Morgan Stanley

INTERNATIONAL WEALTH MANAGEMENT

KPMG

Private Enterprise

Wealth Planning Considerations in the People's Republic of China (PRC)

A GUIDE FOR CLIENTS OF MORGAN STANLEY INTERNATIONAL WEALTH MANAGEMENT

The People's Republic of China (PRC)

Morgan Stanley International Wealth Management offers highly personalized wealth management solutions for global entrepreneurs, high-net-worth families, executives and professionals. Leveraging the global resources and intellectual capital of our Firm, International Client Advisors help clients pursue their personal, family and community goals. This report is part of the Asian Series produced in partnership with KPMG for the educational purposes of Morgan Stanley International Wealth Management clients.

Description of PRC As a Jurisdiction

China's legal system covers laws that fall under seven categories and three different levels. The seven categories are the Constitution and Constitution-related, civil and commercial, administrative, economic, social, and criminal laws, and the law on lawsuit and non-lawsuit procedures. The three different levels are state laws, administrative regulations and local statutes.

a. Legal Considerations

Legal Capacity

According to the PRC Civil Code, although a natural person shall have the capacity for civil rights irrespective of the age, the full capacity for legal conduct is generally acquired by a person at the age of 18 when the person becomes an adult. A minor who has reached the age of 16 and whose main source of income is his or her own income from work will also be deemed to have full capacity for civil conduct. Minors over the age of eight shall either be represented by their legal guardians, or obtain the consent or acknowledgement of the same, in order to conduct a civil juristic act (e.g., entering into a contract). Such minors may, however, independently conduct civil juristic acts that are purely to their own benefit (e.g., accepting gifts), or are compatible with their age and intelligence (e.g., giving away cheap toys). Minors under the age of eight can only be represented by their legal guardians to conduct civil juristic acts, meaning that they cannot perform civil juristic acts independently in any case. Legal guardians shall not dispose the property of minors under the age of eight, unless such disposal may safeguard or benefit the minors' interests.

Marriage

PROPERTY REGIMES (SEPARATE PROPERTY, COMMUNITY PROPERTY)

In general, the property belonging to a party of a couple before marriage constitutes separate property of that party. The parties of a couple may conclude a written agreement to designate how their assets and debts should be divided during the existence of the marriage. The parties of a couple can enter into a prenuptial agreement to arrange a separate property regime. Under this regime, each party of a couple can freely manage or dispose of their separate property (e.g., the property owned by one party before the marriage and the property received by one party as a gift or by inheritance). One party does not have any rights to the other's property and is respectively liable for his/her own debts.

If the parties do not conclude an agreement, according to the PRC Civil Code, the assets obtained during the existence of the marriage by one spouse are deemed to be owned by both spouses in joint possession. Both parties shall enjoy equal rights in the disposition of the community property.

Under this regime, debts incurred jointly by a couple in the form of signatures by the couple shall be deemed as joint debts of the couple. Where a person joins a debt on his/her own, and the signature of his/her spouse is missing, the debt will in principle still be deemed as a joint debt of this couple as well.

PRENUPTIAL/POSTNUPTIAL AGREEMENTS

Prenuptial and postnuptial agreements are both generally recognized under the PRC law. Prenuptial agreements are signed before marriage and become effective after marriage. Postnuptial agreements are entered into after marriage. The parties of a couple may designate the property acquired before and/or during marriage as community property, separate property, partially separate or partially community property by means of agreements. Both prenuptial and postnuptial agreements shall be in written form if they are related to property.

SEPARATION OF ASSETS/DIVORCE

SAME-SEX MARRIAGE

Same-sex marriage is not recognized in the PRC. Therefore, even if a same-sex marriage is established outside the PRC, it would not be deemed valid for any legal purpose in the PRC.

