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## RSM Tax Advisory (Hong Kong) Limited

## 羅申美稅務諮詢有限公司

Welcome to Tax Flash – RSM Tax Advisory (Hong Kong) Limited’s Newsletter Covering Technical Development in Taxation

### EXTENSION OF CERTAIN TRANSITIONAL INDIVIDUAL INCOME TAX (“IIT”) PREFERENTIAL POLICIES

*On 31 December 2021, the PRC Ministry of Finance (“MOF”) and the State Taxation Administration (“STA”) jointly released Public Announcements [2021] No. 42 and 43 to further extend certain transitional IIT preferential policies provided under Circular Caishui [2018] No. 164 <Notice of issues concerning the transitional policies on preferential tax treatments under the amended PRC IIT law>. These preferential treatments were initially extended for three years from 1 January 2019 to 31 December 2021. Public Announcement [2021] No. 42 also extends the exemption of IIT annual reconciliation filing for qualified taxpayers as prescribed under Public Announcement [2019] No. 94 to the end of 31 December 2023.*

*In this Tax Flash, we set out the major IIT preferential policies extended by Public Announcements [2021] No. 42 and 43.*

#### 1. ANNUAL BONUS<sup>1</sup>

Under the new IIT Law effective 1 January 2019, for PRC tax residents, bonus payment should be aggregated with other comprehensive income<sup>2</sup> derived during the same year to calculate the IIT collectively. Compared with taxing the bonus payment separately (i.e. taxed as a separate source of income without aggregation with other comprehensive income), this would result in a higher applicable IIT rate and may profoundly impact taxpayers.

<sup>1</sup> Annual bonus should be determined in reference to the annual financial performance of the company and the annual work performance of the employee on a collective basis and is paid once a year.

<sup>2</sup> Comprehensive Income includes:

- Income from salary and wages (工資、薪金所得);
- Income from provision of independent personal services (勞務報酬所得);
- Income from author’s remuneration (稿酬所得); and
- Income from royalties (特許權使用費所得)

As a transitional measure, Circular Caishui [2018] No. 164 allowed individual taxpayers elect to continue to enjoy the preferential treatment on annual bonus as prescribed under Circular Guoshuifa [2005] No 9 for three years from 1 January 2019 to 31 December 2021:

- Taxpayers can select not to aggregate the annual bonus with other comprehensive income (i.e. taxed as a separate source of income) for IIT calculation; and
- The annual bonus sum would be divided by the number of months related (capped at 12 months) to determine the applicable IIT rate.

**IIT calculation method for “Annual Bonus” (Circular Guoshuifa [2005] No.9)**

$$\begin{aligned} (a) \quad & \frac{\text{“Annual Bonus”}}{\text{No. of Months the bonus related to (limited to 12)}} \quad \Rightarrow \quad \text{Looks for the Applicable IIT Marginal Rate} \\ (b) \quad & \text{IIT liability for “Annual Bonus”} = \text{“Annual Bonus”} \times \text{Applicable IIT Marginal Rate} - \text{Quick Reckoning Deduction} \end{aligned}$$

Public Announcement [2021] No. 42 extends this transitional policy for another two years (i.e. from 1 January 2022 to 31 December 2023).

## **2. EQUITY INCENTIVES GRANTED BY LISTED COMPANIES**

Same as a bonus payment, a PRC tax resident’s equity-based compensation income should also be aggregated with other comprehensive income derived during the year to calculate the IIT collectively under the new IIT regime.

Circular Caishui [2018] No. 164 allowed individual taxpayers to treat qualified equity incentives granted by listed companies (e.g. Employee Stock Option) as a separate source of income and not aggregate with other comprehensive income for IIT calculation purposes. In cases where there are multiple instalments of equity-based compensation income derived during the same year, the related income should be aggregated to apply the preferential tax treatment. This transitional measure was initially valid for three years from 1 January 2019 to 31 December 2021.

Public Announcement [2021] No. 42 now extends the above preferential treatment for another year (i.e. from 1 January 2022 to 31 December 2022).

