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Hong Kong: Automatic exchange of financial information and tax residence

Overview

Automatic exchange of financial information: A law that became effective in Hong Kong on 30 June 2016 provides the legal framework for Hong Kong to implement the automatic exchange of financial account information (AEOI), based on the standards set out by the OECD.

Under the new law, financial institutions (FI) are required to identify financial accounts held by tax residents of "reportable jurisdictions." FIs are required to collect the reportable information of such accounts, and provide it to the Inland Revenue Department (IRD), which will exchange the information with the tax authorities of AEOI partner jurisdictions on an annual basis. Hong Kong intends to carry out AEOI only with jurisdictions that have signed a comprehensive double taxation agreement (CDTA) or tax information exchange agreement (TIEA) with Hong Kong.

Impact on individuals: Individuals who have a financial account, have been living in or are domiciled in jurisdictions other than Hong Kong should be aware that some of their financial information may be automatically shared with overseas tax authorities.

The key terms under the AEOI law are as follows:

- **Financial institutions (FIs):** A broad range of FIs are covered, including but not limited to banks, insurers, wealth and asset managers, and family trusts.
- **Financial information:** The financial information to be reported includes dividends, interest, account balances or value, income from certain insurance products, sales proceeds from financial assets and other income generated with respect to assets held in the account or payments made with respect to the account.
- **Tax residence:** The determination of whether an individual is a tax resident of a jurisdiction can be made based on the individual's physical presence or length of stay in a country (e.g. whether more than 183 days within a specified period, which can be a tax year or a rolling 12 months).

Implementation timeline: The timeline of the AEOI rollout is as follows:

- January 2017: Self-certifications will be required from account holders for all new accounts opened on or after 1 January 2017. For accounts that were opened before that date, FIs can seek self-certification from the account holder to verify his/her tax residence. FIs will be required to collect the required information for reportable accounts.
- September 2018: FIs furnish the information to the IRD for exchange with AEOI partners.

The IRD will announce the list of AEOI partners by the end of 2016, i.e. the jurisdictions with which Hong Kong has entered into AEOI agreements. As at 30 September 2016, Hong Kong had signed 35 CDTAs and seven TIEAs.

Deloitte's view

Data transparency and global connectivity amongst tax authorities is a global trend. The AEOI law is designed to reinforce Hong Kong's support of international initiatives to enhance tax transparency and combat cross-border tax evasion.

Whilst risk exposures associated with disclosure are on individuals, noncompliance with the rules can have a reputational impact on employers. Additionally, efforts to reinforce the disclosure of investment information by other jurisdictions has impacted mobility and assignees' choice of assignment location.

Employers may wish to provide guidance to their employees on how tax residence is determined as part of the self-certification process and ensure that this aligns with current tax filing positions.

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Ireland:
Budget 2017

Overview

The Irish Minister for Finance, Michael Noonan, Teachta Dála (TD), delivered Budget 2017 on Tuesday, 11 October 2016, against a backdrop of strong economic growth, despite uncertainties surrounding how Brexit will affect the Irish economy. From a personal tax perspective, the tax measures introduced see much anticipated cuts to the Universal Social Charge (USC) rates, along with measures to improve Ireland's competitiveness in the international arena.

Universal Social Charge (USC): As had been widely publicized, the minister announced a reduction to the lower USC rates of 1%, 3%, and 5.5%, each by 0.5% effective 1 January 2017. The higher USC rate of 8% will remain in place, which means that the marginal rate will remain at 52% for income levels in excess of €70,044. The marginal rate for those with income of up to €70,044 will be reduced to 49%.

For self-employed individuals, income in excess of €100,000 will continue to be liable to USC at the higher rate of 11%. The USC exemption for those earning less than €13,000 will continue to apply. The new rates and bands for employment income are as follows:

USC Band	USC Rate
First €12,012	0.5%
Next €6,760	2.5%
Next €51,272	5%
Balance	8%

Special Assignee Relief Programme (SARP): The SARP scheme, which was due to expire at the end of 2017, has been extended for another three years until the end of 2020. There were no references made to any changes or enhancements to the scheme.

Foreign Earning Deductions (FED): The FED scheme has also been extended to 2020. In addition, the scheme was tweaked to reduce the minimum number of days to be spent abroad from 40 days to 30 days. The list of qualifying countries was also expanded to include Pakistan and Colombia. This adds to a significant number of countries already covered in Asia and the Middle East, and increases the current scope of coverage in Central and South America, including Brazil, Mexico, and Chile.

