

Value-Added Tax Computation Method

1) Normal taxpayers

The standards to be normal taxpayers are:

a) The taxpayers engaged in production of taxable goods or provision of taxable services or the taxpayers mainly engaged in production of taxable goods or provision of taxable services (i.e., this part of sales value is over 50% of the total of the year) and concurrently engaged in wholesales or retails of taxable goods with the annual sales value over 1 million Yuan.

b) The taxpayers engaged in wholesales or retails of taxable goods with the annual sales value over 1.8 million Yuan.

In addition, some small taxpayers satisfying the statutory conditions may also be verified as normal taxpayers.

To compute the VAT payable, the normal VAT taxpayers should separately calculate the output tax for the period and the input tax for the same period. The balance of output tax for the period after deducting the input tax for the period shall be the actual amount of tax payable.

The formula for computing the tax payable is as follows:

Tax payable = Output tax payable for the period – Input tax for the period

Example:

One shop has an output tax of 1.7 million Yuan for the current month and an input tax of 1.3 million Yuan. The VAT payable shall be calculated as follows:

Tax payable = 1.7 million Yuan – 1.3 million Yuan = 400,000 Yuan

For taxpayers selling goods or taxable services, the output tax shall be the VAT computed and charged to the purchasers on the basis of the sales values and the applicable tax rates.

The formula for computing the output tax is follows:

Output tax = Sales value × Applicable tax rate

Example:

A steal company sold to a machinery company a certain quantity of steal worth of 5 million Yuan. The applicable VAT rate is 17%. The output tax charged to the machinery company by the steal company shall be computed as follows:

Output tax = 5 million Yuan × 17% = 850,000 Yuan

The sales value shall include the total price charges and non-price charges (including commissions, subsidy, funds, pool resources, profit repayment, prizes, indemnity, interest on delayed payment, package charges, rentals for package materials, storage charges, good quality charges, transportation and loading and unloading charges, payment received on behalf, and payment made on behalf, except otherwise regulated by the State.) received from the purchasers by the taxpayers by selling goods or taxable services. The taxpayer shall compute the output tax for the period on the basis of the sales value and collect the tax payable from the purchasers in addition to the payment on goods and services.

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If the sales prices of the goods and services are tax inclusive prices, the taxpayers have to work out the tax exclusive sales value by using the following formula:

$$\text{Tax exclusive sales value} = \text{Tax inclusive sales value} \div (1 + \text{Applicable tax rate})$$

Example:

A bookstore has sales revenue of 1.13 million Yuan (VAT included) for the month. The applicable rate is 13%. The tax exclusive sales value and output tax are computed as follows:

$$\begin{aligned} \text{Tax exclusive sales value} &= 1.13 \text{ million Yuan} \div (1 + 13\%) \\ &= 1 \text{ million Yuan} \end{aligned}$$

$$\text{Output tax} = 1 \text{ million Yuan} \times 13\% = 130,000 \text{ yuan}$$

The sales value shall be computed in Renminbi. The sales value of the taxpayer settled in foreign currencies should be converted into Renminbi at the foreign exchange rate quoted by the People's Bank of China prevailing on the date or that on the first day of the month in which the sales take place (or the rate derived according to relevant regulations), and on the basis of which the tax payable shall be computed. Tax payers shall determine in advance the conversion rate to be adopted. Once determined, no change is allowed within one year.

If the prices of the goods and services are obviously low and the taxpayers have no reasonable argument for that, or if there is no sales value for deemed sales of goods, the tax department may determine the sales value according to the average sales [price of similar goods of the taxpayers in the same month, the average sales price of similar goods in recent months or the composite assessable price. VAT shall be computed and paid on the basis of the sales value thus determined.

The formula for computing the composite assessable price is:

$$\text{Composite assessable price} = \text{Cost} \times (1 + \text{Cost} / \text{profit ratio})$$

For goods subject to Consumption Tax, the composite assessable price should also include the Consumption Tax payable.

