

# CHINA TAX ALERT

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## Deferred individual income tax treatment for Enterprise Annuity and Occupational Pension plans

### Regulations discussed in this issue:

- *Notice on Issues Pertaining to the Collection and Administration of Individual Income Tax on Enterprise Annuities and Occupational Pensions*, issued by the Ministry of Finance, the Ministry of Human Resources and Social Security, and the State Administration of Taxation, Cai Shui [2013] No. 103

### Background

The Chinese pension insurance system was first established in the early 1990s and has been in place for over 20 years. It consists of savings insurance for basic pensions, supplementary pensions and personal pensions. On 6 December 2013, the Ministry of Finance ("MOF"), the Ministry of Human Resources and Social Security ("MHRSS") and the State Administration of Taxation ("SAT") jointly issued Cai Shui [2013] No. 103 ("Circular 103"), providing guidance pertaining to the collection and administration of Individual Income Tax ("IIT") on Enterprise Annuities and Occupational Pensions ("the Plans"). The new rules under Circular 103 are likely to promote the establishment of approved Plans and to widen the national retirement savings base by deferring the point of taxation for voluntary employer contributions to retirement age and allowing a tax deduction for voluntary employee contributions to approved Plans.

Circular 103 comes into force on 1 January 2014.

### Contents

Circular 103 provides for deferred IIT treatment of contributions made under annuity plans established in accordance with *Implementation Rules on Enterprise Annuity* (formerly known as "Notice 20") issued by MHRSS and *Provisional Implementation Rules on Occupational Pension Plans* (Guobanfa [2011] No. 37).

The release of Circular 103 will also see the nullification of Guoshuihan [2009] No. 694 and Public Notice [2011] No. 9 issued by the SAT, which provided less favourable IIT treatment of approved Plans.

Below is a snapshot of the impact on the IIT treatment of annuity plans after 1 January 2014.

Events	Pre-1 January 2014		Post-1 January 2014	
Contribution	Employer Contribution	Employee Contribution	Employer Contribution	Employee Contribution
	Taxable as separate category of monthly salary	Non-deductible	Non-taxable	Deductible (up to 4% of the individual's contribution basis) [Note 1]
	Quarterly, semi-annual or annual contributions cannot be attributed to the respective month for tax computation purposes			
Fund Investment	N/A		Non-taxable	
Payout	N/A		- Monthly payout: Taxable as salary for the month - Quarterly or annual payout: equally allocated to the respective month and taxable as monthly salary for the respective month [Notes 2 and 3]	

**Notes:**

1. Contribution basis: Based on the employee's average monthly salary of the preceding year, subject to a ceiling of 300% of the relevant city's monthly average salary for the preceding year.

2. Individuals who contributed to an approved Plan prior to 1 January 2014, and that subsequently receive a lump-sum payout after implementation of Circular 103, will be taxed on the balance of their total contributions less any contributions which have been subject to IIT under the old rules. For individuals who receive their payout in installments, the same principle applies, and the contributions which have been subject to IIT under the old rules will be equally distributed to the periodic payout for IIT computation purposes.

3. For individuals or beneficiaries/legal heirs who receive a lump-sum annuity payout due to special circumstances (i.e. overseas migration or death), the IIT on the payout may be reported in equal instalments over a 12-month period.

➤ Tax registration of Plans and IIT withholding obligations

Companies shall register newly established Plans or any revisions made to existing Plans with the relevant local tax authorities within 15 days following the end of the month during which establishment or revision occurs. Documents that need to be submitted include all documents pertaining to the Plans and the Letter of Registration Confirmation and Approval issued by the MHRSS in respect of the Plans.

Companies that establish approved Plans and Custodians of the Plans are obliged to withhold IIT at the time when the contributions are made/deducted and when payouts are distributed.

**KPMG Observations**

Currently, individuals are obliged to pay IIT on annuities when a contribution is made. Given that individual taxpayers are likely to be subject to a lower marginal IIT rate when they receive payouts from a Plan, the new rules under Circular 103 will not only defer the point of taxation of contributions made under a Plan to the time of the payout, but also lower the eventual IIT burden on employees to a certain extent. In view of this, Circular 103 is expected to play an important role in encouraging retirement savings, and provides for tax planning opportunities in the design and establishment of Annuity plans.

Companies should set up proper mechanisms to review their current Plans. They should also ensure that they are able to fulfil Plan registration and tax withholding obligations as required by Circular 103.

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