Share Scheme Incentives for Small and Medium-Sized Enterprises (SMEs): Following a public consultation carried out earlier this year, the minister flagged a new share scheme to be introduced in Budget 2018 that will focus on SMEs.

Entrepreneur Relief: The minister announced an amendment to capital gains tax (CGT) entrepreneur relief, which was introduced in Finance Act 2015. On gains up to €1 million, the tax rate applied to gains arising on the disposal of qualifying assets after 1 January 2017 has been reduced from 20% to 10%. Gains in excess of €1 million will still be chargeable at a 33% tax rate. The minister indicated that the €1 million lifetime limit will be reviewed in future budgets.

Rental Properties: The restriction on interest deductibility for loans on rented residential property is being reduced. Effective 1 January 2017, the rate of deduction for rental property loan interest will be 80%, with a view to full deduction phased in over subsequent years. The rate of deduction will be increased by 5% per annum until the full deduction for the interest is met. The income ceiling that applies under the Rent-a-Room scheme has also been increased by €2,000 in the budget, to bring the threshold to €14,000 a year.

Home Carer's Credit: The home carer's credit is being increased by €100 to €1,100.

Pay-as-You-Earn (PAYE) Tax Consultation Process: A consultation process will take place focused on the modernization of the PAYE tax system that will seek to streamline business processes and reduce administrative costs for employers. The consultation will run until 12 December 2016, but any changes will not take effect until 1 January 2019, at the earliest.

Additional Resources for the Irish Revenue Commissioners: The minister has also promised additional employee and technology resources for the Irish Revenue Commissioners for 2017. This is to target non-compliance and is expected to raise €50 million in 2017.

Deloitte's view

The minister announced the terms of reference for a review of the corporate tax system, and we would like to see an equivalent review of the personal tax regime, which has become increasingly complex and contains a range of inequalities. A clear strategy to reduce the personal tax burden on work/earned income remains a key priority for the future.

The extension of the SARP scheme to 2020 provides certainty for mobile workers, but does not enhance the existing scheme.

While the announcement of a new share scheme incentive for SMEs is welcomed, it is disappointing that it will not have a wider focus and implementation will be delayed until 2018. The minster noted that any new scheme would have to satisfy EU State Aid rules. We hope the Department of Finance will consult widely on the proposed SME share scheme to ensure it fits its purpose and achieves its intended goals.

The phased reintroduction of interest relief for residential landlords is "light" in terms of trying to encourage landlords to come back into the market and invest, but in view of limited resources available, at least it is positive and in the right direction.

We hope you will find Deloitte's commentary on Budget 2017 to be useful and look forward to bringing you further insights on the Finance Bill when it is released on 20 October 2016.

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Ireland:
Posted workers: New notification obligations for sending entity

Overview

As of 28 July 2016, Ireland has transposed EU Directive 2014/67/EU ("the Directive") on the enforcement of EU Directive 96/71/EC concerning the posting of workers through the European Union (Posting of Workers) Regulations 2016 (the "Regulations").

The aim of the Regulations is to ensure that workers posted to Ireland can avail themselves of better employment protections and have the ability to enforce the rights that posted workers are entitled to under the original Posted Workers Directive.

The key measures that are being introduced in the Regulations include:

Notification to Workplace Relations Commission (WRC): On posting workers to Ireland, EU-based service providers must notify the WRC of the postings and provide certain information, such as the identity of the service provider, the anticipated number of posted workers and details related to the postings (e.g., duration, location, and the services being provided). The notification must be in English and in a prescribed form.

The service provider must also designate a location to the WRC whereby it will keep and make available information related to the posted workers, including details of the terms and conditions of employment, pay slips, timesheets or equivalents, and proof of payment of wages. The service provider should designate a contact person to liaise with the WRC for document requests. The designated location and contact person do not need to be in Ireland.

"Service provider" is not defined either in the Regulations or the Directive; however, Article 1, Paragraph 3 of EU Directive 96/71/EC sets out the situations involving service providers that fall within the scope of the Directive and the Regulations:

1. Post workers to the territory of a Member State on their account and under their direction, under a contract concluded between the undertaking making the posting and the party for whom the services are intended, operating in that Member State, provided there is an employment relationship between the undertaking making the posting and the worker during the period of posting (i.e., to service a contract in another Member State).
2. Post workers to an establishment or to an undertaking owned by the group in the territory of a Member State, provided there is an employment relationship between the undertaking making the posting and the worker during the period of posting (i.e., an intra group transfer).
3. Being a temporary employment undertaking or placement agency, hire out a worker to a user undertaking established or operating in the territory of a , provided there is an employment relationship between the temporary employment undertaking or placement agency and the worker during the period of posting (i.e., placing an agency worker in another EU state).

