Mobility: tax alert
May 2018

China

China launches Individual Income Tax deferral on commercial pension in pilot areas

Executive Summary
On 2 April 2018, the relevant departments jointly issued a Notice providing Individual Income Tax (IIT) deferral on commercial pension contributions, investment gains and retirement distributions. Caishui [2018] No. 22 (Circular 22) provides that a pilot program will take effect from 1 May 2018 and have a trial period of one year, covering Shanghai, Fujian Province (including Xiamen) and Suzhou Industrial Park Zone.

Key issues

1. IIT treatment
   1) Contribution of commercial pension
      In pilot areas, individuals’ contributions to qualified commercial pension plans through personal commercial pension fund accounts can be deducted from taxable income, within a specified cap. For individuals who receive salaries and continuous labor remuneration, the allowable deduction amount is capped at the lower of 6% of the monthly salary or continuous labor remuneration of the current month or RMB1,000 (USD 157) a month. Where self-employed industrial and commercial households, individual operators, sole proprietorship enterprises and individual partners of partnerships derive income from production and business operations or from contracting or leasing, the allowable deduction is capped at the lower of 6% of the annual taxable income of the current year, or RMB12,000 (USD 1,885) a year.

      Personal commercial pension fund accounts are special private accounts set up by individual taxpayers at commercial banks for the purpose of making contributions to IIT deferral commercial pension plans, collection of investment gains and other relevant payments. They are close-ended accounts solely linked to the individuals’ personal identity details.

   2) Distribution of investment gains
      When gains derived from the investment in commercial pension funds are distributed to an individual’s accounts, no IIT will be imposed on such gains during the pension contribution period.

   3) Distribution from commercial pension funds
      Individuals who reach the retirement age set by the government can receive commercial pension fund distributions on a monthly or yearly basis. In principle, the distribution of commercial pension funds lasts until the end of the person’s lifetime (and/or covers at least 15 years). A one-off withdrawal is possible in the case of death, disability or critical illness (according to the specific terms of the plan).

      Among the qualified distribution payments of the commercial pension fund, 25% of the distribution payment can be exempted from IIT and the remaining 75% will be subject to a tax rate of 10%. Therefore, the total effective tax rate is 7.5%. The distribution payment shall be reported under the category of “other income”. When the individuals receive the distribution payments, the relevant IIT shall be withheld by the insurance companies.
2. Eligible individuals
Eligible taxpayers for the IIT deferral treatment refer to the individuals who receive salaries and continuous labor remuneration (i.e., the taxpayer provides labor services and receives remuneration from the same entity for at least six consecutive months or more), as well as self-employed industrial and commercial households, individual operators, sole proprietorship enterprises and individual partners of partnerships deriving income from production, business operation or contracting/leasing operations whose IIT withholding agent or whose actual operation is located in the pilot areas.

If an individual derives income from two places in the above pilot areas, he or she can only select one area to enjoy the favorable IIT deferral treatment.

3. Related administrative procedures
During the pilot period, the information platform established by China Insurance Information Technology Management Co., Ltd will be used. This information platform will be interfaced with the system of tax bureaus, commercial insurance companies and commercial banks. The information platform will also support account management, information checking, tax review, external supervision, etc.

Individual commercial pension products should focus on safety, consist of a majority of safe products and a minority of aggressive products. The detailed guidelines will be proposed by the China Banking Insurance Regulatory Commission and announced by MOF, the Ministry of Human Resources and the SAT after internal consultation.

EY’s observations of the program
The trial will allow individuals working in the pilot areas to enjoy IIT deferral on commercial pension insurance contributions and investment gains until the distribution stage after retirement and enjoy an effective tax rate of 7.5%. This is good news for eligible individuals. We expect that after the trial, the IIT deferral treatment will likely be expanded to other areas in China and the relevant policies may be adjusted and improved. It will be considered a positive supplement to the existing limited pension scheme.

Next Steps
We suggest that relevant companies and individuals assess the commercial pension insurance product guidelines and related regulations, which will be issued at a later stage, in order to understand how to take advantage of the IIT deferral treatment on commercial pension funds.

If further assistance is required, please do not hesitate to contact one of the EY specialists below.