Deloitte.

Global Employment Solutions

Global InSight

27 February 2015

In this issue:

Malaysia: Moratorium for Expatriate Services at the Immigration Department 1
People's Republic of China: Tax authorities stepping up enforcement of PRC individual income tax 2
Global Rewards Updates: Philippines: Clarification on the tax treatment of share-based awards 5

Malaysia:
Moratorium for Expatriate Services at the Immigration Department

Overview

The Malaysia Immigration Department Headquarters (MYID HQ) has imposed a moratorium period on actions against overstay offences.

Changes to note

The moratorium period will take effect from 10 February 2015 – 31 May 2015, where the MYID HQ in Putrajaya will not take any action against expatriates who have overstayed due to the following reasons:

1. Awaiting approval from MYID HQ for a second Special Pass (SP);
2. Awaiting approval from the Expatriate Services Division (ESD) committee for company registration of ESD portal; or
3. Awaiting completion of immigration audit by the MYID HQ.

Any expatriate who has overstayed due to the above reasons will be granted an SP (gratis). The moratorium period does not apply to expatriates who have overstayed in Malaysia for reasons other than the above.

Deloitte's view

We have observed a significant delay in the processing of applications at the MYID HQ recently. The moratorium period is a temporary measure by the MYID HQ to manage the high number of applications while they continuously strive toward making improvements to the newly implemented ESD system.

The MYID HQ targets for the ESD system to be stabilised by the end of May 2015, where applications are expected to be processed smoothly to meet the initial five working days' turnaround time announced to the public during its launch in June 2014.

— Ang Weina (Kuala Lumpur)
Partner
Deloitte Malaysia
angweina@deloitte.com

Jehan Soraya Noriskandar (Kuala Lumpur)
Assistant Manager
Deloitte Malaysia
jnoriskandar@deloitte.com

Husna Abu Zarim (Kuala Lumpur)
Assistant Manager
Deloitte Malaysia
nabuzarim@deloitte.com

People's Republic of China: Tax authorities stepping up enforcement of PRC individual income tax

Overview

The tax authorities across the country are stepping up their efforts to enhance the collection and administration of individual income tax (IIT) and, as part of this initiative, are carrying out more frequent and more expansive investigations of individuals and companies. This trend is expected to continue in 2015, with an increased focus on both foreigners working in China and Chinese individuals receiving foreign-source income.

Key implications

Foreigners working in China: IIT compliance by foreigners working in China has featured prominently on the radar of the tax authorities in recent years. Below is a brief summary of some of the initiatives taken by the authorities in Beijing, Guangzhou, and Shanghai and Jiangsu.

Beijing: In late 2013, the Beijing Local Tax Bureau set up an International Tax Administration Division (ITA Division) to enhance the collection of IIT and the administration of cross-border secondees. Soon thereafter, the following took place:

- Certain foreign investment enterprises (FIEs) with relatively large populations of foreign employees in five districts (i.e. Chaoyang, Dongcheng, Xicheng, Haidian and Shunyi) were asked to carry out "self-inspections" of the IIT compliance of their foreign employees. Although the inspections have been completed, it is possible that tax audits may be initiated, based on the results of the self-inspections.
- The Beijing Local Tax Bureau entered into arrangements with several municipal departments (such as the Beijing Industrial and Commercial Bureau, Beijing Municipal Human Resources and Social Security Bureau, Beijing Public Security Bureau) to share

and exchange information to improve IIT compliance by foreign individuals working in Beijing. Foreigners that have found to have underpaid tax may not be allowed to depart from China.

In addition to the above, the number of IIT audits are on the rise, and it is likely that the self-inspection initiative will be expanded to FIEs that were not included in the first round of self-inspections.

Guangzhou: An “internal working order” issued by the Guangzhou tax authorities in 2013 (Suidishuihan [2013] No. 98) required the tax bureaus at all levels to begin conducting tax audits or ask companies to carry out self-inspections. Companies with foreign employees (including employees from Hong Kong, Macau and Taiwan) and, particularly senior executives, may be targeted for audit/self-inspection if their employees have the following circumstances:

1. Constant nil filing;
2. Low-income reporting; and
3. Receiving salary income paid from overseas companies.

The Guangzhou Municipal Local Taxation Bureau established the Large Business Division in January 2014 to administer and collect taxes from Guangzhou-based company headquarters and businesses and their subsidiaries, as well as other companies that have more than RMB 30 million in local tax obligations (including tax withholding obligations).

