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GES NewsFlash

China

Deloitte Tohmatsu Tax Co.

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

(1) 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.

(2) Key implications

1) 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.

2) 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

(3) 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.

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