

Hwuason Alerts.

A summary of China tax developments for the fortnight ending 31 September 2009



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SECOND ARRANGEMENTS TARGETED BY SAT

The State Administration of Taxation (SAT) has issued a *Notice Concerning the Inspection of Enterprise Income Tax Collection on Foreign Entities' Provision of Services to Domestic Companies through Secondment Arrangement* (Notice 103). The Notice deals with the circumstances where a non-resident enterprise second employees to a resident enterprise and charges the resident enterprise in respect of the employees' salary.

TESTS FOR OVERSEAS CHINESE

Page 2 of this edition of Hwuason Alerts discusses some recent clarification of the application of the individual income tax, including in relation to overseas Chinese ("Huaqiao" in Chinese Mandarin). To be entitled to the monthly RMB4,800 tax free threshold (as with other foreign employees) overseas Chinese must satisfy the following tests:

1. Have received permanent residency in a foreign country and in fact have lived overseas for at least 2 years;
2. Have not obtained permanent residency, but have lived overseas legitimately for at least 5 years (the total months overseas within the 5 years cannot be less than 30 months)
3. Chinese who study or worked abroad temporarily are not regarded as the Overseas Chinese.

NEW RULES FOR CLAIMING BENEFITS UNDER DOUBLE TAXATION AGREEMENTS

The SAT issued circular Guoshuifa [2009] No.124 entitled "Administrative Measures for Non-Tax Residents to Enjoy Treatments on Income under DTA (Trial)" ("the Measures") on 24 August 2009 to clarify the operation of China's double taxation agreements (DTA).

A detailed analysis of the new requirements will be provided in the October edition of *Hwuason Insights*

The Measures will take effect from 1 October 2009 and set out the compliance requirements for the treaty resident enterprises to claim the benefit of a relevant DTA. It is the first time that the Chinese tax authorities have introduced such comprehensive and detailed administrative rules on this issue.

Hwuason, the first specialist tax law firm in China, is committed to providing the highest level tax law services to clients.

Please feel free to contact us in respect of any China taxation issue at:

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IN FOCUS: NEW RULES CLARIFY VARIOUS INDIVIDUAL INCOME TAX ISSUES

On 17 August 2009, the State Administration of Taxation ("SAT") issued Guoshuifa [2009] No.121 ("Circular 121") to clarify the application of individual income tax ("IIT") in various circumstances:

- "Double pay" (also widely known as "13th month salary") is no longer taxed as separate month income;
- Director's fees and salary income received by executives (including those from related companies) need to be combined and taxed as "salary income";
- Overseas Chinese ("Huaqiao") undertaking employment in China would be entitled to a monthly allowance of RMB4,800 (similar to foreign employees) when calculating their IIT liabilities only if certain tests are satisfied; and
- Real property transferred between spouses due to a divorce settlement is exempt from IIT. In the case of subsequent disposal, the gain (i.e. the sales proceeds less the total original cost base and reasonable expenses) will be subject to IIT unless the real property has been the only family home for at least five years.

See page 1 for details of the relevant tests

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SAT ISSUES CLARIFICATION ON IIT TREATMENT OF SHARE APPRECIATION RIGHTS AND ACQUIRED SHARES

On 24 August 2009, the State Administration of Taxation ("SAT") issued Guo Shui Han [2009] No. 461 ("Circular 461") to provide further clarifications on the Chinese individual income tax ("IIT") treatments of employment income derived from share appreciation rights ("SARs") and restricted shares plans. Circular 461 outlines various issues in relation to the tax treatment of SARs and restricted shares, including:

- The timing (effectively when the rights are realized) and calculation of taxable income.
- The application, and limitation of, the preferential IIT treatment of equity income (pursuant to Cai Shui [2005] No. 35) to SARs and restricted shares.
- The consequences of multiple taxing events occurring in a single year.

A detailed discussion of Circular 461 will be provided in the October edition of *Hwuason Insights*