Several district-level tax authorities, including the Large Business Division, have issued official notices to companies with regard to on-site tax audits or the production of documentation and rounds of city-wide audits and self-inspections. Taxpayers or withholding agents have been asked to provide inspection results and relevant documentation to the tax bureau within short periods of time, with an inspection covering the prior three to five years, depending on the location.

Shanghai and Jiangsu: The Shanghai and Jiangsu tax authorities conduct frequent tax audits and self-inspections on the compliance status of foreign employees of certain FIEs. Additionally, these authorities have begun to strictly enforce registration and reporting requirements relating to equity plans, as well as the rules relating to the employers’ annual tax clearance and the tax de-registration process for foreign individuals, etc.

Chinese individuals receiving foreign-source income

Under current IIT rules, Chinese individuals generally are subject to PRC IIT on their worldwide income, although until recently, the worldwide taxation requirement was not strictly enforced. This is beginning to change. The OECD base erosion and profit shifting (BEPS) initiative signifies strengthened international cooperation on the tax administration of cross-border transactions/mobility, and China has expressed strong support for the project. Hence, individuals engaging in cross-border transactions or receiving foreign-source income could be subject to stricter scrutiny. In many locations, the local tax authorities already have taken or are starting to take steps to improve the administration of Chinese individuals receiving foreign-source income. This trend is in line with the anticipated China IIT reform that is heading towards a comprehensive IIT reporting system.

Beijing: Although the Beijing Local Tax Bureau has not yet announced any concrete plans to tackle the administration of Chinese individuals with overseas income, we understand that this is included on the 2015 project plan for the ITA Division. Additionally, recent tax audits included the compliance status of Chinese outbound assignees and some companies have been challenged by the tax authorities for failing to comply with their IIT withholding obligations on outbound assignees' overseas income paid or borne by Chinese companies during the overseas secondment period.

Guangzhou: Following the issuance of Suidishuihan No. 65 with respect to the IIT collection enforcement of Chinese outbound assignments, 150 large companies recently were asked by the Guangzhou tax authorities to attend a training that focused on the Chinese tax implications of Chinese outbound assignees and the corresponding withholding tax obligations for the companies. More action can be expected in the future.

Shanghai and Jiangsu: Similar to Beijing, the reporting status of outbound assignees has been included in self-review documentation of some tax bureaus and companies may be challenged if they lack proper internal controls. In addition, some local tax bureaus have adopted a strict position on the employer's responsibility in IIT filing for outbound assignees, particularly with respect to their overseas income during the international assignment.

Deloitte's view

In view of the above, companies and individuals should consider the following actions:

- Conduct an internal review of the tax compliance status of foreigners working in China to ensure compliance and enhance internal controls on risk management;
- Ensure that any existing arrangements are in line with prevailing tax regulations and local practice, and are properly documented and reported to the tax bureau, where required;
- Review current tax compliance status of Chinese outbound assignees to ensure that the relevant IIT withholding tax and/or reporting obligations have been fulfilled from a company and an individual perspective; and
- Obtain professional advice as needed.

— Gus Kang (Beijing)
Partner
Deloitte People's Republic of China
gukang@deloitte.com.cn

Huan Wang (Beijing)
Partner
Deloitte People's Republic of China
huawang@deloitte.com.cn

Mona Mak (Hong Kong)
Partner/Principal
Deloitte People's Republic of China
monmak@deloitte.com.hk

Tony Jasper (Hong Kong)
Partner
Deloitte People's Republic of China
tojasper@deloitte.com.hk

Sandy Cheung (Shanghai)
Partner
Deloitte People's Republic of China
sancheung@deloitte.com.cn

Joyce W. Xu (Shanghai)
Partner
Deloitte People's Republic of China
joycewxu@deloitte.com.cn

Fei Fei Li (Shenzhen)
Director
Deloitte People’s Republic of China
ffli@deloitte.com.cn

Global Rewards Updates:
Philippines: Clarification on the tax treatment of share-based awards

Background

The Philippine tax authorities issued Revenue Memorandum Circular 79-2014 (“RMC 79-2014”) on 31 October 2014, to clarify the tax treatment of share option plans.

Although the Circular was issued in relation to the tax treatment of share option plans, historically other plan types (e.g. Restricted Stock Units, Performance Share Plans) have been treated as benefits-in-kind in the same way as share option plans. Therefore, the clarifications provided in the Circular should apply to all share plan types.

