

Tax

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Tax Analysis

Individual Income Tax (IIT) reform: New requirements relating to IIT withholding and self-declarations

China's State Administration of Taxation (SAT) released several regulations on 21 December 2018 that provide guidance on the enforcement of the newly amended IIT law and its implementation regulations. Three bulletins address various aspects of the new IIT rules, specifically, the use of a tax ID, withholding of tax on income derived by both residents and non-residents and the self-declaration:

- Bulletin on an Individual Taxpayer's ID Number (Bulletin of State Administration of Taxation [2018] No. 59 (Bulletin 59));
- Administrative Measures for Withholding and Declaration of Individual Income Tax (Bulletin of State Administration of Taxation [2018] No. 61 (Bulletin 61); and
- Bulletin on Self-Declarations for Individual Income Tax Purposes (Bulletin of State Administration of Taxation [2018] No. 62 (Bulletin 62)).

This Analysis summarizes the key points in these bulletins, all of which apply as from 1 January 2019.

Tax ID bulletin (Bulletin 59)

Highlights

Bulletin 59 clarifies that all taxpayers will be allocated a tax ID that will function as an individual's unique identifier for tax compliance purposes. A taxpayer must provide his/her tax ID to the tax authorities or the withholding agent when filing a tax return, paying tax, requesting a tax refund or tax payment certificate, checking tax filing records, etc. A Chinese citizen's ID number generally will be used as the tax ID and the tax authorities will assign a tax ID to individuals who do not have a Chinese ID.

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When a taxpayer first becomes liable for IIT, he/she must provide valid identification documents and relevant basic information to the withholding agent (often the employer) or the tax authorities. Once a tax ID is assigned, the tax authorities will inform the taxpayer either directly or through the withholding agent. Bulletin 59 provides a detailed list of documents that can be used as valid identification documents.

Deloitte observations

- Bulletin 59 introduces the tax ID as a "unique identifier" for all tax-related matters. According to Bulletin 61, when a withholding agent makes the first payment to an individual, the agent must include information (including the tax ID provided by the individual) in the "IIT Basic Information Form (Form A)" and submit the form to the tax authorities when the agent withholds IIT in the following month. The tax ID will be used during the entire tax compliance cycle, and the centralized management of "One Taxpayer, One Number" will facilitate efficient tax collection and administration.
- Previously, individual taxpayers did not have unique tax IDs. Foreign individuals typically used their passport numbers, even though such numbers could change for various reasons (e.g. issuance of a new passport). Foreigners often had multiple numbers, which gave rise to difficulties in tax administration, so the mandatory tax ID requirement will improve efficiency and facilitate tax collection. However, since foreigners and individuals from Hong Kong, Macau and Taiwan who are working in Mainland China will have to submit information to apply for their tax IDs, employers may need to provide additional assistance to ensure timely compliance.

IIT Withholding (Bulletin 61)

Highlights

Bulletin 61 provides details on methods for withholding, the responsibilities of the withholding agent and the taxpayer.

IIT withholding on total income

- The withholding agent is responsible for withholding IIT on the full amount of payments made to an individual (whether resident or non-resident). The withholding is done either on a monthly or a transaction basis.
- The tax withheld must be remitted to the state treasury by the 15th day of the month following the month of the payment, and the IIT withholding return must be submitted to the tax authorities.
- As noted above, when the withholding agent makes the first payment of income to the taxpayer, it must complete the "IIT Basic Information Form (Form A)," include all relevant information and submit the form to the tax authorities. Taxpayers are required to notify the withholding agent if there are any changes to the basic information, which the withholding agent then must report to the tax authorities.

