0.5
(6) (a) Interest paid to equity owner at a rate less than the market rate	0	0.5
(6) (b) Unrealised exchange loss	0	0.5
(6) (c) Cash discount to customers	0	0.5
(8) Loss not covered by insurance	0	0.5
<i>Less:</i>		
(1) Discount granted in 2015	0	0.5
(2) (a) Dividend from China subsidiary	(20,000)	0.5
(2) (b) Royalty received from China affiliate	0	0.5
(2) (c) Handling income from local government	0	0.5
(3) (c) Additional 50% deduction for research and development expenses	(173,500)	1
(4) (a) Advertising and promotion expenses (maximum deduction of RMB1,692,000 (15% of sales) less RMB567,520)	(1,124,480)	1.5
(7) Income on disposal of national bonds	0	0.5
Taxable profit for 2014	<u>2,127,170</u>	
		<u>11</u>

**(b) Enterprise income tax (EIT) payable for 2014**

	RMB	
Taxable profit 2014 (from (a))	2,127,170	
Taxation losses brought forward		
2009 (820,080 – (1,552,100 – (1,200,040 + 125,300)))	(342,720)	2
2010	(680,500)	0.5
2013	(8,000)	0.5
	<u>1,095,950</u>	
Tax rate	15%	1
EIT payable	<u>164,393</u>	
		<u>4</u>
		<b>15</b>

**6 (a) Mr Wang – Individual income tax (IIT)**

(i) A salary paid to a proprietor (i.e. Mr Wang) is not deductible for IIT purposes and so cannot reduce the taxable income of the sole proprietorship.

1

Interest on a loan calculated on an arm's length basis is tax deductible and so can reduce the IIT payable by the sole proprietorship.

1

2**(ii) IIT liability of Mr Wang's sole proprietorship for 2014**

	RMB	
Sales	2,100,500	
Cost of sales and other expenses	(1,428,000)	
	<u>672,500</u>	0.5
Interest on loan (1,000,000 x 5%)	(50,000)	0.5
Standard deduction per year (3,500 x 12)	(42,000)	0.5
	<u>580,500</u>	

IIT = [(580,500 x 35%) – 14,750] = RMB188,425

0.5

2**(b) Ms Gu – Additional individual income tax (IIT) payable for October 2014**

IIT withheld by Employer A = [(9,500 – 3,500) x 20%] – 555 = RMB645

0.5

IIT withheld by Employer B = [(11,000 – 3,500) x 20%] – 555 = RMB945

0.5

Total IIT payable = [(9,500 + 11,000 – 3,500) x 25%] – 1,005 = RMB3,245

0.5

Additional IIT payable by Ms Gu = (3,245 – 645 – 945) = RMB1,655

0.5

2**(c) Ms Chen – Individual income tax (IIT) for December 2014**

	RMB	
Basic salary	5,000	0.5
Overtime	1,000	0.5
Reimbursement for business trips supported by invoices (exempt)	0	0.5
Meal allowance	<u>2,300</u>	0.5
	8,300	
Statutory employee's contribution for social insurances (deductible)	(450)	1
Statutory employer's contribution for social insurances (exempt)	<u>0</u>	0.5
Taxable salary	<u>7,850</u>	

IIT = [(7,850 – 3,500) x 10%] – 105 = RMB330

0.5

4**(d) Mrs Ink – Individual income tax (IIT)**

(i) Incomes and losses under different categories of income cannot be offset. Each category of income needs to be considered separately and tax paid accordingly.

2

**(ii) IIT payable for 2014**

Gain from trading A-shares in the stock market

Exempt 1

Interest income from a bank deposit

Exempt 1

Royalty income

Taxable

IIT on royalties = RMB170,000 x (1 – 20%) x 20% = RMB27,200

1

3**15**