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Turbulence in the global tax environment – A disruptive storm or an opportunity to outshine?

Asia Pacific Tax Notes 2016

Issue 29

Territories tax updates

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Foreword

The demand for increasing tax transparency for corporations emerges as a key area of focus for governments, tax authorities, the media and the general public around the globe. Using Australia as an example, the lead article in this issue discusses the various measures considered by countries in the Asia Pacific region for increasing tax transparency and enhancing co-operation between tax authorities. Examples of these measures include improved transfer pricing documentation and country-by-country reporting, mandatory disclosure of aggressive tax schemes, a mandatory public tax transparency regime and the automatic exchange of financial account information in tax matters (also known as the Common Reporting Standard). Multinational corporations operating in this changing tax transparency landscape need to carefully manage issues such as the additional costs for complying with the increased tax disclosure, the risks of their tax affairs being misunderstood by stakeholders or the public given that only limited information is publicly disclosed as well as the trend that tax is becoming a significant driver of companies' reputation and brand health.

Following the lead article is the usual round-up of fiscal policies introduced by the governments in the region since the last issue of *Asia Pacific Tax Notes*. This round-up provides readers with an overview of the key tax developments (including budgetary proposals) in the region. I would like to recommend that readers check with their local PwC contacts on the progress of giving statutory effect to the budgetary proposals mentioned in the round-up.

Finally I would like to thank all the contributors from the PwC firms in the region and the editor, Fergus Wong and his team for their efforts in making this edition of *Asia Pacific Tax Notes* an insightful publication.

Tom Seymour
Asia Pacific and Americas Tax Leader

Editor's Note

This publication is designed to alert those interested in or already doing business in the Asia Pacific region to recent tax developments in the region. The information contained in this publication is of a general nature only. It is not meant to be comprehensive and does not constitute the rendering of legal, tax or other professional advice or service by PwC. PwC has no obligation to update the information as law and practices change. The application and impact of laws can vary widely based on the specific facts involved. Before taking any action, please ensure that you obtain advice specific to your circumstances from your usual PwC client service team or your other advisers.

The materials contained in this issue generally cover developments up to January 2016, unless otherwise indicated.

If you have any questions about the publication, please contact our editor Fergus Wong at fergus.wt.wong@hk.pwc.com or assistant editor Anita Tsang at anita.wn.tsang@hk.pwc.com.

Lead article

The new world of tax transparency

The global tax landscape is rapidly changing, and tax transparency is emerging as a key area of focus for governments and tax authorities around the world. With many countries facing large fiscal deficits and growing demand for public infrastructure and services, the amount of tax paid by the companies operating in a country (in particular multinational corporations (MNCs) operating in a number of jurisdictions) is under increased scrutiny by governments, tax authorities, the media and the general public.

'Tax transparency' broadly refers to a range of measures that increase the amount of information available to tax authorities and the public regarding the amounts and types of tax paid by companies, and the circumstances surrounding those tax payments. There are broadly two aspects of tax transparency - transparency of information between taxpayers and tax authorities, and transparency between taxpayers, tax authorities and the general public.

In this article, we highlight a range of transparency measures under consideration by countries worldwide with a focus on the Asia Pacific region. Using Australia as a case study in transparency, we also discuss issues faced by companies operating in the new world of tax transparency.

Global frameworks for transparency

Many countries have implemented specific legislative measures requiring taxpayers to provide additional information to tax authorities beyond that which has historically been provided as part of the annual income tax return filing process. This information is then used by the tax authority to ensure that taxpayers (both companies and individuals alike) adhere to the tax laws and pay the appropriate amount of tax in a particular jurisdiction. In a global context, it is widely accepted that enhanced cooperation between tax authorities is crucial in bringing tax administration in line with the globalised economy and information sharing amongst tax authorities in different jurisdictions is key.

Furthermore, transparency is one of the three pillars of the Organisation for Economic Cooperation and Development (OECD) / G20 Base Erosion and Profit Shifting (BEPS) project and under that broad banner, a number of measures developed in the course of the project will give rise to additional information being shared with, or between, tax authorities.

While the information that is shared between taxpayers and tax authorities is usually subject to privacy rules which restrict the uses to which that information can be put and prevent the release of this information to the public, there is a trend to have greater public transparency of tax information and data - that is, the lawful release of certain tax information into the public domain whether it be on a mandatory or voluntary basis.

It is generally intended that public transparency of tax information can allow for an informed debate about tax policy, and also may discourage corporations from engaging in aggressive tax avoidance practices. It can also be a point of differentiation for corporations to be seen as paying their 'fair share' of tax. In fact, we have seen over the years a number of large, high-profile MNCs voluntarily provide additional information regarding taxes paid in the jurisdictions in which they operate. Very few countries currently have mandatory public tax transparency regimes in place, but this is likely to receive increasing attention in the months and years ahead.

Ideally any initiatives to increase taxpayer transparency need to balance the benefits to the system that come from maintaining confidentiality with the increasing demand from stakeholders for greater public transparency to allow understanding, confidence and debate in the community over the tax laws.

The most recent trigger for greater transparency of tax information has predominantly come from the OECD BEPS project. Table 1 provides some examples of tax transparency initiatives originating from the BEPS project and others that have been emerging well before the project commenced.

Table 1

Examples of tax transparency initiatives:

Initiative	Who will adopt this initiative?
Improved transfer pricing documentation and country-by-country (CbC) reporting	
This formed part of the final report on Action 13 of the OECD BEPS Action Plan, released in October 2015. The OECD has recommended a three-tiered approach to transfer pricing documentation. Taxpayers will be required to provide the following to tax authorities: • a master file providing an overview of the group's global business and transfer pricing policies • a local file specific to each country, identifying material related party transactions, the amounts involved in those transactions and an analysis of the transfer pricing determinations they have made with regard to those transactions, and • a CbC report containing certain information relating to the global allocation of the MNC's income and taxes paid together with specific indicators of the location of economic activity within the global group. The CbC report is to be made available via treaty exchange of information to tax authorities in each country in which a MNC operates.	The Finance Ministers of the G20 have endorsed the final package of BEPS measures released last year. It is likely that all the G20 countries, and many of the OECD member states, will implement these recommendations over time. Countries within the Asia Pacific region that have either already adopted or are expected to adopt these recommendations include Australia, China, Japan, Korea, Singapore, Malaysia, India, Indonesia and New Zealand. As at 31 March 2016, 32 countries have signed the OECD's Multilateral Competent Authority Agreement on the Exchange of Country-by-Country Reports, which provides the framework for tax authorities to exchange CbC reports, including Australia, Japan and Malaysia.
Mandatory disclosure of aggressive tax schemes	
This formed part of the final report on Action 12 of the OECD BEPS Action Plan, released in October 2015. This report provided a modular framework that countries can follow to design a regime that requires taxpayers to disclose aggressive tax schemes to tax authorities to fit their need to obtain early information on potentially aggressive or abusive tax planning schemes and their users.	Unlike many of the other BEPS actions, the recommendations in this report do not represent a minimum standard and countries are free to choose whether or not to introduce a mandatory disclosure regime. Hence, it is currently unclear whether many countries will seek to implement these recommendations. Within the Asia Pacific region, China has indicated it will introduce a mandatory disclosure regime. Australia and India are currently considering this as well.
Standard for Automatic Exchange of Financial Account Information in Tax Matters (also known as the Common Reporting Standard)	
The Common Reporting Standard (CRS) was developed by the OECD and calls on participating jurisdictions to obtain information on financial accounts from financial institutions and automatically exchange that information with other jurisdictions. It sets out the information to be collected and reported to the local tax authorities, which financial institutions are required to report, the types of accounts and taxpayers covered and due diligence procedures to be followed by financial institutions to identify relevant accounts.	Nearly 100 jurisdictions globally have committed to implementing the CRS, with the first exchanges of information to take place in 2017 and 2018. As at 31 March 2016, 80 countries have signed the OECD's Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information which provides the international framework for the exchange of CRS information. From the Asia Pacific region, this includes Australia, China, India, Indonesia, Japan, Korea, Malaysia and New Zealand.
Extractive Industries Transparency Initiative	
The extractive industries transparency (EITI) is a voluntary, global initiative to enhance the transparency of revenues from natural resources. It is an international standard under which governments prepare an annual report disclosing how much revenue they receive from extractive companies operating in their country and those companies disclose how much tax they pay. The EITI is an example of a public transparency measure.	The EITI has been implemented in 31 countries globally, with another 51 countries currently in the process of implementing the EITI but not yet fully compliant. From the Asia Pacific region, this includes Indonesia, Papua New Guinea, Philippines and Myanmar.

A case study on tax transparency: Australia

In Australia, the issue of MNCs paying their 'fair share' of tax continues to be a highly public and political debate. This, combined with growing fiscal deficits has increased the scrutiny of taxes paid by companies operating in Australia and a significant increase in tax transparency measures in recent years.

Australia currently has a range of tax transparency measures in effect (or soon to be), including:

- implementing the OECD's improvements to transfer pricing documentation, including CbC reporting for large taxpayers from 1 January 2016;
- recently enacted legislation to implement the OECD's Common Reporting Standard from 1 July 2017;
- establishing an extensive third-party reporting regime, under which a range of 'third party' entities (including government-related entities, the Australian Securities and Investment Commission, listed companies and trusts, fund managers and custodians and banks) have an annual obligation to report information to the local tax authority regarding a wide range of transactions such as government grants and payments to suppliers, transfers of real property, transfers of shares and units and business payments, commencing from 1 July 2016; and
- recently announcing a number of new conditions that will ensure that foreign investors seeking to invest in Australia are fully compliant with Australian tax laws, including requirements relating to the settlement of outstanding tax debts, ongoing compliance with tax laws, notification of any material transactions to which the transfer pricing or anti-avoidance provisions may apply and annual reporting to the local tax authority.

Transparency measures like these present many challenges for affected taxpayers. The compliance costs associated with the collection and transfer of this information from the taxpayer to the tax authority can be significant, and require careful management. In many cases, taxpayers will be required to implement new systems and processes to identify and collate this information. This may involve both real costs and lost opportunity costs to the business. The increased information flowing between taxpayers and tax authorities (both locally and to overseas jurisdictions via information exchange) may also mean that taxpayers need a new approach to managing tax risks from a global perspective.

In addition to the above measures, Australia is one of the few countries that has a mandatory public tax transparency regime in place. Under this regime, the Australian Commissioner of Taxation has an obligation to annually publish selected income tax information for certain large taxpayers, as outlined in Table 2.

Table 2

Overview of Australia's public tax transparency regime:

Who is subject to these laws?	What information is published?
All companies with total income of at least AUD100 million (as disclosed in its income tax return), except Australian-owned private companies with total income of less than AUD200 million.	• Name • Australian Business Number • Total income for the year * • Taxable income (if any) for the income year * • Income tax payable (if any) for the income year * **As reported in the taxpayer's income tax return*
All Petroleum Resource Rent Tax (PRRT) and the former Minerals Resource Rent Tax (MRRT) taxpayers	• Name • Australian Business Number • Amount of PRRT (or MRRT) payable for the year

This measure represented a significant shift in the tax transparency landscape in Australia, where the notion of privacy of a taxpayer's affairs comes second to the desire for increased transparency regarding tax paid by companies operating in Australia. The implications of such public disclosure of information can be far reaching, particularly the potential for misinformation given the limited nature of the information being published. As the first report under these measures was only released in December 2015, it is too soon to gauge whether these measures will discourage large companies from engaging in aggressive tax avoidance practices and inform public debate about tax policy as intended.

A key challenge for companies operating in this environment is to ensure that their tax affairs are properly understood, bearing in mind the limited information that is being put in the public domain. Managing stakeholder communications and expectations (including those of the general public, consumers and suppliers, employees, investors and regulators) is critical. In fact, the release of tax information under Australia's public tax transparency regime resulted in a number of large Australian companies voluntarily releasing additional information about their tax affairs. They did this to supplement information published by the Australian tax authority and 'tell their own story', particularly in cases where there were large differences between total income (a gross income figure based on accounting concepts) and taxable income (a net figure based on tax concepts), or specific tax concessions that may not be identifiable from the limited information released.

The Australian Government requested that Australia's Board of Taxation develop a voluntary tax transparency code because of this desire for more tax transparency. While the code is not finalised yet, preliminary recommendations have been put forward for additional disclosure of tax information by 'large businesses' (those with turnover in Australia of at least AUD500 million) and slightly less disclosure for 'medium businesses' (those with turnover in Australia of at least AUD100 million but less than AUD500 million). The recommendations include improvements to tax disclosures in financial statements for both large and medium business, and an annual 'taxes paid' report for large businesses. The code is expected to be finalised by May 2016 so as to allow for it to be in operation in time for the reporting period for 2015-16 financial statements or annual reports of those companies that wish to adopt it.

As the debate around tax paid by companies operating in Australia continues to gain momentum, it is likely that more transparency measures will be adopted in the near future. Over the past 18 months, an Australian Parliamentary Committee has been conducting an inquiry into 'tax avoidance and aggressive minimisation by corporations registered in Australia and multinational corporations operating in Australia'. The inquiry is still ongoing and is due to release its final report by 22 April 2016. The interim report published in August 2015 made 17 recommendations, many of which focused on increased transparency including:

- a mandatory tax reporting code;
- a public register of tax avoidance settlements reached with the local tax authority where the value of that settlement is over an agreed threshold; and
- the government to consider publishing excerpts from CbC reports (this is being considered by some other OECD countries including the United Kingdom and the European Union).

The current Australian Government has not indicated that it accepts any of these recommendations. With a federal election due this year, whether any of these recommendations are ultimately adopted by the current or future government remains to be seen.

The future of tax transparency

While the level of interest in taxes paid by companies continues to increase, tax transparency regimes will likely continue to be an area of focus for governments around the globe. Transparency regimes ensure that tax authorities have the information they need to appropriately administer the law. Public regimes can help in some ways to ensure that MNCs pay their 'fair share' of tax and are held accountable in the public court of opinion. It is now well known that tax is becoming a much bigger driver of companies' reputation and brand health than it was say five years ago.

As highlighted above, there are costs and risks attached to increasing tax disclosure. These include the cost of collating the information, which may not be collected in the normal course of business, and risks that commercially sensitive information could be revealed or that disclosures could be misunderstood, misused or misinterpreted. At the same time, some may argue that there may be benefits in having increased transparency to alleviate some of the confusion and uncertainty about whether MNCs are contributing their 'fair share' to the public revenue. In this respect, many companies, rather than waiting for changes to be implemented into law, are already exploring tax disclosure and communication in a way that best explains their own circumstances and tells their own story. Regardless, it is clear that the trend towards increased tax transparency is not likely to slow down and will remain a real issue that all MNCs will need to grapple with.

Australia

Conditions to be imposed on foreign investment into Australia

The Australian Government announced on 22 February 2016 that it will apply new requirements on foreign investment applications to ensure that foreign investors in Australia pay the required amount of tax.

The Treasurer confirmed that a standard set of conditions will be applied to clearance of investment proposals presented to the Foreign Investment Review Board (FIRB). In summary, these conditions require an applicant to do, and use best endeavours to procure its associates to do, the following in relation to an investment proposal:

- comply with Australian tax law in relation to the proposal and associated transactions;
- provide information to the Australian Taxation Office (ATO) in relation to the application or potential application of Australian tax laws to the proposal or associated transactions;
- notify the ATO of any material transactions or dealings it has or will enter into in connection with the proposal or associated transactions, in which the transfer pricing or anti-avoidance provisions of the Australian tax law may apply and the ATO have not been previously notified;
- pay any outstanding tax debt which is due or payable at the time of the proposal; and
- provide annual report to the FIRB of its compliance with the abovementioned conditions.

The Treasurer has foreshadowed the imposition of two additional conditions where a significant tax risk is identified. In this case, an applicant may be required to:

- engage in good faith with the ATO to resolve any tax issues in relation to the proposal; and
- provide information specified by the ATO on a periodic basis, including a forecast of tax payable.

The changes highlight the increasingly important role of the ATO for investors seeking clearance of foreign investment proposals. In particular, FIRB's approvals will now, in part, depend upon the administrative interpretation of tax laws by the ATO.

The Treasurer said in his media statement that 'a breach of these conditions could result in prosecution, fines and potentially divestment of the asset'.

Introduction of multinational anti-avoidance legislation

The Australian Government enacted the new multinational anti-avoidance law (MAAL) on 3 December 2015 which implements a targeted anti-avoidance regime for multinational enterprises (MNEs) with an annual global revenue of AUD1 billion or more.

The MAAL applies from 1 January 2016 and is designed to counter the erosion of the Australian tax base by multinational entities through using artificial or contrived arrangements to avoid the creation of a taxable presence in Australia. The MAAL amends Australia's anti-avoidance law for multinationals that supply goods or services to Australian customers and derive revenue from overseas sales.

The MAAL applies when an Australian related entity of a foreign seller performs activities connected with the sales (e.g. marketing services) and it is concluded that the arrangement was entered into with a principal purpose of avoiding tax in Australia or reducing their foreign tax liability. The MAAL was originally intended to target 30 unnamed multinationals (predominantly operating in the technology sector), but the number of taxpayers who will be impacted is likely to be much higher than this.

Where the MAAL applies, the foreign entity will be taxed as if it had made the sales through an Australian permanent establishment (PE). This means it will be subject to Australian tax on the notional profits attributable to the deemed PE, as well as withholding taxes on royalty or interest expenses attributable to the deemed PE. Penalties will also apply on top of these taxes, generally at a rate of 100%.

MAAL is designed to counter erosion of Australian tax base by multinational entities.

Introduction of country-by-country reporting

Consistent with Action 13 of the Organisation for Economic Cooperation and Development (OECD)'s Base Erosion and Profit Shifting (BEPS) Action Plan, Australia has passed a legislation implementing country-by-country (CbC) reporting.

The CbC reporting law applies for income years beginning on or after 1 January 2016, which is in line with the OECD's recommendations. All Australian and foreign groups with an Australian presence and a global turnover of more than AUD1 billion will need to submit the master file and local file to the ATO. The CbC reports are expected to be filed by the parent company of the group with their home tax authority, so Australian headquartered multinationals will need to file the CbC reports with the ATO.

On 17 December 2015, the ATO issued a Law Companion Guideline on CbC reporting to provide preliminary guidance on how the ATO administers the CbC reporting regime, covering the following:

Expectations for Australian subsidiaries where the parent company is not required to prepare the country-by-country reports and master file

The ATO recognises that it may be outside of an entity's control to provide the ATO with the required information given that other countries have yet to implement CbC reporting as recommended by the OECD.

The ATO encourages entities encountering difficulties in providing information to contact the ATO and discuss whether an exemption is appropriate. For example, where a parent company is not yet required to provide a CbC report and/or master file, the ATO intends to exempt its subsidiaries for the first year from producing the CbC reports and master file. However, the entity will still need to provide a local file.

Local file information requirements

The ATO proposes three different types of local files:

- a full local file;
- a simplified local file; and
- a short form local file.

The eligibility criteria of and specific contents to be included in each type of local file will be covered in later guidance.

Possible exemptions

The ATO will only exercise its discretion to provide exemptions in very limited circumstances. When considering a request for an exemption from lodging a statement in a particular instance for a specified period, the relevant factors the ATO will take into account include:

- the entity's risk profile, including the amount of its overseas dealings;
- the compliance burden on the entity; and
- whether the ATO will receive the relevant statement(s) by alternative means (e.g. via exchange of information).

Approved forms and periods for lodgement

The statements for CbC reporting must be lodged electronically in the approved form within 12 months after the end of the income year or the replacement reporting period to which they relate. For expediency, an entity may choose to lodge one or more of the required statements with their income tax return at the same time.

Changes to financial reporting of 'significant global entities'

Australia enacted new legislation requiring 'significant global entities' (i.e. entities forming part of a group with global income of more than AUD1 billion) to prepare general purpose financial statements for their Australian operations.

The new financial reporting requirements will apply for reporting periods beginning on or after 1 July 2016. While some Australian subsidiaries and branches of multinationals may have already prepared general purpose financial statements, others may have prepared special purpose financial statements (which contain more limited disclosures, particularly in relation to related party transactions), and some do not prepare Australian financial statements at all.

The general purpose financial statements must be submitted by the taxpayers to the ATO by the time they file the income tax returns for the relevant period if they have not previously been filed with the Australian Securities and Investments Commission (ASIC). The ATO will be required to share the financial statements it receives from ASIC. Documents filed with ASIC are available to the public while CbC reporting only requires information to be provided to tax authorities. This change is intended to increase public transparency over the financial affairs of certain multinationals' Australian operations.

Penalties for non-compliance are based on the administrative penalties that taxpayers can incur for failing to lodge their returns, in addition to any reputational impact that may arise from non-compliance.

Federal Court of Australia rules on seminal transfer pricing case: Chevron Australia Holdings Pty Ltd v Commissioner of Taxation

The Federal Court announced its ruling in *Chevron Australia Holdings Pty Ltd v Commissioner of Taxation (No 4)* [2015] FCA 1092 on 23 October 2015. The Federal Court dismissed the taxpayer's appeal against the Commissioner's deemed objection decisions (dismissing the taxpayer's objections) in relation to the amended income tax assessments and administrative penalty assessments issued to the taxpayer in respect of each of the financial years 2004 - 2008. Fundamentally, the dispute focused on the application by the Commissioner of the Australian transfer pricing rules.

In this case, the Commissioner sought to apply the transfer pricing rules in Division 13 of the *Income Tax Assessment Act 1936* for each of the financial years 2004 - 2008, and Subdivision 815-A of the *Income Tax Assessment Act 1997* (ITAA 1997) for each of the financial years 2006 - 2008. Under the amended assessments, the Commissioner disallowed deductions claimed by the taxpayer in respect of interest incurred on loans provided to the taxpayer by a related company resident in the United States. The amended assessments were issued to the taxpayer based on the Commissioner's view that the interest rate applying to the loan exceeded the arm's length rate, and thus the deductions claimed were excessive.

The Court ruled in favour of the Commissioner as it found that the taxpayer did not satisfy the onus of proving that the Commissioner's assessments were excessive.

The Court held that the requirement that the arm's length consideration must be assessed by reference to the total consideration provided by the taxpayer under the cross-border loan agreement. This includes not just the promise to repay principal and interest, but also financial covenants, security and guarantees provided. This analysis enabled the Court in considering the pricing of the interest payable on the loan based on its actual terms and conditions to also have regard to whether those other terms and conditions were consistent with the evidence accepted by the Court as to what an independent party in comparable circumstances would have agreed to.

The Court decided that the consideration provided was inconsistent with what would have been agreed between independent parties. Specifically, the Judge concluded that an independent borrower would have included security, operational and financial covenants in the loan terms, which would have resulted in a lower interest rate although he accepted that the loan would have been denominated in AUD.

The Judge did not consider the hypothesising of all the terms and conditions that make up the arm's length consideration to be a 'reconstruction' or 'recharacterisation' of the transaction. The hypothesising of arm's length terms and conditions has implications not only for the pricing of debt transactions, but also for other transfer pricing arrangements where the Commissioner may form a view that the actual terms are uncommercial, and/or exclude terms that may be found in arm's length transactions.

The taxpayer has appealed the Federal Court's decision to the Full Federal Court. The appeal is expected to be heard later this year.

Board of Taxation

Consultation on proposed anti-hybrid rules

The Board of Taxation (the Board) released its discussion paper on the implementation of the anti-hybrid rules on 20 November 2015.

Under the terms of reference issued by the government on 14 July 2015, the Board has been requested to undertake consultation on the implementation of

new tax laws to neutralise hybrid mismatch arrangements (anti-hybrid rules), pursuant to the recommendations of the G20 and OECD under Action 2 of the BEPS Action Plan, and to examine how best anti-hybrid rules can be implemented in the Australian legal context. In particular, the Board has been asked to identify an implementation strategy regarding the following:

- delivering on the objectives of eliminating double non-taxation, including long-term tax deferral;
- economic costs for Australia;
- compliance costs for taxpayers; and
- interactions between Australia's domestic legislations (e.g. the debt/equity rules and regulated capital requirements for banks), international obligations (including tax treaties) and the new anti-hybrid rules.

Unlike the OECD's final report, the Board's consultation paper is a much shorter document developed to facilitate discussion on the best way to implement these rules into the Australian domestic laws and to identify any issues associated with the implementation.

The consultation paper does not contain any options or express the Board's preliminary views as to how the Australian Government should proceed with these rules. However, it provides a summary of the concepts and recommendations in the OECD report and identifies some Australian specific examples that will likely be caught should the rules be implemented (e.g. US general partnership with Australian partners, limited partnerships, redeemable preference shares, security lending arrangements).

The Board was requested to report to the government by March 2016 to allow this issue to be considered as part of the 2016 Federal Budget (which will be announced in May 2016).

Consultation on the tax transparency code

The Board released a consultation paper on the voluntary tax transparency code (TTC) on 11 December 2015. The paper contains the Board's preliminary recommendations for additional disclosure of tax information by 'large businesses' (with Australian turnover of at least AUD500 million) and slightly less disclosure for 'medium businesses' (with Australian turnover of at least AUD100 million but less than AUD500 million).

The government commissioned the Board to develop the TTC as a way to improve community confidence in the tax system and to encourage all businesses to adopt a low-risk approach to their tax affairs through enhanced public disclosure.

In designing the TTC framework, the Board identified three categories of potential users of the information. They are:

- general users – the 'person in the street';
- interested users – shareholders, analysts, investors, social justice groups, media and politicians; and
- revenue and regulatory authorities – ATO and ASIC.

The TTC was explicitly designed for the first two categories of users, recognising that the ATO already has access to all of the information it needs through tax returns, supporting schedules and information obtained directly from businesses.

Information to be disclosed under the tax transparency code

The Board's preliminary recommendations include:

- medium businesses should adopt Part A, which involves improvements to tax disclosures in financial statements; and
- large businesses should adopt both Part A and Part B, which is the preparation of an annual 'taxes paid' report.

The recommendations in Part A and Part B are summarised below.

Part A	Part B
1. Reconciliation of accounting profit to tax expense and income tax paid/payable	1. Qualitative description of the approach to tax policy, tax strategy and governance
2. Identification of material temporary and non-temporary differences	2. Total tax contribution summary of corporate taxes paid
3. Accounting effective company tax rates for Australian and global operations	3. Qualitative information about international related party dealings, financing and tax concessions

How disclosures should be made

The Board recommends companies that prepare Australian general purpose accounts to include the Part A disclosures as part of their accounts. Businesses that do not prepare general purpose accounts are expected to include the Part A disclosures in a separate document.

The 'taxes paid' report is separate from the financial statements and is expected to be made public. The Board does not intend to prescribe a standard template or form for the report. It is anticipated that many businesses will publish more than the minimum standard of content required under the TTC due to their corporate approach to transparency, international transparency requirements or their particular circumstances warrant further explanation.

There is no proposed timeframe for the preparation of the 'taxes paid' report, but it is recommended to apply from financial year 2015/16 reporting period.

Written submissions in relation to the consultation paper were due on 29 January 2016 and the Board will release its final report by May 2016.

Legislation implementing Common Reporting Standard

The Tax Laws Amendment (Implementation of the Common Reporting Standard) Bill 2015 was passed by Federal Parliament on 29 February 2016. This legislation implements the OECD's Common Reporting Standard (CRS) in Australia. It requires 'reporting financial institutions' (RFIs) in Australia to identify account-holders using prescriptive due diligence procedures. Once Australian financial institutions have identified the relevant account holders, they will be required to report to the ATO the information on financial accounts held by foreign residents. The ATO will then provide the information to the relevant foreign residents' tax authorities. At the same time, the ATO will receive information on Australian residents with financial accounts overseas.

RFIs generally include banks and other deposit-taking institutions. However, retirement and pension accounts and some non-retirement savings accounts are generally treated as 'excluded accounts' and therefore excluded from reporting under the CRS regime.

The CRS will apply to Australian financial institutions from 1 July 2017, with a first reporting deadline of 31 July 2018 (in respect of the six-month period from 1 July 2017 to 31 December 2017).

Cambodia

Modification of fiscal stamp tax rates

The Royal Government of Cambodia (RGC) amended the fiscal stamp tax (FST) rates imposed on certain legal documents, business advertising posters, and sign boards. The details are outlined in the sub-decree which replaces Sub-Decree No. 76 dated 11 October 1995. An exemption is granted for sign boards that are used for non-profit purposes such as promoting social moral and environmental issues, etc.

Value added tax exemption for supply of clean water

According to the above regulation (Prakas), the production and supply of clean water for public use is exempt from value added tax (VAT). Consistently, Article 32 of the sub-decree does not allow taxpayers who make non-taxable supplies to claim input VAT on the purchase of materials or services used for non-taxable supplies. Supply of services or goods other than supply of clean water is subject to 10% VAT. Supply of drinking water is not covered in the Prakas. The Prakas became effective from 25 June 2015.

Suspension of prepayment of tax on profit payment for listed companies

The Ministry of Economy and Finance (MEF) issued a Prakas suspending listed companies from payment of monthly prepayment of tax on profit (PToP) for the period that they are entitled to tax incentives under Sub-Decree No. 01 dated 8 January 2015. The suspension is subject to conditions under Article 8 of the Sub-Decree No. 01.

Rules and procedures for resolving tax appeal at the General Department of Taxation of Ministry of Economy and Finance

The MEF outlined rules and procedures to resolve a tax appeal with the General Department of Taxation (GDT). The taxpayers' appeal can be rejected if they fail to comply with the procedures and requirements set out in this new Prakas properly. However, the tax authority will issue a formal decision which indicates clear reasons for the rejection.

Tax mechanism for finance lease transactions

The MEF issued a Prakas outlining a mechanism to tax finance lease transactions. The key points are highlighted as follows:

Key areas	PwC's comments
Registration requirements	The lessor must be a real-regime registered taxpayer and have a finance lease licence from the National Bank of Cambodia.
Lease period	Must be more than one year.
Conditions	There are various conditions that finance lease transactions must be complied with.
Taxes on finance lease transactions	
VAT	Output VAT applies to the principal and other charges, except for interest. Input VAT is allowed as a credit to both the lessor and lessee.
PToP and minimum tax	The lessor is subject to PToP and minimum tax on all charges and interest, excluding the principal.
Tax on profit (ToP)	The lessor must recognise income at the earlier of the payment to be received is due or paid.
Tax depreciation	The lessee is entitled to tax depreciation on the leased asset.
Withholding tax (WHT)	WHT does not apply to finance lease transactions.
Other related matters	Please refer to the Prakas No. 1704 MEF.PrK dated 9 December 2015.

Prakas on the suspension of PToP payment for garment and footwear manufacturing enterprises

Garment and footwear manufacturing enterprises are not required to pay monthly PToP for another two years, until the end of 2017. However, the payment suspension requires the enterprises to submit the statutory financial audited reports to the tax administration. That means these enterprises must have the financial statements audited by independent external auditors. Otherwise, they will be subject to penalty stipulated in the taxation law.