Cohabitation Relationship/ Community Property

In general, cohabitation without marriage registration cannot be regarded as de facto marriage and is not protected under marriage law. For instance, the property obtained by the cohabiting parties during cohabitation will not be treated as community property. Nevertheless, cohabitation established before the implementation of Regulation on Marriage Registration (February 1, 1994) is still recognized as de facto marriage if both parties met the substantial conditions for getting married. In a marriage relationship where one party of a married couple cohabits with a third person, the court may hold in favor of the other party who claims divorce. When allocating the property, protecting the rights and interests of the innocent party will be given emphasis to.

Inheritance–Estate Planning

INTESTATE SUCCESSION

When no valid will is left or the decedent dies without making bequests, the decedent's estate will be inherited by his or her statutory successors according to the order and the shares prescribed by the PRC Civil Code.

Statutory successors generally include first-in-order successors (i.e., spouses, children, parents) and second-in-order successors (i.e., brothers and sisters, paternal grandparents, maternal grandparents). Second-in-order successors will only be able to inherit the decedent's estate in the absence of the first-in-order successors. Successors in the same order shall, in general, inherit in equal shares.

ESTATE PLANNING/WILL

Any citizen may dispose his personal estate and appoint a testamentary executor by means of a valid will and in accordance with the PRC Civil Code. Once succession commences, it is handled in accordance with the will. A designated successor will be deemed to have accepted his or her share of the estate unless the successor affirmatively refuses to accept the share by means of a written declaration of renunciation of succession.

A testator may designate a person other than the testator's statutory successors as a legatee to inherit his or her estate. A legatee must, within 60 days from the time he or she learns of the legacy, indicate whether he or she accepts it or disclaims it. In the absence of such an indication within the specified period, he or she shall be deemed to have disclaimed the legacy.

TESTAMENTARY INHERITANCE

Wills should reserve necessary shares of the estate for a fetus subject to its living birth and any successor who neither can work nor has a source of income, for example, a severely disabled successor who lacks the ability to work and has no source of income at the time when the will takes effect. Shares reserved for disabled successors refer to court-determined shares of the estate reserved for successors who lack the ability to work and have no source of income at the time when the will takes effect. Shares reserved for unborn children refer to shares reserved for fetuses. The share reserved shall be dealt with pursuant to statutory inheritance if the baby is stillborn. Wills that fail to make reservations as described above may be considered invalid to the extent such reservations were required to be made. In such case, the court may hold in favor of the successor entitled to a reserved share if she/he initiates a lawsuit to claim a necessary partition of the estate.

b. Tax Updates

Tax Regime and General Tax Framework

INDIVIDUAL INCOME TAX REGIME

The PRC tax residents are subject to Individual Income Tax (IIT) on their worldwide income. Nonresident individuals are only subject to the PRC IIT on income sourced from the PRC.

PRC tax residents who are "non-domiciled" individuals and have not resided in the PRC for at least 183 days in six consecutive calendar years may be exempt from the PRC IIT on their foreign-sourced income. If the individual is away from the PRC for more than 30 continuous days in a given tax year within a consecutive period of six years, the counting of the six years can also be reset.

The term "domiciled in the PRC" generally refers to an individual who is habitually residing in the PRC due to his/her household, family or economic situation.

Nonresident individuals are required to file the IIT due/refund with the tax bureau by January 15 following the end of the year if certain conditions are met.

The revised IIT law and regulations effective from January 1, 2019 encompassed the arm's-length principle for the pricing of related-party transactions, a Controlled Foreign Companies (CFC) rule, and a general anti-avoidance rule. These rules are not new in the context of the PRC Corporate Income Tax (CIT) law, but are very relevant to IIT as observed in recent personal income tax evasion cases. For instance, with the IIT anti-avoidance rules being implemented progressively, there will be a firm legal basis for the PRC tax authorities to investigate offshore indirect transfers and assess IIT where inappropriate tax benefits are suspected to be derived.

CORPORATE TAX RATES

To the extent that an investment is made by an incorporated entity in the PRC, investment income earned, and gains realized by such resident enterprise, are generally subject to the PRC CIT at 25%. A tax-resident enterprise is subject to the PRC CIT on worldwide income. From the context of investment income, generally the above income is not exempted except for dividends paid between tax resident enterprises in the PRC which are not taxable except for those received from publicly listed companies where the holding period is less than 12 months. Interest income from government bonds is exempted from the PRC CIT.

