

# Consolidated corporate income tax filing for non-tax resident enterprises - A new alternative is provided

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## In brief

In December 2018, the 7<sup>th</sup> Standing Committee Meeting of the 13<sup>th</sup> National People's Congress (NPC) decided to remove the approval requirement for consolidated Corporate Income Tax (CIT) filing by non-Tax Resident Enterprises (non-TREs) with two or more Establishments or Places (E&Ps) in China<sup>1</sup> and accordingly revised the CIT Law. The new amendment stipulates that non-TREs which have established two or more E&Ps in China may select its main E&P to make consolidated CIT filing as long as they meet the criteria set by State Taxation Administration (STA). This means that qualified non-TREs would be able to utilise tax losses to offset profits among their E&Ps without having to obtain approval from tax bureaus. Later in March 2019, the STA released *Public Notice Regarding CIT Filing for non-TREs*<sup>2</sup> (SAT Public notice [2019] No.12, PN12) to provide detailed rules on implementing the consolidated CIT filing and made corresponding amendments to the non-TREs CIT filing returns<sup>3</sup>.

According to PN12, non-TREs with multiple E&Ps in China should follow the tax collection and administration regulations for Tax Resident Enterprises (TREs) with head office and branches. For non-TREs in the banking, insurance or oil and gas industry that operate with multiple E&Ps and select to conduct consolidated filing, they should follow the new CIT filing method. In view of the significant differences in CIT filing administration between the previous and new method, PN12 will affect the CIT filing and settlement as well as tax internal control and management of those non-TREs which have already obtained approval for consolidated filing previously. We suggest non-TREs to analyse the new consolidated CIT filing method and its compliance requirements based on their own situations before making the selection, and adjust their operation and tax administration accordingly.

## In detail

### Background

According to the CIT Law, non-TREs which have an E&P in China have to pay CIT at the rate of 25% on income that is derived by such E&Ps in China from sources inside China as well as on income that, although derived from sources outside China, is effectively connected with such E&Ps. Prior to the amendment, non-TREs which have established two or more E&Ps in China, normally file CIT at its E&P location separately. It was also possible for them to select the main E&P to conduct consolidated CIT filing with the approval of the tax authorities. The advantage to non-TREs in selecting the CIT consolidated filing is that tax losses from one E&P can be utilised to offset profits generated by other E&Ps, resulting in the reduction of total CIT liability of the non-TREs. However, as the prerequisite was to obtain the approval from the common superior level tax bureau of all the local tax bureaus which are in charge of the E&Ps (especially for cross-province E&Ps which would require the approval of the STA) in order to conduct consolidated CIT filing, it is not common to see approved consolidated filing cases in practice.

To provide more convenience to non-TREs, the Standing Committee Meeting decided at the end of 2018 to remove the approval requirement for consolidated Corporate Income Tax (CIT) filing by non-Tax Resident Enterprises (non-TREs) with two or more Establishments or Places (E&Ps) in China. Thereafter, in March 2019, the STA released PN12, which stipulates that

non-TREs with multiple E&Ps in China are allowed to select its main E&P to conduct consolidated CIT filing, and follow the tax collection and administration regulations for TREs with head office and branches, which requires the overall tax payable to be calculated and adjusted on a consolidated basis and subject to level-to-level management and fiscal adjustments but with provisional tax payment settled separately at the respective E&Ps' locations<sup>4</sup>.

### Scope of Application

The prerequisite for adopting the consolidated CIT filing follows the stipulation in Article 126 of the Detailed Implementation Rules of CIT law which requires the main E&P to assume supervisory and administrative responsibility for the production and business activities of the other E&Ps and keep complete accounting records and vouchers which accurately reflect the income, costs, expenses, and profit and loss position of the respective E&P.

Besides, according to PN12, the following additional criteria relating to the E&Ps have to be satisfied in adopting consolidated filing:

- The E&Ps have performed tax registration with their in-charge tax bureaus and obtained a tax registration number;
- The E&Ps cannot adopt deemed profit method in calculating CIT; and
- Each E&P can accurately calculate the CIT payable allocated to it in accordance with the rules stipulated in PN12 and file tax with its in-charge tax bureau based on the requirement.

Please note that those E&Ps of non-TREs which have adopted the deemed profit filing method due to incomplete accounting records and vouchers cannot be included in the scope of consolidated filing.