Enterprises that support the export activities of garment, textile, footwear, bag, handbag and headwear are not entitled to this suspension.

Prakas on taxpayer classification under the self-declaration regime

Under the self-declaration regime (real regime), taxpayers will be reclassified into three categories based on their turnover (total value of supplies of goods and services), legal form and other criteria. The criteria are summarised below:

Type of taxpayer	Criteria (approximated USD amount)
Small	Sole proprietorship or general partnership: • Annual turnover of USD62,500 to USD175,000 • Total turnover for any three consecutive calendar months exceeds USD15,000 • Total expected turnover for the next three consecutive months exceeds USD15,000 • Participating in bidding, fee consultation or fee surveys for the supply of goods or services
Medium	• Annual turnover of USD175,000 to USD500,000 • Registered as a legal person • Government institutions below national level, associations and non-government organisations
Large	• Annual turnover of over USD500,000 • Branch of a foreign company • Qualified investment projects • Government institutions, diplomatic and consular missions, international organisations and technical cooperation agents of other governments

Rules and procedures for implementing simplified accounting records for small taxpayers

Prakas No. 1820 MEF.PrK, dated 25 December 2015 sets out the rules and procedures for implementing simplified accounting records as well as monthly and annual tax obligations (ToP/minimum tax, VAT, PToP, tax on salary/tax on fringe benefits and WHT) for small taxpayers. Small taxpayers are required to maintain the following three accounting records: a daily purchases book, a daily sales book and an inventory book. Please refer to the Prakas for more details.

Rules and procedures for managing patent tax collection

The Prakas sets out the rules and procedures for collecting patent tax. The amount of tax payable varies depending on the taxpayer's category and turnover.

<table>
<tr><th>Type of taxpayers</th><th>Patent tax (approximated USD amount)</th></tr>
<tr><td>Small</td><td>USD100 per year</td></tr>
<tr><td>Medium</td><td>USD300 per year</td></tr>
<tr><td rowspan="2">Large</td><td>• USD750 for turnover from USD500,000 to USD2,500,000
• USD1,250 for turnover over USD2,500,000</td></tr>
<tr><td>Additional tax of USD750 if the taxpayer has a branch, warehouse, factory or workshop for a business activity in a different city or province.</td></tr>
</table>

2016 Financial Management Law

The Financial Management Law for 2016 was promulgated on 17 December 2015, the key points are summarised below:

- Small taxpayers must follow the simplified accounting rules set out in Prakas No. 1820 dated 25 December 2015.
- Medium and large taxpayers must follow the international accounting and reporting standards of Cambodia, which are similar to International Financial Reporting Standards (IFRS).
- Amounts due to related parties that are not under the self-declaration regime (real-regime) cannot be deducted as an expense until they are actually paid.
- For tax on profit purposes, banks and saving and lending institutions are allowed to record provisions for doubtful debts. The rules and procedures for tax deduction of these provisions will be defined by a Prakas issued by the Ministry of Economy and Finance.

Stamp tax exemption on the transfer of a title deed or possession rights of immovable properties between relatives

The RGC granted a stamp tax exemption on the transfer of a title deed or possession rights of immovable properties (i.e. lands and/or buildings) between blood parents and children, husband and wife, and blood grandparents and grandchildren. The exemption has no retroactive effect and will be included in the Financial Management Law for 2017.

Amendment of customs duty and specific tax rates on certain imported goods

The RGC amended the customs duty and specific tax rates on the following types of imported goods. Relevant authorities are required to implement the sub-decree from 1 April 2016 onwards.

No.	Type of tax	Types of goods (please refer to the corresponding sub-decree for details)	Rate
1	Customs duty	Books	From 7% to 0%
		Toys	From 7% to 0%
		Computers and accessories	Some from 15% to 7%, and Some from 35% to 15%
		Aluminium frame	From 0% to 7%
2	Specific tax	Beer	From 25% to 30%
		Wine	From 20% to 35%
		Cigarette	From 15 to 20%
		Petroleum products	Some from 0% to 15%, Some from 5% to 25%, Some from 10% to 20%, and Some from 10% to 25%.
		Mirror (as construction materials)	From 0% to 10%
		Electronic products	Some from 0% to 10%, Some from 10% to 25%, and Some from 10% to 0%.
		Motor vehicles	Some from 10% to 15%, Some from 10% to 20%, and Some from 10% to 25%.
		Vehicles	Some from 25% to 30%, Some from 50% to 60%, Some from 50% to 65%, Some from 30% to 40%, and Some from 10% to 20%.
		Vehicle accessories	Some from 10% to 15%, Some from 10% to 20%, and Some from 10% to 25%.

The GDT issued a notification to indicate that the increase in the above specific tax rates are also applicable for locally produced beer, wine and cigarettes.

Invoicing of self-declaration taxpayers

The GDT issued an instruction on invoicing requirements (including invoice criteria) for self-declaration taxpayers (i.e. real regime). In addition to the existing criteria of a tax invoice as stated in the VAT regulations, taxpayers are now required to use good quality ink and paper for printing invoices to ensure that they can be maintained in good condition for 10 years. Based on the sample of invoices attached in the GDT's instruction, the buyers also have to sign on the invoices.

More importantly, the invoice must be issued either in Khmer or both Khmer and English.

Any tax invoices not issued according to the existing and new criteria will not be accepted as valid invoices to claim input VAT credit or to support expense deductions.

Organisation and functioning of the Tax Disputation Committee

The RGC issued a sub-decree on the organisation and functioning of the Tax Disputation Committee (TDC). The TDC has the duties to review, solve and decide on disputations filed by taxpayers who disagree with the final decision or measures of the GDT and the General Department of Customs and Excise that creates any obligations on them.

Any taxpayer who is not satisfied with the TDC's decision can file a complaint to the court within 30 working days after receiving the TDC's formal decision.

Procedures for collecting stamp tax on the transfer of title deeds or possession rights of registered and non-registered immovable properties

To ease the transfer of property ownership, the RGC agreed to impose stamp tax at 4% (once only on the ultimate transaction) on the transfer of title deeds of registered immovable properties and the possession rights of non-registered immovable properties.

Notifications of market interest rates on loans for 2015 tax on profit

For 2015 ToP returns, the GDT set the annual market interest rates on (i) loans borrowed in USD at 10.28% based on the average rate of nine major commercial banks in Cambodia and (ii) loans borrowed in KHR at 19.51% based on the average rate of two major commercial banks in Cambodia.

The maximum deductible interest rates are as follows:

Loans in USD	Loans in KHR
• 12.336% for third-party loans (10.28 x 120%) • 10.28% for related-party loans	• 23.412% for third-party loans (19.51 x 120%) • 19.51% for related-party loans

China

Localisation of Base Erosion and Profit Shifting in China

The Organisation for Economic Cooperation and Development (OECD) released the final reports on all of the 15 action points of the Base Erosion and Profit Shifting (BEPS) Action Plan (BEPS package) on 5 October 2015. The G20 finance ministers endorsed the BEPS package in Lima, Peru on 8 October 2015.

China pays a very high level attention to the BEPS project. The State Administration of Taxation (SAT) has expressed its full support to the BEPS project in various occasions. The SAT also formed a BEPS task force when the BEPS project was launched back in 2013. Over the last couple of years, around 50 SAT officials participated in the BEPS project and China submitted over 1,000 comments or suggestions to the OECD, many of which are now reflected in the BEPS package.

The SAT has already been working very hard to localise the BEPS Action Plan through the revision of a series of domestic tax laws and tax treaties. Some of the most important developments include:

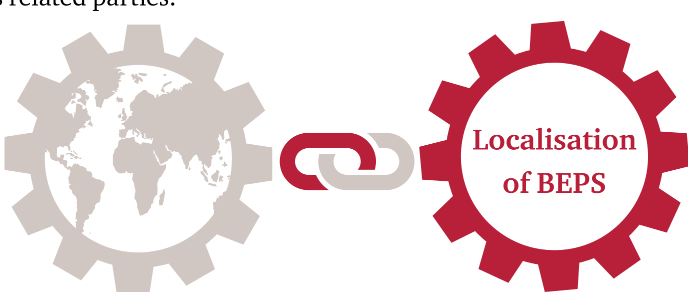
- SAT Public Notice [2015] No.16 which sets out SAT's position from a transfer pricing (TP) perspective in relation to the outbound payments of service fee and royalty fee to overseas related parties.
- SAT Public Notice [2015] No.7 which provides comprehensive guidance for the assessment of general anti-avoidance rule investigation for the indirect transfer of China taxable properties (for more details of SAT Public Notices [2015] Nos. 7 and 16, please see Asia Pacific Tax Notes 2015).
- Inclusion of the Limitation on Benefit clause (which is recommended in the final report of BEPS Action 6 on treaty abuse) in the recently negotiated double tax treaties with Chile.
- Ratification of the Multilateral Convention on Mutual Administrative Assistance in Tax Matters signed by China in August 2013 and which has become effective in China from 1 February 2016. The signing of the Multilateral Competent Authority Agreement in December 2015 allows China to move forward with plans to activate automatic exchange of financial account information in tax matters and commence exchange with other countries in 2018.
- Signing of a Memorandum of Understanding between the SAT and OECD in December 2015 to implement a Multilateral Tax Programme at the OECD-SAT Multilateral Tax Centre in Yangzhou, China. The new Multilateral Tax Centre will deliver a programme open to interested country officials reflecting the OECD's current initiatives for the benefits of all participating countries.

The State Administration of Taxation's action plans in relation to the BEPS project in the near future

We can anticipate that the BEPS package will drive significant changes, over a reasonable time span, in China's TP standards, tax treaties, many parts of domestic tax laws and regulations, and even Chinese tax authorities' behaviours with an aim to counter tax avoidance and reinforce China's taxing rights to get a fairer share of multinational corporations (MNCs) taxation. MNCs need to get ready for the challenges of the new requirements on transparency and substance-tax alignment.

Some of the SAT's action plans are as follows:

- To revise the domestic tax laws and regulations. For example, to include the mandatory disclosure of aggressive tax planning schemes in the amended Tax Collection and Administration Law and to include the general anti-avoidance rules in the amended Individual Income Tax Law.
- To localise the BEPS package on an as-needed basis. The Implementation Measures of Special Tax Adjustment (Guoshuifa [2009] No. 2, Circular 2) was issued in early 2009 and is regarded as a master guide on the TP and anti-tax avoidance rules in China. The SAT issued a discussion draft of the revised Circular 2 in September 2015 which covers a wide range of issues discussed in the BEPS Action Plan including



The SAT is working hard to localise the BEPS Action Plan by revising domestic tax laws and tax treaties.

Action 3 (controlled foreign company), Action 4 (interest deduction), Actions 8 to 10 (intangibles and TP considerations) and Action 13 (TP documentation and reporting). Revised Circular 2 is one of the most important developments for China's localisation of the BEPS recommendations and the final version is expected to be released in 2016.

- To establish a national tax risk monitoring and response system on MNCs on a group basis. The local-level tax authorities in charge of a MNC's headquarter are responsible for monitoring the tax risks of the whole group.
- To use information technology to facilitate international tax administration.

The new self-assessment mechanism for non-tax residents to claim tax treaty benefits

According to Guoshuifa [2009] No. 124 (Circular 124) issued in 2009, non-tax resident taxpayers were required to obtain Chinese tax authorities' approval/record-filing acknowledgement before they could enjoy the tax treaty benefits under the double tax agreements (DTAs) entered into by China. In September 2015, the SAT issued the Administrative Measures on Non-resident Taxpayers Claiming Tax Treaty Benefits (SAT Public Notice [2015] No. 60, Public Notice 60) to replace Circular 124 and introduce a new mechanism of self-assessment on the eligibility for tax treaty benefits (reduced taxation or exemption under the relevant DTAs) by non-resident taxpayers.

New procedure

Public Notice 60 requires non-resident taxpayers and their withholding agents (if applicable) to go through the self-assessment procedure and file certain prescribed forms and other supporting documents when performing tax filing to justify their claims for the tax treaty benefits.

Reporting obligation

Non-resident taxpayers and withholding agents have the following obligations depending on different categories of reporting:

- Self-reporting by non-resident taxpayers: They shall perform self-assessment on their eligibility for tax treaty benefits while filing their tax returns.
- Circumstances where the payer of that income is legally obliged to be the withholding agent or appointed as such: The withholding agent shall check whether the tax treaty benefits should apply according to the forms and documents provided by the non-resident taxpayers. However, Public Notice 60 states that non-resident taxpayers shall still remain to be the party responsible for the authenticity of the information and documents submitted to the Chinese tax authorities.

Assessment of the eligibility to treaty benefits

Non-resident taxpayers and their withholding agents (if applicable) are required to provide a considerable amount of information in the prescribed forms and supporting documents to be submitted to the Chinese tax authorities in order to substantiate the tax residency, types of income and qualification (e.g. beneficial ownership) of the non-resident taxpayer for the tax treaty benefits.

Reporting frequency

Non-resident taxpayers and their withholding agents need to submit the prescribed forms together with the tax returns each time they perform tax filing. The requirement for submitting the supporting documents may be waived by the tax authorities for a certain period of time, depending on the category of income, in order to reduce repetitive submission.

Implementation

The role of the Chinese tax authorities has changed from pre-approver to post-tax filing examiner. The SAT issued Shuizongfa [2015] No.128 (Circular 128) to provide guidelines for local-level tax authorities on how to conduct assessment of the tax treaty benefit claims. Circular 128 sets forth the minimum percentage of treaty benefit claims to be selected for post-filing examination and the timeframe of such examination for the local-level tax authorities. The treaty benefit claims with the following characteristics are more likely to be examined:

- The non-resident taxpayer is from a jurisdiction with low effective tax rate.
- The non-resident taxpayer has a bad credit rating due to the refusal to pay back the taxes on time after an improper benefit claim was discovered, or having committed inappropriate actions such as the refusal to cooperate in previous examinations.
- A large amount of taxes are exempted or reduced.

This new mechanism would bring convenience and efficiency in granting tax treaty benefits and thus speed up the repatriation of funds, which should be welcomed by non-resident taxpayers. However, it would also bring uncertainties and challenges to non-resident taxpayers and their withholding agents. To mitigate the tax risks of being challenged on treaty shopping or treaty abuse, non-resident taxpayers and their withholding agents should ensure that proper documentation is in place and communicate early with their in-charge tax bureaus, where possible.

Completion of the Business Tax-to-Value Added Tax Reform

Business tax (BT) has been levied on the provision of services and the transfer of immovable properties and intangible assets since 1994. In order to mitigate the multiple taxation issues associated with goods and services and support the development of modern service industries, China firstly launched a pilot run of the BT to value added tax (VAT) reform (B2V Reform) in Shanghai in 2012 which covered transportation industry and certain modern service industries. It has been expanded nationwide to cover several additional industries through the recent years. In March 2016, the State Council announced that the remaining industries that are still subject to BT (i.e. construction, real estate, financial services, and consumer services industries) will be subject to VAT starting from 1 May 2016. This earmarks the completion of the B2V Reform and the official removal of BT from China's indirect tax system.

The applicable VAT rates for the four industries are as follows:

Industries	Applicable VAT rate
Construction and real estate	11%
Financial services and consumer services	6%

Tax policies to upgrade industrial structures and boost economy

The Chinese government has been supporting technology companies and encouraging research and development (R&D) activities via various policies, including tax incentive policies, to promote the structural adjustment of economy and industrial upgrading.

New administrative measures for new high-tech enterprises

China's prevailing Corporate Income Tax Law (CIT Law) provides a reduced income tax rate of 15% for qualified new high-tech enterprises (NHTEs). A company has to satisfy several conditions and go through specific assessment procedures as prescribed in a few circulars released in 2008 in order to enjoy the reduced CIT rate. In January 2016, several governmental authorities jointly released a new circular, Guokefahuo [2016] No.32 (Circular 32), to amend the assessment criteria and other administrative matters for NHTEs. The highlights of the amendment in Circular 32 include:

- expanding the high and new technology areas specifically supported by the State and removing certain technologies in the previous areas;
- adjusting certain assessment criteria and retaining the implicit requirement for enterprises to manage their NHTE qualifications systematically; and
- simplifying the assessment procedure to facilitate application processes and establishing an administrative mechanism of selective examination and key examination.

To summarise, starting from 1 January 2016, a company has to meet the following conditions simultaneously to qualify as a NHTE:

- The company has been incorporated for at least one year.
- The company has obtained the ownership of intellectual property rights that has made core technical contribution to its main product (service).
- The technology that makes a core technical contribution to its main product (service) of the company shall fall within the technology area of the 'Catalogue of High and New Technology Areas Specifically Supported by the State'.
- The ratio of the number of personnel participating in R&D to the total number of employees for the current year shall not be less than 10%.
- The minimum ratio of the total R&D expenditures to the total amount of sales revenue for the same year shall meet the following requirements for the last three accounting years:
  - 5% for a company whose sales revenue is less than RMB50 million (inclusive)
  - 4% for a company whose sales revenue is between RMB50 million and RMB200 million (inclusive)
  - 3% for a company whose sales revenue is above RMB200 million.

  In addition, the total R&D expenditures incurred within China shall not be less than 60% of the total R&D expenditures.

- The total amount of income generated from the sale of the new/high tech products (or services) shall not be less than 60% of the total annual income.
- The company shall satisfy the requirement for innovation capability evaluation.
- No serious security or quality accidents, or incidents seriously violating environmental laws or regulations shall happen to the company during the preceding year before application.

It is anticipated that Circular 32 will bring profound impact to NHTEs in China in terms of obtaining the NHTE qualification, retaining the eligible status, and the industry restructuring. Companies are advised to attend to the management of NHTE by enhancing their compliance level and mitigating the relevant risks.

Refined policies on start-ups and innovation

The Ministry of Finance and SAT jointly issued Caishui [2015] No.116 (Circular 116), extending certain income tax incentives implemented in the National Innovation Demonstration Zones nationwide, including:

- CIT preferential treatment for corporate partners of venture capital limited partnerships and for income derived from technology transfer; and
- individual income tax preferential treatment for shares distributed to individual shareholders and for equity awards plan.

The extending of these industry specific incentives nationwide will help to reduce tax policy differences among regions in China and promote a level playing field for enterprises. This will effectively and reasonably direct capitals to flow into innovative sectors and develop the innovative industry in China.

New guidance for research and development super deduction

According to the CIT Law, a company may claim an extra 50% tax deduction for qualified R&D expenses. In November 2015, several governmental authorities jointly released a circular, Caishui [2015] No.119 (Circular 119), to mainly expand the scope of activities and qualified R&D expenses eligible for the super deduction. Circular 119 also provides further clarification and refinement in relation to financial accounting and simplifying the tax administration. It resolves a large number of practical issues and will benefit various major industries with R&D activities.

Milestone reforms on tax administration

In late 2015, several authorities published a plan on deepening the reform of tax collection and administration system of state tax bureaus and local tax bureaus (the Reform Plan), unveiling the most important and comprehensive tax collection and administration reform in China since 1994. As the blueprint for the reform of China's tax administration, the Reform Plan proposed 31 initiatives with an aim to establish a modern tax collection and administration system by 2020. It is expected that the Reform Plan will be followed by a series of implementation regulations and have a profound influence on both tax authorities and taxpayers in the years to come.

One highlight of the Reform Plan is the new concept of tax risk-based administration on different categories of taxpayers (i.e. corporate taxpayers categorised by scale and industry and individual taxpayers categorised by revenue and assets), and centralising tax risk analysis and administration of 'large business enterprises' at the SAT or provincial level tax authorities. These new administration mechanisms will largely change the way tax authorities deploy their resources, tackle tax audits and communicate with taxpayers.

The improvement in tax services and the introduction of risk-based administration mode both rely on the support of information technologies (IT). The Reform Plan reiterates the 'Internet + Taxation' strategy set out in the SAT's 'Internet + Taxation Action Plan' back in September 2015, which requires tax authorities to tap into IT solutions to upgrade their tax administration systems. We observed that tax authorities all over China have already turned to IT solutions to facilitate their daily work, such as on-line tax filing and tax refund, e-invoices, webcast training, etc. In addition, traditional desktop tax audits have gradually been replaced by 'web crawler' technology and various other data collection and analysis systems. Taxpayers should consider upgrading their systems and changing their mindset of internal tax control to get adapted to the new 'Internet + Taxation' era.

Hong Kong

Tax and one-off relief measures are introduced to stimulate the economy.

The 2016/17 budget

The Financial Secretary delivered the 2016/17 budget on 24 February 2016. The tax and one-off relief measures proposed in the budget are summarised below.

Profits tax

The profits tax rates for companies and unincorporated businesses for year of assessment 2016/17 remain unchanged at 16.5% and 15% respectively.

The 2016/17 budget proposed the following two tax measures to promote Hong Kong as an intellectual property trading hub and develop the aviation business in Hong Kong respectively:

- Expanding the scope of tax deduction for capital expenditure incurred for the purchase of intellectual property rights to layout-design of integrated circuits, plant varieties and rights in performance.
- Examining the use of tax concession to boost aircraft leasing business and exploring business opportunities in aerospace financing (the details of the tax concession have yet to be announced).

Salaries tax

There is no change in the progressive tax rates and bands, and standard tax rate of 15%. The basic and married person's allowances, dependent parent/grandparent allowances and single parent allowance will be increased. The increased allowances are shown in the table below:

	2016/17	2015/16
Basic allowance	HKD132,000	HKD120,000
Married person's allowance	HKD264,000	HKD240,000
Dependent parent/grandparent allowance		
Aged 60 or above		
• Not residing with taxpayer	HKD46,000	HKD40,000
• Residing with taxpayer throughout the year	HKD92,000	HKD80,000
Aged 55 to 59		
• Not residing with taxpayer	HKD23,000	HKD20,000
• Residing with taxpayer throughout the year	HKD46,000	HKD40,000
Single parent allowance	HKD132,000	HKD120,000

In addition, the deduction ceiling for elderly residential care expenses will be increased from HKD80,000 (for year of assessment 2015/16) to HKD92,000 (for year of assessment 2016/17).

One-off relief measures

In addition to the above proposed tax measures, the Budget also includes the following major one-off relief measures:

- Waiving 75% of final profits tax for 2015/16 (subject to a HKD20,000 ceiling).
- Waiving 75% of final salaries tax and tax under personal assessment for 2015/16 (subject to a ceiling of HKD20,000).
- Waiving business registration fees for 2016/17.
- Waiving rates for the four quarters of 2016/17, subject to a ceiling of HKD1,000 per quarter for each rateable property.
- Providing one additional month of Comprehensive Social Security Assistance payment, Old Age Allowance, Old Age Living Allowance and Disability Allowance.

The above proposed tax measures will be implemented after the enactment of the relevant legislative amendments.

Key tax legislation enacted/ proposed

Key tax legislation enacted/proposed since the last issue of *Asia Pacific Tax Notes* is summarised below.

Profits tax exemption for offshore private equity funds

The Inland Revenue (Amendment) (No. 2) Ordinance 2015 was gazetted on 17 July 2015.

The ordinance extends the profits tax exemption for offshore funds to include transactions in certain non-Hong Kong private companies (i.e. those that do not carry on any business or hold any immovable property in Hong Kong, subject to a *de minimis* rule) such that non-resident private equity funds may also enjoy the tax exemption if certain prescribed conditions are met.

The exemption applies retrospectively in respect of tax chargeable for any year of assessment commencing on or after 1 April 2015. Further guidance on the implementation of the extended exemption will be issued by the Hong Kong tax authority.

Proposed tax incentives for corporate treasury centres

The Inland Revenue (Amendment) (No. 4) Bill 2015 was gazetted on 4 December 2015. The first part of the bill introduces incentives for multinational corporations to have their corporate treasury centres (CTCs) in Hong Kong. The key tax incentives and related measures are as follows:

- Providing a concessionary profits tax rate of 8.25% for the qualifying profits (i.e. profits derived from qualifying CTC transactions with or in relation to non-Hong Kong associated corporations) of a 'qualifying CTC' (other than a financial institution) if the prescribed conditions are met.
- Allowing tax deduction for a corporation carrying on an intra-group financing business in respect of interest expenses from money borrowed from a non-Hong Kong associated corporation in the ordinary course of that business, provided that certain conditions are satisfied.
- Deeming the interest income and profits from sale, disposal and redemption, etc. of certain debt instruments derived by a corporation (other than a financial institution) that arise through or from the carrying on of an intra-group financing business in Hong Kong as taxable trading receipts, even if the moneys in respect of which the interest is derived are made available outside Hong Kong or the transaction is effected outside Hong Kong.

The Inland Revenue (Amendment) (No. 4) Bill 2015 is currently scrutinised by the Legislative Council. If it is approved by the Legislative Council and enacted into law, the provisions related to the concessionary tax rate for CTCs and the new interest expense deduction rule for intra-group financing business will be applied retrospectively from 1 April 2016.

Proposed tax measures for regulatory capital securities

The second part of the Inland Revenue (Amendment) (No. 4) Bill 2015 addresses the uncertain tax positions in respect of income/expenses related to regulatory capital securities (RCSs) that could be issued by banks in strengthening their capital base within the Basel III capital adequacy requirements. Under the rules proposed by the bill, a RCS will be treated as a debt security for both profits tax and stamp duty proposes such that (i) a distribution (other than a repayment of the paid-up amount of the security) in respect of a RCS will be regarded as interest for taxation and deduction purposes and (ii) the sale or purchase, or other transfers of, a RCS will not be regarded as a sale or purchase or transfer of Hong Kong stock and therefore will not be subject to stamp duty.

The proposed amendments in relation to RCS are expected to be applicable to income/expenses related to RCSs when the Inland Revenue (Amendment) (No. 4) Bill 2015 is legislated.

The proposed open-ended fund company regime

The Securities and Futures (Amendment) Bill 2016 was gazetted on 15 January 2016 to introduce the legal, regulatory and tax framework for an open-ended fund company (OFC) regime in Hong Kong.

Currently, an open-ended investment fund can only be established in Hong Kong in the form of a unit trust. The bill will provide an alternative form of fund vehicle for open-ended funds domiciled in Hong Kong.

The principle of the proposed profits tax and stamp duty treatments of OFCs is to accord them with the same tax treatments as those for unit trusts. The main proposed tax treatments are:

- The existing profits tax exemption regime will be extended to public OFCs and private offshore OFCs, provided that the conditions currently specified in the tax law are satisfied.
- Stamp duty will not be payable on the initial allotment of OFC shares and cancellation of OFC shares upon redemption. However, transfer of shares in OFCs will be subject to stamp duty.
- Each sub-fund of an umbrella OFC would be regarded as a separate OFC for stamp duty purposes. As such, the conversion of interest from one sub-fund to another and the transfer of dutiable assets between different sub-funds will be subject to stamp duty.

The bill is currently scrutinised by the Legislative Council and has to be approved by the Council before it can be enacted into law.

Implementation of automatic exchange of information

Further to Hong Kong's commitment to implement the automatic exchange of information (AEoI) by September 2018, the Inland Revenue (Amendment) Bill 2016, which seeks to put in place a legal framework to implement AEoI in Hong Kong, was gazetted on 8 January 2016. The key proposals in the bill cover the following areas:

- scope of financial institutions (FIs), non-reporting FIs and excluded accounts;
- due diligence and reporting requirements for reporting FIs;
- scope of financial account information to be furnished by FIs;
- scope of reportable jurisdictions; and
- the enforcement provisions, including the powers of the Hong Kong tax authority and sanctions for non-compliance

The bill is currently under the scrutiny of the Legislative Council and has not yet been passed. In order to have the first AEoI by September 2018, the HKSAR Government aims to secure the passage of the bill by July 2016. The HKSAR Government also plans to identify at least one suitable jurisdiction as an AEoI partner of Hong Kong and conclude the negotiations with it by the end of 2016.

Tax treatments of corporate amalgamation

The new Companies Ordinance that became effective on 3 March 2014 introduced, among others, a court-free procedure for amalgamation of wholly owned group companies in Hong Kong.

As there is currently no specific provision in the Hong Kong tax law that addresses the various tax issues arising from corporate amalgamations and that considerable time will be required to introduce a statutory tax framework for corporate amalgamations in Hong Kong, the Hong Kong tax authority issued guidance on its current assessing practice on the profits tax treatment of various issues arising from court-free corporate amalgamations in December 2015 and published its advance rulings in three cases on corporate amalgamation.

The guidance indicates that the universal succession principle will generally be adopted such that the tax attributes (e.g. tax reducing value of depreciable assets) of the amalgamating company (the entity which ceased to exist) will be taken over by the amalgamated company (the surviving entity), with the exceptions of the trading stock of the amalgamating company and tax losses of the amalgamated/amalgamating company where special rules will apply. In particular, the guidance indicates that various conditions will need to be met before the tax losses sustained by the amalgamated/amalgamating company before the amalgamation can be utilised to offset against the profits derived by the amalgamated company after the amalgamation.

In cases where there is an indication that the amalgamation is driven by tax purposes, e.g. for obtaining a tax benefit of utilising a tax loss, the Hong Kong tax authority may invoke the anti-avoidance provisions in the tax law.

Pending the enactment of the specific tax legislation on corporate amalgamations in Hong Kong and further possible clarifications from the IRD, taxpayers contemplating a corporate amalgamation may consider applying for an advance ruling to obtain certainty, especially when the tax amount at stake is significant.

Developments of Hong Kong's tax treaty network

Treaties and protocols signed/ratified

Since the last issue of *Asia Pacific Tax Notes*, three new tax treaties were signed by Hong Kong with Romania, Russia and Latvia. Pending the completion of the ratification procedures, the three newly signed tax treaties have yet to come into force.

The Fourth Protocol to the comprehensive double tax arrangement between Hong Kong and Mainland China (China-HK CDTA) became effective in both China and Hong Kong on 29 December 2015. The protocol provides a tax exemption in China for gains derived by Hong Kong tax residents from disposal of shares of Chinese resident companies listed in recognised stock exchanges under certain conditions, reduces the withholding tax rate for rentals from aircraft leasing and ship chartering to 5%, introduces the 'main purpose test' as an additional anti-treaty abuse measure and expands the scope of information exchange to cover information related to certain non-income taxes in China.

The six tax information exchange agreements (TIEAs) signed with Sweden, Norway, Iceland, Greenland, Faroes and Denmark became effective in Hong Kong on 1 April 2016.

Notes were exchanged between Hong Kong and Japan expanding the scope of Japanese taxes covered for information exchange purpose under the HK-Japan tax treaty and the notes became effective in Hong Kong from 1 April 2016.

Implementation status of the treaty network

As of 15 April 2016, Hong Kong has signed tax treaties with 35 countries. The table on the next page summarises the status of all treaties signed by Hong Kong and the tax years from which these treaties became effective in Hong Kong and the corresponding contracting jurisdictions.

