Answer-to-Question-_1_

Aco is a Chinese resident, Bco is also a Chinese Resident but incorporated in Hainan Free Trade port with some preferrial Enterprise tax treatment. Dco is a resident in Unite Kingdom for manufacturing of electronic automobiles. Eco is a Resident in Hong Kong as distributor for Aco. Bco and Dco is fully owned by Bco. Dco is owned 51% by Bco and 49% owned by a Chinese state-owned enterprise.

The enterprise income tax registered in Hainan Free Trade Port shall be levied at a reduced tax rate of 15%, and for new oversea direct investments shall be exempt from enterprise income tax on the condition that (a) such income is business profits obtained from an oversea subsidiary of which the enterprise holds 20% and (b) the statutory enterprise income tax rate is not less than 5%. It seems that Dco will be qualified for such exemption.

However, it may be chanlleged as Dco obtained the lease of the manufacturing equipment and license from Aco and all products will actually be sold to Eco (which is fully owned by Aco). So the establishment of Dco will be chanlleged by the Chines Tax Authority is merely to take the tax advantage of exemption under Hainan Free Port regulations to use Dco as a oversea subsidiary.

Considering that Dco do not sold any products outside of China (only to a Hong Kong entity and is fully owned by Aco), and all connection were linked to Aco itself. Aco can directly carry out all functions provided by Dco.

Also it is not in a equal foot regarding the tax treatment the profits distributed to Bco (under Hainan Free Trade) and the Chinese State-owned enterprise. As the profit distributed to the State-owned enterprise will be at standard coporate tax rate and will not be benefit from such exemption as distributed to Bco giving no connection to the Hanan Free trade Port. Therefore, the reduced tax rates from the distribution of the same profit will be chanllenged as eventually was distributed to both Chinese resident entities.

Also considering the double taxation agreements between China and United Kingdom (UK), Hong Kong and UK, China and Hong Kong. There might be a treaty shopping risk to be chanlleged.

Royalties paid by Dco to Aco would be taxed in China at a reduced rate not exceeding 10% on the gross amount paid for the purpose of Art.12 (2) of the China and UK treaty.

With respect to the technical assistance provided by Aco (second two of its employees live in China) to UK for 3 months, such income paid by Aco for the work carried out in UK should be taxed in China in terms of Art.4 of China and UK treaty. As both individuals will be considered as residents in China and did not stay in UK for more than 183 days. This is also a sign that Dco's establishment commercial reason is not adeqent to present to the China authority given the limited information provided.

Answer-to-Question-_2_

Gonggao [2020]No.3 with respect to the items of Income that are considered as 'income derived from outside China'

We need to understand the Tax residency of the individual prior to classifying the stream of the income. Given different tax treatment will be starting from whether tax resident or not in China.

Residents in China are subject to Individual Income Tax on worldwide income including income source in China and foreign.

Non-resident in China are subject to tax only on the China-sourced income. Foreign-source income will be on Individual Income tax for non-residents.

The major income types are as follows for the consideration of 'income derived from outside China':

- Wages and salaries referring to compensation for service rendered outside of China;
- Remuneration for labour services as income related to providing labour or professional services outside of China;
- Author's remuneration related to payment received from the use if intellectual property such as patents, trademarks which is used outside of China;
- Dividend, interest and royalties that were derived from foreign

companies;

- Rental income related to renting out properties outside of China;
- Capital Gains related to profit from sale of assets located outside of China;
- Business income related to profits generated from business operation outside of China (i.e from Permanent Establishment)

The above list might not be the full list, one may also need to considering on certain tax treaties depending on which jurisdiction these income are generated.

Answer-to-Question-_3_

XCo is a UK resident Company by its incorporation, YCo is s Chinese resident Company which is fully owns Xco. There is a dividend distribution tax consideration from XCo to Yco interms of Chineses tax laws.

The argument in the question is to see whether Xco is a Chinese resident or not in order to determin the dividend distribution tax treatment.

In terms of Article 4 (3) of tax treaty between China and UK, Xco shall be deemed to be a resident only of the state in which its place of effective management is situated.