INCOME TAX SYSTEM FOR INVESTMENTS

Generally, individual PRC-sourced investment income (including capital gains, dividend and interest) will be subject to the PRC IIT at 20% on a withholding basis. Where there is no withholding agent in the PRC (investment gains realized, for example), individuals should file an IIT return on a self-declaration basis within 15 days of the following month in which the income is received.

There are specific exemptions of IIT, interest income from bank deposits and government bonds, for example. Dividend income received from listed companies may also qualify for exemption if the shares were held for more than one year, or subject to 50% reduction if the holding period was between one month and one year.

ASSET TAX

At present, there is no wealth tax in the PRC other than direct investment in real estate. The above applies to individuals who own properties in Shanghai or Chongqing of the PRC and nation-wide wealth tax has not been in place.

INDIRECT TAX

The PRC value-added tax (VAT) is imposed on the trading of goods and provision of services in general. Income derived from investment products (e.g., listed securities, asset management products, derivatives, etc.) falls within the category of service income and would be subject to VAT. Income derived by an individual, however, might be exempted.

OFFSHORE ASSETS

Effective January 1, 2019, the PRC resident individuals should submit an annual reconciliation filing between March 1 and June 30 following the end of the respective tax year, if certain conditions are met. The rule clarifies the treatment on income earned overseas by PRC tax residents, including:

1. Classification of overseas income
2. Calculation of taxable income
3. Foreign Tax Credit (FTC) claim
4. Administrative requirements

The term “domiciled in the PRC” generally refers to an individual who is habitually residing in the PRC due to his/her household, family or economic situation.

CONTROLLED FOREIGN CORPORATION (CFC) RULES

Based on the new IIT law, the tax authorities are empowered to make certain tax adjustments for controlled foreign corporations. These apply when individual PRC tax residents by themselves, or together with PRC tax resident companies, control an enterprise that is established in a low-tax jurisdiction and the foreign enterprise does not distribute its profits, or reduces the distribution of its profits, for reasons other than reasonable operational needs. There is currently no clear definition of “control” under the PRC law.

GIFT TAX AND ESTATE DUTY

At present, there are no inheritance, estate or gift taxes in the PRC.

OFFSHORE TRUSTS

A PRC tax resident individual beneficiary receiving trust income from offshore trusts could be subject to the PRC IIT. In addition, CFC rules are in place whereby retained profit under the trust could be deemed as distributed and taxable for IIT purpose.

RENUNCIATION OF PRC STATUS

An individual acquiring a foreign passport may still be “domiciled in the PRC” and continue to be subject to PRC taxation on worldwide income basis. The IIT law puts the onus on individuals to perform tax-clearance procedures prior to canceling their PRC household registrations when emigrating overseas.

Pending further guidance from the PRC tax authority on the disclosure details demanded under the tax clearance procedures, individuals who have changed their citizenship, or intend to do so, should review their IIT tax status, including tax-domicile and tax-residence status on a regular basis to assess their compliance with the tax laws in the PRC and relevant tax jurisdictions.

c. Regulatory Reporting and Obligations

Income Tax Treaties—Offshore Treaties

The PRC has signed treaties to avoid double taxation with over 110 tax jurisdictions. Depending on the type of investment income, the tax liabilities arising from the investment income earned in the other jurisdiction may be reduced or exempted under the applicable tax treaties

Exchange of Information

Most income tax treaties signed by the PRC include information exchange clauses. Additionally, the PRC has concluded tax information exchange agreements with some jurisdictions that impose no tax on income. Among others, these include the British Virgin Islands, Bahamas, Bermuda, Cayman Islands, Guernsey, Isle of Man and Jersey. Information may be exchanged automatically or upon request, depending on the agreement with the relevant counterparty jurisdiction.