Jurisdiction	Date of signing	Date of entry into force	Effective from year of assessment (Hong Kong)	Effective from (the other contracting state)
Treaties signed before 2010				
1 Belgium[1]	December 2003	October 2004	2004/05	1 January 2004
2 Thailand[1]	September 2005	December 2005	2006/07	1 January 2006
3 The Mainland	August 2006	December 2006	2007/08	1 January 2007
4 Luxembourg	November 2007	January 2009	2008/09	1 January 2008
5 Vietnam	December 2008	August 2009	2010/11	1 January 2010
Treaties signed in 2010				
6 Brunei	March 2010	December 2010	2011/12	1 January 2011
7 The Netherlands	March 2010	October 2011	2012/13	1 January 2012
8 Indonesia	March 2010	March 2012	2013/14	1 January 2013
9 Hungary	May 2010	February 2011	2012/13	1 January 2012
10 Kuwait	May 2010	July 2013	2014/15	1 April 2014
11 Austria	May 2010	January 2011	2012/13	1 January 2012
12 UK	June 2010	December 2010	2011/12	1 or 6 April 2011
13 Ireland	June 2010	February 2011	2012/13	1 January 2012
14 Liechtenstein	August 2010	July 2011	2012/13	1 January 2012
15 France	October 2010	December 2011	2012/13	1 January 2012
16 Japan	November 2010	August 2011	2012/13	1 January 2012
17 New Zealand	December 2010	November 2011	2012/13	1 April 2012
Treaties signed in 2011				
18 Portugal	March 2011	June 2012	2013/14	1 January 2013
19 Spain	April 2011	April 2012	2013/14	1 April 2013
20 The Czech Republic	June 2011	January 2012	2013/14	1 January 2013
21 Switzerland	October 2011	October 2012	2013/14	1 January 2013
22 Malta	November 2011	July 2012	2013/14	1 January 2013
Treaties signed in 2012				
23 Jersey	February 2012	July 2013	2014/15	1 January 2014
24 Malaysia	April 2012	December 2012	2013/14	1 January 2013
25 Mexico	June 2012	March 2013	2014/15	1 January 2014
26 Canada	November 2012	October 2013	2014/15	1 January 2014
Treaties signed in 2013				
27 Italy	January 2013	August 2015	2016/17	1 January 2016
28 Guernsey	April 2013	December 2013	2014/15	1 January 2014
29 Qatar	May 2013	December 2013	2014/15	1 January 2014
Treaties signed in 2014				
30 Korea	July 2014	Pending	Pending	Pending
31 South Africa	October 2014	October 2015	2016/17	1 January 2016
32 United Arab Emirates	December 2014	December 2015	2016/17	1 January 2016
Treaties signed in 2015				
33 Romania	November 2015	Pending	Pending	Pending
Treaties signed in 2016				
34 Russia	January 2016	Pending	Pending	Pending
35 Latvia	April 2016	Pending	Pending	Pending

1 The Exchange of Information (EoI) article in these two treaties is of the 1995 version which is less liberal than the 2004 version. It is understood that the HKSAR Government is seeking to revise the EoI article of these two treaties to the 2004 version.

Status of tax treaty negotiations

The table below shows the latest status of treaty negotiations between Hong Kong and a list of countries with which negotiations have taken place in the past few years.

Countries with which negotiations have taken place in recent years	
Finland	Second round completed on 21 September 2011
Mauritius	First round completed on 16 January 2013
Bahrain	Second round completed on 12 December 2013
Israel	First round completed on 23 January 2014
Bangladesh	Second round completed on 1 August 2014
Germany	Second round completed on 6 March 2015
Saudi Arabia	Third round completed on 13 May 2015
Macedonia	First round completed on 12 June 2015
Pakistan	Third round completed on 15 October 2015
India	Third round completed on 23 December 2015
Cyprus	First round completed on 30 March 2016

Revised procedures for applying a Hong Kong tax resident certificate under the China-Hong Kong double tax arrangement

In August 2015, the State Administration of Taxation in China issued Public Notice [2015] No. 60 (PN 60) entitled 'Administrative Measures on Non-resident Taxpayers Claiming Tax Treaty Benefits'. PN 60, which became effective from 1 November 2015, introduced a new set of procedures for claiming benefits under the tax treaties of China. Please refer to the China article in this publication for a discussion of the new procedures introduced by PN 60 that apply to all treaty benefit applicants in general.

Two key changes brought about by PN 60 that affect Hong Kong tax residents in particular are:

- A Hong Kong tax resident certificate (HKTRC) is now required to be submitted to the Chinese tax authorities as a supporting document by all applicants from Hong Kong (including Hong Kong incorporated companies); and
- A referral letter from the Chinese tax authorities is no longer required to be presented to the Hong Kong tax authority for the purposes of applying a HKTRC.

Following the issuance of PN 60, the forms for applying a HKTRC under the China-HK CDTA were revised and have to be used from 1 November 2015. The new application forms no longer require an applicant to provide a referral letter issued by the Chinese tax authorities, instead the applicant's Tax Identification Number in China and the relevant in-charge local tax authorities in China are required.

Responses to the Base Erosion and Profit Shifting project

The Organisation for Economic Cooperation and Development (OECD) released the final reports on all of the 15 action items of the Base Erosion and Profit Shifting (BEPS) Action Plan on 5 October 2015.

The HKSAR Government has indicated that it will need to review the domestic tax regime, including the application of existing taxation principles, provision of tax concessions and enforcement of anti-avoidance mechanism, and assess to what extent Hong Kong could meet the emerging international expectations and standards. In particular, the following areas appear to be of priority for Hong Kong:

- Introducing transfer pricing documentation in Hong Kong and reviewing the need of exchanging country-by-country reports with other jurisdictions (i.e. BEPS Action 13).
- Taking into consideration the OECD's recommendations in the reports for BEPS Action 6 (i.e. preventing treaty abuse) and Action 7 (i.e. preventing the artificial avoidance of permanent establishment status) for revising the existing Hong Kong tax treaties and future treaty negotiations.
- Reviewing the need to participate in the multilateral instrument to be developed by the OECD for modifying bilateral tax treaties.
- Participating in multilateral agreement for AEoI.

India

The financial year (FY) 2015-16 has witnessed significant economic growth as a result of a slew of policy measures and regulatory reforms undertaken by the government during this period. Even with the slowdown in global economic growth and contraction of global trade, the gross domestic product increased to 7.6%. The government has undertaken various sectoral reforms to align with the focus on 'ease of doing business'. This was done with a view to ease operational difficulties and to substantially relax the compliance regime.

Further, the Union Budget 2016 bears the imprimatur of the Finance Minister (FM) and the current government's 'Transform India' focus. With its various visionary and development initiatives like 'Make in India', 'Skill India', 'Digital India' and 'Start-up India', the government is transforming India's image from a tax aggressive regime to a tax friendly regime.

Policy and regulatory measures

Foreign Investment

Liberalisation in various sectors

With an objective to liberalise the foreign investment regime and bolster the regulatory framework, reforms have been brought into various sectors like defence, construction, banking, e-commerce, broadcasting, insurance and pension, asset-reconstruction companies, marketing of food products, non-banking financial corporations, stock exchanges and listed central public sector enterprises (other than banks). Such reforms *inter alia* include easing of approval process, enhancement of foreign direct investment (FDI) caps, opening of new sectors for FDI, etc.

Other reforms

- FDI in limited liability partnerships (LLPs) is permitted under the automatic route. In addition, 100% FDI in LLPs is allowed for businesses operating in sectors where 100% FDI is allowed. Further, similar to companies, an LLP having foreign investment will be permitted to make a downstream investment in another company or LLP subject to certain conditions.
- The threshold limit for FDI approvals that may be considered by the Foreign Investment Promotion Board (FIPB) was raised to INR50,000 million. FDI proposals above this threshold will be placed for consideration of Cabinet Committee on Economic Affairs.
- Eligible FDI instruments will include hybrid instruments under certain conditions.
- Investment by companies/trusts/partnerships owned and controlled by NRIs on a non-repatriation basis will be treated as domestic investment.

External commercial borrowings

With a view to liberalise the external commercial borrowing (ECB) framework, the regulatory body has relaxed the guidelines and norms for long-term foreign currency borrowings, which *inter alia* include fewer restrictions on end uses, higher all-in-cost ceiling, etc. The extended term makes repayments more sustainable and minimises roll-over risks for the borrowers.

The overarching revised framework also includes a more liberal approach for rupee-denominated ECBs, where the currency risk is borne by the lender. The limit for small value ECBs with minimum average maturity of three years has been raised to USD50 million from the existing USD20 million.

Exemptions to private companies under Companies Act 2013

To relax the governing and compliance regimes, various exemptions and relaxations have been provided to private companies (other than subsidiaries of public companies) from certain provisions of the Companies Act 2013, including relaxations in related party transactions, loans to directors, disclosure requirements by directors for board meetings and other compliance requirements.

Secretarial standards

Secretarial standards were issued with a view to instil confidence in the minds of investors in order to attract foreign investments through capital infusion, funding new projects, modernisation and expansions. The secretarial standards, with sound and reliable corporate procedures, provide adequate guidance to corporations and professionals to ensure smooth compliance with the existing regulatory framework.

Direct tax

International tax updates

Tax rates

In line with his previous budget announcements, the FM proposed to reduce the corporate tax rate from 30% to 29% for domestic companies with total turnover/gross receipts not exceeding INR50 million. Therefore, the effective tax rate for these companies will be 31.96% (inclusive of surcharge and cess). Tax rates for other domestic companies and foreign companies remain unchanged.

An option is provided to newly set-up domestic manufacturing companies to tax their income at 28.84% (inclusive of surcharge and cess). However, benefits of various other incentives, e.g. tax holiday, additional depreciation, etc., will not be available. This is consistent with the proposal to reduce corporate tax rates and phase out tax exemptions/ incentives.

For individuals having taxable income exceeding INR10 million, surcharge has been increased from 12% to 15%, thereby leading to an effective tax rate of 35.54% (inclusive of surcharge and cess).

General anti-avoidance rules

In the previous budget, the implementation of general anti-avoidance rules (GAAR) was deferred to 1 April 2017. The FM has reiterated his commitment to implement GAAR from the said date.

Place of effective management

To determine the residency of foreign companies in India, the concept of place of effective management (PoEM) was introduced in the previous budget. However, it was deferred for one year and became effective from 1 April 2016.

Draft guidelines for determination of the PoEM, thus the residential status, of a company were introduced. The guidelines laid down the active vs. passive business test as the guiding principle/rule to determine the existence of PoEM. Factors which can be used to determine the PoEM of a company are passive income, total asset base, number of employees and payroll expenses inside and outside India.

Higher withholding tax rate no longer apply to non-residents in absence of permanent account number

Previously, non-residents were subject to higher withholding tax (WHT) on accounts without a Tax Identification Number (i.e. Permanent Account Number [PAN]) in India. It is proposed that a higher WHT rate will not apply to non-residents in absence of PAN if they furnish certain forms to the deductor (the forms are yet to be prescribed).

Equalisation levy

In light of the provisions on Action 1 of the Base Erosion and Profit Shifting (BEPS) Action Plan, a new levy, namely equalisation levy', at the rate of 6% is proposed. It applies to digital economy transactions with respect to the amount received by non-residents. In order to avoid double taxation, the income chargeable to the equalisation levy would be exempt from tax.

Digital economy transactions include online advertisement, any provision for digital advertising space or any other facility or service for the purpose of online advertisement and any other service as may be notified.

Indian patent box regime

Action 5 of the BEPS Action Plan recommended the nexus approach which prescribes that income arising from exploitation of intellectual property should be attributed and taxed in the jurisdiction where substantial research and development (R&D) activities are undertaken rather than the jurisdiction of legal ownership only.

To encourage indigenous R&D activities and to make India a global R&D hub, it is proposed that royalty income of a resident (patentee) in respect of a patent developed and registered in India will be taxable at 10% on the gross amount of royalty (plus surcharge and cess). Further, no minimum alternate tax (MAT) will be levied on such income.

Tax incentives for start-ups

To stimulate the start-up ecosystem in the country, a 100% profit-linked deduction is proposed for eligible start-ups, which engage in eligible businesses, subject to certain conditions and the applicability of MAT. The said deduction is available for three consecutive years in the five-year period beginning from the date of incorporation. Certain capital gains exemptions have also been provided under specified conditions. Eligible business includes the innovation, development, deployment or commercialisation of new products and processes or services that are driven by technology or intellectual property.

Other budget proposals

- Tax deduction for Special Economic Zone units will be available to activities commenced before 31 March 2020.
- Exemption is provided in respect of foreign company's income derived from storage and sale of crude oil stored as part of strategic reserves.
- Income derived from investments in securitisation trust will be taxable directly at the investor level.
- Capital gains arising from the appreciation of rupee-denominated bonds will be exempt from tax in order to provide relief to non-residents bearing the risk of currency fluctuation.

Clarification announcements to reduce tax litigation

Minimum alternate tax on foreign companies

The government clarified that MAT, also known as book profit tax, does not apply to a foreign companies starting from FY 2001-02, provided that the foreign company does not have a PE in India and the double tax treaty provisions apply.

Beneficial tax treatment for non-residents on sale of shares of a private company

Currently, long-term capital gains arising on transfer of securities, whether listed or unlisted, are taxed at the rate of 10%. Beneficial tax treatment for non-residents on sale of shares of private companies was a subject matter of litigation. With a view to clarify its position, the government stated that long term capital gains arising from a transfer of shares of a company in which the public is not substantially interested will be charged at the rate of 10%.

Benefit available to UK partnerships under India–UK double taxation avoidance agreement

Since UK partnerships are considered fiscally transparent entities under UK laws, there has been continuous litigation concerning the application of the India-UK tax treaty benefits for these partnerships. The government therefore clarified that UK partnerships will also be eligible for the tax treaty benefits under the India-UK double taxation avoidance agreement (DTAA).

Not treating consortium formed for engineering procurement and construction contracts as association of persons

To settle the ongoing litigation with respect to treatment of consortium formed for executing engineering procurement & construction/turnkey contract, it has been clarified that such consortium would not be treated as association of persons for tax purposes, subject to certain conditions. It, however, would not apply to consortiums having associated enterprises as members.

Social Security Agreements

India signed social security agreements (SSAs) with Austria, Canada and Australia. The Indian Provident Fund authorities notified these SSAs and they became effective from 1 July 2015, 1 August 2015 and 1 January 2016 respectively.

This is a welcome step as it will help in cost savings and protection of international assignees in respect of deputation agreement for employees, which in turn could lead to an increase in economic activity between the countries.

Tax treaty network

As discussed in the last issue of *Asia Pacific Tax Notes*, India and Mauritius are in the process of negotiating the DTAA. Concerns relating to treaty abuse, round-tripping of funds, double non-taxation and revenue loss are being discussed.

India is also amending its DTAA with various countries for sharing and exchange of information in order to curb tax evasion.

India currently has signed tax information exchange agreements (TIEAs) with over 100 countries. India signed a TIEA with Seychelles on 26 August 2015 and TIEA negotiations are in the pipeline with approximately 20 more countries.

Other developments during the year

- Various committee formations and representations have been witnessed to address the grievances of taxpayers and thereby creating a more tax friendly environment.
- In line with the government's initiative to provide a non-adversarial tax regime, dividend declared and paid by a foreign company outside India, in respect of shares which derive their value substantially from assets situated in India, would not be deemed to be income accruing or arising in India.
- With an intention to resolve complex cross-border tax issues and high value cases locked up in dispute, the government has concluded various mutual agreement procedures with various countries, including the US, the UK, Japan and China.
- India signed an inter-governmental agreement with the US to implement the Foreign Account Tax Compliance Act (FATCA) in India. It has also committed to the early adoption of the Organisation for Economic Cooperation and Development (OECD)'s common reporting standard (CRS). With the formal adoption of FATCA and CRS, India has demonstrated its commitment to the global tax transparency by curbing tax evasion.

Transfer pricing

Country-by-country reporting

The Union Budget 2016 proposed to introduce the three layered transfer pricing documentation requirement from FY 2016-17. Taxpayers will now be required to prepare a master file, local file and country-by-country (CbC) report, following the recommendations in the OECD's final report on Action 13 of the BEPS Action Plan.

Indian-headquartered multinational enterprises (MNEs) with global consolidated revenues exceeding Euro750 million i.e. INR53,950 million in the previous year are required to file CbC reports before the return filing due date.

For Indian subsidiaries having parent resident outside India, the CbC reports will ordinarily be filed by the parent entity in their home country or by a designated entity in its home country. The Indian tax authorities will access the CbC reports through the mutual exchange of information agreements with the home countries.

Indian subsidiaries of foreign MNEs are required to furnish CbC reports to the prescribed authority if the parent entity of the group is:

- a resident of a country which does not have an exchange of information agreement with India;
- a resident of a country that is not exchanging information with India even though there is an agreement; or
- intimate with the prescribed authority.

Prescribed authority may, for the purpose of verifying the CbC reports, request for further details which need to be furnished within 30 days. Such deadline can be further extended by 30 days.

Significant penalty provisions for non-compliance and furnishing inaccurate information have been proposed.

The requirement for master files, which can provide high-level overview of MNE's global transfer pricing practices, will also be introduced. However, the detailed rules regarding the documentation to be maintained as part of the master file are yet to be announced.

Revenue's right to appeal withdrawn

The Union Budget 2016 proposed to withdraw the revenue authorities' right to appeal against the directions of the dispute resolution panel with effect from 1 June 2016.

A new milestone – arm's length price computation

On 19 October 2015, the Central Board of Direct Taxes (CBDT) notified that the final rules to incorporate the 'range concept' and 'use of multiple year data' will be applicable to international transactions and specified domestic transactions undertaken on or after 1 April 2014 (i.e. from FY 2014-15 onwards).

Multiple year data concept

- Applicable if the method for determination of arm's length price (ALP) is transactional net margin method (TNMM), resale price method (RPM) or cost plus method (CPM).

- The data should relate to the current year for each comparable. However, in case the data is unavailable at the time of furnishing the return of income, data pertaining up to two preceding financial years may be used.
- Current year data, if available during assessment, shall be used.
- If a comparable is selected on the basis of preceding year data, but is not found to be comparable on the basis of qualitative or quantitative reasons for the current year, the comparable would need to be rejected from the set.
- When using the multiple year concept, data for each comparable would be the weighted average for three years.

Range concept

- Applicable if method for determination of ALP is TNMM, RPM, CPM or comparable uncontrolled price.
- Minimum of six comparable companies are needed.
- The arm's length range would be data points lying between the 35th and 65th percentile of the data set.
- If the transaction price falls within the percentile range, it will be deemed to be at arm's length. If not, the ALP will be the median of the data set.
- If the number of comparables is less than six, the arithmetic mean will continue to apply along with the benefit of tolerance range of +/- 3%.

Reference to transfer pricing officer during revenue audit

The CBDT has rolled out an updated guidance on procedures carried out by assessing officers (AOs) and transfer pricing officers (TPO). Previously, a simplistic approach based on the aggregate quantum of international transactions was adopted for selection of cases by the AOs for making a reference to TPOs. Since September 2014, the quantum based threshold is no longer used for case selection. Instead, risk based parameters will be used, which is in line with the international best practices.

Indirect tax

Goods and service tax

The goods and services tax (GST) was the most awaited tax reform in India and has been the top priority of the current Indian Government. In May 2015, the Constitutional Amendment Bill was passed in the Lower House of the Parliament and it is now pending with the Upper House of the Parliament.

Various steps have been taken by the government to create an ecosystem for GST implementation, including:

- Allocation of the GST network contract to a major IT company in India.
- Resolution of reservations raised by key manufacturing states, e.g. Tamil Nadu, Gujarat and Maharashtra.
- Report of Chief Economic Advisor Committee was issued, recommending a standard rate of 17% to 18% and a lower rate of 12% (revenue neutral rate between 15% and 15.5% is suggested).
- The Joint Committee issued reports on business processes for GST relating to GST registration, returns, payments and refunds. This provides an insight on the likely procedures/key provisions under GST.

In the Union Budget 2016, while the FM did not mention GST in his speech, the current government and its allies are likely to have a majority in the Upper House of the Parliament this year. It is expected that the Constitution Amendment Bill for GST could be passed this year.

Measures taken towards 'ease of doing business'

Rationalisation of Special Valuation Branch procedures

The Central Board of Excise and Customs issued two circulars in February 2016, amending the procedures of Special Valuation Branch (SVB) proceedings. In the past, long-drawn SVB proceedings and delays in getting refunds of extra duty deposits paid in course of the SVB proceedings had been a significant area of concern for importers. The changes are welcomed and would significantly reduce time and procedural compliances for SVB proceedings. These amendments are true steps towards 'ease of doing business', and it is hoped that the amended procedures would be implemented in true spirit.

Provisional sanction of refund to exporters within five working days

Circular for a speedy issuance of refund for accumulated Central Value Added Tax (CENVAT) credit to exporters was issued. This scheme applies to refund claims pending at the first adjudication level and filed on or before 31 March 2015. The exporter is required to submit a declaration from its Statutory Auditor in the prescribed form along with an undertaking.

Based on the documents filed, the adjudicating authority would issue 80% of the refund on a provisional basis. The refund claim would be then verified as per the applicable norms. If any part of the refund is found to be inadmissible, a show cause notice would be issued for denying the refund (and recovery of the refund already paid, if the final refund amount is lower than the amount provisionally sanctioned).

Key proposed amendments in the Union Budget 2016

The amendments proposed from an indirect tax perspective in the Union Budget were focussed on facilitating various government initiatives e.g. 'Make in India' and 'ease of doing business'. The key amendments proposed have been highlighted as follows:

Customs duty

- To promote 'Make in India', various amendments have been made to the rates of customs duty and central excise duty in specific sectors e.g. information technology hardware, capital goods, defense production, textiles, chemicals and petrochemicals, maintenance, repair and overhauling of aircraft and ships, etc.
- Customs duty exemption on certain finished products has been withdrawn, for example:
  - Import of chargers/adapters, wired headsets/speakers used for manufacturing of mobile phones. (however, import of inputs to manufacture these goods are exempt from customs duty); and
  - Import of populated printed circuit boards for manufacturing of mobile phones and personal computers.
- Warehousing period for Export Oriented Unit (EOU)/Electronic Hardware Technology Park (EHTP)/Software Technology Park (STP) units now applies up to the time of clearance (capital goods)/ consumption (all goods other than capital goods). Hence, there is no more requirement to periodically renew the warehousing period of goods.
- Facility for deferred payment of customs duty for a certain class of importers was proposed. The details and date are yet to be announced.
- Interest rate on delayed payment of customs duty has been reduced from 18% to 15%.

Central excise

- General rate of excise duty remains unchanged at 12.5%.
- Excise duty on ready-made garments with retail price of INR1,000 or more has been increased from 0% to 2% (without CENVAT credit).
- Tariff rate of ready-made garments has been increased from 30% to 60%, leading to an increase in the effective rates of excise duty and import duty (to the extent of counter vailing duty levied on the import of goods).
- Rate of interest on late payment of excise duty has been reduced from 18% to 15%.
- The number of returns to be filed by a medium and large manufacturer under central excise has been reduced from 27 returns in a year to only 13 returns in a year. Revision of returns has also been extended to central excise which was not allowed in the past.

Service tax

- General rate of service tax remains unchanged at 14%.
- Krishi kalyan cess (KKC) is proposed to be levied, with effect from 1 June 2016, at a rate of 0.5% on the value of taxable services. Therefore, the effective rate of service tax would increase to 15% (14% of service tax, 0.5% of Swachh Bharat Cess and 0.5% of KKC) from 14.5%. Credit of KKC paid on input services will be allowed to be used for payment of KKC only.
- Filing of annual return was introduced under service tax. The return must be filed by 30 November of the succeeding financial year. . The return format has not been published yet.
- Interest rates on delayed payment of service tax rationalised at 15%, except in cases when service tax is collected but not deposited (the interest rate will become 24%).

Other key Budget announcements

- Rules pertaining to the refund of CENVAT credit were amended to clarify that the application for refund of CENVAT credit can be made within 1 year from the date of receipt of foreign exchange (where services are completed before payment receipt) or 1 year from date of issuance of invoice (where consideration is received in advance). This is a welcomed amendment as it has clarified when refund claims should be filed.
- Infrastructure cess varying from 1% to 4%, which is not creditable, was proposed to be levied on the manufacture of motor vehicles.
- Rules pertaining to the reversal of proportionate CENVAT credit were simplified for the provision of taxable and exempt/non-taxable services. This has led to more clarity and would help to reduce litigation.

Other key developments

Continuous focus to promote exports

The new Foreign Trade Policy 2015-2020 (FTP) was unveiled on 1 April 2015. The new FTP seeks to provide a stable and sustainable policy environment for foreign trade in goods and services.

The policy introduced two new schemes, namely 'Merchandise Export from India Scheme' (MEIS) and 'Service Export from India Scheme' (SEIS). These schemes replace the existing schemes such as Focus Product Scheme, Market Linked Focus Product Scheme, etc.

- **MEIS**: This scheme rewards export of certain goods to certain markets. The benefit is provided in form of fully transferable duty credit scripts, payable as a percentage of the free on board value realised in free foreign exchange.
- **SEIS**: This scheme rewards export of notified services. The benefit is in form of full transferable duty credit scripts, payable as a percentage of net foreign exchange earned.

E-commerce

With the significant growth in e-commerce transactions in India, various states such as Uttarakhand, Uttar Pradesh, Gujarat etc. have levied or proposed to levy taxes on entry of goods, ordered through e-commerce platforms, into the states.

Furthermore, some states have introduced filing of monthly or quarterly statements for e-commerce companies which provide facility of e-portals and/or websites to dealers for sale of goods. Such measure was introduced mainly to ensure that there is no evasion of taxes by the vendors selling over the internet.

Indonesia

In the past 12 months, the government issued the following tax incentives to enhance the Indonesian economy:

- Temporary revamping of the fixed asset revaluation facility from 20 October 2015 to 31 December 2016 that provides lower tax rates on the excess of the fair market value over the tax book value of the revalued assets.
- Introduction of new tax and investment concessions called Special Economic Zone (SEZ) in order to develop several areas in Indonesia.
- Improvement in corporate income tax (CIT) reduction (previously known as tax holiday) and income tax allowance facilities, where the government has tried to streamline the process through a one door policy in order to speed up the application process.
- Lower interest withholding tax (WHT) on export proceeds placed in time deposit bank accounts in Indonesia.
- Introduction of several value added tax (VAT) facilities to boost the national transportation industry. This is in line with the President's maritime-axis doctrine.

Numerous regulatory changes have also been put in place as follows:

- Proposal to update the negative list of investment (NLI) which is intended to accelerate both foreign and domestic investments distributed across Indonesia and to develop the country's competitiveness in the international market. The new NLI also aims to protect national strategic business and Indonesian small and medium enterprises.
- Requirement to use Rupiah for general onshore transactions to maintain the stability of Rupiah.
- Tax payments must be made using e-billing system developed by Director General of Taxes (DGT) starting from 1 January 2016.
- Flexibility for investment proposals that satisfy certain criteria, whereby the relevant investment license can be issued within three hours.
- Domestic services subject to 2% WHT on the gross amount under Article 23 of the Income Tax Law is expanded to include 62 types of services.
- The debt to equity ratio of 4:1 will be applied starting from fiscal year 2016.
- The policies on safeguard import duty and anti-dumping import duty on imports of certain goods for securing national industry development will be continued.

Indonesia also continues the reform of the tax system. The proposed bill on tax law amendments in the national regulatory programmes will be discussed in the Parliament in the next five years. The government has also put the tax amnesty bill in the programme for discussion in 2016. Subject to the finalisation of the discussion, the tax amnesty law is expected to be applied in 2016 and is intended to cover all undeclared assets including offshore assets.

Regarding the international tax developments, Indonesia signed protocols to the double taxation agreements (DTAs) with China and the Netherlands. As a member of G20 and the Global Forum on Transparency and Exchange of Information for Tax Purposes, Indonesia has made some notable international tax commitments to show its effort in resolving issues such as base erosion and profit shifting. Indonesia is also updating domestic regulations on the exchange of information.

Tax concessions

Income tax concessions

CIT reduction

A CIT reduction facility has been provided to certain companies which:

- are in pioneer industries;
- were incorporated in Indonesia not earlier than 15 August 2011;
- have a legalised new capital investment plan of a minimum IDR1 trillion or IDR500 billion for telecommunication and information industries;
- commit to deposit a minimum of 10% of their planned investment value in a bank/banks located in Indonesia; and
- meet the debt to equity ratio of 4:1.

The facility covers reduction of 10% to 100% of the CIT due for five to fifteen years from the start of commercial production. A maximum reduction of 50% may be provided to telecommunication and information industries with a new capital investment plan of IDR500 billion to IDR1 trillion. The period may be extended to 20 years if it is deemed necessary for national interest.

Currently this facility is available for the following business sectors:

- upstream metal;
- oil refinery;
- base organic chemicals sourced from oil and gas;
- machinery;
- telecommunication and information;
- sea transportation;
- processing industry on agriculture, forestry, and fishery products;
- processing industry in SEZ; and
- economic infrastructure other than those under the cooperation between the government and business entities.

An application must be submitted to the Chairman of Investment Coordinating Board. A proposal for the Minister of Finance (MoF)'s approval will be made by the Board Chairman after carrying out research on the applicant. The proposal can be submitted to the MoF until 15 August 2018.

Income tax allowance

Income tax allowance is now applicable to 143 eligible types of investment (previously 129 types of investment either in designated business sectors and/or regions). Key new additions include the construction of smelters for mining products and the manufacturing of communication devices, motor vehicles and ships.

Income tax allowance now covers all forms of investment, including intangible assets. Thus, accelerated amortisation of intangible assets will be added to the tax facility. Other main features of the new regulation include the addition of options to extend the tax-loss carry forward facility and elimination of some requirements perceived as difficult for investors to demonstrate.

Zone-based concessions

Special economic zone

Currently, there are eight areas which have been designated as SEZ. CIT reduction facility may be granted for new taxpayers with new capital invested in the production chain of main activities in SEZ as described below:

<table>
<tr><th>Investment plan
(IDR in billion)</th><th>Reduction period
(in years)</th><th>CIT reduction</th></tr>
<tr><td>> IDR 1,000</td><td>10 – 25</td><td rowspan="2">20% – 100%</td></tr>
<tr><td>IDR 500 up to IDR 1,000</td><td>5 – 15</td></tr>
<tr><td>< IDR 500</td><td>5 – 15</td><td>MoF's discretion</td></tr>
</table>

Taxpayers being rejected for the CIT reduction facility and taxpayers carrying out other activities in SEZ may apply for similar income tax allowance as mentioned above.

