

## THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2019

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### MODULE 2.02 – CHINA OPTION

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#### ADVANCED INTERNATIONAL TAXATION (JURISDICTION)

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TIME ALLOWED – 3¼ HOURS

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This exam paper has **three** parts: **Part A**, **Part B** and **Part C**.

You need to answer **five** questions in total.

You must answer:

- **Both** questions in **Part A** (25 marks each)
- **The** question in **Part B** (20 marks)
- **Two** questions from **Part C** (15 marks each)

#### Further instructions

- All workings should be made to the nearest month and in Renminbi (Chinese Yuan, RMB), unless otherwise stated.
- Start each answer on a new page and clearly indicate which question you are answering. 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.
- Marks may be allocated for clarity of presentation of your answers.
- The time you spend answering questions should correspond broadly to the number of marks available for that question. You should therefore aim to spend approximately half of your time answering Part A, and the other half answering questions in Parts B and C.
- The first 15 minutes of the exam is reading time. You will be allowed to annotate the question paper during this time; however, you will **not** be permitted to start writing or typing your answer. The Presiding Officer will inform you when you can start answering the questions.

For your information this paper is accompanied by:

**Agreement between China and the United Kingdom for the Avoidance of Double Taxation (including Protocol)**

**PART A**

**You are required to answer BOTH questions from this Part.**

1. ACo is a pharmaceutical company resident in the United Kingdom, which intends to expand its business in the Chinese market. For this purpose, ACo's management team have developed the following business plan:
  - 1) Establishment of a subsidiary (BCo), a holding company resident in Hong Kong, contributing the patent of a medicinal product. Except for holding and licensing the patent, BCo will not have any other business.
  - 2) Entry into an agreement with a Chinese domestic company (DCo), under the terms of which ACo will rent its pharmaceutical manufacturing equipment and BCo will license its patent to DCo, and all products made by DCo will be sold to FCo, a wholly-owned sale company set up by ACo in China. FCo will then supply the products in the Chinese market.
  - 3) Providing technical assistance in the production of medicines, ACo will appoint two UK-resident employees as technical consultants to DCo. Each employee will spend five months in China and be paid by DCo for their work.

**You are required to explain the Chinese income tax implications of ACo's business plan. Are any aspects of the plan likely to be challenged by the Chinese tax authorities?** (25)

2. **List the comparability factors in the Chinese transfer pricing regime which are to be used to compare intra-group transactions with third-party transactions and conduct transfer pricing investigations.** (25)

**PART B**

**You are required to answer THIS question.**

3. Happy Study Co is a United Kingdom-resident company (UK HS), involved in the development of intelligent teaching software for secondary schools. In order to expand its business in China, UK HS established a wholly-owned enterprise in Xiamen (China HS).

China HS entered into a business agreement with a high school in Xiamen on behalf of UK HS, with UK HS dispatching a software engineer, Joan Krever, to Xiamen to develop the product in collaboration with the high school, using related supporting software owned by UK HS.

Joan is a UK-resident contractor and held a work contract with UK HS for the duration of her work in China. She spent four months in Xiamen developing the product, during which she used China HS's office as her work base according to the contract with UK HS. Joan reported directly to UK HS on the development of the product and trained China HS's personnel in supporting the intelligent teaching software which she had developed.

**You are required to explain the Chinese income tax implications of Joan Krever's work in China, both for UK HS and for Joan.** (20)

**PART C**

**You are required to answer TWO questions from this Part.**

4. **You are required to answer the following questions related to the Chinese Individual Income Tax:**

- 1) **How does the Chinese domestic income tax law define a ‘non-resident individual’ in China?** (5)
- 2) **What is the tax liability of an individual without Chinese domicile in China under the Chinese domestic income tax law ?** (10)

Total (15)

5. XCo Ltd was incorporated in Shanghai and is jointly owned by two United Kingdom-resident companies. XCo’s directors are all UK-resident individuals. Most of XCo’s directors’ meetings are held in the UK, with the remainder taking place in Shanghai.

XCo’s principal business is investing in shares and securities listed on various Asian stock markets, including Hong Kong, Singapore and Shanghai. All securities transactions are carried out by authorised investment advisers in the respective markets.

XCo appointed an investment manager in Shanghai to supervise investments in China. The investment manager acted under the instructions of XCo’s directors. In 2017, XCo derived the following income:

	<u>Income (\$)</u>
Receipts on trading securities listed on Shanghai stock market	4,000,000
Receipts on trading securities listed on non-Shanghai markets	2,000,000
Dividend from Chinese-listed company shares	200,000
Income incidental to the trading of Chinese-listed company shares	500,000
Interest income from Chinese bank deposits	300,000

**You are required to explain the Chinese income tax implications of these activities for XCo.** (15)

6. Li Dongfang, a Chinese citizen, has been offered a position as a lecturer at a university in the United Kingdom, and will, should he accept, teach there for ten years. He has never before lived or and worked outside China.

During his employment, Mr Li will spend eight months working at the university each year. As part of his salary, he will be provided with an apartment in London. However Mr Li will be invited to teach for one month per year at his previous university in China, even if there is no employment contract between them.

Mr Li owns a house in China, in which his wife and children currently live. Although they intend to retain their house and spend holidays there, Mr Li’s wife and children will move to London with him if he accepts the offer.

**You are required to explain the Chinese income tax implications for Mr Li if he accepts the employment offer.** (15)

7. RCo Ltd, an insurance company resident in the United Kingdom, supplies insurance services to a number of construction projects involving Chinese enterprises and various countries as part of the 'Belt and Road' initiative. Occasionally RCo extends its insurance services into China and insures risks therein.

In order to facilitate its business in China, RCo has appointed Yang Damin, a Chinese resident, as its contact person in China. Mr Yang will be responsible for contacting RCo clients in China and collecting premiums relating to RCo's Chinese business. With the expansion of Chinese business and further opening of the Chinese insurance market, RCo's management team now plans to establish a branch in China.

**You are required to explain the Chinese income tax implications for RCo of its business activities in China.** (15)