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Advance IIT withholding on comprehensive income derived by residents

One of the main changes made by the new IIT law is the consolidation of four previous separate types of income (i.e. salaries and wages, remuneration for independent services, author's remuneration and income from royalties) into a single category called "comprehensive income." Comprehensive income is subject to progressive tax rates ranging from 3% to 45%. The IIT on comprehensive income derived by residents is assessed on an annual basis, but is collected through the advance withholding of tax, which is remitted to the tax authorities by the payer (i.e. withholding agent) on a monthly or transaction basis, followed by a final reconciliation and settlement by the taxpayer at the time the taxpayer files the annual tax return. The IIT on comprehensive income derived by non-residents is assessed on a monthly or transaction basis and is collected through the withholding of tax, which is remitted to the tax authorities by the payer.

Withholding method

- When a withholding agent pays wages and salaries to a resident individual, it must calculate the IIT using a cumulative salaries-based approach, which effectively is based on cumulative annual wages and salaries, but tax is withheld on a monthly basis.
- When a withholding agent pays remuneration for independent personal services, author's remuneration and income from royalties to a resident individual, it must withhold advance tax on a monthly or a transaction basis.

Annual reconciliation

- The amount of tax withheld during the year should be equal to the taxpayer's annual IIT liability. If there is a disparity, a resident individual must make a reconciliation at the time he/she files the annual income tax return between 1 March and 30 June of the year following the tax year. Any overpayment of tax will be refunded and underpayment must be paid.

The taxable income and applicable tax rate on comprehensive income earned by resident individuals and the annual reconciliation are summarized as follows:

Comprehensive income	Advance IIT Withholding		Annual Reconciliation	
	Taxable income	Applicable tax rate	Taxable income	Applicable tax rate
Wages and salaries	Cumulative taxable income = cumulative income – cumulative tax-exempt income – cumulative standard deductions and itemized deductions - cumulated additional itemized deductions - cumulated other deductions under the IIT law	3%-45% Seven tax brackets	Annual taxable income = annual income - RMB 60,000 (standard deduction) - itemized deductions - additional itemized deductions - other deductions under the IIT law	3%-45% Seven tax brackets
Remuneration for independent personal services	Taxable income is the amount remaining after deducting expenses for each payment. If the income does not exceed RMB 4,000, the deduction is RMB 800; for income exceeding RMB 4,000, the deduction is calculated at 20% of the gross amount.	20%-40% Three tax brackets	Taxable income is the amount remaining after deducting 20% as a deemed expense. An additional 30% deduction is allowed for author's remuneration.	
Income from royalties	An additional 30% deduction is allowed for author's remuneration.	20%		
Author's remuneration		20%		

IIT withholding on comprehensive income derived by non-residents

Withholding method

- When a withholding agent pays comprehensive income to a non-resident individual, IIT must be withheld and paid on a monthly or a transaction basis according to the following methods:

Income	Taxable income	Applicable tax rate
Wages and salaries	Taxable income is the amount remaining after taking the standard deduction of RMB 5,000	Monthly rate is based on the annual rate applicable to comprehensive income
Remuneration for independent personal services	Taxable income is the amount remaining after deducting 20% as a deemed expense (an additional 30% deduction is allowed for author's remuneration.).	
Income from royalties		
Author's remuneration		

Annual Reconciliation

- Non-resident individuals are not required to make an annual reconciliation, and their withholding method will remain unchanged during a tax year. However, if a non-resident individual subsequently meets the criteria to qualify as a Chinese tax resident, he/she must notify the withholding agent and make an annual reconciliation.

See Deloitte Tax Analysis of 21 December 2018 for a discussion of the IIT withholding calculation method on comprehensive income for both resident and non-resident individuals.

IIT withholding on other income

When the withholding agent pays dividends, interest, leasing income, income on the transfer of property or incidental income, it must withhold IIT on a monthly or a transaction basis.

Tax treaty benefits for non-resident individuals

If a non-resident is entitled to benefits under an applicable tax treaty, he/she must inform the withholding agent and submit all relevant information and documents. The withholding agent then will withhold IIT based on the treaty.