Taxpayers in SEZ are also entitled to the following tax facilities:

- non-collection of VAT and luxury-goods sales tax (LST) on importation or domestic purchases of certain goods;
- non-collection of VAT and LST on the deliveries of certain goods between taxpayers in SEZ;
- non-collection of import income tax under Article 22 of Income Tax Law;
- postponement of import duty on capital goods and equipment, and goods and materials for processing; and
- exemption of excise on goods to be used to produce non-excisable goods.

On top of the tax facilities, the government also provides investment facilities in other aspects e.g. traffic of goods, manpower, immigration, land procurement and licensing.

Income tax

Debt to equity ratio

After having been stipulated in the Income Tax Law for over three decades, the government finally determines the debt to equity ratio for tax calculation purposes starting from fiscal year 2016. A single ratio of 4:1 is generally applicable, which means the amount of debt allowable in order to obtain full deductibility of the financing cost is limited to four times of the equity amount. Exemption applies to certain taxpayers.

Revaluation of fixed assets

The excess of the fair market value over the tax book value of the revalued assets is subject to final income tax at a rate of 10%. There is a special programme for revaluation of fixed assets for submissions made between the period from 20 October 2015 to 31 December 2016 which is subject to different rules. Below are the key features of this special programme:

- lower final income tax rates of 3%, 4% and 6% apply to the applications submitted in 2015, the first half of 2016, and the second half of 2016, respectively;
- revaluation can be conducted on some or all tangible fixed assets owned by a taxpayer; and
- the following are the additional eligible taxpayers:
  - corporate taxpayers who maintain English bookkeeping in USD currency;
  - corporate taxpayers who carried out their last asset revaluation within five years; and
  - individual taxpayers who maintain bookkeeping.

Lower withholding tax rate on time deposit interest for exporters

As part of the effort to maintain Rupiah's stability, the government has provided a lower final tax rate on time deposit (TD) interest derived from export proceeds placed in Indonesian banks starting from 28 December 2015. The lower rates are as follows:

- TD in USD:
  - 10% for TD with a one month period
  - 7.5% for TD with a three month period
  - 2.5% for TD with a six month period
  - 0% for TD with more than a six month period
- TD in IDR:
  - 7.5% for TD with a one month period
  - 5% for TD with a three month period
  - 0% for TD with a six month period or more

Changes in Article 22 of the Income Tax Law (Article 22)

Certain consumer goods subject to Article 22

Certain consumer goods, such as household appliances and electronic devices, are no longer considered as luxurious and therefore are now excluded from LST objects. With no more LST in the cost components, it is expected that the sale price of these consumer goods can be lowered and thus the goal of boosting purchasing power can be achieved.

According to Article 22, the import of these goods is now taxable at 10%. Previously, the rate was 2.5% (when using an importer identification number (IID) or 7.5% (when not using an IID). Such tax is imposed on the import value and will become the tax credit for importers in the calculation of their annual income tax due.

New taxable events under Article 22

The following transactions are now subject to tax under Article 22:

No.	Taxable event	Tax rate	Tax base
1	The export of coal, metal and non-metal minerals by exporters other than those engaged in a mining cooperation agreement or a contract of work with the government	1.5%	Export value
2	The purchase of coal, metal and non-metal minerals from companies or individuals holding a mining license	1.5%	Selling price
3	The sale of gold bars	0.45%	Selling price

International tax

China-Indonesia DTA

Indonesia and China signed the first protocol and a Memorandum of Understanding (MoU) to the 2001 tax treaty on 26 March 2015. Indonesia has subsequently ratified them on 12 January 2016. They will enter into force once the exchange of ratification instruments has been completed by both countries.

The protocol introduced provisions on the operation of aircrafts in international traffic, while the MoU outlines the financial institutions that are controlled by governments which are exempt from interest WHT.

Netherlands-Indonesia DTA

Indonesia and the Netherlands signed the first protocol to the 2002 tax treaty on 30 July 2015. It will become effective once the exchange of ratification instruments has been completed by both countries.

The key changes which make this tax treaty more attractive include: (i) the 5% WHT rate on dividends received by companies (other than partnerships) which directly hold at least 25% of the capital and (ii) the 5% WHT rate on interest for loans made for a period of more than two years or paid in connection with the sale on credit of any industrial, commercial or scientific equipment.

Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information

Following the launch of the Standard for the Automatic Exchange of Financial Account Information in Tax Matters, Indonesia has signed the associated Multilateral Competent Authority Agreement (MCAA) on 4 June 2015. It is expected to become effective from September 2018. The government will be required to annually exchange the financial account information obtained from financial institutions (FIs).

This commitment has been implemented in domestic regulations by authorising the DGT to automatically provide information to a country partner on detailed information on tax withholding/collection, or information related to the customers of FIs. Indonesia's Financial Services Authority has also issued a regulation to support this policy by regulating the administrative procedures for identification of foreign customers and FIs' reporting mechanism with the Common Reporting Standard issued by the OECD.

Value added tax

New strategic goods

The government has added raw skins and raw material of silver craft as strategic goods exempted from VAT. Anode slime is also considered as a strategic good and the VAT on deliveries of these goods for further process in producing gold bars is not collected.

Other values used as value added tax base

VAT is calculated by applying the VAT rate to a relevant tax base. In most cases, the tax base is the transaction value agreed between the parties concerned. For certain cases, other values must be used as the tax base. Below are the recent changes on the list of other values used as the tax base:

No.	Goods	VAT base
1	Tobacco products	Retail selling prices which is the same value used as excise imposition base on tobacco products
2	Fertilizers for agricultural sector that is partly subsidised by the government	100/110 of the government subsidy value and 100/110 of the highest retail price determined by the Minister of Agriculture

Value added tax facility to develop transportation industry

The government has changed the VAT treatment on imports and deliveries of certain means of transport and the related services from VAT-exempted to VAT not-collected so that importers or producers in these areas can now credit their input VAT. This will reduce the production costs and is expected to strengthen the national transportation industry. This is in line with the President's maritime-axis doctrine.

Regarding the sea transport companies that serve international routes, VAT is exempted on certain port services utilised by them. Furthermore, VAT is not collected on the deliveries of certain fuels for these international route ships.

Social security system

Pension benefit programme

In addition to the existing social security benefits (i.e. accident insurance, death insurance and old age savings), the Social Security Agency for worker's social security now also covers pension benefit for all citizens at the rates of 2% and 1% of regular salaries, borne by employers and employees respectively.

Japan

2016 Tax Reform Proposal

Continuing on from the 2015 Tax Reform, the main objective of the 2016 Tax Reform Proposal is to implement the second stage of *Abenomics*. Particularly, the proposal seeks to enhance economic recovery by enhancing competitiveness of Japanese companies and further reducing the corporate tax rate. At the same time, it seeks to improve the government deficit through a series of tax base-broadening measures.

The effective corporate tax rate of 32.11% is scheduled to be further reduced in two stages: first to 29.97% in 2016 and then to 29.74% in 2018. Efforts to increase the taxable base include increasing the size-based component of the enterprise tax, allowing only straight-line depreciation on selected assets and the scheduled expiration of tax incentives on investments in the assets for productivity improvement.

The 2015 revisions to net operating loss (NOL) carryforwards and the size-based component of the enterprise tax are further amended in 2016. The taxation of small and medium-sized enterprises (SMEs) and not-for-profit organisations remain as they were.

The regional revitalisation efforts introduced in 2015 to shift Japan's economic concentration away from Tokyo have also been expanded.

The consumption tax increase to 10% from 1 April 2017 remains on schedule. Concessions have been introduced with lower rates for selected goods to lift some of the burden for taxpayers in the lower income tax brackets. To cope with the multiple consumption tax rates, an invoicing method will be introduced on 1 April 2021, with transitional measures in place for an interim period of four years.

Based on the recommendations in the final report on Base Erosion and Profit Shifting (BEPS) Action 13 issued by the Organisation for Economic Co-operation and Development (OECD) in October 2015, new transfer pricing documentation and reporting obligations will be implemented.

Key corporate tax changes

Reduction of corporate tax rates

From fiscal year beginning between 1 April 2016 and 31 March 2017, the national corporate tax rate will be reduced from 23.9% to 23.4%. The rate will be further reduced to 23.2% from 1 April 2018.

The tax rate for the income portion of the size-based enterprise tax will be reduced from 4.8% to 3.6% for fiscal years beginning on or after 1 April 2016.

The effective tax rate for large corporations will be reduced from 32.11% to 29.97% (vs. 33.06% to 30.86% in the Tokyo Metropolitan area) from 1 April 2016. The tax rate will be further reduced to 29.74% (vs. 30.62% in the Tokyo Metropolitan area) for fiscal years beginning on or after 1 April 2018.

	Current			Proposed amendments					
	FY 2015			FY 2016			FY 2018		
	Statutory tax rate		Effective tax rate (Note 1)	Statutory tax rate		Effective tax rate (Note 1)	Statutory tax rate		Effective tax rate (Note 1)
	> JPY8 million	≦ JPY8 million (Note 3)		> JPY8 million	≦ JPY8 million (Note 3)		> JPY8 million	≦ JPY8 million	
Large corporation	23.9%		32.11% (33.06% for Tokyo)	23.4%		29.97% (30.86% for Tokyo) (Note 4)	23.2%		29.74% (30.62% for Tokyo) (Note 4)
SMEs (Note2)	23.9%	15%	34.33% (35.36% for Tokyo)	23.4%	15%	33.80% (34.81% for Tokyo) (Note 4)	23.2%	-	33.59% (34.59% for Tokyo) (Note 4)
Non-profitable organisations (NPOs)	19%, 22%	15%	-	19%, 22%	15%	-	19%, 22%	-	-

(Note 1) Effective tax rate = [Corporate tax rate × (1 + inhabitants tax rate) + enterprise tax rate] / (1 + enterprise tax rate)
(Note 2) SMEs are ordinary corporations with capital not exceeding JPY100 million and not wholly owned by a corporation with capital of JPY500 million or more.
(Note 3) Under the Special Taxation Measures Law, the tax rates apply to fiscal years beginning on or after 1 April 2015 and prior to 1 April 2017.
(Note 4) The effective tax rates of Tokyo/Metro for FY 2016 and beyond are determined on an estimated basis.

Expansion of the tax base

As the 2016 Tax Reform Proposal decreases the effective corporate tax rate by 2.37% beginning from 2018, the taxable base will be expanded, affecting low-profit or non-profitable corporations. Along with changes to the size-based enterprise tax, there are further amendments to the changes brought by the 2015 Tax Reform to the limitation on NOL carryforwards and the allowable depreciation methods. As a guide to further changes in future reforms, the taxation of SMEs will be examined from next year.

2015 Tax Reform	2016 Tax Reform	To be examined after 2017
Limitation on NOL carryforwards	Limitation on NOL carryforwards	Taxation of SMEs and NPOs
Reduction of dividend income exclusion	Review of depreciation method	
Review of local corporate taxation, focusing on enterprise tax	Review of local corporate taxation, focusing on enterprise tax	
Review of tax incentives, such as the research and development credit	Review of tax incentives, including productivity efficiency investments and wage growth measures	

Limitation on net operating loss deduction

The changes in the limitation on the NOL deduction will be implemented in three steps, i.e., the limitation ratio will be decreased by 5% annually, and ultimately reduced to 50% in FY2018. The expiry period of losses will be extended from nine to ten years for losses incurred on or after fiscal years beginning on or after 1 April 2018.

		FY 2015	FY 2016	FY 2017	FY 2018
Limitation ratio for large corporations	Current	65%		50%	
	Proposed	65%	60%	55%	50%
Carryover period for loss as well as assessment by tax authorities and request for downward adjustment by taxpayer (assuming proper financial documentation for the loss period is maintained)	Current	Nine years		Ten years	
	Proposed	Nine years			Ten years (Note 5)

(Note 5) Applicable to tax losses incurred in fiscal years beginning on or after 1 April 2018.

Depreciation method

For certain fixed assets acquired on or after 1 April 2016, only the straight line method is permitted. The declining balance accelerated depreciation method will no longer be allowed. As an exception, companies in the mining industry can choose the production basis or the straight line depreciation methods.

Asset type	Asset acquisition date			
	From 1 April 1998	From 1 April 2007	From 1 April 2012	From 1 April 2016
Buildings	Straight line method			
Structures and attachments to buildings	Straight line or declining balance method	Straight line or 250% declining balance method	Straight Line or 200% declining balance method	Straight line method
Equipment and machinery, vehicles, ships, aircraft				Straight line or 200% declining balance method
Assets used in mining				
• Buildings, attachments to buildings and equipment	Straight line, declining balance, or units-of-production method	Straight line, 250% declining balance, or units-of-production method	Straight line, 200% declining balance, or units-of-production method	Straight line or units-of-production method
• Assets other than the above				Straight line, 200% declining balance, or units-of-production methods
Intangible assets	Straight line method			
Foreign leases	Straight line method	Straight line over life of the lease		

Review of tax incentives

In line with the 2015 Tax Reform, a number of tax incentives were examined and allowed to expire as scheduled or were cancelled altogether.

Tax incentives which expired as scheduled (selected example):

Tax incentive	Applicable period
Tax incentives for investments on increasing productivity	• Assets acquired and placed in service by 31 March 2017

Tax incentives with scope and tax benefit changed as a result of prioritisation (selected examples):

Tax incentive	Proposed amendments
SME related special depreciation	• Changes were made to narrow the type of corporation qualifying for the incentive • Applicable period extended for two years
Investment incentive granted to machineries in the national strategic area or international strategic area	• Excess credit carry-over regime will be abolished • Applicable period extended for two years
Employment promotion credit	• Review of the requirements • Applicable period extended for two years
Special depreciation related to clean energy	• Review of the requirements • Applicable period extended for two years

Certain high priority incentives were enhanced (selected examples):

Tax incentive	Proposed amendments
Entertainment expenses related to meals and drinks and SMEs	• Applicable period extended for two years

Local tax revisions

It has been proposed to (1) increase the tax rates for the value added based and the capital based enterprise tax and (2) decrease the tax rates for the income based enterprise tax. To minimise the growing economic gap between urban and rural areas, the national local corporate tax rate will be increased while the local inhabitant tax rate will be reduced. The local corporate special tax is scheduled to be abolished from 1 April 2017. It will be replaced with an increase in the enterprise tax rate. A phase-in of tax increases will apply to companies with a value added base of less than JPY4 billion, the same as that proposed in the 2015 Tax Reform.

Changes to the enterprise tax and local corporate special tax

The tax rates for the income based enterprise tax will decrease to approximately 60% of the current rates (or approximately 50% of the rates prior to the 2015 Tax Reform). However, the tax rate for the capital based enterprise tax will increase by 1.67 times (or 2.5 times when compared to the rate before the 2015 Tax Reform). The changes are applicable from 1 April 2016.

The local corporate special tax is computed as a percentage of the amount of income based enterprise tax. The percentage used for computing the local corporate special tax will increase from 93.5% to 414.2% for fiscal years beginning after 1 April 2016. However, this tax will be abolished from 1 April 2017 and replaced by an increase in the enterprise tax rate (including a size-based tax regime).

Applicable tax rates will change as indicated in the following table (the table shows only the standard rate, whereas rates for Tokyo and other metropolitan areas are likely to be higher when announced):

		Before 2015 Tax Reform	Current (per 2015 Tax Reform)	Proposed under 2016 Tax Reform
Fiscal year beginning		1 April 2014	1 April 2015	1 April 2016
Value added base		0.48%	0.72%	1.2%
Capital base		0.2%	0.3%	0.5%
Income base (Note 6)	≦ JPY4 million	3.8% (2.2%)	3.1% (1.6%)	1.9% (0.3%)
	> JPY4 million, ≦ JPY8 million	5.5% (3.2%)	4.6% (2.3%)	2.7% (0.5%)
	< JPY8 million	7.2% (4.3%)	6.0% (3.1%)	3.6% (0.7%)
Local corporate special tax (computed as a percentage of the amount of income based enterprise tax at the rates shown) collected as national tax by filing corporate tax returns		67.4%	93.5%	414.2% (Note 7)

(Note 6) The rates shown for the income base is the total income based enterprise tax including (a) the portion collected as part of the national tax return and (b) the portion included as part of the enterprise tax return. The portion in parentheses of the income base column shows the amount collected as enterprise local tax (where the difference is collected as a national tax). The above rate changes for the income based enterprise tax may not affect taxpayers who have elected consolidated taxation since consolidation is not applicable to local tax purposes.

(Note 7) The local corporate special tax will be abolished from 1 April 2017 and replaced with an increase in the enterprise tax rate.

Phased increase in the corporate enterprise tax

The enterprise tax will be increased in phases from 1 April 2016 to 31 March 2019 for companies with a value added base of less than JPY4 billion. A portion of the tax increase as compared to the pre-tax reform year (i.e. 31 March 2016) will be available as a deduction.

	Amount to be deducted from enterprise tax in the event of an increased burden		
Value added base	Fiscal years from 1 April 2016	Fiscal years from 1 April 2017	Fiscal years from 1 April 2018
JPY3 billion or less	Tax increase (Note 8) x 75%	Tax increase x 50%	Tax increase x 25%
Over JPY3 billion and up to JPY4 billion	Fixed portion of tax increase (max 75%)	Fixed portion of tax increase (max 50%)	Fixed portion of tax increase (max 25%)

(Note 8) The tax increase is equal to that year's corporate enterprise tax less the corporate enterprise tax calculated by the pre-tax reform year (i.e. 31 March 2016) rates.

Changes to the local corporate tax and inhabitant tax

For fiscal years beginning after 1 April 2017, the local corporate tax rate will increase whereas the inhabitant tax rate will decrease as follows:

	Current		Expected from 2017	
	Standard rate	Maximum rate	Standard rate	Maximum rate
Inhabitant tax – Prefectural tax rate	3.2%	4.2%	1.0%	2.0%
Inhabitant tax – Municipal tax rate	9.7%	12.1%	6.0%	8.4%
Local corporate tax rate	4.4%		10.3%	

International Tax

Japan – Taiwan income tax agreement

The de facto diplomatic organisations representing Japan and Taiwan respectively completed negotiations on a comprehensive income tax agreement on 26 November 2015. Besides treating residents and domestic corporations in each jurisdiction the same, the following items were also agreed:

- Residency tie-breaker rules
- Income of Taiwan residents to be non-taxable for Japanese income and corporate tax purposes
  - Business profits will not be subject to Japanese income and corporate taxes if there is no permanent establishment (PE) in Japan
  - Withholding tax for dividends and interest will be decreased (dividends will be taxed at 10%, interest will be non-taxable)
  - Capital gains will be non-taxable
  - Income from provision of personal services will be non-taxable if certain conditions are met
- Arbitration measures to be put in place for transfer pricing
- Special measures on requests for downward transfer pricing adjustments in case of the confirmation of the tax authorities
- Information exchange measures

Transfer pricing documentation

The OECD released the final BEPS reporting package in October 2015, including the final report on Action 13 on transfer pricing and related documentation. Taking into consideration the compliance costs for taxpayers along with the need for increased transparency, the 2016 Tax Reform Proposal requires the following documentation in order to adhere with the BEPS project:

<table>
<tr><th>Document</th><th>Required information</th><th>Submission deadline</th><th>Applicability</th></tr>
<tr><td>Country-by-Country Report</td><td>Revenue, pre-tax income, taxes payable, etc. by country</td><td rowspan="2">Must be e-filed within one year of the last fiscal day of the ultimate parent</td><td rowspan="2">Fiscal year of the ultimate parent entity beginning on or after 1 April 2016</td></tr>
<tr><td>Master file</td><td>Group company structure, business outline, financial conditions, etc.</td></tr>
<tr><td>Local file</td><td>Transfer pricing documentation of the local entity</td><td>By the due date of filing the corporate tax return, to be retained for seven years</td><td>Fiscal years beginning on or after 1 April 2017</td></tr>
</table>

Controlled Foreign Corporation regime

As Japanese companies seek to expand their overseas activities and competitiveness, the 2015 Tax Reform reduced the tax rate that triggers the application of the anti-tax haven (or controlled foreign corporation (CFC)) rules and revised the conditions for the specified exceptions. The 2016 Tax Reform Proposal specifically addresses CFCs of insurance businesses operating in the UK Lloyd's market and foreign tax credit regime for CFCs.

Revised items		Content of revisions
Conditions for exception	Application of the substance and control test to CFC wholly owned by a Japanese insurance company operating in the UK Lloyd's market	If the CFC in its jurisdiction of the head office meets the substance and control test, then the substance and control test for the CFC regime is regarded as being met
	Application of the unrelated party transaction test to intra-transaction between CFCs wholly owned by a Japanese insurance company operating in the UK Lloyd's market	Intra-transaction between 100% owned CFCs is no longer treated as related party transaction
Foreign tax credit determination	Calculation of foreign corporate taxes paid for the foreign tax credit under CFC rules	• Foreign tax = Foreign Taxes paid by the CFC x ratio of taxable income
	Calculation of foreign taxes paid for the foreign tax credits under the anti-corporate tax inversion rules	• [Revision point] For the calculation of the ratio of income (includable income / total income of CFC), if dividend received by CFC from its subsidiary is not subject to the taxation on CFC level, such dividend income will be excluded from total income of CFC.

These revisions will apply to CFCs with fiscal years starting on or after 1 April 2016.

Rules on attribution of income

The 2014 Tax Reform introduced the international tax principle of attribution of income to replace the entire income principle, which applies to fiscal years beginning after 1 April 2016. The 2016 Tax Reform Proposal clarifies the following issues regarding the rules on attribution of income:

- For calculating the amount of foreign sourced income in determining the foreign tax credit for a Japan domestic corporation:
  - when the foreign sourced income that is not attributable to any foreign business is in a negative amount (i.e. a loss), the amount will be taken as zero.
  - when the foreign sourced income attributable to a foreign business is in a negative amount (i.e. a loss), the negative amount will be taken into consideration in calculating the foreign sourced income.
- When a PE (in Japan) of a foreign corporation is acquired by another foreign corporation (which previously had a PE in Japan with accrued tax loss) in a tax qualified transaction, the tax loss accrued by the former PE cannot be carried over to set off against future profits. On the other hand, the tax loss of the acquired PE can be carried over.

These changes apply to national and local taxes.

Consumption tax

Multiple rates

In response to the increase in the consumption tax rate to 10% from 1 April 2017, lower consumption tax rates on certain goods will be introduced. The 8% reduced consumption tax rate will still apply to food (excluding food purchased in restaurants) and newspaper subscriptions (when there are at least two issues per week).

Also, an invoice system will be introduced from 1 April 2021 to address the multiple tax rates. Several measures will be implemented during the four-year transitional period after the introduction of the invoice system.

Until the invoice system is introduced, the credit for consumption taxes paid will follow the current method for tracking, with the lower tax rates for applicable items to be indicated on the invoices. With the increased administration cost of tracking the different rates, a simplified method of determining the consumption taxes payable will be allowed.

After the new invoice system is introduced, qualified invoices issued by the registered businesses (Note 9) should be maintained for claiming credits of the consumption taxes paid.

(Note 9) Businesses (other than exempt entities) will need to file an application with their tax office to qualify for issuing qualified invoices indicating necessary details e.g. the business registration number and the applicable tax rate.

SME directed measures

For consumption taxpayers other than those applying the exemption or simplified taxation method, entering into the following high value transactions will prevent them from using the simplified method for tax credit and being exempt from consumption tax afterwards:

Transaction	Period in which the exemption and simplified taxation methods do not apply
Purchase or import of any inventory or adjusted real property whose value is JPY10 million or more	Three years starting from the commencement date of the taxable period in which the transaction took place
Building construction project with expenses totaling JPY10 million or more	Three years starting from the commencement date of the taxable period in which the construction completed

These changes will apply to high value asset transactions taking place on or after 1 April 2016 unless the contract for the asset concerned was finalised by 31 December 2015.

B2B digital services

With the 2015 Tax Reform, consumption tax is now imposed on digital services based on the location of the recipient of those services. From 1 January 2017, the sourcing of B2B digitally provided services will be based on the following rules:

Transaction	Sourcing
Where a Japanese domestic business with a foreign branch receives a digital service or product and that transaction is only for the purpose of the foreign business	Foreign (out of the scope of consumption tax)
Where a foreign business has a Japanese branch and the digital service or product is provided in Japan only and for the purpose of the domestic business	Domestic (consumption tax is applicable)

Korea

Tax law changes for 2016

Korea's National Assembly approved bills to amend eight series of tax laws including the Corporate Income Tax Law (CITL) and the Value Added Tax (VAT) Law on 2 December 2015. Subsequent to the amendment of the tax laws, the relevant presidential decrees were amended and proclaimed on 12 February 2016. The changes contained in the amended tax laws and regulations became effective from 1 January 2016 unless otherwise specified.

Corporate Income Tax Law

Deferred taxation for deemed dividends in a reverse merger between foreign subsidiaries

In a merger where the dissolved company's domestic shareholder receives shares in the surviving company as consideration for its ownership in the dissolved company and the value of the shares received exceeds the acquisition cost of the dissolved company's shares, the difference shall be deemed as dividends to the shareholder.

Currently, in a reverse merger where a domestic company is merged into its 100% domestic subsidiary, the CITL allows a tax deferral of the deemed dividends in the hands of the shareholder of the dissolved domestic company in order to help facilitate corporate restructuring. The amended regulations of the CITL allow the deferred taxation with respect to the deemed dividends of a domestic shareholder in a reverse merger between a foreign company and its 100% foreign subsidiary.

The following conditions must first be satisfied:

- the foreign companies in a reverse merger transaction are corporations established in the same foreign country which has a tax treaty with Korea, and
- the foreign country allows non-taxation or tax deferral on deemed dividends of a domestic shareholder.

New restriction in deductible company car expenses

The recently amended CITL includes a new deduction rule for expenses relating to company cars provided to officers or employees and a new requirement of having appropriate operation records or sufficient evidence to claim the deduction. The new deduction rule will apply to depreciation expenses, rental or lease fees, fuel expenses, property tax, car insurance, repair expenses, interest expense on financial leases and other expenses incurred for the acquisition and maintenance of company cars from the fiscal year starting 1 January 2016 (1 January 2017 for sole proprietors subject to double-entry book keeping).

In the absence of the operation records, if the required insurance is taken out, a taxpayer will be allowed to deduct the actual company car related expenses or KRW10 million, whichever is the lesser. The deduction of deprecation on company cars (or equivalent depreciation on leased company cars) is limited to the depreciation expense (or equivalent depreciation expense) multiplied by a business usage ratio, and must not exceed KRW8 million a year. Unless a taxpayer maintains the required operation records, the business usage ratio will be 100% if the company car related expenses are KRW10 million or less. If the company car related expenses exceed KRW10 million, the ratio will be computed at KRW10 million divided by the company car related expenses.

The depreciation expense over the limit can be carried forward to subsequent years and deducted when the depreciation expense multiplied by the business usage ratio is less than KRW8 million (any remaining amount will be entirely deducted in the year that represents the tenth anniversary of the disposal or expiration date). A taxpayer will be required to depreciate company cars purchased from the fiscal year starting 1 January 2016 over five years under a straight line method. On the other hand, the company car related expenses incurred for personal purpose rather than business purpose will be treated as income (e.g. dividend, bonus) to the users of the company cars.

Extended due date for request for return filing extension

Prior to the amendment, if a company expects that the external audit on it will not be completed in time, triggering a delay in book closing, it can request for an extension of the corporate income tax return filing deadline by one month with the payment of interest at 2.5% per annum. Under the amended law, the request must be filed three days (rather than two weeks) before the return filing due date (i.e. three months from the fiscal year-end date).

Special Tax Treatment Control Law

New tax credit to support youth job creation

The Special Tax Treatment Control Law (STTCL) has been amended to allow a company to claim a tax credit worth KRW5 million (KRW2 million for a large company) for the increased number of regular youth employees (aged between 15 and 29 as at the end of each month). However, the increased number of regular youth employees eligible for the tax credit is limited to the lesser of the increased number of regular employees or the increased number of full-time employees. If there is a decrease in the number of regular youth employees, regular employees or full time employees in the two years after receiving the tax credit, the tax credit will be recaptured and tax will be assessed at KRW5 million multiplied by the decreased number of regular youth employees, regular employees or full-time employees, whichever is the largest.

Special Tax Treatment Control Law

New tax credit to support youth job creation

New tax benefits for individual saving accounts

R&D tax credit for core technologies and strategic growth industries

All corporations except those engaged in certain consumption-oriented service businesses (e.g. amusement/ drinking businesses as well as hotels and inns, excluding tourist accommodation business) will be eligible for the new tax credit if the specified conditions are met. The new tax credit will be available from the fiscal year that includes 31 December 2015.

New tax benefits for individual savings accounts

The recently amended STTCL introduces a new investment arrangement (i.e. individual savings account (ISA)) qualifying for a favourable tax treatment. Residents having wage and salary income or business income as well as agriculture or fishing farmers are eligible for making use of the account for their investment. Residents subject to aggregate tax on income from financial assets will not be eligible for the favourable tax treatment. The account will be exempt from income tax on the investment returns up to KRW2 million. The amount in excess of KRW2 million will be separately taxed at a 9% rate. For a wage and salary income earner whose annual compensation totals KRW50 million or less or global income is KRW35 million or less, the exemption threshold will be KRW2.5 million.

To qualify for the tax benefits, deposits must be held in an ISA for at least five years. ISAs can include savings deposits, instalment savings, deposit money, funds, derivative-linked securities (e.g. equity-linked securities), securities and bonds with repurchase agreements and shares in real estate investment trusts (REIT) as defined in the REIT Act. No more than the annual limit of KRW20 million can be deposited into the account. Those who wish to enjoy the tax benefits must subscribe to an ISA no later than 31 December 2018.

Additional core technologies and strategic growth industries eligible for research and development tax credit

Currently, companies can claim a tax credit for qualifying research and development (R&D) expenditure in relation to core technologies that are authorised by government ministries and pre-designated strategic growth industries. Prior to the amendment, a list of 116 categories of technologies were eligible for the R&D tax credit. Intelligent Internet of Things (IoT), wearable smart apparatus, flexible displays, smart healthcare, hyper plastic materials, smart vehicles, unmanned aerial vehicles, high-tech material processing system and smart-farm technology, etc. are now added to the list of eligible technologies. However, three categories of technologies including alternative crude oil purifying fuel system are no longer eligible for the tax credit.

Individual Income Tax Law

New withholding obligation of domestic companies with foreign secondees

Currently, a foreign secondee working in Korea who receives employment income from a foreign corporation outside Korea is not subject to payroll withholding tax on Korean sourced employment income. Rather the individual can voluntarily join a taxpayers' association to pay monthly payroll withholding tax via the association to enjoy a 10% tax credit. Effective 1 July 2016, the amended Individual Income Tax Law (IITL) requires a domestic company with foreign secondees to withhold payroll income tax at 17% when the domestic company pays service fees to the foreign corporation which has dispatched the foreign secondees.