### Calculation Method

According to PN12, non-TREs selecting consolidated CIT filing should calculate its CIT payable on a consolidated basis and allocate the tax payable as follows:

- tax payable allocated to the main E&P = Consolidated CIT Payable x 50%
- total tax payable allocated to E&Ps having production and operation function ("Other E&Ps") = Consolidated CIT Payable x 50%
- tax payable allocated to each Other E&P = total tax payable of Other E&Ps x allocation ratio of that E&P.

The portion of CIT payable allocated to Other E&Ps is determined by three main factors, namely operating income, salary and total assets of each E&P, with weighting of 0.35, 0.35 and 0.30 respectively. These three factors should be based on the annual operating income and salary of the preceding year and the total assets at 31<sup>st</sup> December of the preceding year.

In addition, the E&Ps that satisfy the following criteria can be included in the scope of consolidated filing but without allocation of CIT to at its location:

- do not undertake production and operation functions, but are only involved in internal auxiliary management or service activities; and
- do not derive income externally (only derive income from E&Ps included in the scope of consolidated filing).

### Administration on consolidated filing

Before the amendment of the CIT Law, non-TREs which have obtained approval for consolidated filing would file the consolidated CIT return and settle the consolidated CIT payable at the local tax bureau at where their main E&P was located and obtained the *Certification of Non-TREs Consolidated CIT Filing*. The Other E&Ps only need to submit several supporting documents, including this certificate to their in-charge tax bureaus. This administrative method of requiring the taxpayers to deal with only one particular tax bureau is relatively convenient to non-TREs in terms of tax calculation and settlement. However, it may create a mismatch between the locations at where the operational activities occurred and where the tax revenue are collected.

After PN12 came into effect, following the tax collection and administration regulations for TREs with head office and branches, non-TREs selecting consolidated filing shall calculate the total consolidated CIT payable. Meanwhile, both the main E&P and Other E&Ps shall file and pay provisional CIT and perform annual CIT reconciliation filing to the in-charge tax bureau at its location respectively. Under this new method, the locations at where the operation activities occurred and where the tax revenue are collected can, to a certain extent, match the operational activities occurred; however, as compared with the previous method, taxpayers would have to deal with more than one tax bureau, which would have a higher requirement in terms of tax management and coordination capabilities of the taxpayers.

### Transitional Policies

According to PN12, non-TREs which have obtained approval and conduct consolidated filing under the previous method, can now select to conduct consolidated filing with the new method, or conduct the quarterly provisional and annual CIT filings for 2018 and 2019 using the previous method. From 2020 onwards, all non-TREs have to follow the new method for consolidated filing.

However, PN12 has not clarified that in the event that non-TREs decide to follow the previous method, whether their newly established E&Ps can be included in the scope of consolidated filing. As the approval obtained from STA previously may not include these newly established E&Ps, it is likely that they cannot be included in the scope of consolidated filing.

Non-TREs which have not conducted consolidated filing before, if eligible, can conduct consolidated filing at the 2018 annual CIT filing. The quarterly provisional CIT payments made before the annual CIT filing can be used to offset the consolidated CIT payable at the time of the 2018 annual CIT filing.

### The takeaway

Undoubtedly, providing non-TREs the autonomy to select CIT consolidated filing without having to obtain approval from the tax authorities brings greater convenience to taxpayers. Moreover, the allocation of tax payable among E&Ps under this new method would solve the mismatch between locations at where the operational activities occurred and where the tax revenues are collected. Nevertheless, this new method has a higher compliance requirement for non-TREs in terms of tax calculation and coordination with the tax authorities. In particular, for taxpayers in the banking, insurance and oil and gas which have a large number of E&Ps in China, the compliance burden would likely increased since they have to file and pay CIT at each of the E&P locations.