Obligation of withholding agent to provide information to taxpayers

- A withholding agent that pays salaries and wages must provide the taxpayer with information, such as the amount of income and the tax withheld, within two months of the following year (i.e. by the end of February) and if the taxpayer requires the information at any time during the tax year.
- A withholding agent that pays income other than wages and salaries must provide the taxpayer with information, such as income and the tax withheld, immediately after withholding.

Measures to be taken where taxpayer's information is not consistent with facts

- The withholding agent must calculate the IIT and withhold tax based on the information provided by the taxpayer, and it may not arbitrarily change the information.
- Where the withholding agent discovers that information provided by the taxpayer is inconsistent with the facts, the agent can ask the taxpayer to revise the information. If the taxpayer refuses, the withholding agent must report this fact to the tax authorities.

- Where the taxpayer finds that its information, income, tax withholding information, etc. provided or reported by the withholding agent is inconsistent with the facts, the taxpayer can ask the withholding agent to make a correction. If the withholding agent refuses, the taxpayer must report this fact to the tax authorities.

Safekeeping and confidentiality of tax documents and information

- A withholding agent must properly maintain the additional itemized deduction information form provided by the taxpayer for future inspection.
- A withholding agent is required to keep all tax information and documents submitted by taxpayers confidential.

Withholding service fees

- A withholding agent is entitled to a rebate equal to 2% of the tax withheld (except for taxes paid as a result of an audit).
- The withholding agent has discretion on how to use the rebate (e.g. it may use the rebate to improve the tax technical skills of its personnel, etc.).

Measures where taxpayer refuses to withhold taxes

The withholding agent is obliged to withhold tax, and the taxpayer may not resist or impede the withholding. Otherwise, the withholding agent must report this to the tax authorities.

Deloitte observations

Bulletin 61 clarifies the withholding methods for all types of taxable income under the new IIT law, as well as the obligations of taxpayers and employers with respect to the withholding of tax (see Deloitte Tax Analysis of 21 December 2018 on the actions to be taken by the withholding agent and the taxpayer under Bulletin 56). Withholding agents and taxpayers should be aware of the following:

Taxpayers

- Under the cumulative advance IIT withholding method and the calculation of withholding, the net take-home salary can vary from month to month, which may impact individual taxpayers' cash flow so some advance planning for cash flow may be needed.
- Resident individuals who receive remuneration for independent personal services, author's remuneration and income from royalties may claim the additional itemized deductions only at the time the annual reconciliation is made. Since the tax calculation method for advance IIT withholding differs from that used for the annual reconciliation on comprehensive income, resident individuals will need to understand these differences, make the annual reconciliation accurately and in a timely manner, and seek professional assistance, where necessary.
- Foreigners and individuals from Hong Kong, Macau and Taiwan who are working in Mainland China for a short period of time will need to assess their tax residence status and communicate with the withholding agent in a timely manner to comply with their tax obligations.

Withholding agents (employers)

- Employers will have increased administrative obligations since Bulletin 61 stipulates that withholding agents must provide withholding information to taxpayers and ensure the confidentiality of the information.
- Since the cumulative advance IIT withholding method and additional itemized deductions apply as from 1 January 2019, companies will need to adjust their payroll systems, set up processes to collect and report additional itemized deductions submitted by employees and provide training to relevant personnel. Efficient and sophisticated systems will be particularly important for companies with large work forces.

- Companies should proactively communicate with employees about the new IIT law to help them understand the advance withholding and annual reconciliation requirements, and the potential for fluctuation of monthly net salary.
- Multinational companies with many foreign employees or employees from Hong Kong, Macau and Taiwan will need to closely monitor and track tax residence status, set up proper internal processes to correctly fulfil withholding obligations, and assist employees with tax ID applications, where necessary.
- Companies that conclude independent personal service contracts with individuals need to be aware of the withholding method for remuneration for such services as stipulated in Bulletin 61.