The new withholding obligation applies to a domestic company if all of the following conditions are met:

- the total amount of the service fees paid to a foreign corporation (or multiple foreign corporations involved) in return for services provided by it via foreign secondees exceeds KRW3 billion per year;
- the sales revenue of the domestic company making such service fee payment exceeds KRW150 billion or the total amount of assets exceeds KRW500 billion during the preceding fiscal year; and
- the domestic company engages in air transportation, construction or professional, scientific and technical service business.

Affected foreign secondees will be the employees of a foreign corporation without a Korean permanent establishment (PE) who provide services to a domestic company. For the withholding tax withheld and paid by the domestic company, the foreign company dispatching the foreign secondees will be allowed to claim a refund of any overpaid withholding tax via a year-end settlement of the payroll withholding tax by submitting a copy of the contract executed between the domestic company and the foreign secondees and documents to support the wages or salaries paid by the foreign company to the secondees. These procedures may be undertaken by the domestic company on behalf of the foreign company.

Clarification on the computation of the 183-day threshold for residency test

Under the 183-day rule for testing the residency of those who have Korean nationality and reside in foreign countries, an individual is considered a Korean resident if the individual is present in Korea for at least 183 days during the current year or during two consecutive years including the current year. For the purpose of counting the 183-day threshold, any day of presence in a foreign country for temporary purposes such as travel or medical treatment shall be counted. However, the amended law clearly states that any day of presence in Korea for temporary purposes of travel or medical treatment shall not be counted for the 183-day threshold if it is supported by adequate evidences including admission tickets, medical reports and other underlying documents supporting presence in Korea.

New taxation for ministers of religion

From January 2018, ministers or practitioners of religious services will be subject to tax on income earned from religious organisations for their services. However, tuition fees paid for trainings related to religious activities by ministers or practitioners, meal expenses (up to KRW100,000 a month), payments in the nature of reimbursement of expenses such as travel, night duty, religious costume, etc. and the provision of housing owned or rented by religious organisation free of charge or at lower price will not be taxed.

Value Added Tax Law

Application of zero-rated VAT for professional services and business support services on a reciprocal basis

According to the VAT Law, zero-rated VAT is available on the supply of certain services by a taxpayer if they are provided to a Korean non-resident or foreign enterprise without a PE in Korea and the taxpayer earns the consideration for the supply in foreign currency.

From 1 July 2016, in case of professional services and business support services supplied to a Korean non-resident or foreign enterprise without a PE in Korea, the zero-rated VAT will apply only if the foreign country where the non-resident or foreign enterprise is established gives similar VAT treatment (including VAT exemption) on the supply of similar services by a Korean resident (i.e. zero-rated VAT on a reciprocal basis). Professional services include legal services (those rendered by lawyers, patent attorneys and judicial scriveners), accounting and tax services, advertising services, market survey and management consulting services. Business support services include human resources outsourcing, activities of employment placement agencies, office support services, etc.

The VAT Law change is to give equal VAT treatment for professional services and business support services received by a domestic resident or company and a non-resident or foreign company in light of the fact that those services are actually consumed in Korea.

Deferral of import VAT and custom duties until VAT filing

From 1 July 2016, the VAT law will offer the VAT and duties deferment scheme that would permit an importer to defer the import VAT and custom duties on imported raw materials and goods directly used for the importer's business. To enjoy the deferment, certain conditions must be met, including being a small and medium size manufacturing company, a minimum requirement for exports (i.e. 30% of the total value of annual supplies) and a three-year consecutive operation.

Importers will be required to file an application with customs offices to enjoy the scheme. The application should cover the import VAT and duties due on imported goods for one year.

Law for Coordination of International Tax Affairs

New reporting requirement to examine cross-border transactions of multinationals

The recently amended Law for Coordination of International Tax Affairs (LCITA) includes a new requirement for multinationals in Korea to submit information on their cross-border transactions. The requirement is applicable to both Korean companies and foreign companies having a PE in Korea if their sales revenue exceeds KRW100 billion and their international related party transactions exceed KRW50 billion in a fiscal year.

Under the requirement, companies must submit their master file and local file of cross-border related party transactions together with the documentation on their international transactions currently required under the LCITA. The failure to comply with the reporting requirement will be subject to a penalty of KRW30 million.

The master file should provide information relating to group organisation, business, intangible assets, financial transactions as well as financial and tax information. Local file should include information relating to each entity organisation, business, transfer pricing information on significant related party transactions and financial status. The master file should be submitted by the ultimate parent company. In the event that a foreign parent company is not present in Korea, a Korean subsidiary or a PE of the foreign parent in Korea must obtain the required file from the foreign parent and submit it. The local file should be submitted by a Korean company or a foreign company having a PE in Korea that meets the specified thresholds of gross sales and related party transactions. When submitting the local file, it is required to indicate the party that submits the master file.

The required files must be submitted with the corporation tax return (i.e. within three months after the end of the taxpayer's fiscal year). However, taxpayers may request an extension on the filing deadline of up to one year if there is any justifiable reason to be specified by the Presidential Decree. In addition, the required files may be submitted electronically. Local files must be prepared in Korean, while the master file may be prepared in Korean or English (with Korean translation submitted within one month of submitting the English file).

Adoption of automatic exchange of information and Common Reporting Standard

The amended LCITA provides a legal framework for Korea to implement the Common Reporting Standard (CRS) on 1 January 2016 and participate in the automatic exchange of information in 2017 with other participating jurisdictions. Based on the amended law, Korea's Financial Services Commission issued a final guidance on the Automatic Exchange of Financial Information in December 2015. The guidance requires financial institutions to determine whether they are reportable financial institutions under the CRS.

Reportable financial institutions will have the following obligations:

- obtain a list of reportable accountholders through the due diligence process specified in the CRS for both new and pre-existing accounts, and
- report the list of reportable accountholders and their financial account information to the local tax administration.

In addition, reportable financial institutions must collect self-certification forms from the accountholders which typically include the name, address, country of tax residence, nationality, tax identification number, telephone number, etc. during their on-boarding process for new account holders.

New legislation to facilitate business restructuring

Korea has enacted a new legislation to facilitate business restructuring. It is expected that the legislation will strengthen the industrial competitiveness and revitalise the economy. Dubbed the 'One-shot Act', this special legislation will be implemented temporarily for a period of three years when it is enforced as scheduled in August 2016.

The new legislation will affect companies engaged in businesses suffering from excess supplies which raise the need for an improvement in productivity and financial soundness. Affected companies will be forced to set specific goals of improvement and implement restructuring measures. Regulatory barriers will be suspended and special treatment will be provided to help companies achieve the established goals for improvement.

The new legislation mainly addresses special treatment or deregulation in three categories of law including the Commercial Act, the Anti-Monopoly and Fair Trade Act and the tax laws. Special treatments under the Commercial Act will ease the existing restrictions or requirements for small-scale spin-off, small-scale mergers and acquisitions and simplified mergers to expedite the restructuring. Special treatments under the Anti-Monopoly and Fair Trade Act will focus on suspending the existing restrictions for a specified period for companies authorised to implement restructuring measures. In addition, tax incentives for a specified period are available through various amendments of the tax laws including the Special Tax Treatment Control Law and the Local Tax Special Treatment Control Law to remove tax barriers which might likely deter business restructuring.

Update on the Foreign Exchange Transaction Law

The amended regulations of the Foreign Exchange Transactions Law, which became effective 1 July 2015, include two significant changes concerning the payment gateway and the bank levy for foreign exchange quality.

A payment gateway which is a provider of electronic payment and settlement agency services as authorised under the Electronic Financial Transaction Act is allowed to provide the electronic payment and settlement agency services for cross-border trade of goods and services. It is expected to facilitate domestic customers' direct online purchases from foreign sellers and online sales by domestic companies to offshore customers and should result in reducing payment service fees paid to global credit card companies.

The bank levy for foreign exchange quality which is currently imposed on banks must also be imposed on non-bank financial institutions such as securities companies, insurance companies and specialised credit finance companies. However, the non-bank financial companies would not be subject to such levies if the average of the monthly ending balance of foreign-currency borrowings incurred from 1 July 2015 and thereafter is less than USD10 million. Regardless of a maturity term, a fixed rate (i.e. 10 basis points) of the levy shall be applicable to the outstanding foreign-currency borrowings for which the remaining maturity period is one year or shorter.

Laos

The most significant development in taxation law and regulation from 1 March 2015 to 31 January 2016 in Laos, officially the Lao People's Democratic Republic, is the enactment of the new Value Added Tax (VAT) Law.

The new Value Added Tax Law

VAT Law No. 52/NA replaces VAT Law No. 04/NA dated 26 December 2006. The new law is effective from 3 July 2015. On the whole, the principles and rules under the old VAT Law remain although some provisions for certain articles have been revised.

The list of VAT exempt goods and services were amended to include the following items:

- sale of live animals, dead animals or unprocessed animal meat;
- animal feeds and raw materials for production of animal feeds;
- importation and sale of equipment and machinery for agriculture;
- importation of modern teaching equipment;
- importation and sale of human blood;
- raw materials for production of fertilisers;
- veterinary services; and
- sale of goods on board an aircraft.

VAT exempt goods and services were amended to include these items:

Sale of live animals or dead animals or unprocessed animal meat

Animal feeds and raw material for production of animal feeds

Importation and sale of equipment and machinery for agriculture

Importation of modern teaching equipment

Importation and sale of human blood

Raw materials for production of fertiliser

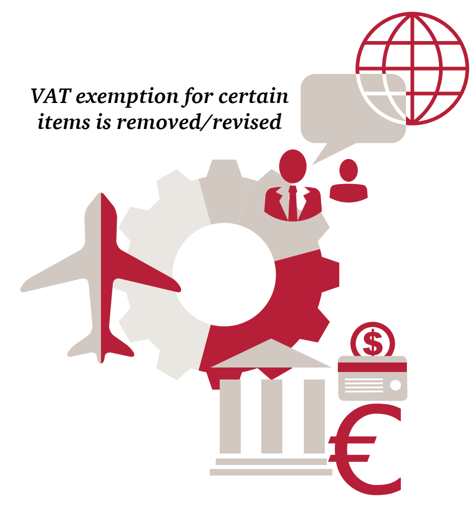
Veterinary services

Sale of goods on board an aircraft

VAT exemption for the following items has either been removed or revised:

- commercial banks and financial institutions;
- goods supplied to diplomats, foreign embassies and international organisations; and
- goods for air transportation.

Under the old VAT Law, banking and financial activities were eligible for VAT exemption. However, there were different interpretations between taxpayers and the tax authorities as to what constitutes a financial institution, particularly for financial leasing companies. Some financial leasing companies claimed that they were exempt from VAT as financial institutions and had no obligation to collect VAT from their customers in hire purchase transactions. However, the tax authorities took the view that only the portion of interest from such transactions was exempt from VAT and the sale price and other related fees were not exempt. As such, financial leasing companies should collect VAT from their customers. The tax authorities insisted that financial leasing companies must follow the Prime Minister's decree on the implementation of the VAT Law and the instruction on implementation of the VAT Law that stated clearly that only the portion of interest was exempt.



To avoid these different interpretations, commercial banks and financial institutions are no longer listed as VAT exempt items and only interest earned from deposits and interest generated from lending by commercial banks are exempt under the new VAT Law.

Under the old VAT Law, goods imported for sale to diplomats, embassies and international organisations were exempt from VAT with authorisation from the Ministry of Foreign Affairs. The new VAT Law limits the scope of exemption to only goods for official use by foreign embassies and international organisations.

Under the old law, aircraft, petrol, oil, goods and equipment for air transportation were exempt from VAT. Under the new law, goods and equipment for air transportation have been removed from the exemption list whereas aircraft, petrol and oil for air transportation remain to be VAT exempt. In addition, sale of goods on board an aircraft is added as a VAT exempt item.

Under the new law, input VAT from purchases of petrol, electricity and fixed assets is only partially deductible. It is still unclear how much of the input VAT on such purchases is deductible. Normally, after the enactment of a new law, the Prime Minister will issue an implementing decree to give more instructions and guidelines on the implementation of the law. We believe that the decree to be issued will give more details about the deductibility of input VAT for these items.

Under the new law, the 6-month time limit for carrying forward input VAT for future offsetting against output VAT derived from purchase of goods and services can be extended with an approval from the tax authorities. Input VAT from fixed assets can be carried forward until it is fully consumed.

The tax official may also reassess VAT within three years from the purchase date of goods and services in determining if VAT is correct and based on accurate evidences.

Other provisions of the old VAT Law have also been revised to remove ambiguity, vagueness and loopholes and make the provisions clearer and easier to interpret and understand.

The new VAT Law also refers to other specific regulations that have not yet been issued. So, it is very difficult to know the complete scope of changes under the new law at the moment.

Foreign contractor withholding tax - profit tax rates and input value added tax credit

Withholding tax (WHT) on payments to foreign contractors applies when a Lao business operator contracts with an overseas party that is not registered and does not maintain a presence in Laos.

This WHT, which is called the foreign contractor withholding tax (FCWT), comprises both profit tax (PT) and VAT elements if the business activity is undertaken offshore. However, in practice, the Government of Lao requires that PT and VAT be withheld before payments are made to foreign contractors even for onshore business activity.

In the case of goods, the WHT represents the PT element only since VAT should be paid before the goods enter Laos. The FCWT is the final tax on the overseas party.

PT is calculated based on a deemed percentage of turnover. The deemed rate is determined according to the nature of the contract or activity. The rates for different types of business activity are as follows:

Type of business activity	Deemed profit margin (% of business revenue)	Deemed PT rate
Commerce	5%	1.2%
Production	8%	1.92%
Transportation and construction	10%	2.4%
Services	20%	4.8%

The WHT (i.e. PT and VAT) is computed based on the value of the contract. The Lao business operator has the obligation to withhold PT from purchases of goods and services from an overseas provider and has an additional obligation to withhold 10% VAT from purchases of service from an overseas provider. According to the Lao Tax Department, the VAT withheld cannot be claimed as input VAT credit against the output VAT liability of the Lao business operator.

Macau

Recent major tax developments in Macau

Tax incentives for financial year 2016

The Legislative Assembly approved several tax incentives proposed by the Chief Executive of the Macau SAR in his Budget for the financial year 2016 on 17 December 2015. The key measures include the following:

1. The tax free income threshold for Macau complementary (corporate) tax will continue to be increased from MOP32,000 to MOP600,000 for income derived in tax year 2015. Taxable profits over MOP600,000 are taxed at 12%.
2. The tax free income threshold for Macau professional tax will continue to be increased from MOP95,000 to MOP144,000 for income derived in tax year 2016. Taxable income between MOP144,000 and MOP424,000 is taxed at progressive rates scale ranging from 7% to 11%. Taxable income above MOP424,000 is taxed at 12%.
3. There is a 30% reduction in the Macau professional tax liabilities for income derived in tax year 2016. Together with the standard 25% deduction on the taxable income granted under the Macau Professional Tax Law, the effective tax rate for Macau professional tax is below 6.3%.
4. There is a refund of 60% of the Macau professional tax paid by Macau resident identity card holders for the tax year 2014, subject to a cap of MOP12,000.
5. The standard MOP3,500 reduction in the Macau property tax liabilities will continue to be available for assessments in tax year 2016 for both self-use and rental properties.
6. Macau tourism tax will continue to be exempt for restaurants in tax year 2016.
7. Macau stamp duty for insurance policies written or renewed in tax year 2016 and for banking transactions in tax year 2016 will continue to be exempt.
8. Macau stamp duty on admission tickets for performances, exhibitions, and entertainment programmes will continue to be exempt in tax year 2016.
9. Macau industrial tax for tax year 2016 will continue to be fully exempt.
10. An adult, who holds a Macau permanent resident identity card and who does not own any properties other than one car-parking space, is eligible to enjoy an exemption on Macau stamp duty levied on the purchase of a residential property for self-use purposes for the first MOP3,000,000 of the transfer consideration. The transfer consideration in excess of MOP3,000,000 will be subject to Macau stamp duty.

    For husband and wife acquiring a residential property in joint names, if either one of them does not own any properties other than one car-parking space, even if one of them does not hold a Macau permanent resident identity card, the acquisition will still be eligible for exemption on Macau stamp duty for the first MOP3,000,000 of the transfer consideration.

    For other joint name acquisition with acquirers not being husband and wife, only the acquirer(s) who meet the criteria of being an adult, holder of Macau permanent resident identity card and not owner of any properties other than one car-parking space will be eligible to enjoy the exemption on Macau stamp duty on the first MOP3,000,000 of the transfer consideration.

    The exemption for each individual qualified acquirer will be granted on a pro-rata basis. The Macau stamp duty exemption has a three-year 'lock-in' period, such that unless the residential property so purchased is transferred as part of a deceased estate, the purchaser will have to pay the Macau stamp duty that was originally exempt on the purchased property if such residential property is sold within three years after the grant date of the Macau stamp duty exemption.
11. Licence fee for advertisements posted or placed in public areas, and the stamp duty thereon, will continue to be exempt in tax year 2016.
12. Land rentals with an amount below MOP100 will not be collected by the Macau Finance Bureau in tax year 2016. However, any such amount already collected will not be refunded.

The overall aim of the above tax incentives is to lessen the burden of small and medium-sized enterprises, and to improve the livelihood of the general public in Macau.

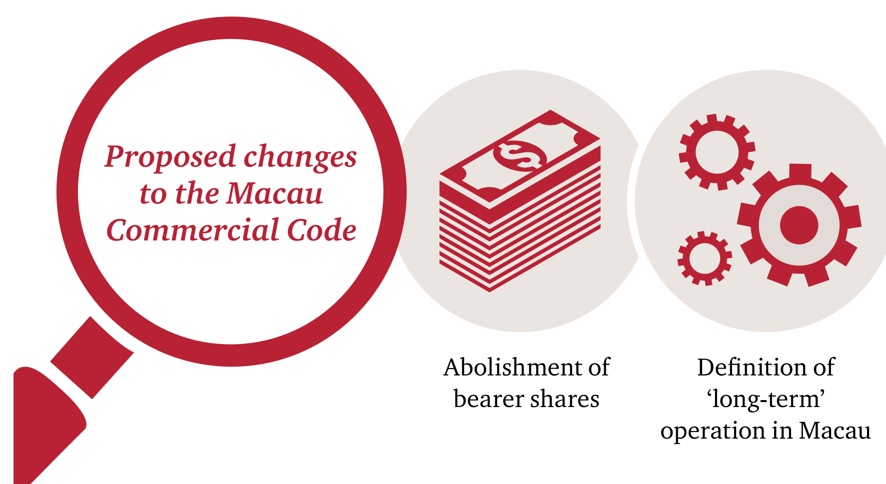
Proposed changes to the Macau Commercial Code

Abolishment of bearer shares

The second phase peer review by the Organisation for Economic Cooperation and Development Forum on Transparency and Exchange of Information for Tax Purposes in 2013 showed that Macau 'mostly complied with the standard but still needs to be improved'. To prepare for the third phase peer review in 2016, bearer shares have been abolished in Macau such that owners of shares could be identified. The abolishment of bearer shares also aims at promoting anti-money laundering and counter-terrorism financing.

Definition of 'long-term' operation in Macau

According to the Macau Commercial Code, foreign companies with long-term operation in Macau should be subject to registry laws and regulations. In June 2015, the Macau Commercial Code was modified to include the definition of 'long-term operation'. A 'long-term operation' is defined as operation that continues for more than one year, or discontinuous operation that exceeds three months each year in five consecutive years. The concept of long-term operation is closely connected to the concept of permanent establishment in international taxation. Foreign companies intending to carry on business in Macau for period crossing the defined threshold will be required to perform registration both with the Macau Commercial Registry and with the Macau Finance Bureau.



Macau Offshore companies and offshore financial institutions

In addition to having very low corporate and individual tax rate, profits derived by approved offshore financial and non-financial institutions from prescribed offshore activities are exempt from all forms of taxes, such as complementary tax, annual industrial tax (currently exempt for all taxpayers), and stamp duties. The executives and/or staff at supervisory level of the qualified institutions are exempt from professional tax for three years by application.

Offshore financial institutions include banks, insurance companies, re-insurance companies, trust management companies, and more importantly, fund management companies.

For offshore non-financial institutions, there are eight permissible offshore activities:

1. hardware consultant
2. software consultant
3. data processing
4. database related activities
5. back office activities
6. research and development activities
7. tests and technical analysis activities
8. management and administration of ships and aircraft

It might be worth exploring the possibility of setting up a Macau offshore institution (MOI) for companies in the relevant industries or, where it is commercially viable, for some of the above-listed back office and support functions to be relocated to Macau.

Although trading is no longer available as a permissible offshore activity for newly set up MOI, it may be possible to acquire existing MOI with trading business scope (trading MOI), such that the new investor can inherit the tax exempt status of the trading MOI, subject to approval from the regulatory authority.

Alternatively, consideration can be given as to whether a MOI (which has been approved to provide back office activities) can provide all the requisite services, such as procurement, quality control, marketing, and liaison services pertaining to trading transactions, to support another trading entity within the group, such that an arm's length service fee can be charged to the trading entity. The permanent establishment risk in other tax jurisdictions may be mitigated through the use of such a MOI, if appropriately structured.

Consideration can also be given as to whether a MOI can be set up for hosting and maintenance of servers for internet businesses such that the taxable presence exposure created by the physical presence of servers in other tax jurisdictions, if any, can be better managed.

Aside from benefiting from the tax exempt status of a MOI, individual investors meeting certain minimum investment threshold may also apply for Macau residency status under the Macau Investment Migration Scheme. Under the Scheme, the applicant may apply for a Macau permanent residency card after maintaining the business in Macau for seven years consecutively.

Nevertheless, as MOIs are focus of investigations for many tax jurisdictions, it is important to ensure that such companies have adequate commercial substance in Macau and the companies' transfer pricing policies are supported by appropriate transfer pricing documentation and transfer pricing studies.

Malaysia

2016 budget

The 2016 budget, themed *Prospering the Rakyat* (prospering the citizens), was announced on 23 October 2015. The focus of the 2016 budget is to strike a balance between capital economy and people economy by addressing the development needs of the country and alleviating the burden of rising cost of living for the people. This budget also seeks to strengthen economic resilience, and increase productivity and innovation.

Key tax initiatives

The key tax initiatives are mainly aimed at spurring growth in the manufacturing sector and providing more reliefs for individual taxpayers. Other initiatives include enhancing and extending existing tax incentives to give a boost to the Small and Medium Enterprise and Capital Markets sectors.

Special reinvestment allowance

The reinvestment allowance (RA) incentive was introduced in year of assessment (YA) 1998 and proved to be popular among manufacturers. As a company is only allowed to enjoy the incentive for a maximum of up to 15 YAs, most companies would by now be at the tail end of their eligible incentive period. Hence, in order to encourage reinvestment in Malaysia, a special RA incentive has been provided by extending the existing incentive period for up to three years, i.e. from YA 2016 to YA 2018.

This incentive is also available to the agriculture sector.

Individual income tax rates and tax reliefs

The 2016 budget introduced numerous measures relating to the welfare and interests of the people. With effect from YA 2016, individual taxpayers will enjoy new and increased tax reliefs. These include increases ranging from 33% to 100% of existing amounts of a range of personal reliefs comprising spousal, child, disabled child and higher education reliefs. Two new reliefs, parental care and social security contribution reliefs, were also introduced.

However, on the flip side, the chargeable income bands and the corresponding tax rates for individuals will be increased from YA 2016 with the introduction of two new tax bands as follows:

Current maximum tax rate:	25% on chargeable income exceeding MYR400,000
Increased tax rates:	26% on chargeable income exceeding MYR600,000 but not more than MYR1,000,000 28% on chargeable income exceeding MYR1,000,000

The tax rate for non-resident individuals has also been increased from 25% (YA 2015) to 28% effective from YA 2016.

More recently, during the budget recalibration announced on 28 January 2016, a one-off special personal tax relief of MYR2,000 was provided to individuals with monthly income of MYR8,000 and below for YA 2015. These initiatives will certainly help buffer against the rising cost of living in the current economic environment.

Corporate tax incentives

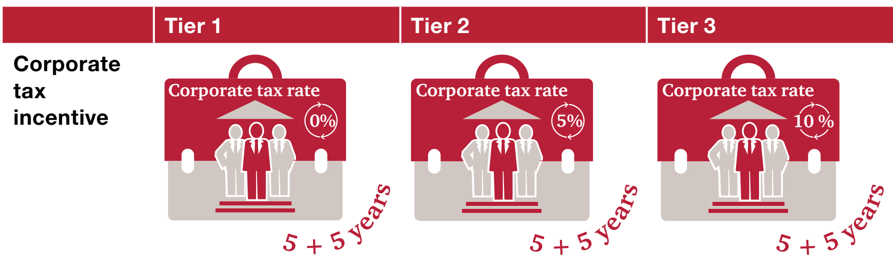
The government introduced several incentive measures during the last 11 months, including the Principal Hub incentive.

The Principal Hub incentive scheme

A principal hub is a locally incorporated company based in Malaysia for conducting its regional and global businesses and operations through management, control and support of key functions. The incentives given to a principal hub are to encourage foreign companies to leverage on Malaysia's position in ASEAN and Asia Pacific, and to encourage Malaysian companies to function as a regional headquarters.

Effective from 1 May 2015, the Principal Hub incentive scheme has replaced the incentive schemes for International Procurement Centres, Regional Distribution Centres and Operational Headquarters. Applications for the Principal Hub incentive scheme must be received by the Malaysian Investment Development Authority during the period from 1 May 2015 to 30 April 2018.

Notable features of the Principal Hub incentive scheme are as follows:

<table>
<tr><th></th><th>Tier 1</th><th>Tier 2</th><th>Tier 3</th></tr>
<tr><td>Corporate tax incentive</td><td colspan="3">
</td></tr>
<tr><td>Other incentives</td><td colspan="3">• No local equity/ownership conditions
• Foreign exchange administration flexibilities and posts for expatriates
• Customs duty exemption for certain groups of items and materials</td></tr>
<tr><td>Common key conditions</td><td colspan="3">These include minimum amount of paid up capital, annual trade sales and minimum number of qualifying services to be provided.</td></tr>
<tr><td>Specific key conditions</td><td colspan="3">Key conditions which vary between the three tiers, to be fulfilled over a given timeframe, include:
1. Provision of the following qualifying services to a minimum number of countries:
a. Strategic services:
• Business unit management
• Strategic business planning and corporate development
• Corporate finance advisory services
• Brand management
• Intellectual property management
• Senior level talent acquisition and management
b. Other business and shared services
c. Regional P&L service which focuses on growth and resource allocation of the company, including regional/global direction, monitoring of budget expenditure, net income and generation of return on investment
2. Minimum number of high value job positions, key management positions and positions filled by Malaysians
3. Minimum annual spending</td></tr>
</table>

Incentives for less developed areas

As an enhancement to the existing incentive package available in the Economic Corridors, and to promote growth and inclusiveness in the less developed areas, the following incentives have been made available, for applications submitted up to 31 December 2020:

- 100% income tax exemption up to 15 YAs (5+5+5) commencing from the first YA in which statutory income is derived, or
- 100% of qualifying capital expenditure (Investment Tax Allowance) can be used to offset against 100% statutory income

Other incentives available for less developed areas are:

- stamp duty exemption on transfer of lease of land or building;
- withholding tax exemption on fees for technical advice, assistance or services, or royalty relating to manufacturing and services activities, up to 31 December 2020; and
- import duty exemption on raw materials and components, machinery and equipment, which are not produced locally and used directly in the manufacturing or services activity.

Incentives for MSC status companies[1]

With effect from YA 2015, a Malaysian incorporated and resident company with MSC status and operating outside of the designated MSC cyber cities and cyber centres will be eligible for the following:

- 70% income tax exemption of statutory income from qualifying activities for the first five years, while operating outside the designated MSC cyber cities or cyber centres; and
- 100% income tax exemption of statutory income from qualifying activities for an extended exemption period (another five years) on condition that the company relocates to within the designated MSC cyber cities or cyber centres.

Tax administration

There have been several notable tax administrative measures adopted by the government during the year.

Tax amnesty

In efforts to encourage tax compliance and expedite tax collection for the government, the tax amnesty programme was first introduced for the period from 1 May 2015 to 30 November 2015. For cases involving the filing of backlog returns and the settlement of taxes in arrears, the tax amnesty programme provided a reduction in penalty and a waiver of increase in tax with respect to income and real property gains taxes.

A second round of the tax amnesty programme was introduced for the period from 1 March 2016 to 15 December 2016. The programme has been expanded to include cases involving petroleum income tax and stamp duty. The reduction in penalty or the waiver of increase in tax will be considered on a case-by-case basis provided that the conditions for reduction or waiver are met.

Deferment of thin capitalisation rules

The provision for thin capitalisation was introduced on 1 January 2009 and is meant to disallow tax deduction on interest expense arising from excessive financial assistance. There have been several deferrals of the implementation date of the thin capitalisation rules, the last being to 31 December 2015. The implementation date has recently been further deferred to 31 December 2017.

Specific tax audit frameworks

The following specific tax audit frameworks were issued in 2015:

- Tax audit framework – financial and insurance

  Effective from 1 June 2015, this framework is applicable to the financial and insurance industry, including Islamic finance, insurance and financial intermediaries. The framework provides guidance on the scope and process of a tax audit in this industry.

- Tax audit framework – withholding tax

  Effective from 1 August 2015, this framework outlines the scope and process of a withholding tax audit.

1 MSC Malaysia status is awarded to both local and foreign companies that develop or use multimedia technologies to produce or enhance their products and services as well as for process development.

New Zealand

Introduction

In the last 12 months, the developments in international tax were driven by the New Zealand Government, at least in part, alongside the global development of the Base Erosion and Profit Shifting (BEPS) project. Recent proposals and enacted law amendments, with the above objectives, are related to areas such as intra-group debt capitalisation and debt remission, non-resident withholding tax (NRWT) on related party lending, goods and services tax (GST) on online products and services and the taxation of non-residents. There has also been a heightened focus on information collection and exchange of information with overseas tax authorities including the upcoming country-by-country (CbC) reporting in the Organisation for Economic Cooperation and Development (OECD) countries (including New Zealand) and the government's endorsement of the Automatic Exchange of Information in Tax Matters.

New Zealand's international tax regime is likely to be prominent in the tax reforms over the next 12 to 24 months. The government is considering its responses and strategies on implementing a number of BEPS measures. Inland Revenue has indicated recently that the key areas of interest in BEPS relate to the potential changes of New Zealand's anti-hybrid and interest limitation rules. Consultation papers are expected to be issued in the next few months.