Taxable amount

Previously, it was common practice for share options to be taxable on exercise, based on the difference between the Fair Market Value (FMV) at exercise and the exercise price.

RMC 79-2014 clarified that the taxable amount on the exercise of share options should be the difference between the book value (value in the company’s accounts) at exercise or the FMV of the shares at exercise (whichever is higher) and the exercise price.

Although the Circular does not directly address other award types (e.g. Restricted Stock Units, Performance Share Plans), it implies that the taxable amount for share awards should be the higher of the book value at delivery and the FMV at delivery.

Fringe benefit tax

Managerial and supervisory employees: Previously, it was unclear whether share options/awards received by managerial employees (i.e. those vested with powers to lay down and execute management policies and/or to be involved in all functions of hiring other employees) or supervisory employees (i.e. those who, in the interest of the employer, effectively recommend such managerial actions if the exercise of such authority requires the use of independent judgment) should be taxed as compensation or fringe benefits. The tax treatment of awards received by such employees was dependent on the rules and structure of the relevant plan.

RMC 79-2014 clarified that share options/awards received by managerial or supervisory employees should be treated as fringe benefits and subject to fringe benefit tax, regardless of the plan rules and structure.

Fringe benefit tax is an employer liability in the form of a final withholding tax imposed on the grossed-up monetary value of the benefit received by the individual. Employers will therefore be required to pay fringe benefit tax (at up to 32%) on the grossed up taxable amount of share options/awards received by managerial or supervisory employees.

It should be noted that fringe benefit tax is only applicable if the award costs are recharged to the local Philippine entity, an expense relating to the awards is recorded in the Philippine entity's accounts or a cash payment is made via the Philippine payroll.

If this is not the case, then no fringe benefit tax would be payable, even for managerial and supervisory employees. Instead, the awards would be subject to income tax. No employer withholding would be required; instead the employee should settle any taxes due via their annual tax return.

Rank and file employees: Share options/awards received by rank and file (i.e. non-managerial or non-supervisory) employees have historically been clearly defined, and therefore treated, as compensation. Such awards continue to be liable to income tax, subject to employer withholding in certain circumstances. While income tax is applied at the same rate (up to 32%) as fringe benefit tax, this is payable on the taxable value with no gross-up being applied and is an employee, rather than an employer, liability.

Additional filling requirements

RMC 79-2014 also introduced the following new reporting requirements for companies granting share options (which should also be applicable to share awards):

Share option/share award grant: Within 30 days of the date of grant, the grantor should submit to the relevant Revenue District Office, a statement under oath indicating the following:

- Terms and conditions of the share option/award;
- Names, TINs and positions of the grantees;
- Book value, fair market value, par value of the shares at the grant date (if applicable);
- Exercise price, exercise date and/or period (if applicable);
- Taxes paid on the grant, if any;
- Amount paid for the grant, if any.

These apply to all awards granted after 1 November 2014.

Share option exercise/share award delivery: The grantor should file a report on or before the 10th day of the month following the month of exercise/delivery including the following:

- Exercise/delivery date;
- Names, TINs and positions of those who exercised the option/received the share award;
- Book value, fair market value, par value of the shares at the exercise/delivery date;
- Type of settlement (i.e. cash or equity);
- Taxes withheld at exercise/delivery, if any;
- Fringe benefits tax paid, if any.

These apply to all awards exercised/delivered after 1 November 2014.

The new requirements apply in addition to existing reporting requirements in relation to share options/awards treated as compensation or as fringe benefits.

Deloitte view

Employers should ensure they calculate the taxable amount arising in relation to share option exercises and share awards deliveries using the method specified in RMC 79-2014.

Employers should ensure they are applying the correct tax treatment to awards received by their employees, taking into account the employee's role and position and whether there is a recharge of costs to the Philippine entity, an expense relating to the awards is recorded in the Philippine entity's accounts or a cash payment is made via the Philippine payroll.
Employers should ensure they comply with the new additional reporting requirements in relation to the grant and exercise of share options/delivery of share awards, whilst continuing to comply with existing applicable reporting requirements.

— Sean Trotman (New York)
Partner
Deloitte Tax LLP
strotman@deloitte.com

Rive Rutke (Chicago)
Director
Deloitte Tax LLP
rrutke@deloitte.com

Peter Simeonidis (New York)
Principal
Deloitte Tax LLP
psimeonidis@deloitte.com

Mark I. Miller (San Jose)
Senior Manager
Deloitte Tax LLP
mamiller@deloitte.com