To look at the effective of management we need to look at where the board members are situated and where the management decisions were taken, also the company’s record location etc.

XCo has three executive directors, two of whom lived with their families in Guangzhou, so we can conclude that the majority directors are base in China and are Chinese tax residents. XCo’s business decisions were made in Guangzhou and all of the Company’s records were kept in Guangzhou. On this basis, it is arguable to say that the effective management of XCo is situated in Guangzhou, China.

Therefore, the dividend distribution from XCo to Yco can be looked at Chinese domestic law on the withholding taxes on dividend income (if qualified for exemption as if XCO is a qualified TREs). Of which the tax bureau in Guangzhou may need to looked into further on this, but it is likely to argue that Xco is a resident in China on the effective management situated in China.

Answer-to-Question-_6_

Ms Liu is a Chinese national and postgraduate student at a Chinese University so prior to her study in United Kingdom (UK), she is considered to be tax resident in China.

Following her study in UK which she has stayed in UK from 1 February 2021 to 5 December 2021, which is more than 183 days for calendar year so UK may also consider Ms Liu is a tax resident in UK.

In terms of article 4 (2) of the tax treaty between China and UK, using the tier-breaker rule to determine Ms Liu's tax residence. Ms Liu lived in China with her parent and maintains her household registration here which confirm that her permanent home is available to her in China. In UK is a temporary home for her study purpose in China. Ms Liu's centre of Vital Interest is in China given her family connection and study link with China as well, we can also conclude that she has an habitual adobe in China. Ms Liu is a Chinese national, which can enhance the links to China.

In view of the above facts, we can conclude that Ms Liu is considered to be a Chinese resident in terms of the treaty.

On this basis, Ms Liu receive the following streams of income:

- Scholarship of RMB 100,000 from the Chinese Ministry of

Education (Chinese Government)
- RMB 15,000 from her short blog article about her life in UK on a Chinese social media’s website (Chinese company)
- RMB 10,000 from her academic article published by a UK academic magazine (UK company)

In terms of Article 20 (students) of the tax treaty between China and UK, payment which a student who was immediately before visting a contracting state (UK) a resident of the other contracting state (China) and who is present in the first mention state (UK) solely for the purpose of her education services (Ms Liu’s case) for the purpose of this maintenance or education shall not be taxed in that state (UK) as such payments arise from source outside that UK (i.e source in China). So the scholarship income RMB 100,000 should be taxed in China only.

Author’s income should be taxed in the jurisdiction where this publition were used (UK or China).

on this basis, the short blog article income of RMB 15,000 should be taxable in China due to its publition in China. While the academic article income of RMB 10,000 published in UK academic magazine should be taxable in UK.

Answer-to-Question-_7_

ICo is a UK resident company, manufactures and sells appliances. Ico owns a small warehouse in Xiamen to store a small number of large items which are identical to some of those on display in the KCo store. KCo is a Chinese resident company, which owns a store selling appliances acquired from ICo.

To see whether the warehouse constitutes a permanent establishment (PE) of ICo in China, we need to look at Article 5 of the tax treaty between China and UK.

PE means a fixed place of business through which the business of an enterprise (ICo) is wholly or partly carried on, including warehouse.

However, from the facts provided, when a customer buys one of these large item from Kco store, KCo employees visits the warehouse where they take possession of the item before delivering to the customer, so the ownership of the item is only transferred from ICo to KCo when the item leaves the warehouse.

Article 5 (4) provided that the term PE shall be deemed not to include the use of the facilities (warehouse) for the purpose of storage, or delivery of goods or merchandise belonging to the enterprise.

It seems that the warehouse is merely a place to assist ICo for the storage and the transfer of ownership is depending on the departure of the item from the warehouse, the warehouse is more of a preparatory or auxiliary character other than independently carries the business activity on behalf of ICo given also no mentioned employees of ICo at the warehouse (but the Kco’s employees) who is acting on behalf of ICo for the transaction, which enhance the argument that the warehouse is a preparatory nature to facilitate the transfer other than acting independently for ICo.

In view of the above, it is more likely to argue that the warehouse do not constitute a permanent establishment (PE) of ICo in China.