

# Fake Cultural Development Company, July 14, 2011, Points of Argumentation and Cross-examination

## I. Taxation Bureau's allegations:

1. From January 2006 to December 2010, decals were not properly assigned to 7 survey and design contracts for construction projects and 2 contracts for construction and installation engineering contractors. For failure to assign decals as required by law, the company is to be triply fined, totaling fines of RMB 13,106.01;

2. From November 29, 2000 to December 13, 2010, income was not reported for a total of 3 different projects, respectively:

Renovations costing a total of RMB 1,107,716 for Boya Gardens #3 and #1701, work for which began in April, 2002;

Design fees totaling RMB 500,000 and renovation fees totaling RMB 932,8118.36 for the Upper Garden, with work beginning in October, 2006;

Design fees totaling RMB 380,000 and renovation fees totaling RMB 4,507,809 for Three Shadows Photography Art Centre, with work beginning in April 2006.

The cost of the above three projects together amounts to RMB 880,000, taxes on which are to be calculated with a 5% tax rate for the payment of overdue business taxes; taxes for the project loan, which totaled RMB 1,943,724.36, are calculated based on a 3% tax rate on payment of overdue business taxes; together, total payments due on the above come to RMB 492,311.73. Overdue payments of urban construction taxes come to RMB 32,467.93, and overdue payments of corporate income taxes come to RMB 4,344,497.64. The above sums, incurring fines at a multiple of 1.5, result in a total of RMB 7,303,915.96 in overdue payments.

3. Invoices were issued inconsistent with the history of the company's purchasing unit, and false invoices were also accepted by the company. For each of these two violations respectively, the company shall be fined RMB 10,000.

## II. Our appeals with regard to the above allegations:

First, on the issue of decals, we have asked to see the relevant contracts, and can verify that there were indeed no decals on the contract. The contracts themselves had amassed stamp duties, but considering how small the amount was, we were not overly concerned about the issue.

Second, on the issue of the Boya Gardens project, we would like to remind the Bureau that

according to the provisions of the Law on the Administration of Tax Collection, if illegal activity has not been discovered within five years of its occurrence, only the original tax payments due may be pursued, but no further penalties can be administered. Even if the Boya Gardens project did have a history of tax evasion, this cannot be taken as basis for punishment. The Bureau did not originally understand this rule, but after we highlighted its existence, they accepted it.

In order to support claims of tax evasion regarding the above three projects, the Bureau provided third-party evidence, namely the accounting records of contract signees and attached check stubs and photocopies of cash payment receipts. We maintain that these forms of documentation do not accord with accounting standards, and as they are not the original documents but instead mere photocopies, their authenticity is dubitable. Furthermore, without access to the accounting books and records of Fake Cultural Development Co., Ltd, we are entirely unable to confirm the authenticity of the above allegations.

Another important factual discrepancy, central to the case, relates to the matter of the calculation of corporate income taxes. We would like to point out here that there exist two different scenarios in which income might not be recorded. The first is the scenario whereby the cost of a project, but not the income, is recorded; in such a scenario, cost is to be adjusted for income. The second is the scenario whereby neither the cost nor income of a project are recorded; in such a scenario, reasonable methods should be adopted for the purposes of appraising and verifying taxable income. We know that the State Taxation Administration's designated taxable income rate for the construction industry is clearly stipulated in the range of 8% to 20%. Knowing this, we asked the Bureau to determine whether or not Fake Cultural Development Co., Ltd had in fact recorded its costs; the Bureau began by saying it could not determine this. We said, then, that since the Bureau was unable to confirm, the Bureau should seek a reasonable method of appraising and verifying taxable income, as stipulated above. The Bureau then proceeded to deny its original assertion, and stressed that it had in fact already made adjustments according to both on- and off-balance-sheet income. However, we hold that the portion of the cost obtained from third parties is extremely small, and is completely out of proportion with actual income.

In addition, we would like to emphasize that as we currently do not have access to the accounting records of Fake Cultural Development Co., Ltd, we have no way of confirming prior years' losses. We therefore demanded that the Bureau provide relevant data and evidence, but received no reply with regard to these demands. At the same time, we also reminded the Bureau to take note of the time at which each sum of money was received, as this related to changes in tax rates (corporate income tax before 2007 was 33%, and after 2008 was 25%). However, because the sums were too numerous, we were unable to record them ourselves one-by-one.

As to the matter of invoices, the Bureau produced two invoices obtained from third-party sources, alleging that these invoices were issued by our company. However, neither the issuer of the

invoice nor the receiving company were in fact Fake Cultural Development Co., Ltd, and we maintain that third-party testimony alone is not sufficient proof that these two invoices were issued by our company. On the question of the authenticity of the invoices received, we demand to be provided with the relevant invoices and invoice numbers, and demand that their authenticity be checked out through the tax system. We also hold that even if the invoices received were fake, 1. as the facts related to this are not clear; 2. as, in general, financial and management personal would have difficulty distinguishing these with the naked eye; and 3. as each invoice cannot possibly be checked individually, then any mistake that may have been committed was not done so intentionally, and should not merit high-level penalties.

Above is the content of our cross-argument. For all procedural matters, lawyer Xia Lin gave a superb address, and I am sure will also be able to give an extremely detailed summary. As such I will not repeat their contents here.

Du Yanlin

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