Bulletin 61 clearly stipulates that withholding agents have the right to ask taxpayers to make relevant changes if the tax information is inconsistent with the facts, and vice versa. In practice, when employees are under a split payroll (mostly international assignees), companies often only withhold IIT on income paid within Mainland China. Technically, where an employee works for a domestic company, the domestic company is required to withhold IIT on wages and salaries even if the income is paid or borne by an overseas affiliate. If a taxpayer discovers that the IIT withholding is inconsistent with the actual situation, he/she can report it to tax authorities. Therefore, where employees have complicated payroll arrangements, companies that are withholding agents should review current tax practice and take appropriate steps to ensure compliance with the Chinese tax rules.

Self-declaration of individual income tax (Bulletin 62)

Highlights

Bulletin 62 requires an individual to make a self-declaration in the following situations, and sets out requirements relating to the time and place for submitting the declaration, documentation, etc.:

- The individual receives comprehensive income and is required to make an annual reconciliation;
- The individual earns income from the operation of a business;
- The individual receives taxable income, but the withholding agent does not fulfil its withholding obligations;
- The individual receives income derived outside China;
- The individual deregisters his/her Chinese household registration (hukou) because he/she is moving abroad; or
- A non-resident individual receives wages and salaries from two or more employers in China.

The bulletin adds a new situation (i.e. income earned from the operation of a business) to the other circumstances listed in Article 10 of the amended IIT Law. However, the bulletin does not address the situation where an individual receives taxable income without a withholding agent; as a result, the individual must submit his/her tax return to the tax bureau and pay IIT by the 15th of the following month.

Specific requirements and guidelines relating to the self-declaration

- *Taxpayer receives comprehensive income and has to make an annual reconciliation*

Taxpayer	Deadline for filing declaration	Place for filing declaration
(a) Receives comprehensive income from two or more sources, and the total comprehensive income net of itemized deductions exceeds RMB 60,000	Between 1 March and 30 June of the following year	<p><u>With an employer:</u></p> <ul style="list-style-type: none"> - Submit the tax return to the responsible tax bureau where the employer is located - Where the taxpayer has two or more employers, he/she may choose to submit the tax return to the responsible tax bureau where one of the employers is located <p><u>Without an employer:</u></p> <ul style="list-style-type: none"> - Submit the tax return to the responsible tax bureau where the taxpayer's Chinese household registration (hukou) is located or where the taxpayer habitually resides in China
(b) Receives remuneration for personal services, authors' remuneration and/or income from royalties, and the total comprehensive income net of itemized deductions exceeds RMB 60,000		
(c) The amount of the advance IIT payment is lower than the IIT liability in the relevant tax year		
(d) Claims a tax refund		

- *Taxpayer receives income from the operation of a business*

Taxpayer	Deadline for filing declaration	Place for filing declaration
(a) Income derived by individual industrial and commercial households, sole proprietorships or partnerships from their production and business operations	<p>Advance filing: Within 15 days of the end of each month or quarter</p> <p>Annual reconciliation filing: Before 31 March of the following year</p>	<ul style="list-style-type: none"> - Submit the tax return to the responsible tax bureau where the business operations take place - Where the taxpayer receives the income from two or more business operations, he/she may choose to submit the tax return to the responsible tax bureau where one of the business operations takes place
(b) Income derived by individuals engaged in the provision of educational, medical, consultancy and other compensated service activities		
(c) Income derived by individuals for contractual or leasing operations, subcontracting and subletting of enterprises and institutions		
(d) Income derived by individuals engaged in other production and business operations		

- *Taxpayer receives taxable income, but the withholding agent does not fulfil its withholding obligations*

Taxpayer	Deadline for filing declaration	Place for filing declaration
(a) Resident individual receives comprehensive income	See "Taxpayer receives comprehensive income and has to make an annual reconciliation"	
(b) Non-resident individual receives wages and salaries, remuneration from independent personal services, authors' remuneration and/or remuneration from royalties	<ul style="list-style-type: none"> - Before 30 June of the following year - Where a non-resident leaves Mainland China (except for a temporary departure) before 30 June of the following year, he/she must file the self-declaration before leaving the country 	<ul style="list-style-type: none"> - Submit the tax return to the responsible tax bureau where the withholding agent is located - Where the taxpayer has two or more withholding agents and no tax is withheld, he/she may choose to submit the tax return to the responsible tax bureau where one of the withholding agents is located
(c) Taxpayer receives dividends, interest, income from the leasing of property, income from the transfer of property or incidental income	Before 30 June of the following year	Submit tax return to the responsible tax bureau