### 3. IIT ANNUAL RECONCILIATION FILING EXEMPTION

Under the new IIT regime, IIT on comprehensive income is assessed on an annual basis, but IIT withholding would be performed by the withholding agent (e.g. the PRC employer) on a monthly basis (or when taxable income arises). Final settlement/refund for IIT on comprehensive income will be made at the time the taxpayer performs his/her annual IIT reconciliation filing during the period from 1 March to 30 June next year.

According to the Public Announcement [2019] No. 94 jointly issued by MOF and STA, an individual taxpayer would be exempted from 2019 and 2020 IIT annual reconciliation filing<sup>3</sup> for comprehensive income if:

- The individual's annual gross comprehensive income for the respective year was not more than RMB 120,000 (even with annual IIT underpayment); or
- the individual's annual IIT underpayment on comprehensive income not exceeding RMB 400.


Public Announcement [2021] No. 42 extends the above policy to 31 December 2023.

### 4. TAX-EXEMPT BENEFITS FOR FOREIGN EMPLOYEES

A PRC tax resident is eligible to claim the following deductions under the new IIT regime:

Standard Deduction	<ul style="list-style-type: none"><li>• RMB 60,000 per annum (i.e. RMB 5,000 per month)</li></ul>
Specific Deductions (专项扣除)	<ul style="list-style-type: none"><li>• Basic pension insurance (基本养老保险)</li><li>• Basic medical insurance (基本医疗保险)</li><li>• Unemployment insurance (失业保险)</li><li>• Housing fund (住房公积金)</li></ul>
Itemized Deductions for Specific Expenditure (专项附加扣除)	<ul style="list-style-type: none"><li>• Children's education expenses (子女教育)</li><li>• Continuing education expenses (继续教育)</li><li>• Serious illness medical expenses (大病医疗)</li><li>• Housing mortgage interest (住房贷款利息)</li><li>• Housing rental (住房租金)</li><li>• Expenditures on supporting the elderly (赡养老人支出)</li></ul>
Other Deductions (其他扣除)	<ul style="list-style-type: none"><li>• Qualified enterprise annuities and occupational annuities (企业年金、职业年金)</li><li>• Qualified commercial health insurance and commercial pension plans (商业健康保险、税收递延型商业养老保险)</li></ul>

<sup>3</sup> To qualify for the filing exemption, the IIT withholding agents must have duly fulfilled the withholding obligation.



As a transitional measure, Circular Caishui [2018] No. 164 allowed foreign employees who are PRC tax residents (i.e. reside in China for 183 days or more during the calendar year concerned) to elect either:

- Claim itemized deductions under the new IIT regime; or
- Continue to claim tax exemption on certain fringe benefits<sup>4</sup> as prescribed under Circular Guoshuifa [1997] No 54, i.e. housing reimbursement, language training expenses and children's education expenses.

Due to the relatively low deduction limits for itemized deductions and the additional reporting procedures, the above tax-exempt expatriate benefits are generally more favorable on the potential amount of available deduction.

This transitional measure was initially valid for three years from 1 January 2019 to 31 December 2021. Public Announcement [2021] No. 43 now extends the tax exemption treatment of benefits-in-kinds provided to foreign nationals working in the PRC for another two years (i.e. from 1 January 2022 to 31 December 2023).

## **OUR ASSISTANCE**

The release of Public Announcements [2021] No. 42 and 43 is in line with the government's strategy to ensure the overall reduction of tax burdens for individual taxpayers, especially during the COVID-19 difficult time. Taxpayers should stay abreast of and familiarize themselves with the changes, closely monitor the regulatory and practice developments and seek professional assistance where necessary.

For further information on the above subject and discussion on the potential impact on your group, please feel free to contact us.

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<sup>4</sup> Proof of the authenticity of the expenses in the form of a fapiao is required.

## RSM Tax Advisory (Hong Kong) Limited

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- Assist clients to discuss and clarify matters with tax officials, including transfer pricing and advance rulings
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