Inland Revenue has also commenced a very significant business transformation programme with the goal to simplify tax administration in New Zealand and leverage on digital platforms to fundamentally change how Inland Revenue interacts with taxpayers. The programme involves a large scale technology platform upgrade, updates to tax policies and legislations and improvements to Inland Revenue's business processes and customer services. A discussion document on business tax, which include proposals to simplify tax payments and introduce methods for businesses to provide information to Inland Revenue directly from their existing systems, was released in March 2016.

Going forward, Inland Revenue's compliance focus for 2015/2016 reiterates the priorities previously identified. In particular, Inland Revenue will continue to focus on the following areas relating to cross-border taxation:

- Transfer pricing: lack of transfer pricing documentation, major downward shifts in profitability, widely differing profits between local entities and their global group members, unsustainable levels of royalties or management fees, transactions with low or no tax jurisdictions and chronically recurring losses;
- Controlled foreign companies (CFCs): technical compliance, possible New Zealand tax residency of CFCs through local management control or director decision making;
- BEPS issues: taxation of digital goods and services provided over the internet, hybrid mismatches as a result of variances in tax treatment between countries and misuse of tax treaties;
- GST: associated party transactions, non-routine transactions and zero rating of goods or services; and
- Transactions with non-residents and non-resident contractors.

Base Erosion and Profit Shifting

New Zealand is generally considered to have robust international tax and transfer pricing rules already in place. However, as an active OECD participant, we still expect to see changes to further align New Zealand's international tax regime to the OECD preferred model. It remains to see how and to what extent New Zealand will adopt the OECD's BEPS proposals. However, announcements by the government and the updated Tax Policy Work Programme for 2016 indicates that the OECD's recommendations in respect of transfer pricing, hybrid mismatches and interest deductibility would have the greatest impact on New Zealand's domestic tax laws.

Further to the OECD's final recommendations released in October 2015, the Minister of Finance and the Minister of Revenue issued a joint statement in the same month, commending the OECD's work in combatting BEPS. It was noted that the BEPS project provided a good opportunity to scrutinise and possibly reform New Zealand's international tax regime. However, New Zealand's commitment to the BEPS project would have to be balanced to ensure New Zealand remained attractive to foreign investors.

In November 2015, Inland Revenue released its intended approach to implement the OECD's recommendations for transfer pricing documentation and CbC reporting. Inland Revenue is still considering whether legislative change is required or whether the current law is sufficient to implement CbC reporting requirements. Inland Revenue anticipates that the new CbC reporting requirements will affect only a small number of New Zealand headquartered corporate groups, and is liaising with each group directly to ensure that they are adequately prepared for the new CbC reporting requirements. However, a significant number of New Zealand subsidiaries will also be impacted to the extent that their offshore parent companies are required to prepare CbC reporting for their home jurisdictions.

Several international tax and BEPS-related measures are expected to be introduced during 2016. In particular, New Zealand's response to the anti-hybrid mismatch rules and interest limitation rules will be considered and Inland Revenue will publish discussion documents for consultation on these topics during the upcoming calendar year.

Automatic Exchange of Information in Tax Matters

New Zealand has endorsed the OECD's initiative on Automatic Exchange of Information in Tax Matters (AEoI), which is an agenda item on the government's 2016 Tax Policy Work Programme. The AEoI standard is similar to the United States' Foreign Account Tax Compliance Act and serves as part of a global information sharing initiative to help tackling tax evasion.

The Minister of Revenue commented that 'tax evasion respects no borders so global cooperation is the way to combat it. Sharing information is a powerful weapon in that fight'. The government's commitment to AEoI means that financial institutions in New Zealand will be required to undertake due diligence on account holders and report information to Inland Revenue. The information will automatically be exchanged with relevant treaty partners. An officials' issues paper was released in February 2016 outlining proposals for implementing AEoI in New Zealand.

Debt remission

Inland Revenue released an officials' issues paper in February 2015, clarifying the government's policy on related party debt remission/ capitalisation. The issues paper concluded that debt remission/ capitalisation taking place between companies within New Zealand tax base should not give rise to any taxable income. When two parties are within the same wholly owned group, the wealth of the group as a whole is not altered by the debt remission, thus the tax outcome should reflect that accordingly.

However, the tax treatment of debt capitalisation in a cross-border context (i.e. where the creditor is a non-resident and debtor is a New Zealand resident) was left open due to BEPS concerns. The Minister of Revenue subsequently released a media statement and a supporting technical information sheet in September 2015, confirming Cabinet's approval to provide tax relief for related party debt remission. In addition, it was confirmed that the proposals would also be extended to inbound cross-border debt (e.g. New Zealand subsidiaries of foreign companies).

Below are the key proposals in the media statement and supporting technical information sheet:

- Core proposals: there should be no debt remission income for the debtor when the debtor is in the New Zealand tax base, including CFCs and New Zealand subsidiaries of foreign companies, and
  - they are members of the same wholly owned group of companies; or
  - the debtor is a company or partnership (including look-through companies (LTC) and limited partnerships) and:
    - all of the relevant debt is owed to shareholders or partners in the debtor; and
    - the relevant debt is remitted or capitalised pro-rata to ownership.
- The core proposals will extend to amounts lent by relatives of the owner (e.g. loan to a LTC by the spouse of the owner). Therefore, no debt remission income would arise in these circumstances.

The Minister of Revenue intends to introduce legislative amendments in March/April 2016. Once enacted, the legislation should apply retrospectively from 1 April 2006.

Non-resident withholding tax proposals

On 7 May 2015, Inland Revenue released an officials' issues paper, proposing several changes to the NRWT rules in relation to interest earned by non-residents from related party and branch lending. If enacted as it is, these proposals will have a broad-reaching impact. In general, the proposals in this issues paper cover three areas:

- Better alignment of the NRWT and financial arrangements rules;
- Restricting the eligibility for the 2% approved issuer levy (AIL); and
- Limiting the onshore and offshore branch exemptions.

Specifically, the following measures were proposed:

- Broadening the type of instruments that can give rise to interest income subject to NRWT: NRWT will be imposed on the amount provided to a New Zealand resident by an associated non-resident under a financial arrangement where the New Zealand resident borrower is entitled to a deduction under the financial arrangement rules in relation to the funding.
- Aligning the rules for determining the amount of interest income subject to NRWT with the financial arrangement rules: NRWT will apply to an amount of interest received by a non-resident from an associated New Zealand resident, when the New Zealand resident is entitled to a deduction under the financial arrangement rules.
- To better align the timing to impose NRWT on interest income derived by the non-resident lender with the timing of deduction on interest incurred by the New Zealand resident borrower under financial arrangement rules.
- Introducing more restrictive AIL registration criteria: the issues paper suggests three changes to the AIL rules with the intention to prevent AIL from imposing on interest paid either directly or indirectly to a non-resident associated lender.
- Interest paid by an offshore branch of a New Zealand resident will be treated as New Zealand-sourced interest (and subject to NRWT) unless the interest relates to money borrowed for the purpose of a business outside New Zealand and does not involve lending to New Zealand residents.
- Interest earned by a non-resident with a New Zealand branch will be included as non-resident passive income (and subject to NRWT) unless the money lent is used by the non-resident for the purposes of a business it carries on through its New Zealand branch (in such case, the onshore exemption will apply).

Some exemptions and special transitional rules are also proposed for banking groups.

The submissions received on those proposals have been considered by Inland Revenue and the government. Draft legislation is expected to be released in April 2016. Subject to consultation, the proposed rules would be enacted in late 2016. The proposed rules will apply to all arrangements entered into on or after the enactment of the legislation, and transitional rules are expected to deal with existing arrangements.

GST on online products and services

Draft legislation was introduced into the New Zealand Parliament in November 2015 to impose GST on digital products (e.g. music, movie and game downloads) and other services (e.g. webinars, e-learning, publishing and consultancy) purchased online from offshore sellers by New Zealand consumers.

The key legislative changes include:

- Services and intangibles supplied remotely by an offshore supplier to New Zealand resident consumers will be treated as supplied in New Zealand and therefore subject to GST.
- The new rules will only apply to business-to-consumer transactions and not to business-to-business transactions.
- From 1 October 2016, offshore sellers will be required to register and return GST if their supplies of services to New Zealand resident consumers exceed NZD60,000 in a 12-month period. The first return will be filed for a special 6-month period from 1 October 2016 to 31 March 2017 and offshore sellers will be required to pay GST quarterly starting from 1 April 2017.
- The GST registration will be a 'pay only' system as most offshore sellers will not have any New Zealand costs. However, if the offshore seller is already GST-registered, they should be able to use their current GST registration and filing procedures.
- In some situations, instead of the principal offshore seller, an 'electronic marketplace' or intermediary will be required to register.

In relation to imported goods, the government has indicated that there are various issues in devising an effective solution for low value goods imports (covered by the current so-called NZD400 threshold or the minimum duties/taxes NZD60 concession). Progress has been made on a solution for collecting duties/GST on imported goods in the most efficient way. A discussion document on this issue is expected to be issued by April 2016.

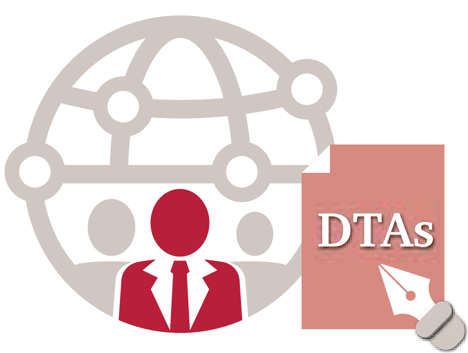
Double Tax Agreements

Canada – New Zealand Double Tax Agreement

New Zealand's new Double Tax Agreement (DTA), together with an amending protocol, with Canada entered into force on 26 June 2015. Under the DTA, the withholding tax (WHT) rates are:

- 5% for dividends for an investor who holds at least 10% of the shares in the company paying the dividend;
- 10% for royalties, or 5% for royalties relating to copyright, computer software and others; and
- 10% for interest.

In New Zealand, the DTA is effective for WHT from 1 August 2015. For other provisions, the agreement is effective generally for income years beginning on or after 1 April 2016. In Canada, the DTA is effective for WHT from 1 August 2015. For other provisions, the agreement is effective generally for income years beginning on or after 1 January 2016.



New Zealand's new DTAs with Canada and Samoa entered into force in 2015 and 2016 respectively.

Samoa – New Zealand Double Tax Agreement

New Zealand signed a new DTA with Samoa in July 2015. The new DTA replaces the existing tax information exchange agreement between New Zealand and Samoa. Under the new DTA, the WHT rates are:

- 15% for dividends, or 5% for an investor who holds at least 10% of the shares in the company that pays the dividends;
- 10% for interest payments; and
- 10% for royalties

In New Zealand, the DTA is effective for WHT from 1 February 2016. For other provisions, the agreement is effective generally for income years beginning on or after 1 April 2016. In Samoa, the DTA is effective for WHT from 1 February 2016. For other provisions, the agreement is effective generally for income years beginning on or after 1 January 2016.

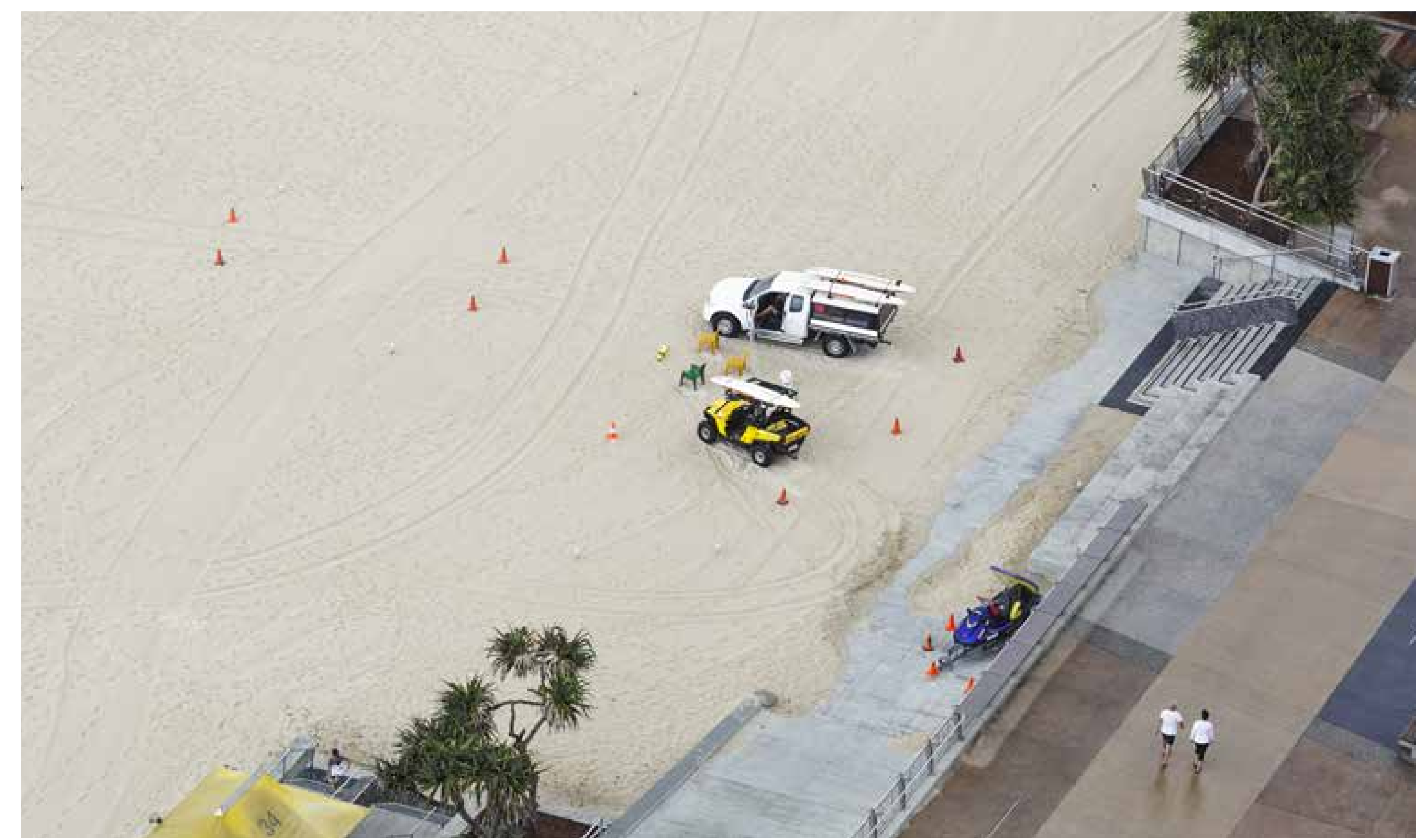
Property measures

As part of the Budget 2015, the government announced various new property tax measures to strengthen the property tax rules in New Zealand and improve the information in relation to property transactions collected by Inland Revenue. A key objective of these measures is to ensure non-residents who purchase property in New Zealand comply with their New Zealand tax obligations.

Administrative property tax rules

Effective from 1 October 2015:

- Buyers and sellers of property are required to provide their Inland Revenue Department numbers (IRD numbers) at the time of property transfer. Those who are not tax resident in New Zealand also have to provide a tax identification number from their home jurisdiction. There is an exemption for New Zealand residents' main home.
- Offshore persons are required to have a New Zealand bank account to get a IRD number. This includes New Zealand people who have been out of the country for three or more years. It also includes New Zealand companies with significant non-resident shareholdings.



Residential property bright-line test

A new objective 'bright-line' land sale test has been introduced to impose tax on gains derived from the sale of certain residential properties which are bought and sold within two years (unless a specified exemption applies, e.g. exemption for New Zealand residents' main home). The bright-line test only applies to residential properties purchased on or after 1 October 2015.

Residential land withholding tax

A new residential land withholding tax (RLWT) for 'offshore persons' selling residential property has been introduced (expected to be enacted in April 2016). The RLWT will act as a collection mechanism for the new bright-line test outlined above. It is proposed that RLWT will be payable from 1 July 2016, and will generally be required to be withheld by the vendor's conveyancing agent.

In general, the amount of RLWT is the lesser of the amounts calculated under the following two formulas:

- 33% (or 28% if the vendor is a company) x (current purchase price – vendor's acquisition cost); and
- 10% x current purchase price.

Where the paying agent is the vendor's conveyancer and the amount of RLWT exceeds the amount available from the total purchase price once a mortgage obligation with a New Zealand-registered bank or non-bank deposit taker has been discharged, the amount of RLWT will be the lesser of the amounts calculated above and a remainder amount (the current purchase price – the security discharge amount).

Papua New Guinea

Taxation developments and amendments

In the 2016 Budget, handed down on 3 November 2015, the government introduced several taxation policy measures and a number of minor technical and administrative amendments as part of the government's ongoing effort to refine the tax system and improve its efficiency and fairness.

The budget introduced a potentially significant measure with respect to Goods and Services Tax (GST) – a GST deferral scheme for imports. This measure is to improve cash flow for importers and to reduce the administrative burden on the Internal Revenue Commission (IRC) and Papua New Guinea (PNG) customs.

To improve the exchange of taxpayer information, the government will continue to support PNG's membership of the Multilateral Convention on Mutual Administrative Assistance in Tax Matters. Meanwhile, the government suspends negotiations of any new Double Tax Agreements (DTAs) until the Base Erosion and Profit Shifting (BEPS) reports released by the Organisation for Economic Cooperation and Development (OECD) have been fully considered by PNG.

The government has received the report from the Taxation Review Committee following two years of work by the committee. It will consider the recommendations in the report and carry out consultation with stakeholders during 2016.

Corporate and personal tax rates

There was no change to the general corporate income tax rates of 30% for residents and 48% for non-residents. There was also no change to the personal income tax rates that have applied from 1 July 2012.

From 1 January 2016, the personal income tax rates for resident individuals will continue to be as follows:

Taxable income (PGK)	Tax thereon (PGK)	Rates on tax on excess (%)
10,000	Nil	22
18,000	1,760	30
33,000	6,260	35
70,000	19,210	40
250,000	91,210	42

From 1 January 2016, the personal income tax rates for non-resident individuals will continue to be as follows:

Taxable income (PGK)	Tax thereon (PGK)	Rates on tax on excess (%)
Nil	Nil	22
18,000	3,960	30
33,000	8,460	35
70,000	21,410	40
250,000	93,410	42

Import GST deferral scheme

The 2016 Budget introduced a GST deferral scheme to improve the operation of the GST refund system.

The GST Act provides for GST to be imposed on the importation of goods at the time they are imported. The GST paid by importers is refunded to the taxpayers on lodgement of the next GST return by input tax credit. Hence the GST imposed on the importation results in no net revenue being collected by the State.

The requirement for taxpayers to pay GST on importation and then seek to have the same GST refunded by the IRC reduces cash flow for business and creates unnecessary administration for the IRC and PNG customs.

Under a GST deferral scheme, the payment of the GST on importation is deferred until the time the taxpayer lodges its next GST return and an input tax credit for the same amount is allowed in the same return, so there is no cash tax payable.

The measure came into effect on 1 January 2016.

At this stage there is limited information as to how the scheme will be operated and administered in PNG. The proposed legislative amendment simply provides that '*The Commissioner may operate a deferral scheme … for the payment of goods and services tax on imported goods*'. In other jurisdictions where a GST deferral scheme operates, taxpayers are required to apply for approval to participate in the scheme, and approval is granted (and can be withdrawn) based on the compliance record of the taxpayer.

The IRC has not provided official guidance as to who will be eligible to participate in the scheme or the procedures for any approvals by the IRC other than the release of an application form. It is also not clear whether these procedures will ultimately be governed by legislation or practical administration by the IRC. However, we understand that the IRC will approve applications in which the taxpayer makes regular and significant imports and has a good IRC and PNG customs compliance history (i.e. new taxpayers with no compliance history are unlikely to be approved).

Suspension of Negotiation of Double Tax Agreements

The OECD has been undertaking a review of BEPS practices. Such practices may be used by taxpayers to reduce tax liabilities and move tax liabilities to lower tax jurisdictions. They may also be used by governing authorities in some jurisdictions to attract taxpayers through non-transparent and low tax regimes. The OECD has expressed some concerns that DTAs can result in the unintended outcome of not taxing income in any jurisdiction.

In light of the OECD's review, the government has postponed entering into new DTA negotiations until after the BEPS report can be fully considered by PNG. Once the BEPS reports have been considered, the government believes it may be appropriate to renegotiate its existing DTAs to ensure PNG gets its fair share from the treaties.

PNG currently has DTAs with Australia, Canada, China, Fiji, Malaysia, Singapore, Korea, the United Kingdom, New Zealand and Indonesia. While it is of course not desirable (and not the intention) for DTAs to result in income not being taxed anywhere, DTAs do facilitate foreign investment by preventing the double taxation of income. The expansion of PNG's DTA network can have the effect of opening new markets for foreign investment entering into and going out from PNG.

Multilateral Convention on Mutual Administrative Assistance on Tax Matters

The government believes that, as taxpayers are increasingly operating across borders, collaboration between tax administrators is important to address offshore tax evasion. In addition, PNG can obtain information more efficiently by becoming a member of the Multilateral Convention on Mutual Administrative Assistance in Tax Matters.

PNG has recently become a member of the Global Forum on Transparency and Exchange of Information, which is a prerequisite to joining the Multilateral Convention on Mutual Administrative Assistance in Tax Matters.

Taxation review report and recommendations

The PNG Taxation Review Committee, which was formally launched in September 2013, issued its report to the Treasurer in October 2015. The report contained 91 recommendations and the government has committed to acting on the reforms proposed in the report. However, imposing changes that have wide impacts requires consultation with those affected and a lead time for taxpayers to prepare for the changes. The government will be working with the stakeholders in 2016 on these changes for the 2017 Budget.

The Tax Review Committee applied five principles in guiding its consideration of reforms for a better tax system. The government will apply these principles while it considers and implements recommendations from the report. These principles provide that the tax system should:

- raise sufficient revenue to enable the government to deliver services that meet the community's expectations;
- promote economic growth and create more jobs, higher incomes, less poverty and more services;
- treat taxpayers fairly;
- be as simple as possible to understand and comply with; and
- build trust in the government and support government accountability.

The Tax Review Committee's key findings are that PNG relies too heavily on salary or wages tax, which is borne by less than 400,000 taxpayers out of an estimated population of 7.5 million, and PNG's corporate income tax rates are not regionally competitive. On the other hand, the GST rate of 10% is comparatively low, the tax base is not sufficiently broad and tax incentives have been over-used.

In this context, below are some of the key recommendations of the Tax Review Committee:

- A reduction in the corporate income tax rate from 30% to 25%
- A reduction in dividend withholding tax from 17% to 15%
- An increase in the tax free threshold for individual taxpayers from PGK10,000 to PGK15,000, and ultimately to PGK20,000, together with a reduction of the tax rate applying to income below PGK33,000
- An increase in the GST rate from 10% to 15%
- Improvement of tax administration and the establishment of a Centralised Revenue Board to oversee the IRC and PNG customs
- The introduction of an additional profits tax to apply to mining sector in PNG
- Alignment of income tax, dividend withholding tax and interest withholding tax rates applying to the extractive industries with the rates for corporate taxpayers generally
- A reduction in tax incentives and transparent management and reporting of incentives granted
- Abolition of the training levy and a double deduction for training
- Introduction of a tax on capital gains, initially apply only to some classes of real property (including interests in resource licences, but not the family home or customary land), but in the longer term extended to other assets
- A simpler and less costly tax system for small business with a turnover up to PGK250,000. Payment and filing arrangements for the sector should also be streamlined

The Taxation Review Committee has proposed a staged introduction of the reforms over the next few years and it is likely the first changes will be made in the 2017 National Budget in November 2016.

Philippines

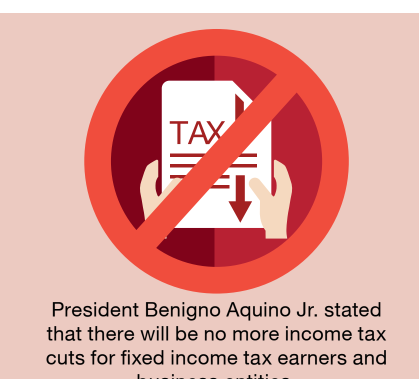
No major tax laws were passed by the Philippine Congress in 2015 except for the enactment of Republic Act (RA) No. 10653[1] in early 2015. It has been projected that the implementation of RA 10653, which increases the tax-exempt amount of certain employment income, would cause billions of pesos loss in tax revenue.

In spite of this, the revenue collection target of the Bureau of Internal Revenue (BIR) for 2015 remained high, at PHP1.72 trillion, as indicated in the Revenue Memorandum Circular (RMC) No. 3-2015 released at the start of 2015. RMC No. 3-2015 also outlines the BIR's Priority Programmes that help attaining its revenue target.

Plugging tax leaks remains to be the most difficult challenge for the BIR in 2015. This is mostly because of the rampant tax evasion committed by individual and corporate taxpayers.

President Benigno Aquino Jr. mentioned in a statement that there will be no more income tax cuts for fixed income tax earners and business entities. This signals a dearth of tax laws benefitting employees or businesses in the foreseeable future and reduces the likelihood of lowering the individual and corporate income tax rates in the Philippines (which are amongst the highest in the South-eastern Asia region) to a more manageable tax rate. The President's blanket statement was aimed at controlling the big tax cuts already brought about by other existing incentives such as the tax exemptions provided by RA 10653 mentioned above.

As a balancing measure, and to ease the negative impact of this statement on the electorate in the last few months of his presidency, President Aquino signed RA 10754 into law in March of this year. RA 10754 amends the Magna Carta for Persons with Disability which provides disabled persons an exemption from value added tax (VAT) for certain goods and services. RA 10754 or 'An act expanding the benefits and privileges of persons with disability'—will be discussed further in the next section of this article.



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Legislation

There are persistent critics of the government for the non-passage of the Freedom of Information Act, the Anti-Political Dynasty Act and the bill that seeks to lower both the individual and corporate income tax rates. Another bill the business sector has lobbied hard for its passage is the Public-Private Partnership Act. The bill aims to amend the current Build Operate and Transfer Act to further strengthen the legal framework to institutionalise public/private partnerships so as to facilitate the accomplishment of more infrastructure projects. Advocates of these bills are still hoping they will become laws before the end of the Aquino presidency.

Below are a summary of the major laws related to business that were passed in 2015.

Philippine Competition Act (RA 10667) was signed into law on 21 July 2015. It aims to establish measures that:

- safeguard market competition and customer protection;
- prohibit practices that allow entities to restrict market competition through anti-competition agreements or abuse of their dominant position;
- specify policies that require proposed mergers and acquisitions to be cleared by the Philippine Competition Commission; and
- prohibit selling of goods or services at reduced prices or with the objective of driving competition out of the market.

The Act levels the business playing field for all companies operating in the Philippines, from large foreign multinationals to local small and medium-sized enterprises, both of which are considered as potential drivers of economic and inclusive growth.

1 Please refer to the country update of Philippines in the last issue of *Asia Pacific Tax Notes* for a discussion of RA 10653 entitled 'The Act adjusting the 13th month pay and other benefits ceiling'.

Amendments to the Cabotage Law (RA 10668), which was enacted almost at the same time as the Anti-Competition Act, lowers the shipping costs for export and import shipments by allowing foreign flagged vessels to carry imported cargo directly to the final Philippine port of destination. This law helps the traders, importers and exporters to lower shipping costs and will eventually benefit the end-consumers as the high costs of transporting goods is essentially passed to and absorbed by the end consumers.

Sugarcane Industry Development Act (RA 10659), which seeks to boost the Philippines' production of sugarcane and sugar, was passed in the middle of April 2015. This Act institutionalises the Block Farm Programme. The programme consolidates small farms, including farms of agrarian reform beneficiaries, into one larger farm with a minimum area of 30 hectares within a two-kilometre radius. It seeks to ensure a more efficient use of farm machinery and equipment and deployment of workers. Under the Act, the government will appropriate a PHP 2-billion fund starting from 2016 to help develop the sugar industry, which contributes more than PHP70 billion annually to the economy.

To enhance fiscal accountability and transparency in granting and managing tax incentives, the **Tax Incentives Management and Transparency Act (RA 10708)** became effect in late 2015. The Act mandates that all registered business entities entitled to special incentives are required to file tax returns and annual tax incentives' reports to the relevant investment promotion agencies. Non-compliance with such reporting requirements is subject to penalties of PHP100,000 (1st violation) or PHP500,000 (2nd violation) or withdrawal of the tax incentive granted (3rd violation).

Cybercrime Prevention Act of 2012 (RA 10175) took effect on 3 October 2015. Although not related to tax, the Act can have significant impact on businesses. RA 10175 is the first law in the Philippines which criminalises computer crimes, e.g. illegal computer access ('hacking'), cybersquatting and child pornography using the internet, etc.

Finally, the **Persons with Disability (PWD) Act (RA 10754)** was signed by President Aquino in March 2016. It grants a 12% VAT exemption to disabled persons on certain goods and services similar to what is provided to senior citizens. Family members and relatives taking care of their kin with disabilities also benefit from the newly signed law.

Other government regulations, circulars and orders

Bureau of Internal Revenue

Revenue Regulations (RR) No. 3 - 2015 dated 9 March 2015 effectively amends the relevant provisions of RR No. 2-98 and implements the provisions of RA No. 10653, which increases the total amount of exclusion from gross income for 13th month pay and other benefits to PHP82,000.

The BIR was quick to point out that the exclusion of PHP82,000 applies only to the 13th month pay and other benefits of salaried employees. It does not cover other types of compensation under an employer-employee relationship, e.g. basic salary and other allowances. In addition, the exclusion does not apply to gross income of self-employed individuals and income generated from business.

RR No. 6-2015 dated 31 March 2015 implements earlier regulations imposing advance business tax (VAT or percentage tax) payments on sugar and for other related purposes. Under this RR, owners or sellers of raw and refined sugar are required to pay 12% VAT or 3% percentage tax in advance before any warehouse receipts or invoices are issued, or before the sugar is withdrawn from any sugar refinery or mill. For raw sugar classified as category 'A', or intended for export to the United States (US), no advance VAT will be collected. However, deficiency VAT plus penalties will be collected if, upon audit, it is found that the raw sugar is not exported to the US and not paid for in acceptable foreign currency according to the rules and regulations of the Central Bank of the Philippines.

RR No. 7-2015 dated 31 March 2015 further amends the provision of Section 2.57.2 of RR No. 2-98, as amended. In particular, Subsection (AA) introduced by RR No 11-2014 and relating to the income payments on locally-produced raw sugar and other matters was amended. Further, buyers of refined sugar, whether locally produced or imported, should withhold the 1% creditable withholding tax based on the actual selling price. Sugar owners that are small sugar planters with gross receipt for a year amounting to PHP300,000 or less are exempted from the following:

- paying the registration fee after submitting minimal basic documentary requirements;
- complying to the issuance of registered invoices or receipts;
- maintaining books of accounts;
- preparing financial statements to support the Income Tax Returns (ITRs) filed; and
- filing advance percentage taxes on a monthly basis.