- *Taxpayer receives income derived outside China*

Taxpayer	Deadline for filing declaration	Place for filing declaration
Resident individual receives foreign-source income	Between 1 March and 30 June of the following year	<p><u>With an employer in Mainland China:</u></p> <ul style="list-style-type: none"> - Submit tax return to the responsible tax bureau where the employer is located <p><u>Without an employer in Mainland China:</u></p> <ul style="list-style-type: none"> - Submit tax return to the responsible tax bureau where the taxpayer's Chinese household registration (hukou) is located or where he/she habitually resides in China - In the event of an inconsistency between the location of the taxpayer's Chinese household registration and the place of habitual residence, he/she may choose to submit the tax return to the responsible tax bureau in either of the locations - If there is no household registration in China, the individual may submit the tax return to the tax bureau where the individual habitually resides

- *Taxpayer deregisters Chinese household registration (hukou) for emigration from China*

Taxpayer	Deadline for filing declaration	Place for filing declaration
(a) Taxpayer receives comprehensive income for the year in which the hukou is deregistered	- Make annual reconciliation before applying for hukou de-registration - If an annual reconciliation was not made in the previous year, make that reconciliation at the time the reconciliation is made for the year in which the hukou is to be deregistered	Submit tax return to the responsible tax bureau where the taxpayer's Chinese household registration (hukou) is located
(b) Taxpayer receives income from the operation of a business for the year in which the hukou is deregistered		
(c) Taxpayer receives dividends, interest, income from the leasing of property, income from the transfer of property or incidental income for the year in which the hukou is deregistered	Declare the tax compliance status on relevant income before deregistering the hukou	
(d) Taxpayer has outstanding tax liabilities	- Settle the outstanding tax payment before deregistering the hukou - If the taxpayer pays the outstanding tax by instalment, he/she must settle the outstanding tax before deregistering the hukou	

- *Non-resident individual receives wages and salaries from two or more employers in China*

Taxpayer	Deadline for filing declaration	Place for filing declaration
Non-resident individual receives wages and salaries from two or more employers in China	By the 15 th of the following month	Submit the tax return to the responsible tax bureau where one of the employers is located

Documentation requirements for self-declaration

Bulletin 62 publishes a series of forms to be used for the self-declaration and stipulates that taxpayers should prepare relevant information relating to income, itemized deductions, additional itemized deductions, other eligible deductions, donations, preferential tax treatment, etc., when they make the annual reconciliation, and maintain supporting documentation in the event of a tax audit.

Taxpayers who perform the tax filing for deregistering a Chinese household are required to submit relevant forms to the tax bureau to claim the additional itemized deductions and other deductions.

Bulletin 62 also stipulates that taxpayers must submit any information requested by the tax bureau when they file the declaration.

Form Summary

Form	Circumstances
IIT Basic Information Form (Form B)	§ Taxpayer makes an initial filing or changes his/her basic personal information
IIT Annual Self-Declaration Form	§ Taxpayer makes an annual reconciliation of comprehensive income
IIT Self-Declaration Form (Form A)	<ul style="list-style-type: none">§ Taxpayer receives dividends, interest, income from the leasing of property, income from the transfer of property or incidental income, but the withholding agent does not fulfil its withholding obligations• Non-resident individual receives wages and salaries, remuneration for independent personal services, author's remuneration and/or remuneration from royalties, but the withholding agent does not fulfil its withholding obligations§ Taxpayer receives dividends, interest, income from the leasing of property, income from the transfer of property or incidental income for the year in which the hukou is deregistered§ Non-resident individual receives wages and salaries from two or more employers in China
IIT Business Operation Income Filing Form (Form A)	§ Taxpayer earns income from the operation of a business and pays advance tax
IIT Business Operation Income Filing Form (Form B)	§ Taxpayer earns income from the operation of a business and makes an annual reconciliation
IIT Business Operation Income Filing Form (Form C)	§ Taxpayer receives income from the operation of a business from two or more business operations

