Chartered Institute of Taxation
Excellence in Taxation

THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2015

PAPER 2.02 – CHINA OPTION

ADVANCED INTERNATIONAL TAXATION (JURISDICTION)

TIME ALLOWED – 3¼ HOURS

- You should answer **FOUR** out of the six questions: **ONE** question from Part I, **ONE** question from Part II, and **BOTH** questions from Part III.
- Each question carries equal marks.
- Start each answer on a new sheet of paper. If you are using the on-screen method to complete your exam, you must provide appropriate line breaks between each question, and clearly indicate the start of each new question using the formatting tools available.
- All workings should be made to the nearest month and Renminbi (RMB) yuan, unless the question requires otherwise.
- Marks are specifically allocated for good presentation.
- For your information this paper is accompanied by:

  Avoidance of Double Taxation Arrangement between China and the United Kingdom (including Protocol)

PART I

You are required to answer ONE question from this Part.

1. Mr Wing is a Hong Kong resident who has been living in Hong Kong since before 2009. On 1 January 2009 Mr Wing married Ms Zhang, who has lived in Shanghai her entire life and has her permanent household registration in Shanghai. Since the marriage, Mr Wing has lived in Shanghai, where he works as a senior manager at a listed company and earns a salary of RMB 50,000 per month. Mr Wing also owns shares in a listed company registered in Hong Kong, one house in Hong Kong, two houses in Shanghai, and two luxury cars. Each month, Mr Wing received RMB 10,000 in rental income on his house in Hong Kong, RMB 10,000 in rental income on one of his houses in Shanghai. In October 2014, Mr Wing received RMB 100,000 dividends from the Hong Kong listed company mentioned above.

   You are required to explain the Chinese income tax implications of these transactions for Mr Wing in 2014. (25)

2. Ms Fang is a Chinese citizen who is still single and has lived in Hangzhou with her parents and has her household registration there. On 1 January 2014, as a postgraduate student of Zhejiang University, Ms Fang was granted a scholarship worth RMB 120,000 from the Chinese Ministry of Education and attended the University of Cambridge in the United Kingdom as a visiting student for ten months. Ms Fang returned to China on 5 October 2014. During her study in the UK, Ms Fang translated an academic book from Chinese into English; the book was published by a British publisher and Ms Fang earned an income of RMB 50,000 from her translation. In addition, Ms Fang also wrote an academic article which was published by a British academic magazine and earned her an income of RMB 10,000.

   You are required to explain the Chinese income tax implications of these transactions for Ms Fang in 2014. (25)

PART II

You are required to answer ONE question from this Part.

3. Michael is a resident in London. In March 2014 Michael and Yan Li, a Chinese citizen who has a permanent household registration in Shenzhen, established a general partnership enterprise in Shenzhen to provide investment consultancy services. According to their partnership contract, Michael and Yan Li hold 50% shares respectively in the enterprise. In addition, Michael will come to Shenzhen four times per year, and spend ten days during each stay in Shenzhen to work with Yan Li in conducting their partnership enterprise. During the rest of the year, Michael will continue to run the operations of the partnership enterprise via telephone, emails and Skype in London. Yan Li will manage the day-to-day operations of their business in Shenzhen throughout the whole year.

   In the course of 2014, Michael actually visited Shenzhen three times, spending a total of 30 days in Shenzhen. In 2014, the partnership enterprise earned RMB 2 million in business income from the provision of consultancy services. The enterprise paid a total of RMB 1 million to Michael and Yan Li as their salaries and RMB 500,000 for other costs, expenses, fees and taxes arising in the course of the enterprise's operations. At the end of 2014, Michael and Yan Li decided to distribute all profits of their enterprise to themselves.

   You are required to explain the Chinese income tax implications of these transactions for Michael in 2014. (25)

4. X Ltd is a company which provides catering services. It was established in Beijing in 2005 and is a subsidiary of Y Ltd, a corporation resident in the United Kingdom. In March 2014, X Ltd was selected to be a provider of catering services for a large sporting event. In order to provide better catering services, X Ltd entered into a labour dispatch contract and consultancy contract with Y Ltd on 20 March 2014. The term of both contracts is the same, from 5 April 2014 until 31 December 2014.

   Under the labour dispatch contract, Y Ltd dispatched 100 workers to Beijing to assist X Ltd in providing catering services for the sports event. X Ltd paid a total of RMB 45 million to Y Ltd as salaries for these workers.

   Under the consultancy contract, Y Ltd provided X Ltd with consultancy services relating to the catering project for the sports event, including operational guidance, guidance on food production, menu making, personnel training, marketing and financial support, for which X Ltd paid Y Ltd RMB 25 million in fees.

   You are required to explain the Chinese income tax implications of these transactions for Y Ltd in 2014. (25)

PART III

You are required to answer BOTH questions from this Part.

5. **Describe the Chinese State Administration of Taxation's position on the income tax treatment of capital gains derived from indirect alienation of shares in a Chinese domestic company by a non-resident corporation of China.** (25)

6. Mr Li and Mr Hu are both Chinese citizens and have their respective household registration in the same city within China. They jointly own three companies in China, in each of which they respectively hold equal shares. In October 2013, Mr Li and Mr Hu jointly established a holding company in the British Virgin Islands (BVI) on the same equal-share basis, to which they alienated all their shares in the three Chinese domestic companies. In practice, the BVI holding company has no place of business and personnel, has an equity capital of just RMB 10, and has been effectively managed by Mr Li and Mr Hu from their base in China. In May 2014, the BVI holding company received a loan from the Bank of London, issued its shares to a private equity fund based in the UK, and provided debt financing to its Chinese subsidiaries.

   You are required to explain the Chinese income tax implications of the above transactions arranged by Mr Li and Mr Hu. (25)