FOREIGN EXCHANGE RULES

The PRC law imposes strict capital accounts' control, and limits PRC individuals to the equivalent of U.S. $50,000 per year in foreign exchange. In addition, there are prescribed investment routes that PRC individuals must follow in order to make an offshore investment. Financial investments such as offshore fixed income investment and equity investment should be made via banks and fund management companies that are under the Qualified Domestic Institutional Investor (QDII) Program. Investment on designated listed securities and wealth management products are also allowed under the Stock Connect Program and Cross-Boundary Wealth Management Connect Scheme of the Guangdong-Hong Kong-Macao Greater Bay Area.

FATCA

In late June 2014, the PRC government reached "agreement in substance" status with the United States (U.S.) on the terms of a Model 1 Intergovernmental Agreement (IGA). However, at the publication of this report, the PRC-US IGA has not yet been signed, and the financial institutions in the PRC have only partially started implementing FATCA.

COMMON REPORTING STANDARD (CRS)

The PRC has entered into the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information. In May 2017, the relevant PRC authorities jointly issued the Administrative Measures on Due Diligence Procedures for Nonresidents Financial Account Information in Tax Matters (the Measures) to implement CRS in the PRC, under which financial institutions established in the PRC are required to carry out due diligence procedures on financial accounts starting July 1, 2017. The PRC completed the exchange of the first round of financial account information in September 2018. As of March 2022, the PRC has activated 67 exchange relationships with more than 100 jurisdictions that are committed to the CRS.

About KPMG

KPMG member firms and its affiliates operating in mainland China, Hong Kong and Macau are collectively referred to as "KPMG China." KPMG China is based in 31 offices with around 14,000 partners and staff in Beijing, Changsha, Chengdu, Chongqing, Dalian, Dongguan, Foshan, Fuzhou, Guangzhou, Haikou, Hangzhou, Hefei, Jinan, Nanjing, Ningbo, Qingdao, Shanghai, Shenyang, Shenzhen, Suzhou, Taiyuan, Tianjin, Wuhan, Xiamen, Xi'an, Zhengzhou, Hong Kong SAR and Macau SAR. Working collaboratively across all these offices, KPMG China can deploy experienced professionals efficiently, wherever our client is located.

KPMG is a global network of professional services firms providing audit, tax and advisory services. We operate in 146 countries and territories and have more than 238,000 people working in member firms around the world. The independent member firms of the KPMG network are affiliated with KPMG International Limited ("KPMG International"), an English entity. Each KPMG firm is a legally distinct and separate entity and describes itself as such. In 1992, KPMG became the first international accounting network to be granted a joint venture license in mainland China. KPMG was also the first among the Big Four in mainland China to convert from a joint venture to a special general partnership, as of August 1, 2012. Additionally, the Hong Kong firm can trace its origins to 1945. The early commitment to this market, together with an unwavering focus on quality, has been the foundation for accumulated industry experience, which is reflected in KPMG's appointment for multidisciplinary services (including audit, tax and advisory) by some of China's most prestigious companies.

Our Team

KARMEN YEUNG

National Head of Private Enterprise
KPMG China
+852 2143 8818
karmen.yeung@kpmg.com

WILLIAM GUO

Partner, Private Enterprise, NCN
KPMG China
+86 10 8508 5000
william.guo@kpmg.com

EDWARD YU

Partner, Private Enterprise, EWCN
KPMG China
+86 21 2212 2888
edward.yu@kpmg.com

KOKO TANG

Partner, Private Enterprise, SCN
KPMG China
+86 755 2547 4180
koko.tang@kpmg.com

SYLVENE FONG

Partner, Private Enterprise, Hong Kong
KPMG China
+852 2522 6022
sylvene.fong@kpmg.com

TRAVIS LEE

Partner, Private Enterprise
KPMG China
+852 2143 8524
Travis.lee@kpmg.com

DAVID CHIU

Senior Manager, Private Enterprise
KPMG China
+852 2978 8299
david.chiu@kpmg.com

Regional Account Lead

TOM JENKINS

Partner, Account Regional Lead
KPMG China
+852 2143 8570
tom.jenkins@kpmg.com

Private Enterprise

kpmg.com/cn/socialmedia

CRC 3670659 01/25 CS 1175591-4722137 12/24