Method for making self-declaration

Taxpayers can file the self-declaration using the digital filing system, regular mail, etc. or bring the form to the responsible tax bureau in person. Bulletin 62 states that specific measures applicable to taxpayers who are required to make an annual reconciliation of comprehensive income and the filing requirements for taxpayers that receive foreign-source income will be announced separately.

Deloitte observations

Further development of IIT self-declaration regime

With the introduction of annual reconciliation of comprehensive income for tax residents, as well as tax clearance requirements for individuals who deregister Chinese households before emigrating, China's tax filing system is transitioning to an advance withholding/withholding plus self-declaration system. Taxpayers need to be aware of the changes and ensure they are complying with all reporting and filing requirements.

Bulletin 62 provides guidance for situations where a withholding agent fails to comply with its withholding obligations, the taxpayers' obligations to be compliant with the tax regulations and settle any outstanding tax via the self-declaration. A withholding agent's failure to withhold is not a justifiable excuse for an individual taxpayer to avoid his/her tax compliance obligations. A withholding agent may still be subject to penalties for its failure to fulfil the withholding obligations even if the individual taxpayer has made the self-declaration. These measures should enhance tax administration and the collection of IIT.

Bulletin No. 62 also facilitates IIT filing. For example, individuals who receive foreign-source income previously had to make the self-declaration with the responsible tax bureau in the place where the household was registered or the place where the individual habitually resided in China. In practice, individuals may not live or work in the hukou location and thus taxpayers found it inconvenient to file the declaration. Bulletin 62 provides that individuals who receive foreign-source income and who have an employer in China can file the declaration with the responsible tax bureau in the place where the employer is located.

Self-declaration by non-resident individuals

Although non-resident individuals are not required to make an annual reconciliation with respect to their comprehensive income, if IIT has been withheld by the withholding agent on a monthly or transaction basis, the non-resident will still have to make a self-declaration in the following situations:

- The non-resident receives income from the operation of a business;
- The non-resident receives comprehensive income, dividend, interest, income from the leasing of property, income from the transfer of property or incidental income, but the withholding agent does not fulfil its withholding obligations;
- The non-resident receives wages and salaries from two or more employers in China; and
- The non-resident receives taxable income but there is no withholding agent.

Due to the fact that most non-resident individuals are foreigners, such individuals may face greater challenges in complying with the self-declaration requirement, due to language obstacles, cultural differences, length of physical presence in China, and the level of familiarity with Chinese tax regulations and procedures, etc. Non-resident individuals and enterprises with a large population of non-resident employees should ensure they understand the filing obligations and requirements relating to various categories of income and seek professional assistance where necessary to ensure compliance.

Tax clearance upon hukou de-registration for emigration from China

The new tax clearance requirement has garnered considerable attention from individuals that have plans to move to another country. Bulletin 62 provides clear guidance on the requirements, i.e. a taxpayer intending to emigrate must be in compliance with his/her tax obligations for the current year and previous year. A taxpayer must make an annual reconciliation for comprehensive income and income from the operation of a business for the year in which de-registration is to be made (along with an annual reconciliation for the previous year if that was not completed), and declare the tax compliance situation for dividend, interest, income from the leasing of property, income from the transfer of property and incidental income for the year of de-registration and settle the tax due, if any. In addition, if tax is settled by instalment payments, these must be finalized before de-registering the household. Affected taxpayers should understand these rules and ensure they have taken appropriate actions to remain in compliance.

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