
Answers

Section B

Marks

1 (a) Lizz Ltd – Interest payable to foreign bank

	RMB	
Net of taxes interest (RMB8,000,000 x 12%)	960,000	0.5
Tax base (960,000 ÷ (1 – 10%))	1,066,667	1
Value added tax (VAT) (1,066,667 x 6%)	64,000	1
Withholding tax (1,066,667 x 10%)	106,667	0.5
Gross interest (960,000 + 64,000 + 106,667)	1,130,667	1
		<u>4</u>

Tutorial note: Input VAT on interest expense is not creditable and should be treated as a cost of borrowing of Lizz Ltd.

(b) Wawa Ltd – Enterprise income tax (EIT) on foreign income for 2016

	RMB	
Total income before tax from Country A (100,000 + 50,000)	150,000	0.5
EIT at 25%	37,500	0.5
Total foreign income tax paid in Country A (20,000 + 30,000)	50,000	0.5
Foreign tax credit from Country A carried forward (50,000 – 37,500)	12,500	0.5
Total income before tax from Country B (150,000 + 40,000)	190,000	0.5
EIT at 25%	47,500	0.5
Total foreign income tax paid in Country B	40,000	0.5
Additional EIT payable in China	7,500	0.5
		<u>4</u>

(c) FFF Insurance Co Ltd is a non-resident enterprise.

It is registered outside China with a place of management outside China.

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1210

2 (a) Chen – Individual income tax (IIT)

		RMB	
1 October 2016	Granting of stock option – not taxable	0	0.5
1 November 2016	Gain on stock option ((1.8 – 0.5) x 6 x 7,000) = 54,600		0.5
	Find tax rate: 54,600 ÷ 6 = 9,100 → 25%		1
	IIT on exercise of stock option		
	(((54,600 ÷ 6) x 25% – 1,005) x 6]	7,620	1
2 November 2016	IIT on gain on disposal [(1.9 – 1.8) x 6 x 3,000 x 20%]	360	1
1 January 2017	Loss on disposal, no IIT	0	1
			<u>5</u>

(b) Ms Huang – Individual income tax (IIT)

(i) IIT withheld by Egg Ltd

	RMB	
Basic salary	40,000	0.5
Overseas working allowance	10,000	0.5
Reimbursement of air ticket (not taxable)	0	0.5
Employer's contribution (not taxable)	0	0.5
Less: Employee's contribution	(800)	0.5
Taxable salary	49,200	
Less: Allowance (3,500 + 1,300)	(4,800)	1
	<u>44,400</u>	
IIT on salary (44,400 x 30% – 2,755)	10,565	0.5
		<u>4</u>

(ii) Additional IIT payable

Income from another employment is taxed under the category of service income.

$$\text{IIT} = (3,000 - 800) \times 20\% = \text{RMB}440$$

1

10**3 (a) Wee Ltd – Value added tax (VAT)**

	RMB	
Model A		
Input VAT on local purchases (800,000 x 17%)	136,000	0-5
Other input VAT	130,000	0-5
Irrecoverable input VAT (1,500,000 x (17% – 5%))	(180,000)	1
VAT refundable	<u>86,000</u>	
VAT refunded (capped at 1,500,000 x 5%)	75,000	0-5
Model B		
Import of materials under import processing (no input VAT)	0	0-5
Other input VAT	130,000	0-5
Irrecoverable input VAT ((1,500,000 – 900,000) x (17% – 5%))	(72,000)	1
VAT refundable	<u>58,000</u>	
VAT refunded (capped at ((1,500,000 – 900,000) x 5%))	30,000	0-5
		<u>5</u>

(b) Scarce Ltd – Customs duty and value added tax (VAT)

	RMB	
(i) Export customs duty ((60,000 – 3,000) x 6 x 30%)	102,600	1
(ii) VAT refund on export (200,000 x 9%) or (34,000 ÷ 17% x 9%)	18,000	1

(c) Koo Ltd – Customs duty and consumption tax (CT)

	RMB	
Customs valuation of 50 watches (2,000 x 6 x 50)	600,000	0-5
Customs duty at 15%	<u>90,000</u>	0-5
	690,000	
Composite value for CT (690,000 ÷ (1 – 60%))	1,725,000	0-5
CT (1,725,000 x 60%)	1,035,000	0-5
The two additional watches are also taxable.		
Customs duty for two watches (90,000 x 2/50)	3,600	0-5
CT for two watches (1,035,000 x 2/50)	41,400	0-5
		<u>3</u>
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4 (a) GY Ltd – Land appreciation tax (LAT)

	RMB	RMB	
Sales		95,000,000	0.5
Land use right	20,000,000		0.5
Deed tax	600,000		1
Construction costs	15,000,000		0.5
Total development costs	35,600,000		
Administrative and management expenses (capped at 35,600,000 x 5%)	1,780,000		1
Interest (fully deductible for borrowing from financial institutions)	2,100,000		0.5
Sales tax: City maintenance and construction tax, education levy and local education levy	720,000		0.5
Additional deduction for developer (35,600,000 x 20%)	7,120,000		0.5
Total deductions		(47,320,000)	
Land appreciation value		47,680,000	
% of land appreciation (47,680,000/47,320,000)		101%	0.5
LAT [(47,680,000 x 50%) – (47,320,000 x 15%)]		16,742,000	0.5
			<u>6</u>

Tutorial note: *The amount of sales is after VAT and VAT is not a deductible cost for LAT.*

(b) Liability to land appreciation tax (LAT)

- (1) Not subject to LAT
- (2) Taxable
- (3) Exempt from LAT [*standard residential property with land appreciation of less than 20%*]
- (4) Not subject to LAT
- (5) Not subject to LAT
- (6) Exempt from LAT [*sale of residential property by an individual is temporarily tax exempt*]
- (7) Taxable
- (8) Not subject to LAT [*neither Lill Ltd nor Lar Ltd are engaged in the real estate industry, so the merger is temporarily not taxable*]

8 items, 0.5 mark each

4

10

5 Lei

(a) Tax registration

As an individual, Lei cannot be tax registered even though he is carrying out business transactions as this is outside the scope of tax registration under the Tax Collection and Administrative Law.