They are still required to file the ITRs.

Revenue Memorandum Circular (RMC) No. 7-2015 issued on 6 March 2015 reiterates the tax treatment of interest income derived from long-term deposits or investment certificates, as described in RR No. 14-2012. The tax treatment has been clarified in RMC Nos. 77-2012 and 81-2012.

The following characteristics and conditions must be present for the interest income from long-term deposits or investment certificates to be exempt from income tax:

- the depositor or investor is an individual citizen (resident or non-resident) or resident alien or non-resident alien engaged in trade or business in the Philippines;
- the long-term deposits or investment certificates should be under the name of the individual and not under the name of a corporation, the bank or the trust department or unit of the bank;
- the long-term deposits or investments must be in the form of savings, common or individual trust funds, deposit substitutes, investment management accounts and other investments evidenced by certificates in such form prescribed by the Central Bank of the Philippines;
- the long-term deposits or investment certificates must be issued by banks only and not by other entities or individuals;
- the long-term deposits or investments must have a maturity period of not less than five years;
- the long-term deposits or investments must be in denominations of PHP10,000 or other denominations as may be prescribed by the Central Bank of the Philippines;
- the long-term deposits or investments should not be terminated by the original investor before the fifth year (otherwise the related interest income earnings shall be subject to the progressive rates of 5%, 12% and 20%); and
- except those specifically exempt by law or regulations, any other income, e.g. gains from trading, foreign exchange gain, will not be covered by the income tax exemption.

To further plug the tax leak from the non-issuance of receipts by business establishments and self-employed individuals, the BIR issued several circulars and orders on proper issuance of receipts.

RMC No. 30-2015 dated 8 June 2015 implements strict non-issuance of provisional permit to use (PTU) cash register machines (CRM), point-of sale (POS) machines, other sales machines or receipting software to prospective and new users. The Tax Office has directed all Revenue District Offices (RDOs) to no longer accept applications for PTUs. This circular encourages all concerned taxpayers to get BIR-accredited CRMs, POS, other sales machines, and receipting software. The updated list of accredited CRM, POS, other sales machines, and receipting software with their corresponding suppliers is posted on the BIR website (www.bir.gov.ph).

All existing final PTUs, including those provisional PTUs that will be converted to final PTUs on or before 31 July 2015, will have a five-year validity period effective 1 August 2015. All new applications for accreditation of machine or software of suppliers, distributors, dealers and vendors will be processed at the level of BIR National Office only. The machine or software will have a five-year validity period upon registration and approval of the corresponding final PTUs.

RMC No. 36-2015 dated 28 June 2015 specifies the mandatory one-time submission of inventory list of all CRMs, POS machines, special purpose machines (SPMs) and/or any other similar machines generating sales invoices or receipts.

The Commissioner of Internal Revenue (CIR) required all concerned taxpayers to submit an inventory list of all CRMs, POS machines, SPMs and/or any other similar machines generating sales invoices or receipts that were used by establishments in business operations or otherwise, and were physically located in such business establishments/ premises as of 30 June 2015.

In **RMC No. 64-2015** dated 2 October 2015, the CIR reiterated that the VAT receipts, invoices or other commercial invoices for sales amounting to PHP1,000 or more and made to a VAT-registered person must contain the following information:

- name of client, purchaser or customer;
- address;
- taxpayer identification number (TIN); and
- type/mode of business, if any.

This information must also be reflected in invoices or receipts generated from CRMs or POS machines. If a CRM/ POS machine cannot show this information, a manually pre-printed invoice or receipt with approved authority to print must be issued to the client. Non-compliance with these requirements will be subject to corresponding penalties according to existing revenue issuances.

Even the type of paper used for receipts has been regulated by the tax office. **RR No. 10-2015** dated 21 September 2015 mandates the use of non-thermal paper for all CRMs, POS and other invoice or receipt-generating machines and software.

The growth of the private car service industry in the Philippines (e.g. Uber and Grab Taxis) has led the BIR to issue **RMC No. 70-2015** dated 29 October 2015. The circular describes the tax treatment of these transport network companies (TNCs). According to RMC No. 70-2015, if a TNC has been granted a certificate of public convenience (CPC), it is regarded as a common carrier and its gross receipts are subject to the 3% common carriers tax under the Tax Code. However, if a TNC is not a holder of a valid and current CPC, it will be classified as a land transportation service contractor subject to 12% VAT.

If the partner of a TNC is a land transportation service contractor, it may register either as a VAT taxpayer subject to 12% VAT (if its gross annual sales and/or receipts do not exceed PHP1,919,500) or a non-VAT taxpayer subject to the 3% percentage tax under the Tax Code. The BIR requires each TNC and its partner to register their business with the BIR, maintain manual books of accounts or a computerised accounting system and issue receipts for the sale of services. Payments made are not allowed as deductible expenses unless they are properly substantiated by a valid official receipt and the related taxes are properly withheld and remitted to the BIR.

An official receipt must be issued for all payments received from a passenger or customer. Violating the rules on registration, issuance of official receipts and withholding taxes will be subject to both civil and criminal liabilities under the Tax Code.

The BIR issued **RR No. 15-2015** dated 28 September 2015, essentially to reflect certain VAT exemptions. These exemptions are as follows:

- transport of passengers and cargo by international carriers; and
- sale, importation or lease of vessels and aircraft for domestic or international transport operations.

The exemption from VAT on the importation and local purchase of passenger and/or cargo vessels shall be subject to the requirements on restriction on vessel importation and mandatory vessel retirement programme of the maritime industry.

Office of the President

Pursuant to the mandate of **Executive Order (EO) No. 184**, the tenth Regular Foreign Investment Negative List (FINL) was released in June 2015. The FINL identifies areas and business activities which are open to foreign ownership and those which have foreign equity limitations or restrictions. The tenth FINL removed some of the foreign restrictions on certain industries, e.g. those in lending, investment houses and financing companies (with a 60% cap). It also trimmed down the number of professions reserved for Philippine nationals under the principle of reciprocity. This means that the country of origin should also allow Philippine citizens to practice these professions in the country.

Securities and Exchange Commission

Securities and Exchange Commission (SEC) Memorandum Circular (MC) No. 5 issued on 29 May 2015 amended the guidelines for using corporate names. The word 'investments' may only be used by entities organised as an investment house or investment company. The word 'capital' may only be used by entities organised as an investment house, an investment company or a holding company.

Another SEC circular on the use of corporate names was issued in June 2015. **SEC MC 6-2015** no longer allows the use of the corporate name of a dissolved or revoked entity except in extraordinary cases based on the en banc decisions of the SEC.

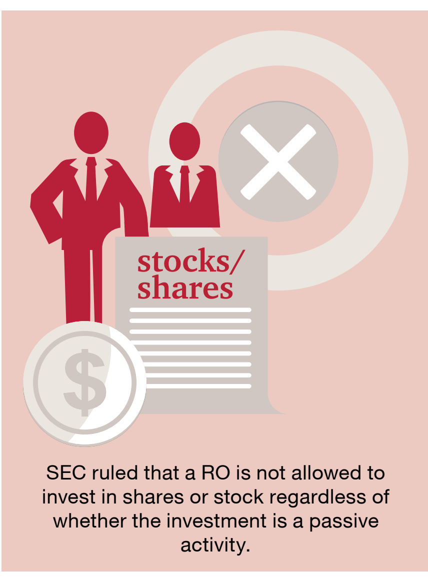
SEC MC No. 9 issued in July 2015 directs all non-stock, non-profit corporations (including non-governmental organisations and foundations) engaging in microfinance activities to use the word 'Microfinance' or 'Microfinancing' in their corporate names. These corporations shall state in the purpose clause of their Articles of Incorporation that they will conduct microfinance operations according to Republic Act No. 8425 or the Social Reform and Poverty Alleviation Act.

In addition to the above circulars, several significant rulings and opinions were issued by the SEC in 2015. One of these was issued in July of 2015 where the SEC ruled that a representative office (RO) is not allowed to invest in shares or stock regardless of whether the investment is a passive activity. It is because a RO is prohibited from deriving any income and is fully subsidised by its head office. Furthermore, the permitted business activities of an RO, as mentioned in its licence, are limited to information dissemination and promotion and do not include investment in shares or stock.

In **SEC Opinion No. 15-08** dated 27 July 2015, the SEC reiterated that Section 36(9) of the Corporation Code provides that foreign and domestic corporations are absolutely prohibited from giving donations to any political party, candidate or for any partisan political activity.

In **SEC-OGC Opinion No. 15-02** dated 2 July 2015, the SEC pointed out that as a general rule and according to Section 51 of the Corporation Code, stockholders' meetings should be conducted in the city or municipality where the principal office of the corporation is located.

However, for a corporation whose principal office is located in one of the component cities or municipalities of Metro Manila (e.g. Makati City), stockholders' meetings may be conducted in another component city or municipality of Metro Manila (e.g. Quezon City), provided that notice of the time, date and particular place of the meeting is given in a timely manner to all the stockholders. Such flexibility may be desirable due to the nature of the business of a corporation. Also, the exception only applies if the corporate by-laws are silent about the venue of the meetings. Where the by-laws expressly provide for a specific place, the provisions of the by-laws prevail.



SEC ruled that a RO is not allowed to invest in shares or stock regardless of whether the investment is a passive activity.

Singapore

Preparing for a new global tax order

Over the last 15 months, Singapore has introduced various measures to better align itself with the international developments in taxation driven by the Organisation for Economic Cooperation and Development (OECD) to counter Base Erosion and Profit Shifting (BEPS).

On the transfer pricing front, we saw a step-up in administration as the Inland Revenue Authority of Singapore (IRAS) introduced contemporaneous documentation requirements in January 2015. One year later, the IRAS revised its transfer pricing guidelines on mutual agreement procedure (MAP) and advance pricing arrangement (APA).

There were two tax cases in 2015 which dealt with requests from overseas tax authorities for exchange of information. In addition the Singapore-US Foreign Account Tax Compliance Act (FATCA) Model 1 Intergovernmental Agreement (IGA) and Regulations entered into force during 2015. More recently, Singapore ratified the Convention on Mutual Administrative Assistance in Tax Matters (CMAA) and published draft legislative changes to implement the Common Reporting Standard (CRS).

Transfer pricing

A new chapter in Singapore's transfer pricing regime began on 6 January 2015 when the IRAS released an update to its Transfer Pricing Guidelines (the Guidelines) to introduce contemporaneous transfer pricing documentation requirements in Singapore for the first time.

Subsequently, the IRAS again revised its Guidelines on the MAP and APA processes and the application of the cost plus method on 4 January 2016.

Changes to advance pricing arrangement process

The IRAS has maintained a stringent timeline that APA applicants should meet for a pre-filing meeting and the submission of requisite pre-filing meeting materials at least nine months and ten months respectively before the first day of the proposed APA covered period (i.e. 'first day of covered period').

Previously, an APA applicant should be able to obtain a broad indication of the IRAS's inclination to accept its APA request at the pre-filing meeting based on the IRAS's review of requisite pre-filing meeting materials submitted and supplementary explanation and clarification provided in the pre-filing discussion. This relatively forthright and open process provides APA applicants a degree of certainty and comfort early in the APA process.

Under the new Guidelines, the IRAS will only indicate its inclination to accept an APA request no later than four months before the first day of covered period. This means that APA applicants will have to wait up to five months after the pre-filing meeting before they can get some certainty of the IRAS's inclination to accept their APA request.

In the case of bilateral APAs, the new rules can be used by the IRAS to coordinate a more streamlined process for the taxpayers concerned, so that similar information requested by the two competent authorities can be prepared at the same time. Hopefully, despite the potential higher uncertainty, the new rules will mean that the post-filing process will be shorter and lead to a faster negotiation and outcome for successful applications.

To mitigate the potential negative impact on taxpayers, the IRAS has complemented the change with a relaxation of the requirement for APA applicants to file the APA applications six months before the first day of covered period. The applicants are now only required to file the APA applications within three months of a go-ahead indication given by the IRAS. Like before, the IRAS has also committed to issue its APA acceptance letter within one month from the receipt of an APA application.

Application of cost plus method

The 2016 revisions to the Guidelines also provide clarification on the application of the cost plus method. An example is now provided to emphasise and illustrate the need for taxpayers to ensure the correct cost base is determined for the purpose of applying the cost plus method. In particular, the IRAS may now deem additional costs to be included in the cost base of the provider of services and/or goods even if these additional costs are not actually incurred and booked in the accounts.

The above change seeks to ensure that group service providers incur the correct level of costs and consequently earn the correct level of remuneration, regardless of whether they are charged with full costs for providing the services. While this is a theoretically sound approach to adopt, it appears to ignore the practical difficulties faced by taxpayers in complying with this approach. As a result, it exposes group service providers which may not have the wherewithal to dictate or ensure that other group entities charge them with appropriate costs, to potential non-compliance issues and associated penalties. Also, group service providers may not find it feasible to put in place an elaborate mechanism to track and/or compute the costs incurred by other group entities that may be attributable or allocable to them for the purpose of adjusting their cost base.

Expectations and obligations arising from mutual agreement procedure and advance pricing arrangement processes

The Guidelines clarify that the IRAS is not precluded from conducting a tax audit on a taxpayer if there is non-compliance with Singapore tax laws in the event that the IRAS or the foreign Competent Authority rejects the taxpayer's MAP or APA application. It is unclear under what circumstances the IRAS will seek to do this (i.e. reject an APA or MAP application) and conduct an audit on the taxpayer concerned. Doing so would put the taxpayer in the precarious position of being exposed to double taxation, for which it has no avenue to mitigate the associated risks other than through domestic legal and judicial proceedings.

Implications on taxpayers

Two rounds of revisions to the Guidelines within a year indicates that the IRAS is closely monitoring the evolving international tax developments and their implications on transfer pricing compliance in Singapore, and that it stands ready to make changes to further tighten the transfer pricing regime and related aspects in Singapore to address or respond to the evolving needs.

While most of the requirements laid out in the 2015 revisions are not new and should not require major changes in taxpayers' practices for the preparation of transfer pricing documentation, they provide specific details of documentation requirements and address ambiguity on common topics for compliance with the arm's length principle. It is also likely to provide increased visibility for group transfer pricing policies. The Guidelines appear to prepare local taxpayers for the recent outcomes under BEPS with regard to the requirements on master file and local file documentation and country-by-country reporting, as well as the potential reactions from other tax authorities.

In addition, in the post-BEPS world, taxpayers all over the world expect to face and deal with a rising number of cross-border tax disputes. They have expressed increasing desire to receive greater support from the Competent Authorities of their home jurisdictions in bracing the looming storms. From this perspective, changes introduced to tighten the APA process in Singapore may need to be closely monitored to ensure that they create the intended effect, including better streamlined information gathering processes and the highlighting of key issues at an earlier stage to facilitate issue resolution.

Under such challenging circumstances, what Singapore taxpayers can do, and must do, to effectively mitigate transfer pricing risks is to ensure they have robust transfer pricing and related documentation in place to serve as a strong first level of defence against potential challenges by tax authorities. In addition, having robust transfer pricing policies, practices and related documentation would put them in a good position to seek or access APA should they decide to pursue such cross-border tax dispute prevention strategies to mitigate their transfer pricing risks.

Exchange of information

Tax cases

There were two court cases relating to the exchange of information in 2015.

In *ABU v Comptroller of Income Tax* [2015] SGCA 4, the Court of Appeal considered an exchange of information request made pursuant to the Singapore-Japan treaty. The case concerns whether a substantive review ought to be undertaken for the merit of the request, whether the laws permit exchange of information for periods before the new exchange of information article was given effect in Singapore and whether the account holders had the right to intervene. In its judgment handed down on 22 January 2015, the Court of Appeal held that the request from the Japanese tax authorities met the requirements for such a request and granted the application of the Comptroller of Income Tax (the Comptroller) with an order to allow the release of the information sought.

In *AXY & Ors v Comptroller of Income Tax* [2015] SGHC 291, the Comptroller sought to obtain information in respect of the applicant's banking activities in Singapore on behalf of National Tax Service of Korea (NTS). Under the request, the Comptroller issued notices to various banks in Singapore for information on the banking activities of the applicants and their companies from 2003 onwards. The applicants applied for judicial review of the Comptroller's decision to issue the notices and sought a prohibition order against the Comptroller from disclosing any banking activity relating to the applicants to the NTS and a quashing order against the notices issued. The applicants also sought the production of certain categories of documents for inspection while the Comptroller applied to expunge the documents from the court record.

In its judgment handed down on 4 November 2015, the High Court ordered the production of certain categories of the documents sought on the basis that they were relevant and necessary for the fair disposal of the case. The court noted that, since the filing of the summons for discovery, the governing legislation had been amended to state that in the context of judicial review proceedings, the court shall not grant leave for discovery of the request issued by a foreign tax authority and related documents if the court was satisfied that the foreign tax authority had requested the Comptroller not to disclose the said documents to any person. While the court noted that this had effectively restricted the right of taxpayers to apply for discovery of documents relating to an exchange of information in judicial review proceedings, it was not applicable to the present case because the application for judicial review was filed before the effective date of the amendment. In addition, the NTS no longer objected to the disclosure of the redacted copies of NTS-related documents.

It should be noted that the law has been amended since these cases were first heard, such that the Comptroller no longer needs to seek a court order to obtain information from banks for exchange of information purposes. That being said, certain principles established in these cases remain relevant, including the test for the reasonable foreseeability standard, the temporal application of the exchange of information legislation and applications for judicial reviews.

Singapore-US Foreign Account Tax Compliance Act Intergovernmental Agreement

The Singapore-US FATCA Model 1 IGA and Regulations entered into force on 18 March 2015. FATCA is a US law which targets non-compliance with tax laws by US persons using overseas accounts. Under FATCA, all financial institutions (FIs) outside the US are required to submit information on financial accounts held by US persons regularly to the US Internal Revenue Service (IRS). The Singapore-US IGA facilitates Singapore-based FIs' compliance with FATCA, by allowing them to fulfil their reporting obligations through the IRAS instead of reporting directly to the US IRS.

Convention on Mutual Administrative Assistance in Tax Matters

Singapore ratified the CMAA on 21 January 2016. Internationally, the CMAA will provide the basis on which tax authorities cooperate in various aspects of tax administration, including the exchange of information. Singapore became a signatory to the CMAA on 29 May 2013 to enhance its international tax cooperation framework. Following the ratification and domestic implementation legislation, it will become effective from 1 May 2016 and thus expand Singapore's network of partners for exchange of information on request by 34 jurisdictions. It should, however, be noted that Singapore has made various reservations in implementation in accordance with the local laws, including not providing assistance in the recovery of foreign taxes.

The Ministry of Finance (MOF) published a draft bill, namely Income Tax (Amendment No. 2) Bill 2016, for public consultation on 1 March 2016. The proposed amendments to the Income Tax Act are intended to allow Singapore to implement its international commitment to commence automatic exchange of financial account information (AEOI) in 2018. The MOF has announced that AEOI exchanges will be carried out on a bilateral basis with jurisdictions which has signed Competent Authority Agreements with Singapore, subject to the following:

- There is a level playing field among all major financial centres, including Dubai, Hong Kong, Luxembourg and Switzerland, to minimise regulatory arbitrage.
- Our AEOI partners are having strong rule of law and ability to ensure the confidentiality of information exchanged and prevent any unauthorised use of such information.
- There is full reciprocity with AEOI partners in terms of information exchanged.

In this regard, the MOF has indicated that Singapore will prioritise the implementation with jurisdictions with strong rule of law, such as the UK and France.

Conclusion

The global developments that are taking place at an unrelenting pace will chart the future of taxation. The successful implementation of measures to curb BEPS activities so as to create a level playing field among nations is dependent on coordinated international responses to abusive practices. It is equally important to having effective dispute resolution mechanisms in place to reduce obstacles to international trade in goods and services in form of double taxation. Reflecting its role as a financial centre and trading hub, Singapore is taking proactive, albeit cautious, steps to align with the new norms in international taxation. It now remains to be seen how the broad consensus in addressing BEPS concerns translates into concrete actions by individual countries.

Sri Lanka

Corporate income tax

Tax rates

- Concessionary tax rates, varying from 10% to 12%, have been consolidated to a single rate of 17.5%.
- The standard rate of 28% and the higher rate of 40% on tobacco and liquor businesses still apply.

Taxation of capital gains

Taxation of capital gains will be reintroduced from tax year 2016/17.

Personal income tax

Taxation of capital gains

Taxation of capital gains will be reintroduced from tax year 2016/17.

Economic service charge

Increase in tax rate

The economic service charge (ESC) is an alternative minimum income tax though it is turnover based. The ESC rate has been increased from 0.25% to 0.5% for liable turnovers.

Offsetting economic service charge against income tax

The period for carry forward of ESC to offset against income tax payable has been shortened from five years to three years.

Ceiling on chargeability to ESC

The ceiling on chargeability to ESC of LKR120 million per year has been removed.

Removal of exclusion

Present exclusion of profit making businesses from the charge to ESC has been removed. Accordingly, ESC should be paid by every person or partnership in respect of the relevant turnover of any trade, business, profession or vocation and not limited to a person or partnership which is tax exempt or incurs a tax loss, as before the change.

These changes to the ESC are effective from 1 April 2016.

Value added tax

Increase in tax rate

The value added tax (VAT) rate will be increased from 11% to 15%.

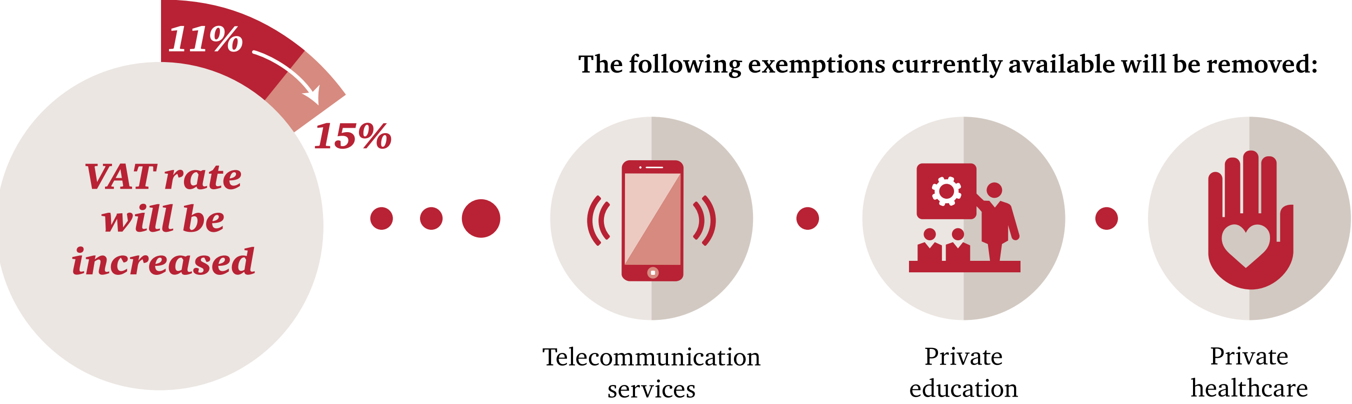
Exemptions

The following exemptions currently available will be removed:

- Telecommunication services
- Private education
- Private healthcare

Value added tax on wholesale or retail trade

The concept of 'deemed supplies' whereby a specified percentage of 'exempt supplies' was brought within the charge to VAT on wholesale or retail trade was removed.



Nation building tax

Registration threshold

The threshold of liable turnover for the nation building tax (NBT) has been reduced from LKR3.75 million per quarter to LKR3 million per quarter.

The threshold of LKR25 million per quarter previously applicable to the following has been removed:

- Operates a hotel, guest house, restaurant or other similar business
- Provides educational services through establishing a local institution
- Supplies labour (i.e. manpower)

Customs duty

The customs tariff structure has been simplified into three rate bands.

Raw materials and items of machinery	0%
Intermediate goods and spare parts	15%
Motor vehicles and other finished goods	30%

This rate change is effective from 20 November 2015.

Ports and airports development levy

The ports and airports development levy (PAL) rate has been increased from 5% to 7.5%. For certain electronic and electrical items, the rate has been decreased to 2.5%.

These changes to the PAL are effective from 20 November 2015.

Stamp duty

- Stamp duty at 1.5% on credit card usage for local purchasing has been removed. The stamp duty for credit card usage on overseas purchases has been increased to 2.5%.
- Stamp duty chargeable on issue and transfer of shares has been removed.

These changes to the stamp duty are effective from 1 January 2016.

Land (restriction on alienation) tax

The tax on leasing of land to foreigners levied at 15% of the full rental value over the whole term of the lease agreement has been removed.

The restriction placed on ownership of land by foreigners on certain investments has also been removed.

These changes to the land (restriction on alienation) tax are effective from 1 January 2016.

Miscellaneous taxes

The following taxes have been removed:

- Share transaction levy
- Construction industry guarantee fund levy
- Luxury and semi-luxury motor vehicle tax
- Tourism development levy

These tax removals, other than the removal of the tax on luxury and semi-luxury motor vehicle, are effective from 1 January 2016. The tax on luxury and motor vehicle has been removed from 1 April 2016.

Taiwan

Entities selling business tax exempt goods or services may switch to taxable status retroactively if certain conditions are met

According to Article 8 of the Business Tax Act, business entities selling business tax exempt goods or services must apply to the Ministry of Finance (MOF) to waive this exemption. They must also calculate their business tax before they can issue Government Uniform Invoices (GUI) bearing 5% value added tax (VAT).

On 7 May 2015, the MOF issued Tax Ruling No. 10304633410 and announced that where a business entity has not obtained pre-approval to waive its VAT exemption status but has already issued GUIs bearing 5% VAT and reported the taxable sales amount in VAT returns, the entity may be approved to waive its VAT exemption status. This approval is based on the premise that no business tax evasion is involved and guidance received from the competent authority after submitting the required application documents to waive the VAT exemption status.

Once an approval is obtained, the waiver may be applied retroactively to the period when the GUIs were first reported. No changes to a business' taxable status may be made within three years once the VAT exemption status is changed to taxable status and approved by the MOF.

Head offices and underlying branches should issue GUIs separately for goods or services sold

A head office and its underlying branches are regarded as different business entities and each entity must issue GUIs separately for goods or services actually sold. Otherwise, penalty will be imposed.

Scenario	Penalty
Company A is an entity running franchise shops that sell drinks, and has set up a branch, Branch B. To expand its business, Company A recently established a new branch, Branch C. As Branch C was unable to complete its business registration on time, Branch C issued GUIs in Branch B's name when selling drinks to customers.	Penalties for underreporting VAT or failing to provide the correct GUIs to purchasers, whichever is higher, will be imposed on Branch C. • Penalties for tax evasion: Pursuant to Article 51 of the Business Tax Act, the taxpayer will be fined no more than five times the amount of taxes under-reported. • Penalties for failing to provide proper GUIs to purchasers: As Branch C failed to provide GUIs issued in its own name to customers, a fine equivalent to 5% of the total sales amount will be imposed in accordance with Article 44 of the Tax Collection Act.

New Real Property Tax regime in Taiwan

The Legislative Yuan passed amendments to the Income Tax Act (ITA) and Article 6-1 of the Specifically Selected Goods and Services Tax Act (i.e. 'Luxury Tax Act') on 5 June 2015. Effective from 1 January 2016, these amendments introduced a new Real Property Tax regime and sales of land or building in Taiwan will no longer be taxed under the Luxury Tax Act.

A summary of the new Real Property Tax regime for profit-seeking enterprises is as follows (individual income tax implications are not included below):

Item	Description
Taxation scope	• Sales of any of the following after 1 January 2016 will be subject to the new Real Property Tax regime, except where various criteria are met (please refer to the 'Exclusions' section below): – Building – Building and land where the building is situated thereon – Land eligible for being granted a construction permit • Exclusions: If the building or land is sold after 1 January 2016, and meets any of the following criteria, the sale will be subject to the current taxation regime* instead: – Building or land was acquired prior to 2 January 2014 – Building or land was acquired on or after 2 January 2014, but before 1 January 2016, and has been held for over two years *Note: Under the current taxation regime, income tax is only levied on the sale of building, with sale of land being exempt from income tax and subject to land value incremental tax instead.
Tax base	Proceeds from sale of building or land minus: • Costs • Expenses • Total amount of land value increment calculated based on the Land Tax Act, i.e. the tax base of land value incremental tax
Tax rate	• Taiwanese profit-seeking enterprises: 17% (same as current taxation regime) • Profit-seeking enterprises with foreign head-offices located outside of Taiwan, i.e. Taiwan branch: – Building/land held for no more than one year: 45% – Building/land held for over one year: 35%
Taxation method	• Taiwanese profit-seeking enterprises: Combined with annual corporate income tax return filings (same as current taxation regime) • Foreign head-offices of Taiwan branches: Tax of the foreign head-office should be calculated separately by the Taiwan branch according to the prescribed tax rate, and reported in the Taiwan branch's annual corporate income tax return.

Amendments to the Business Mergers and Acquisitions Act

The amended Mergers and Acquisitions (M&A) Act (passed by the Legislative Yuan on 15 June 2015) has significant impacts on companies that undergo a merger, an acquisition, or a reorganisation from 8 January 2016. The key points of the amendments are summarised as follows:

Relax the limitation imposed on types of consideration acceptable in M&A transactions

- In addition to issuance of new shares, cash or other assets can also be used as consideration in a share exchange or spin-off.
- Different combinations or types of consideration can be distributed to different shareholders, provided that the consideration received by each shareholder is of equal value.
- The 'triangular merger' commonly seen in the U.S. is introduced to eliminate the pre-emptive rights of employees and existing shareholders to subscribe new shares, where a parent company issues new shares as consideration for its subsidiary's M&A transaction.