When selling goods or taxable services, the taxpayers should issue special VAT invoices to the purchasers and should indicate the sales value and output tax. The purchasers may credit the VAT indicated in the special VAT invoices when computing the VAT payable. However, in case of selling goods or taxable services to final consumers, or in case of selling tax - free items, or when small taxpayers sell goods or taxable services, the normal invoices shall be issued without listing the sales value and the VAT.

The VAT paid or borne by the VAT taxpayers on their purchases of goods or taxable services shall be the input tax for the taxpayers.

The following input taxes can be credited against the output taxes:

- a. For taxpayers purchasing goods or taxable services (including purchase of raw materials, fuel, power, etc.), it is the VAT indicated on the special VAT invoices obtained from the sellers.
- b. For taxpayers importing goods, it is the VAT indicated on the tax payment receipts

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obtained from the customs office.

c. For taxpayers purchasing the tax – exempt agricultural products from agriculture workers and the tax – exempt grains from the State grain purchase/sale enterprises, the input tax may be computed on the basis of the payment shown on the sale receipts or invoices and 13% credit rate (formula: input tax = purchase value \times 13%).

d. For transportation expenses paid by taxpayers purchasing goods (excluding fixed assets) or selling goods, the creditable input tax is calculated based on the transportation expenses (excluding the loading and unloading expenses, insurance expenses related to transportation.) listed in the transportation payment vouchers (or invoices) and on a 7% credit rate (the formula is: input tax = transportation payment \times 7%). But, the transportation expenses for purchasing or selling tax-exempt goods are not allowed for computing the input tax creditable.

e. The enterprises making use of waste and used materials may compute their input tax by the purchase price times 10% rate (formula: input tax = purchase value \times 10%).

When VAT taxpayers have purchased goods or taxable services, the taxpayers have to go to the tax department to claim for the input tax credit within 90 days the issuance of the special VAT invoices issued by the anti-false tax control system. Otherwise, they would not be allowed for the credit of the input tax. Regarding the special VAT invoices issued by the anti-false tax control system having passed the verification, the taxpayers should account and claim for the input tax credit by rules within the current month of the verification. Otherwise, the credit would not be allowed.

If a taxpayer meeting the norms for a normal VAT taxpayer has not gone to the tax department for identification procedures or is unable to provide accurate tax information due to its imperfect accounting system, the competent tax department shall collect VAT on its output and shall neither allow the taxpayer for input tax credit nor the use of special VAT invoices.

Where taxpayers purchasing goods or taxable services have not obtained or kept the VAT credit documents in accordance with the regulations or where the VAT paid and other relevant items are not indicated on the VAT credit documents in accordance with the regulations, the input tax shall not be allowed for credit against the output tax.

The input tax on the following items shall not be allowed for credit against the output tax:

a. Fixed assets purchased (including the machinery, transportation tools and other equipment and tools related to production and business operation with a use life over 1 year, and the materials not mainly related to production or business operation with use life over 2years and worth more than 2000 Yuan).

b. Goods or taxable services purchased for the use on non-taxable items (including provision of non-taxable services, transfer of intangible assets, sales of immovable assets and fixed assets in construction), except for the enterprises in Liaoning Province, Jilin Province and Heilongjiang Province where the scope of input VAT credit has been extended.

c. Goods or taxable services purchased for the use on tax-exempt items.

d. Goods or taxable services purchased for collective welfare or private consumption.

e. Abnormal losses of goods purchased (e.g., losses incurred due to natural disasters, bad management).

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f. Goods or taxable services purchased and consumed in the products-in-progress or finished products that suffer abnormal losses.

If, however, the taxpayers use the purchased goods or taxable services, the input tax of which has been already credited, for non-taxable items, tax-exempt items, collective welfare, private consumption or abnormal losses, the relevant input tax of the said purchases should be deducted from the input tax of the current period.

Example:

Let's take the production and dealing of food staff as an example to demonstrate the computation of VAT payable:

a. Farm sells wheat to flour factory B at the price of 1 million Yuan. According to tax law, this sum of income of the farm is VAT free.

b. B grinds the wheat into flour and sells it to cake factory C at the price of 2 million Yuan (exclusive of VAT, the same hereinafter). The applicable VAT rate is 13%.