From the perspective of enterprises, they are suggested to consider and pay close attention to the following aspects:

- Non-TREs, different from those TREs operating cross-regions, have the option on whether to conduct consolidated filing or not. Enterprises should assess and decide whether to adopt this approach based on their own situation and needs. E&Ps that had previously settled CIT adopting deemed profit method, can self-assess on the feasibility to convert into an actual basis filing method, so that they can conduct CIT consolidated filing to improve liquidity and reduce overall tax burden;
- The new method is complex and raises higher requirement on non-TREs' tax management. Enterprises that have decided to select CIT consolidated filing should adjust their internal management and be prepared in the following aspects including financial and tax personnel arrangement, internal information sharing and communication mechanism, CIT filing procedure, bank account and fund arrangement so to ensure that the CIT payable is accurately allocated among the E&Ps and complete CIT provisional payments, annual CIT filing and other information submission on time. As the new method may result in CIT refund and additional CIT payment in different locations, enterprises should also keep an eye on those procedures and timely communicate and coordinate with the in charge tax bureaus;
- The CIT Law and the new method sets out requirements for the main E&P. Taxpayers should select its main E&P by taking into consideration the functions, risks borne by each E&P and communicate with the tax bureaus beforehand to have a better understanding on how it is assessed in practice;
- After the implementation of the new method, as taxpayers have to deal with more than one tax bureau, they may have to face different interpretations on the same issue by different tax bureaus (e.g., the deduction of assets loss). However, PN 12 clearly stipulates that the in charge tax bureaus cannot have different tax treatments for the same issue. If they cannot agree on the same treatment, the in charge tax bureaus should bring the matter to the common superior level tax bureau for making a decision;
- For non-TREs which have obtained approval for consolidated filing previously, they can select to conduct tax filing for 2018 and 2019 with either the new or previous method. However, from 2020 onwards, they have to strictly follow the new method for CIT consolidated filing. In view of the fact that the differences between the new and previous approach may lead to changes in tax compliance procedure, we suggest these relevant non-TREs to clarify with their in-charge tax bureaus beforehand on relevant issues such as, if all the E&Ps under consolidated filing are under the jurisdiction of the same provincial tax bureau, whether a simpler practical method can be adopted, etc.;
- To facilitate the implementation of the new method for CIT consolidated filing, the STA has amended the non-TREs CIT filing return, taxpayers should complete the CIT filing using the updated CIT returns and the accompanying filing instructions.

### Endnote

1. Please refer to [President's Order \[2018\] No.23](#) for details.
2. Please refer to *Public Notice Issued by the STA, the MOF and the PBOC Regarding Consolidated Corporate Income Tax Filing for Non-Tax Resident Enterprises (Non-TRE)* ([STA Public Notice \[2019\] No.12](#)) for details.
3. Please refer to *Public Notice Issued by the STA Revising the Forms and Filing Instructions of the <PRC Provisional CIT Returns for Non-Tax Resident Enterprises (Non-TREs)> (2019 Version) the <PRC Annual CIT Returns for Non-TREs> (2019 Version) and the <PRC Withholding CIT Report for Non-TREs> (2019 Version)* ([STA Public Notice \[2019\] No.16](#)) for details.
4. Please refer to *Public Notice Issued by the STA Publishing the <Administrative Measures on Consolidated Corporate Income Tax Filing for Enterprises with Cross-regional Business Operations>* ([STA Public Notice \[2012\] No.57](#)) for details.



## Let's talk

For a deeper discussion of how this issue might affect your business, please contact **PwC's China Tax and Business Service Team**:

Peter Ng  
+86 (21) 2323 1828  
peter.ng@cn.pwc.com

Spencer Chong  
+86 (21) 2323 2580  
spencer.chong@cn.pwc.com

Edwin Wong  
+86 (10) 6533 2100  
edwin.wong@cn.pwc.com

Alan Yam  
+86 (21) 2323 2518  
alan.yam@cn.pwc.com

Charles Lee  
+86 (755) 8261 8899  
charles.lee@cn.pwc.com

Jeremy Ngai  
+852 2289 5616  
jeremy.cm.ngai@hk.pwc.com

Iris Pang  
+86 (10) 6533 3110  
iris.pang@cn.pwc.com

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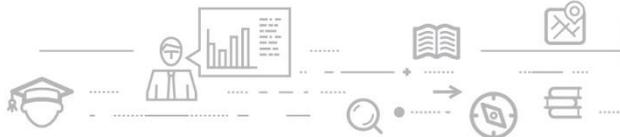
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For more information, please contact:

Matthew Mui  
+86 (10) 6533 3028  
[matthew.mui@cn.pwc.com](mailto:matthew.mui@cn.pwc.com)

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