Simplify M&A procedures to increase efficiency

- Simplified M&A: For merger between sister companies with a common parent company (which owns at least 90% of the shares of the sister companies), share exchange between a parent company and its 90% or more owned subsidiary, and spin-off where a subsidiary transfers assets to its parent company, the resolution procedure via shareholders' meeting for both counterparties is waived.
- Asymmetric M&A: when the number of shares newly issued as consideration for share exchange or spin-off does not exceed 20% of the company's total outstanding voting shares, and the total value of cash or other assets given as consideration does not exceed 2% of the company's net asset value, the resolution procedure via shareholders' meeting is waived.
- The simplified M&A models are summarised as follows:

Merger	Simplified merger between parent and subsidiary	Article 19 (newly added)
	Simplified merger between sister companies	Article 19 (newly added)
	Asymmetric merger (acquiring party)	Item 7, Article 18 (newly added)
Share exchange	Asymmetric share exchange (acquiring party)	Item 6, Article 29 (newly added)
	Simplified share exchange between parent and subsidiary	Article 30 (newly added)
Spin-off	Asymmetric spin-off (acquiring party)	Article 36 (newly added)
	Simplified spin-off between parent and subsidiary	Article 37 (newly added)

Enhance protection of rights and interests of shareholders, employees, and creditors

- A public company, before holding a board meeting for M&A resolution, shall set up a special committee to evaluate the M&A transaction, and report the results to the board of directors and shareholders. For a company that has already set up an audit committee, the aforementioned evaluation shall be conducted by the audit committee.
- Strengthen the right of dissenting shareholders to require the company to buy back their shares: when a company and the dissenting shareholders are unable to reach a consensus on the buyback price, the company must take the matter to court to determine the fair price of the shares. The company shall first pay the dissenting shareholders the deemed fair price, and then pay the difference once the court determines the fair value of the shares.
- In the case where a public listed company becomes delisted due to an M&A transaction, or the surviving or newly incorporated company is not publicly listed, the M&A transaction is subject to consent by shareholders representing two-thirds or more of the total number of shares issued by the public listed company.
- When a director of a company has conflict of interests in an M&A transaction, the director must explain to the board of directors and shareholders' the important details of the conflict of interests, as well as the reason in favor of or against the M&A transaction.
- If a company acquires more than 10% of the total shares issued by a public company for the purpose of effecting the M&A transaction, the company must report to the securities and exchange authority within ten days of the acquisition. Failure to do so will result in loss of voting rights of the acquired shares exceeding 10% of the total shares issued.

Amendments to the relevant tax benefits provided

To be in line with the loss carryforward period which was extended to ten years under the ITA as well as the diversification in the types of consideration available for M&A transactions, several tax benefits are amended or added as follows:

Revision	Statutes
Deferral/exemption of transaction taxes: • If shares with voting rights are used as consideration for spin-off, the value of such shares must now not be less than 65% of the total consideration. This requirement must continue to be met during the three years after the land title has been transferred and the land value increment tax has been deferred. • The deferral/exemption is also applicable to a parent company acquiring a 90% owned subsidiary via share exchange.	Article 39 (formerly Article 34)
The loss carryforward period is extended from five to ten years.	Article 43 (formerly Article 38)
Corporate income tax may be exempted in a spin-off if the value of the voting shares acquired constitutes not less than 80% of the total consideration and the shares are all transferred to the shareholders.	Article 44 (formerly Article 39)
A parent company holding 90% or more of the total number of shares issued by a subsidiary as a result of M&A transactions, including via share exchange, may elect to file a consolidated corporate income tax return for itself and its Taiwanese subsidiaries beginning from the fiscal year in which it holds the subsidiary for 12 months within a given tax year.	Article 45 (formerly Article 40)

Tax ruling on tax deductibility of pension expense due to appropriation of labour pension reserve fund

According to Article 56 of the Labour Standards Act (LSA), amended on 4 February 2015, profit-seeking enterprises must assess the balance in the designated labour pension reserve fund account before the end of each year. If the amount is insufficient to pay pension liability due to employees who become eligible for retirement in the subsequent year according to Article 53 or Article 54 of the LSA, the employer is required to make up the difference in one lump-sum amount before the end of March of the following year.

Since the one-time appropriation required by the amended LSA may result in pension expense exceeding the 15% tax deductible limit prescribed in Article 33 of the ITA, the MOF issued Tax Ruling No. 10400608350 on 10 November 2015 to clarify that the appropriation to labour pension reserve fund in accordance with the amended LSA can be fully tax deductible in the same year without taking into consideration the 15% tax limit.

Amendments to the 'Statute for Industrial Innovation'

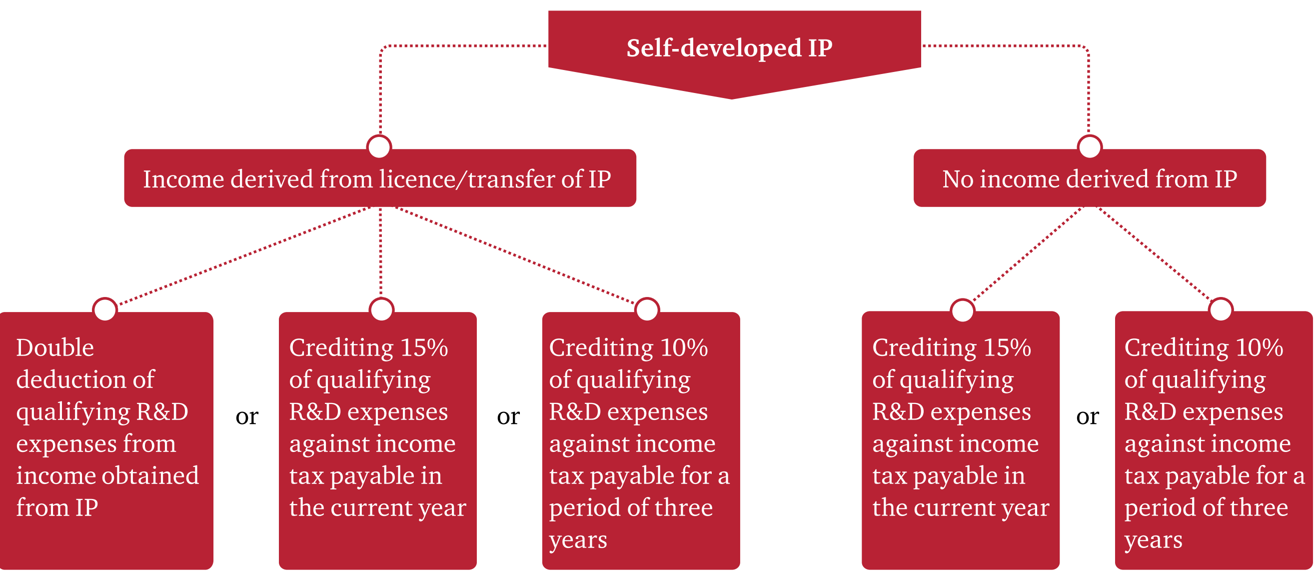
Considering the serious outflow of domestic talent and Taiwan's insufficient technical capability in recent years, the Legislative Yuan passed amendments to the Statute for Industrial Innovation on 15 December 2015. The amendments are effective from 1 January 2016 to 31 December 2019 and aimed at enhancing the competitive advantage of domestic industries. The key points of the amendments are summarised as follows:

Double deduction or investment tax credits for research and development expenses

The amendments to the Statute for Industrial Innovation provide an alternative for companies to claim research and development (R&D) credit of 10% of qualifying R&D expenses against income tax payable within a period of three years starting from the current year.

These amendments encourage continued investment in innovative R&D activities, meet the actual needs of different industries and achieve policy results. In addition, these amendments facilitate the circulation and application of innovative R&D results, and promote industrialisation of innovative technologies. This is particularly true in areas where individuals/companies derive income from transfer or license of their self-developed intellectual property (IP).

The amendments also allow the individuals/companies to either deduct qualifying R&D expenses up to 200% (capped at the corresponding income derived from the IP) in the current year or claim R&D tax credits against income tax payable.



Five-year income tax deferral for employee share-based compensation schemes

Given talents are the key element of industrial development, to assist companies in retaining talents as well as to encourage employees to participate in company operations and share business profits, employees who are granted share-based compensation (where the annual fair market value of the shares granted is equal to or less than NTD5 million) may elect to defer the income tax payable on the share-based compensation to the fifth year starting from the year following receipt of the share based compensation. No revocation is allowed once an individual has elected to defer income tax payable on the share-based compensation.

- **Applicable scope:** All major types of share-based compensation, including stock grants, subscription right to capital increase using cash, treasury stocks, stock option certificates and restricted stock units, are eligible for the tax deferral.
- **Applicable persons:** Employees of both the company that issues the share-based compensation mentioned above, and its qualified subsidiaries (i.e. where the invested shares of the subsidiary exceed 50% of the total outstanding voting shares of the subsidiary, or the paid-in capital of the subsidiary exceeds 50% of the total paid-in capital of the subsidiary) are eligible for the tax deferral. Chairman, members of the board of directors, and supervisors that concurrently serve managerial positions are excluded.
- **Restriction:** Employees receiving share-based compensation may elect either a full deferral or no deferral of income tax payable. Partial deferral of income tax payable is not available. If the title of the shares obtained from share-based compensation scheme is transferred through sale, gift, inheritance, stock cancellation due to capital reduction, liquidation, or if the shares are transferred from marketable securities book-entry custody account held by the company to securities account held by the employees during the tax-deferral period, the employees will be taxed in the year in which the share title is transferred or when the shares are transferred from company held book-entry custody account to employee held securities account.

Thailand

Development in tax laws and regulations from March 2015 to January 2016

Significant tax measures announced over the past year include continuous reduction of personal income tax, corporate income tax and value added tax rates and imposition of an inheritance tax and a gift tax. In addition, various tax incentives and measures to encourage tax compliance under the Revenue Code have been introduced.

Reduction of tax rates

Personal income tax rates

The following reduced personal income tax rates are effective for one more tax year until 31 December 2016.

Net income (THB)	Tax rate
0 – 150,000	Nil
150,001 – 300,000	5%
300,001 – 500,000	10%
500,001 – 750,000	15%
750,001 – 1,000,000	20%
1,000,001 – 2,000,000	25%
2,000,001 – 4,000,000	30%
Over 4,000,000	35%

Corporate income tax rate

The corporate income tax rate of 20% was treated as a temporary reduction of the statutory rate of 30% under the Revenue Code since 2013. The statutory rate has now been officially changed to 20% under the Revenue Code for accounting periods beginning on or after 1 January 2016.

Corporate tax rates for small and medium-sized enterprises

Tax rates for small and medium-sized enterprises (SMEs) were announced during the year. For accounting periods beginning on or after 1 January 2015, the tax rates are as follows:

Net profit (THB)	Tax rate
0 – 300,000	Nil
300,001 – 3,000,000	15%
Over 3,000,000	20%

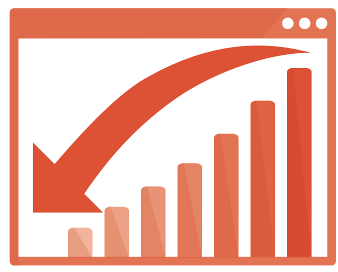
To be eligible for the reduced tax rates, a corporation must meet the following conditions:

- Paid-up capital on the last day of any accounting period must not exceed THB5 million; and
- Income from the 'sale of goods and provision of services' must not exceed THB30 million in any accounting period.

In October 2015, the Thai Cabinet approved to replace the above SME corporate tax rates with a single rate of 10% applicable to net profits exceeding THB300,000 for two accounting periods beginning on or after 1 January 2015 but not later than 31 December 2016. However, at the time of writing, the relevant Royal Decree has not yet been issued.

Value added tax rate

The 10% standard rate of value added tax (VAT) has been reduced to 7% until 30 September 2016. Unless the applicable period of the reduced rate is extended, the rate will revert to 10% on 1 October 2016.



Rates of personal income tax, corporate income tax and value added tax are reduced.

Inheritance tax and gift tax

The Inheritance Tax Act and the Revenue Code Amendment Act (gift tax) became law on 5 August 2015 and effective from 1 February 2016.

Inheritance tax

A legacy received by an individual or a juristic entity, regardless of the individual's or the entity's nationality, from a deceased testator is exempt from personal income tax under the Revenue Code but will be subject to inheritance tax. Heirs will be subject to the inheritance tax on the value of a legacy that exceeds THB100 million obtained from one testator on either one or several occasions.

The inheritance tax rate is 10% except in the cases where the heirs are an ascendant or a descendant of the deceased testator, in which case the rate is 5%. A legacy received by the spouse of a deceased testator is exempt from the tax.

Property subject to the inheritance tax is immovable property, securities as defined in the Securities and Exchange Law, bank deposit accounts or other money of a similar nature which the testators have the right to call back or claim from financial institutions or persons holding the money, registered vehicles and financial assets to be prescribed in Royal Decrees.

Gift tax

The Revenue Code Amendment Act introduces a gift tax which is levied when a gift is given by a living person. The gift will be subject to personal income tax under the Revenue Code. The tax is collected on assets or money given to parents, ascendants, descendants, spouse or others as a gift and based on the value of the gift when the prescribed threshold is exceeded, which depends on the type of gift and donor. The assets or money given that do not exceed the threshold are exempt from personal income tax.

The following gifts are exempt from personal income tax:

- The deemed income derived by a parent from the transfer of ownership or possessory right in an immovable property without any consideration to a legitimate child (excluding an adopted child), but only up to the portion of income not exceeding THB20 million throughout a tax year.
- Maintenance income or gifts from ascendants, descendants or spouse, but only up to the portion of income not exceeding THB20 million throughout a tax year.
- Maintenance income obtained under a moral obligation or gifts made in a ceremony or on occasions in accordance with established custom from persons that are not ascendants, descendants or spouse, but only up to the portion of income not exceeding THB10 million throughout a tax year.
- Income from gifts where the persons receiving the gifts use them for religious, educational or public benefit purposes according to the intention of the donors under the criteria and conditions mentioned in the Ministerial Regulations.

Income/gifts in excess of the thresholds noted in items 1-3 above will be subject to personal income tax at the rate of 5%.

Tax incentives

Tax incentives for international headquarters

Tax incentives that attract firms to establish international headquarters (IHQs) in Thailand became effective on 2 May 2015. These new IHQ incentives are intended to make Thailand an attractive investment centre for multinational companies.

An IHQ is defined as a company incorporated under the law of Thailand for the purpose of providing managerial, technical or supporting services or financial management to its associated enterprises or branches situated in Thailand or abroad. An IHQ can also carry on a business as an international trading centre (see 'tax incentives for international trading centre' below).

The criteria for being an IHQ are as follows:

- A company formed under the Thai law with minimum paid-up capital of THB10 million.
- Managerial, technical or supporting services (and financial management in the case of treasury centres as stated below) are provided to foreign affiliates (companies with at least 25% common group ownership, directly or indirectly).
- Operating expenses related to IHQ activities are of at least THB15 million per year.

The tax concessions are as follows:

- 10% corporate income tax on net profit from qualified services provided to domestic affiliates and royalties derived from domestic affiliates.

- Full corporate income tax exemption on net profit from qualified services provided to foreign affiliates, royalties and dividends derived from foreign affiliates and capital gains from the transfer of shares in foreign affiliates (subject to certain conditions).
- Withholding tax exemption on dividends paid to foreign corporate shareholders from the tax exempt net profit Expatriates employed by an IHQ can choose to be taxed at a flat rate of 15% from the date the IHQ becomes qualified until the date the IHQ is no longer qualified or the employment is terminated.

Other features of the tax incentives are as follows:

- A qualified IHQ will be granted the above tax privileges for 15 accounting periods.
- The total income subject to tax at the 10% rate must not exceed the total income from qualified services and royalties which are exempt from tax.
- If an IHQ becomes disqualified in any accounting period, the right to the tax privileges will be suspended only for that accounting period.

Tax incentives for treasury centres

Effective from 2 May 2015, an IHQ that has obtained a treasury centre (TC) licence from the Bank of Thailand can request approval from the Revenue Department for enjoying the tax concessions available for carrying on a business of financial management for its associated enterprises or branches situated in Thailand or abroad.

Financial management includes the following:

1. Financial management of a TC permitted under the law governing exchange control.
2. Borrowing and lending of Thai currency in the following cases:
    a. borrowing of funds from Thai financial institutions or affiliates in Thailand; and
    b. lending of funds obtained from the operations in 1 or 2 (a) in Thai currency to affiliates in Thailand.

The tax concessions are as follows:

- withholding tax exemption on interest paid to foreign companies not carrying on business in Thailand on loans borrowed for re-lending to affiliates;
- exemption from specific business tax on interest received from loans to affiliates; and
- other tax concessions available for the TC activities are the same as those for IHQs discussed above.

A qualified TC will be granted the above tax privileges for 15 accounting periods. The criteria for being a TC are the same as those for an IHQ as discussed above.

If a TC becomes disqualified in any accounting period, the right to the tax privileges will be suspended only for that accounting period.

Tax incentives for international trading centre

The regulations regarding the international trading centre (ITC) regime became effective on 2 May 2015. Tax incentives are granted under the regulations to attract firms to establish ITCs in Thailand.

An ITC is defined as a company established under the law of Thailand and engaging in the business of buying and selling goods, raw materials and parts, including providing services relating to international trade to foreign juristic entities. Services relating to international trade include procuring goods, maintaining goods awaiting delivery, packaging, transporting goods, providing insurance for goods, providing technical services and training relating to goods, and providing other services as prescribed by the Director-General of the Revenue Department.

An IHQ is entitled to obtain an approval for carrying on a business as an ITC and enjoying the tax concessions for an ITC.

The criteria for being an ITC are as follows:

- a company formed under the Thai law with minimum paid-up capital of THB10 million; and
- operating expenses related to ITC activities are of at least THB15 million per year.

The tax concessions are as follows:

- exemption from corporate income tax on income from buying and selling goods abroad without importing such goods into Thailand (out-out), including income from services relating to international trade provided to foreign juristic entities and received in or from a foreign country;
- withholding tax exemption on dividends paid to foreign corporate shareholders from the tax exempt net profit; and
- expatriates employed by an ITC can choose to be taxed at a flat rate of 15% from the date the ITC becomes qualified until the date the ITC is no longer qualified or the employment is terminated.

A qualified ITC will be granted the above tax privileges for 15 accounting periods.

If an ITC becomes disqualified in any accounting period, the right to the tax privileges will be suspended only for that accounting period.

Tax incentives for investment in special economic development zones

Special economic development zones (SEZs) are border areas, whether inside or outside of industrial estates, created to promote economic connectivity with the neighbouring countries and to prepare for entry into the ASEAN Economic Community (AEC).

In the first phase, SEZs include certain areas (sub-districts) in the provinces of Trat, Tak, Mukdahan, Songkla, and Sa Kaew.

In the second phase, SEZs include certain areas (sub-districts) in the provinces of Nong Khai, Kanchanaburi, Chiang Rai, Nakhon Phanom, Narathiwat.

Tax incentives for investment in these SEZs will be granted by both the Revenue Department and the Board of Investment (BOI).

Tax incentives granted by the Revenue Department

With effect from 10 September 2015, the corporate tax rate has been reduced to 10% for 10 years for juristic entities with a place of business in a SEZ regardless of where their head offices are situated. This tax rate applies to income earned from goods manufactured or services rendered and used in the SEZ.

Tax incentives granted by the Board of Investment

With effect from 1 January 2015, the BOI has granted tax incentives for investment in eligible target and general activities in a SEZ.

To be eligible for the tax privileges as a promoted entity in a SEZ, certain general and specific conditions must be fulfilled e.g. modern production processes and new machinery, paid-up share capital at the required amount, adequate environment protection systems, debt to equity ratio not exceeding 3:1 and required area for operating the business.

Tax incentives for eligible target activities are as follows:

- exemption from corporate income tax for a period of eight years, with the maximum corporate income tax exemption not exceeding 100% of the investment cost (excluding the cost of land and working capital);
- 50% reduction in the corporate income tax rate for five years, commencing from the date on which the tax holiday expires;
- double deduction of transportation, electricity and water supply costs for a period of 10 years, commencing from the date on which revenue begins to be generated from the business;
- 25% deduction of the investment cost of the installation or construction of facilities in addition to normal depreciation;
- exemption from import duty on machinery; and
- exemption from import duty on raw materials and essential goods used in the production of goods for export for a period of five years.

In addition, permission will be granted to employ foreign unskilled workers in promoted projects according to the conditions prescribed by the BOI.

Tax incentives for eligible general activities are as follows:

- additional corporate income tax exemptions for three years, but not exceeding eight years in total;

- 50% reduction in the corporate income tax rate for five years, commencing from the expiry date of the applicable tax holiday; and
- other incentives are the same as those for the eligible target activities.

The application for the above tax incentives must be submitted by 31 December 2017.

Measures to encourage tax compliance under the Revenue Code

No tax audits for certain companies and juristic partnerships

With effect from 1 January 2016, tax audits and assessments (including the related criminal fines that may be imposed according to the Revenue Code) will be waived for companies and juristic partnerships that are subject to corporate income tax on net profit (instead of gross income) in respect of:

- corporate income tax for accounting periods beginning before 1 January 2016;
- value added tax and specific business tax for tax bases occurring before 1 January 2016; and
- stamp duty for instruments executed before 1 January 2016.

To be eligible for this waiver, the companies and juristic partnerships must meet the following conditions:

- Revenue earned must not have exceeded THB500 million in the past full 12-month accounting period which ended on or before 31 December 2015.
- Registration must be made through the website of the Revenue Department between 15 January 2016 and 15 March 2016.
- Any tax returns due from January 2016 onwards must be filed and any related taxes must be paid.
- Bookkeeping and financial statements must be prepared in accordance with the actual results of the business for the accounting periods beginning on or after 1 January 2016.
- There must be no action taken from 1 January 2016 onwards that indicates an evasion of tax.

Any company and juristic partnership that has registered and been granted a waiver of tax audit will not be entitled to the waiver in certain cases e.g. a summons for tax investigation has been issued before 1 January 2016, a tax refund claim has been submitted in respect of a period prior to 1 January 2016, fake tax invoices have been issued or used and tax cases involving the company/juristic partnership are still under legal process.

If a company or juristic partnership obtaining a waiver of tax audit fails to comply with the above conditions, the Director-General of Revenue will revoke the waiver. Such entity will then be treated as if it never received a waiver.

Tax exemption and reduction for small and medium-sized enterprises

SMEs which have registered for the above waiver of tax audit are entitled to obtain additional benefits in the form of income tax exemption and reduction.

To be eligible for these benefits, the SMEs must meet the following conditions:

- Paid-up capital on the last day of any accounting period must not exceed THB5 million.
- Income from the sale of goods and provision of services must not exceed THB30 million in any accounting period.
- Registration for a waiver of tax audit must have been made as mentioned above.
- The waiver of tax audit must not have been revoked.

The exemption from and reduction in the rate of corporate income tax granted to qualifying SMEs established before 1 January 2016 are as follows:

- For the accounting period beginning between 1 January 2016 and 31 December 2016, all net profit will be exempt from corporate income tax.
- For the accounting period beginning between 1 January 2017 and 31 December 2017, the rate of corporate income tax will be:

Net profit (THB)	Tax rate
0 – 300,000	Nil
Over 300,000	10%

- For accounting periods beginning on or after 1 January 2018, the tax rates will revert to the previous rates, which are:

Net profit (THB)	Tax rate
0-300,000	Nil
300,001-3,000,000	15%
Over 3,000,000	20%

Vietnam

Top current tax issues

Taxing foreign companies

Transfer pricing

Tax audits

Compared with recent years, there were relatively fewer legislative developments in the tax system in Vietnam over the last year. However, it does not mean that things were static as the process of bedding-down and implementation of changes continue, and various new tax initiatives are bringing significant implications to taxpayers. Below are the top three current tax issues in Vietnam.

Expanded scope of foreign contractor tax

In the past, although there are various regulations on taxation of permanent establishment (PE) in the tax law of Vietnam, foreign contractor tax (FCT) is imposed on foreign companies deriving income from Vietnam in the form of withholding taxes in practice. In late 2014, a new withholding tax regulation, which dramatically widens the scope of taxable supplies to Vietnam, was introduced.

The new regulation, Circular 103/ TT-BTC dated 6 August 2014 (Circular 103), widens the scope of such withholding tax (i.e. FCT) to include certain supplies of goods which was previously outside the scope of withholding tax. In particular, when a foreign supplier is involved in the onshore distribution and is responsible for price setting, advertising, monitoring the quality of the goods, etc., the sales could now be subject to withholding tax.

It is interesting to review how companies have reacted to this new regulation after implementation.

In some cases, the overseas supplier has sought protection from withholding tax under a tax treaty on the basis that there are no profits attributable to a PE in Vietnam. Such claims are made on a self-assessment basis, so the view of the tax authorities on such claims has generally not been tested yet. However, where the overseas supplier has any onshore presence, e.g. a representative office, the activities performed onshore may be scrutinised during future tax audits. Therefore, eligibility for treaty protection in this regard needs to be carefully assessed.

In other cases, the overseas suppliers may consider the insertion of an intermediate overseas entity into the supply chain to ring-fence the roles and functions which create tax exposures under Circular 103. If structured properly, this could substantially reduce the tax exposure, particularly if the overseas entities are also residents of tax treaty partner jurisdictions.

This is still a new and developing area and the Ministry of Finance is proposing to amend, and possibly rein-back, some of the more contentious provisions in Circular 103. For companies providing goods and/or services to Vietnamese customers, this will be an important area for ongoing monitoring.

Developments in transfer pricing

Vietnam's transfer pricing environment continues to develop with a steady increase in tax audit activities concerning transfer pricing, even though there are fewer tax audit activities carried out in Vietnam and these activities are comparatively less sophisticated when compared with some other countries in the region.

Below are the two significant developments in transfer pricing since the last issue of *Asia Pacific Tax Notes*:

- In late 2015, specialist transfer pricing teams were established in the tax authorities in four key provinces, including Ho Chi Minh City, Hanoi, Binh Duong and Dong Nai. These teams are tasked inter alia with conducting transfer pricing focused investigations on companies, as well as dealing with Mutual Agreement Procedure cases and applications for Advance Pricing Agreements (APAs).
- Vietnam's APA regime continues to develop with three official submissions (all bilateral) currently under review.

Some new tax audit approaches

Recently there have been many giveaways on the tax front, including reduction in the corporate income tax rate, introduction of various corporate income tax incentives and removal of the cap on the tax deductibility of advertising and promotion expenses.

These giveaways require substantial money from the State, so a tougher approach of tax audits through the involvement of the State Auditor is expected.

The State Auditor is a body established by and reporting to the National Assembly. Its main functions include auditing the performance of agencies and institutions which manage and use the State budget funds and assets.

What has been observed over the last year is the State Auditor has conducted reviews of the work of the provincial tax authorities, specifically the results of the tax audits performed by them. Typically, the State Auditor will focus on specific high value and contentious areas, including the claiming of corporate income tax incentives and withholding taxes, etc.

While the State Auditor is in principle reviewing the work of the provincial tax authorities and focuses on the prior tax audits of taxpayers, the State Auditor may disagree with the provincial tax authorities on the results of the tax audits and seek to re-assess taxes. Therefore, the years which have already been audited may be opened up again and taxpayers may have to contend with a new re-assessment of certain issues and years which were expected to be already 'closed'.

In other cases, the State Auditor has approached companies directly to review certain areas. Again, this is often conducted for periods which have already been subject to tax audits conducted by the provincial tax authorities. The State Auditor will instruct the provincial tax authorities to collect the taxes that they believe are due. In practice, taxpayers may have to deal with both the State Auditor and their local tax authority to resolve these issues.

The taxes being re-assessed could be substantial, with the impact compounded by the imposition of interest on the tax overdue at 18% per annum and statutory penalties.

Given the loss caused to the State budget by the various tax reductions, concessions and free trade agreements, a tougher tax audit approach is certainly anticipated. As ever, companies which are well-prepared with a robust technical defense and sufficient supporting documentation should have the least to worry about.

Another key development has been an increase in post-clearance audits performed by the customs authority. These audits have led to a dramatic increase in tax collections as re-assessments have been commonly made in relation to classification, valuation, origin and export production/toll manufacturing (liquidation, consumption norms issues, etc.).

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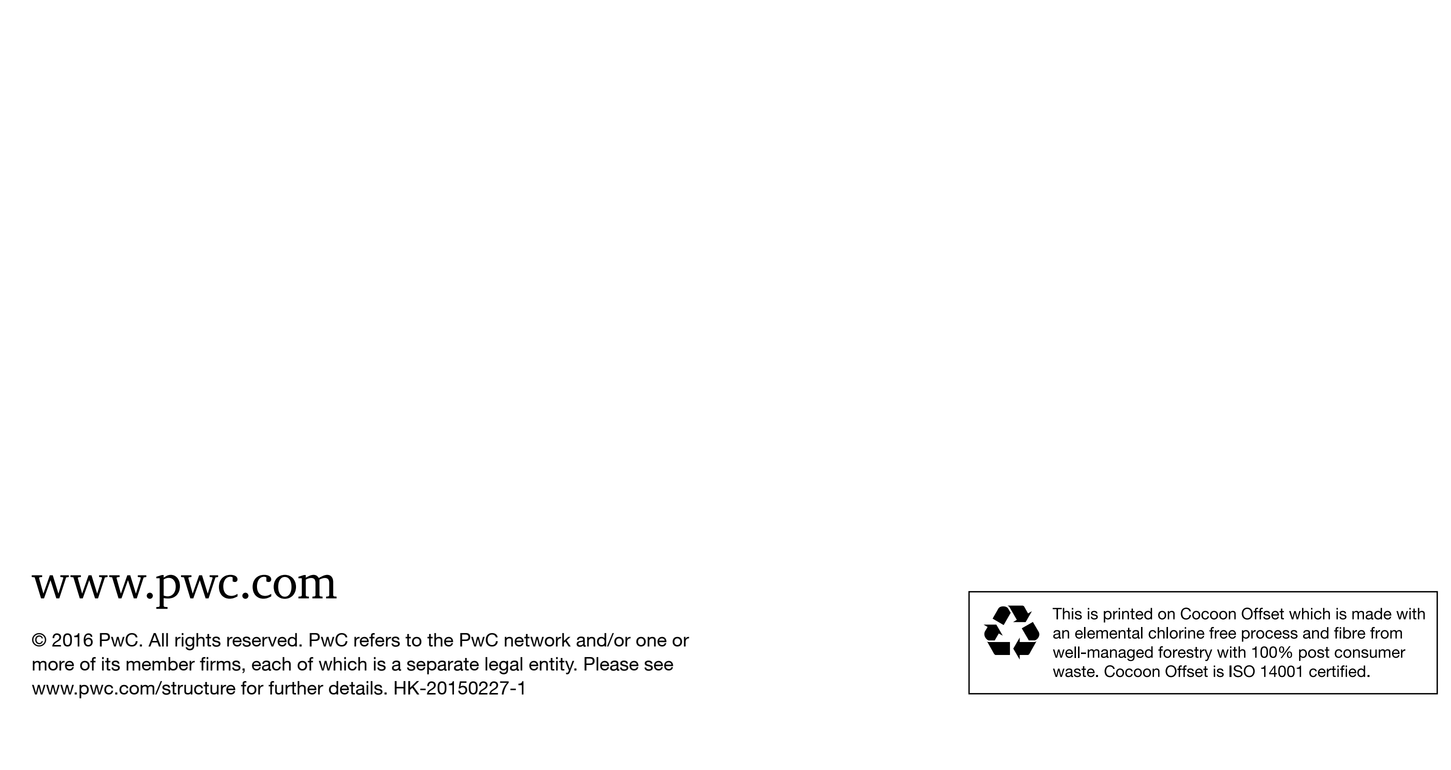

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