The output tax is 260,000 Yuan, i.e., 2 million Yuan x 13% = 260,000 Yuan. The add-up of price and the tax is 2.26 million Yuan, i.e., 2 million Yuan + 0.26 million Yuan = 2.26 million Yuan.

The input tax allowable for credit is 130,000 Yuan, i.e., 1 million Yuan x 10% = 130,000 Yuan.

The VAT payable by B is 130,000, i.e., 260,000 Yuan – 130,000 Yuan = 130,000 Yuan.

c. C produces the cakes with the flour purchased from B and sells to store D at the price of 8 million Yuan. The applicable rate is 17%.

The output tax is 1.36 million Yuan, i.e., 8 million Yuan x 17% = 1.36 million Yuan. The add-up of price and tax is 9.36 million Yuan, i.e., 8 million Yuan + 1.26 million Yuan = 9.36 million Yuan.

The allowable input tax credit is 260,000 Yuan (that is the output tax of B).

The VAT payable by C is 1.10 million Yuan, i.e., 1.36 million Yuan – 0.26 million Yuan = 1.10 million Yuan.

d. D sells out the cakes purchased from C at the price of 10 million Yuan. The applicable VAT rate is 17%.

The output tax is 1.7 million Yuan, i.e., 10 million Yuan x 17% = 1.7 million Yuan. The add-up of price and tax is 11.7 million Yuan, i.e., 10 million Yuan + 1.70 million Yuan = 11.70 million Yuan,

The input tax credit allowable is 1.36 million Yuan (that is the output tax of C).

The VAT payable by D is 340,000 Yuan, i.e., 1.7 million Yuan – 1.36 million Yuan = 340,000 Yuan.

According to the current price system in China, the retailing price is tax – inclusive price that is the add-up of the tax- exclusive price and the output tax. That means the price of the cake to the final consumers is 11.7 million Yuan, i.e., 10 million Yuan + 1.7 million Yuan = 11.7 million Yuan.

The above example may be summarized as the following table:

Example of VAT computation

Unit; 10,000 Yuan

Enter priess	Commodity	Sales price (no tax) (100000yuan)	Applicable rate (%)	VAT(100000yuan)		
				Output tax *	Input tax	Tax payabl e **
A	Wheat	100		0	0	0

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B	Flour	200	13	26	10	16
C	Cake	800	17	136	26	110
D	Cake	1000	17	170	136	34

*: $Output\ tax = Sale\ price\ exclusive\ of\ VAT \times Applicable\ rate$

** : $Tax\ payable = Output\ tax - Input\ tax$

When computing the VAT payable by the taxpayers, the excessive part of the input tax may be carried forward to the next period for credit if the output tax of the current period is not enough to credit the input tax or may be offset against the VAT owed, if any, by the taxpayers.

The VAT returned to the purchasers due to the sales return or discount should be deducted from the output tax of the current period. The VAT recovered due to purchase return or discount should be deducted from the input tax of the current period.

In addition to the above computation method, the normal taxpayers manufacturing the following goods may use the simple method in computing the VAT at 6% levying rate (however, the method can not be changed within three years once chosen) and may issue special VAT invoices:

- a. The electric power produced by the small hydropower units below county level.
- b. The sand, earth and stone used for construction of for producing the materials of construction.
- c. The bricks, tile and lime continuously produced with the sand, earth, stone and other minerals dug by themselves.
- d. The wall material made of the raw materials mixed with gangue, bone coal, powder coal, slag of coal boiler and other waster slag.
- e. The bio-products made of microorganism, metabolite of microorganism, toxin of animals, blood or tissues of human being or animals.
- f. Supplied water (when computing the tax, the taxpayers may credit the VAT listed in the special VAT invoices at 6% levying rate obtained when purchasing the supplied water from the independent accounting water supply factory).