It is important for the non Irish service provider who is posting workers to Ireland to be aware of this WRC notification obligation in all circumstances, as failure to comply is a criminal offense with a maximum potential fine of €50,000. The WRC notification is in addition to any employment permit requirements that may be applicable to the postings.

Introduction of subcontracting liability: The Regulations also introduce a new subcontracting liability in the construction sector to ensure posted workers in this sector are paid the applicable statutory rates of pay by their direct employers (i.e., the subcontractors). If the applicable rates are not paid, the contractors can also be held liable for any shortfalls despite not being the direct employer of the posted workers. It is also worth noting that the relevant statutory rates of pay may not necessarily be limited to the national minimum wage rates in circumstances in which there are registered employment agreements governing the construction sector.

However, there is a defense of due diligence for contractors in any claims for non-payment of statutory rates of pay. Contractors may claim this defense if they can show that they have taken all reasonable steps to ensure that the subcontractors have complied with the Regulations.

Similarly, as the Regulations are based on EU legislation, Irish-based employers should also ensure that they comply with the local notification requirements if they are posting workers to other EU.

Deloitte's view

The above measures will be relevant to contractors and subcontractors alike, as well as EU-based employers and/or Irish employers with EU operations.

The Regulations do not stipulate a minimum duration for assignments before the obligation to notify arises. Consequently, even though this cohort may not be the intended target of the Regulations, strict compliance will require a declaration to be made for short-term (including same-day) business travelers whose activities fall into one of the three scenarios set out above.

It is important that relevant stakeholders are aware of the Regulations related to business travelers, as well as traditional assignments/secondments to Ireland, in order to take the steps necessary to comply with the notification requirements.

The new subcontracting liabilities will likely mean increasing oversight by contractors over subcontracting arrangements in order to potentially avail themselves of the due diligence defense provided by the Regulations, which, in some cases, may negate the benefits of subcontracting.

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Malaysia:
Budget 2017

Overview

The 2017 National Budget was announced by the Minister of Finance, Malaysia, on 21 October 2016. Below are the relevant issues from the individual tax perspective:

Tax relief for lifestyles

Under the current legislation, the following tax reliefs are available to encourage individuals to develop reading habits, adopt healthy lifestyles, and use computers and the Internet:

Tax relief	Tax relief (max) (RM)
Purchase of reading materials (excluding newspapers and banned reading materials)	1,000
Purchase of sports equipment	300
Purchase of a computer (claimable once in every three years)	3,000

To provide more flexibility for taxpayers, it is proposed that the above reliefs be combined into a new relief known as "lifestyle relief," with a limit of up to RM 2,500 per year. The scope of this new relief will include the following:

1. Purchase of printed daily newspapers
2. Purchase of smartphones or tablets
3. Internet subscriptions
4. Gymnasium membership fees

Effective date: Year of assessment 2017

Tax relief for fees paid to child care centers and kindergartens

To alleviate the cost of child care and early childhood education paid by working parents, a new tax relief of up to RM 1,000 is proposed for individual taxpayers (either parent) who enroll their children up to six years old in child care centers or kindergartens registered with the Department of Social Welfare or the Ministry of Education.

Effective date: Year of assessment 2017

Tax relief for the purchase of breastfeeding equipment

To encourage and support women to return to work while continuing to breastfeed their infants, a new tax relief for the purchase of breastfeeding equipment (including manual/ electric breast pumps, cooler bags, and containers for collection and storage) is provided to women taxpayers with children up to two years old. This relief can be claimed once every two years.

Effective date: Year of assessment 2017

Deloitte's view

Despite the strong headwinds brought by the slowdown in the global economy during the past year, declines in oil and commodity prices, Ringgit depreciation, and political instability, our economy is still holding up modestly well due to its diversity, resilience, and solid fundamentals.

The 2017 National Budget, titled “Ensuring Unity and Economic Growth, Inclusive Prudent Spending, Well-Being of the People,” mainly focuses on enhancing the well-being of the people by raising their disposable income, while also mitigating the rising cost of living, in order to achieve the ultimate goal of transforming Malaysia into a developed and high-income economy.

From an individual tax perspective, the 2017 National Budget has strong social aspects that are meant to encourage people to develop reading habits, adopt healthy lifestyles, and use computers and the Internet. For young middle-income families with working parents, new tax reliefs have been introduced (i.e., to purchase breastfeeding equipment or to alleviate the cost of registered child care centers, nurseries, or kindergartens). This is to support and encourage women to remain in the workforce even after having children.

Only resident tax payers are eligible for the above mentioned tax reliefs.