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(b) (i) Individual income tax (IIT)

	RMB	
Option 1: Sole proprietorship		
Net profit	340,000	0.5
Add: Salary	360,000	0.5
	700,000	
Less: Allowance	(42,000)	0.5
	658,000	
IIT on sole proprietorship (658,000 x 35% – 14,750)	215,550	0.5

	RMB	Marks
Option 2: Partnership		
Share of profit	720,000	0-5
Less: Allowance	(42,000)	0-5
	<u>678,000</u>	
IIT on partnership (678,000 x 35% – 14,750)	<u>222,550</u>	0-5
Option 3: Limited company		
IIT on salary (((30,000 – 3,500) x 25% – 1,005) x 12)	67,440	1-5
IIT on dividend (255,000 x 20%)	51,000	1
	<u>118,440</u>	
		<u>6</u>
(ii) After-tax income receivable		
	RMB	
Option 1:		
Salary 360,000 + profit from proprietorship 340,000 – IIT 215,550	484,450	1
Option 2:		
Share of profit 720,000 – IIT 222,550	497,450	1
Option 3:		
Salary 360,000 + dividend 255,000 – IIT 118,440	496,560	1
		<u>3</u>
(c) EE Ltd – Obligations as a withholding agent		
The payment to Alima Ltd is for a sale of goods, the profit on which is not sourced from China. EE Ltd will not be a withholding agent in respect of this payment.		1
The payment to Cal plc is a payment to a non-resident enterprise in respect of China sourced income (a royalty). Therefore, EE Ltd is a withholding agent in respect of this payment.		1
EE Ltd has an obligation to withhold both enterprise income tax (EIT) (withholding tax) at 10% and value added tax (VAT) at 6%.		1
		<u>3</u>
(d) Mr Liu – Individual income tax (IIT)		
	RMB	
Director's fee as an independent non-executive director:		
Taxed under service income (40,000 x (1 – 20%) x 30% – 2,000)	7,600	1
Director's fee as an executive director:		
Taxed as employment income (salary) ((50,000 – 3,500) x 30% – 2,755)	11,195	1
		<u>2</u>
		<u>15</u>

6 Biocat Ltd

(a) Enterprise income tax (EIT) for 2016

	RMB	
Net profit	4,233,350	
(1) No adjustment (FIFO is an acceptable method)	0	0-5
(2) No adjustment (depreciation period longer than 20 years)	0	0-5
(4) Accelerated depreciation (full depreciation in 2016) $(70,000 - 70,000 \div 2 \times 6/12)$	(52,500)	1
(5) Deemed sales	5,500,000	0-5
(6) Additional deduction for disabled employees	(380,000)	0-5
(7) Bonus accrued (no adjustment)	0	0-5
(8) Total advertising including deemed sales $(6,000,000 + 5,500,000) =$ RMB11,500,000; Maximum deduction $(81,350,000 \text{ (sales)} + 5,500,000 \text{ (deemed sales)}) \times 15\% =$ RMB13,027,500 Amount already booked in the accounts = RMB6,000,000, so souvenirs are deductible	(5,500,000)	1-5
(9) Provision for labour union fees (not deductible)	80,000	0-5
(10) Capitalised interest $(8,000,000 \times 7\% \times 6/12)$	280,000	0-5
(11) Special provision for bad debt	45,000	0-5
(12) Interest income from government bonds (exempt)	(74,000)	0-5
(13) Profit on disposal of government bonds (no adjustment)	0	0-5
(14) Government subsidies (no adjustment)	0	0-5
(15) Dividend from Chengdu subsidiary (exempt)	(85,000)	0-5
(16) Grossed up of tax paid in US on dividend $((9,000 \div (1 - 10\%)) \times 10\% \times 6)$	6,000	0-5
(17) Withholding tax on dividend paid by Biocat Ltd	200,000	0-5
(18) Inventory loss (no adjustment)	0	0-5
(19) Donation income (lorry)	40,000	0-5
(19) Depreciation of lorry $(40,000 \div 4 \times 6/12)$	(5,000)	1
(20) Surplus on stock take	14,200	0-5
Adjusted profit	<u>4,302,050</u>	
EIT at 15% (high and new technology enterprise)	645,308	0-5
(3) Tax credit on energy saving equipment $(934,000 \times 10\%)$	(93,400)	1
(16) Foreign tax credit (maximum credit: $(10,000 \times 6 \times 15\%) = 9,000$)	(6,000)	0-5
EIT payable	<u>545,908</u>	
		<u>14</u>

- (b) The loss of Silvercat Ltd cannot be offset against (deducted from) the profit of Biocat Ltd because there is no consolidated tax filing available for a parent and subsidiary in China.

1

15