The commercial concrete produced and sold by the normal taxpayers may also be taxed at 6% VAT levying rate, but special VAT invoices can not be issued.

2) The computation method for small – scale taxpayers

The small-scale taxpayers include the following two types of VAT taxpayers:

a. For taxpayers engaged in the production of taxable goods or the provision of taxable services: those engaged principally in the production of goods or provision of taxable services (that is the sales value of this part exceeds 50% of the total annual taxable sales value) and concurrently in wholesaling or retailing of goods whose annual taxable sales value is below one million Yuan are small-scale taxpayers.

b. Taxpayers engaged in wholesaling or retailing of goods whose annual taxable sales value is below 1.8 million Yuan are small-scale taxpayers (excluding the gas stations selling finished petroleum).

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The individuals and non-enterprise units (those meeting the norms for normal VAT taxpayers and frequently involved in taxable conducts may be identified as normal VAT taxpayers) whose annual taxable sales value exceed the standards for small-scale taxpayers but are not frequently involved in taxable conducts are deemed as small-scale taxpayers.

The small-scale taxpayers are taxed in a simplified manner: the VAT payable is computed on the basis of the sales value of goods and/or services and the prescribed applicable VAT levying rate. The VAT is collected together with the payment for sales from the purchasers and handed over to the tax department.

For the small-scale taxpayers engaged in goods wholesaling or retailing and principally engaged in goods wholesaling or retailing and concurrently in goods production or provision of taxable services, the VAT levying rate is 4%. All other small-scale taxpayers are liable to 6% VAT levying rate.

Besides, 4% VAT levying rate is also applicable to the commission shops on sales of goods on commission, to the mortgage businesses on sales of dead mortgages, to sales of second-hand commodities, to the approved duty-free shops on sales of tax-exempt goods, and to the auction firms on trusted auctions of taxable goods.

The formula for calculating the tax payable is as follows:

Tax payable = Sales value × Applicable levying rate

If the sales prices of the goods or services are tax inclusive prices, the taxpayers have to work out the tax exclusive sales value = Tax inclusive sales value ÷ (1+Applicable levying rate)

Any adjustment to the levy rates shall be determined by the State Council.

The sales value rebated to the purchasers by small-scale taxpayers due to sales return or discount should be deducted from the sales value of the current period.

Example:

A shop runner Mr. Zhang has a sales value of 11,000 Yuan (including VAT) for the current month, and has sales return of 600 Yuan. The applicable VAT levying rate is 4%. The tax-exclusive sales value and he tax payable for the month are computed as follows:

$$\begin{aligned} \text{Tax exclusive sales value} &= (11000 \text{ Yuan} - 600 \text{ Yuan}) \div (1+4\%) \\ &= 10000 \text{ Yuan} \end{aligned}$$

After approval by the competent tax department, the small-scale taxpayers engaged in goods wholesaling or retailing and principally engaged in goods wholesaling or retailing and concurrently in goods production or provision of taxable services may be not regarded as small-scale taxpayers and compute and pay VAT as normal VAT taxpayers, if they meet the conditions of annual taxable sales value over 300,000 Yuan, having a sound financial accounting system, being able to account accurately the output tax, input tax and tax payable as required and providing precise tax information. Once the above small-scale taxpayers are identified as normal VAT taxpayers, they will not be allowed to turn back to small-scale taxpayers.

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3) Computation of tax on imported goods

For imported goods, the VAT payable shall be computed and paid on the basis of the composite assessable prices and the applicable tax rates prescribed. No input tax will be allowable for credit.

The formula for computing the tax payable is as follows:

Tax payable = Composite assessable price \times Applicable VAT rate

Composite assessable price = Customs dutiable value + Customs Duty

For taxpayers importing taxable goods subject to Consumption Tax, Consumption Tax should be added to the composite assessable price.

Example:

One foreign trade company imports a batch of agricultural machines. The composite assessable price is 10 million Yuan and the applicable rate for VAT is 13%.

The VAT payable by this company shall be calculated as follows:

Tax payable = 10 million Yuan \times 13% = 1.3 million Yuan.



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