Pending the issuance of the Finance Bill, the above comments were formed solely based on the Budget Speech read by the Minister of Finance. We will provide an update if there are any further amendments to the current tax legislation arising from the Finance Bill that will impact the individual income tax.

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People’s Republic of China: Favorable tax treatment extended to more equity compensation plans / contributions of technology

Overview

China’s Ministry of Finance (MOF) and the State Administration of Taxation (SAT) jointly issued a circular on 20 September 2016 (Caishui [2016] No. 101 (Circular 101)) that provides detailed guidance on the preferential individual income tax (IIT) policies relating to equity compensation plans (i.e. stock options, restricted and unrestricted stock awards) and capital contributions made to a Chinese company in the form of technology. On 28 September 2016, the SAT issued Bulletin 62 to provide further guidance on the implementation of Circular 101. Both Circular 101 and Bulletin 62 apply as from 1 September 2016.

The key IIT incentives provided in the new rules on equity compensation plans are as follows:

- Favorable IIT treatment is extended to equity compensation plans offered by unlisted companies;[1] specifically, taxation of equity awards granted to employees may be deferred until the time the employee disposes of the equity;
- Equity compensation plans offered by companies listed on the Shanghai and Shenzhen stock exchanges continue to benefit from the tax treatment provided in earlier guidance, but Circular 101 extends the period for the individual to settle the tax due; and
- Favorable IIT treatment is offered to investors that make equity investments in Chinese companies using achievements in technology.

Key implications

Equity compensation plans offered by unlisted domestic companies

Prior to Circular 101 and Bulletin 62, preferential IIT treatment was available only for equity compensation plans offered by listed companies and qualifying high-tech companies (discussed below). For employees of most unlisted companies, the relevant income derived from these plans was subject to Chinese IIT as "employment income" at the time of exercise/vesting at a progressive tax rate ranging from 3% to 45%. Capital gains realized at the time of disposal of the relevant equity were subject to tax as a "transfer of property" at a flat rate of 20%.
The new guidance, however, provides for deferred taxation on income derived from qualified equity compensation plans (including stock options and restricted and unrestricted stock awards) granted by unlisted domestic companies.

Qualified Plans:

Tax deferral point: Unlike the previous treatment, under which income derived from equity compensation plans was taxed separately as employment income and capital gains at two different points of taxation, Circular 101 provides that the taxation of income can be deferred to the time the relevant equity is sold; thus, the income will be taxed only as a "transfer of property" at a flat rate of 20% at the time of sale. Taxable income for these purposes is defined as the gross proceeds from the sale of the equity reduced by the original cost (e.g. the exercise price paid by an employee) and reasonable taxes and expenses incurred.

The impact of deferred taxation could be significant: it will benefit employees that may not have sufficient cash flow to pay tax at the time the option is exercised or the restricted stock is vested, and will reduce the tax burden by applying a flat rate of 20%.

Qualifying industries: Circular 101 introduces a "negative list" of industries in which companies operating in a listed industry will not be able to apply for the deferred treatment for its employees. Industries on the negative list include real estate development, wholesale and retail sales, accommodations and catering, etc.

Conditions: Circular 101 sets out a number of requirements that must be met for an equity compensation plan to qualify for the deferred treatment:

- The unlisted company offering the plan must be a Chinese resident company;
- The plan must be approved by the company's board of directors and shareholder meetings (or by the relevant government authorities where no shareholder meeting has been set up for certain state-owned companies);
- The underlying shares of the plan must be those of the granting company, i.e. if the plan grants shares of the company's affiliates, the plan will not qualify for deferral treatment (however, for stock award plans, the underlying shares may be shares of other domestic resident companies that were obtained by the granting company in exchange for contributions relating to achievements in technology);
- The eligible participants in the plan must be core technical personnel and senior management employees determined by the board of directors or shareholder meetings, and the total number of participants cannot exceed 30% of the average active employee population in the previous six months;
- The shares must be held for a minimum period, as follows:
    - For stock options, the period between the grant date and the sale date must be three years or more, and the shares must be held for one year or more after the employee exercises the option;
    - For restricted stock awards, the shares must be held for three years or more from the grant date, and one year or more after the restriction lapses or is removed; and
    - For unrestricted stock awards, the shares must be held for three years or more.
- For stock option plans, the period between the grant date and the exercise date cannot be longer than 10 years; and
- The business of the relevant company cannot be in one of the industries on the negative list, determined by reference to the main business revenue of the company in the previous year.

If a plan fails to meet all of the above requirements, deferred taxation will not apply and the equity income will be taxed as income from a nonqualified plan.

Nonqualified Plans: Where employees acquire shares from their employer at a price lower than the fair market value (FMV), but the equity compensation plan does not qualify for deferred taxation, the income derived from the "nonqualified” equity compensation plan (i.e. the difference between the lower acquisition price and the FMV) must be taxed at the time the shares are acquired. However, Circular 101 provides for a special method to calculate tax due (initially introduced by Caishui [2005] No. 35 (Circular 35) for listed companies) in this situation, under which the income may be divided by the “number of stipulated months” in the vesting period (capped at 12), to determine the applicable tax bracket.

Although less favourable than the deferred taxation method available for qualified plans, the application of the special tax calculation method may be beneficial to nonqualified plans, if compared to the previous treatment under which all of the equity income would be added to the normal salary, likely resulting in a much higher marginal tax rate for the relevant month.

Equity compensation plans offered by listed companies

The tax treatment of equity compensation plans offered by listed companies basically remains unchanged (i.e. the rules under Circular 35 continue to apply). Employees will be taxed at the time an option is exercised (for stock options) or when a restriction lapses or is removed (for restricted stock awards), and the relevant income will be taxed as employment income, but separately from the normal salary, under the preferential tax calculation method provided in Circular 35.

However, Circular 101 offers one favourable development for senior executives. Since such individuals may not have sufficient cash to pay the tax when exercising the option, the previous guidance required the tax to be paid in instalments over a six-month period where the income derived from qualifying equity plans offered by companies listed on the Shanghai and Shenzhen stock exchanges. Circular 101 extends the instalment period from six to 12 months.

Capital contributions made in the form of technology achievements

Where a taxpayer makes a capital contribution to a Chinese company in the form of a technology achievement, the taxpayer is considered to be disposing of the technology achievement for income tax purposes and, therefore, will be subject to tax on any gains derived from the disposal. However, an individual taxpayer may pay the tax in instalments over a five-year period, and a corporate taxpayer may spread the gains over five years for income tax purposes.

Circular 101 introduces a new deferral tax treatment for the situation described above, under which the taxpayer may elect to defer the tax until the disposal of the relevant shares. The taxable gains will be calculated by deducting the original cost of the achievement in technology, as well as any reasonable expenses and taxes, from the gross income derived from the sale of the shares. To qualify for the treatment, the technology achievement used for the capital contribution must be in the form of patented technology, software copyright, etc.

Filing requirements

Where a taxpayer elects for a type of tax deferral treatment provided by Circular 101, the relevant company must submit certain information and documents relating to the plan (e.g. the names of the participants, description of the plan, meeting minutes of the board of directors, etc.) to the competent tax authorities; otherwise, the deferral treatment will be denied.

Where the tax deferral treatment has been granted to an individual, the relevant company, acting as the IIT withholding agent, must submit an annual report detailing the relevant information until disposal of the underlying shares. The report must be submitted within 30 days of the subsequent year.

Once the IIT is triggered when the underlying shares are disposed of, the withholding agent and the taxpayer must provide documents to substantiate the income, original cost, expenses and taxes to the competent tax authorities for assessment purposes.

Deloitte’s view

Circular 101 is a new benchmark for the favorable IIT treatment offered to equity compensation plans of Chinese companies. It provides substantial tax benefits to domestic resident companies that implement equity compensation plans, particularly unlisted companies. Before Circular 101, preferential tax treatment was available only to equity compensation plans granted by listed companies or stock awarded by qualifying high-tech companies. Circular 101 expands the scope of beneficial tax treatment and the potential beneficiaries:

- For qualifying equity compensation plans granted by unlisted companies (including companies whose shares are quoted on the NEEQ), taxation may be deferred to the time the relevant shares are sold, and a flat rate of 20% will be imposed on the gains.
- For nonqualified stock incentives acquired by employees from an unlisted employer, the special tax calculation method provided in Circular 35 may be applied; previously, this method applied only to plans offered by listed companies.
- For Chinese listed companies, the relevant tax payment on employment income derived from equity compensation plans by senior executives may be made in installments over a 12-month period, which is longer than that under the previous treatment.

To enjoy the preferential tax treatment described above, taxpayers and the relevant companies must comply with the tax filing and reporting requirements set out in Circular 101. It is worth noting that, according to Circular 101, the tax authorities will expand cooperation and information sharing with company registration authorities to ensure that tax can be timely collected when the underlying shares are disposed of.

Companies already operating equity compensation plans, or that are considering the rolling out such plans, should consider conducting an internal assessment or seeking professional advice on qualifying for the incentives, and comply with the reporting and withholding requirements.

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