

Asia Financial Services Tax Quarterly Developments Report

January to March 2007



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Introduction

For a number of years the PricewaterhouseCoopers Financial Services tax network in Asia has been sharing within the network a quarterly report on tax developments. We have now decided to share this knowledge with clients.

This PwC Asia Financial Services Tax Quarterly Developments Report covers the period ended 31 December 2006. It very briefly lists tax developments in the Asia region that are relevant to financial services operations.

The report is sorted by Asian territory. Please contact your local PwC tax adviser if you wish to obtain further information on any development listed in this report.

We hope you find the report useful. I would be delighted to receive comments on the report.

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Australia

Sector: Banking and Capital Markets

Date: January 2007

Contact: Jason Heng - Sydney

Taxation of Financial Arrangements (TOFA) stages 3 and 4 - exposure draft legislation released

The Government released for public comment a second exposure draft of a Bill to implement the remaining stages of reforms to the Taxation of Financial Arrangements (TOFA). The *Tax Laws Amendment (Taxation of Financial Arrangements) Bill 2007*, released by the Government on 3 January 2007, contains measures which:

1. Define what arrangements constitute a 'financial arrangement', and are therefore subject to the rules;
2. Removes the capital/revenue distinction by treating most financial arrangements on revenue account (ie assessable or deductible)
3. Propose new tax timing methods for allocating gains and losses to the relevant income years for tax purposes
4. Propose hedging rules designed to facilitate matching between the tax treatment of the gain or loss on the hedging arrangement and the underlying transaction.

The proposed rules will have potentially broad application to various financial arrangements; however, there are numerous exclusions from the scope of the rules. Also, there is an exclusion from the rules for individuals and entities with an annual turnover of less than AUD \$20 million in certain circumstances.

It is proposed that the new regime will mandatorily apply to income years beginning on or after 1 July 2008, however, taxpayers can elect to apply the rules for income years beginning on or after 1 July 2007. In addition, a taxpayer may elect to bring into the new regime all financial arrangements which existed prior to the relevant commencement date which the taxpayer continues to have at the start of that income year.

Sector: Banking and Capital Market

Date: March 2007

Contact: Jason Heng - Sydney

ATO Discussion Paper on equity override rule released

When a company obtains finance from an associate which itself obtained the finance from another party, there is a risk that, even though the finance obtained by the company satisfies the 'debt test', it may be classified as equity under what may be described as the 'equity override rule'. This rule is clearly relevant for financing arrangements involving corporate groups where finance is provided through a chain of entities within the group.

The ATO has released its preliminary views on the application of the equity override rule in a discussion paper dated 19 March 2007. The ATO's views are a serious concern for corporate Australia as it applies a literal interpretation of the words which would have the effect of treating many arrangements otherwise structured to be debt, as equity interests. Comments on this paper were due to be made by 27 April 2007.

Sector: Banking and Capital Market

Date: March 2007

Contact: Jason Heng - Sydney

Proposed interest withholding tax exemption measures omitted

Tax Laws Amendment (2006 Measures No. 7) Bill 2006, introduced into the House of Representatives on 7 December 2006, proposed changes to clarify the rules regarding the exemptions from interest withholding tax under section 128F and 128FA of the *Income Tax Assessment Act 1936*. The Bill was introduced into the Senate on 7 February 2007 and was debated and passed through the remaining stages in the Senate on 28 March 2007 with one Government amendment. The House of Representatives agreed to the amendment on 29 March 2007. The Bill ultimately received Royal Assent on 12 April 2007; however, the measures relating to the proposed exemptions from interest withholding tax were omitted from the final Bill (to be covered in the next edition of this report).

Sector: Property

Date: February 2007

Contact: George Stamoulos - Sydney

CGT and foreign resident rules: Impact of intra-group loans on the principal assets test

The CGT and foreign resident rules contained in Division 855 apply to disregard a capital gain or capital loss made by a foreign resident from a CGT event that happens in relation to a CGT asset that is not Taxable Australian Property (TAP).

The purpose of the division is to improve Australia's international competitiveness in attracting investment through ensuring interests in an entity remain subject to Australia's capital gains tax laws if the entity's underlying value is principally derived from Australia. The application of Division 855 requires the satisfaction of the following threshold tests:

1. Does the interest constitute TAP – an asset is TAP if one of the items in the table in s855-15 applies;
2. Does the interest pass the non-portfolio test as provided in s960-130 and s960-135 – this is satisfied if the sum of the direct participation interests held by the holding entity and its associates in the test entity is 10% or more. Direct participation interests in this context broadly refer to the greatest percentage that the entity holds, or is entitled to acquire, of the paid up share capital, rights to vote and rights to distribution of capital.
3. Does the interest pass the 'principal asset test' as provided in s855-30- this is broadly satisfied where the sum of the market values of the entity's TARP assets is greater than the sum of the market value of its non TARP assets.

Clients should be aware that there is an "anti-stuffing rule" (s855-30(5)) which applies to disregard the market value of any asset acquired if the acquisition was done for a purpose of ensuring failure of the 'principal asset' test.

Sector: Property

Date: February 2007

Contact: George Stamoulos - Sydney

Application of Div 6C to trusts with US REIT Subsidiary

The ATO is currently considering whether an Australian trust is subject to the public trading trust rules in Division 6C as a result of activities carried on by a US Real Estate Investment Trust (REIT) subsidiary. The nature of the activities carried on by the relevant entity must be examined to determine whether they constitute 'eligible investment business', specifically whether investment activities involve investing in land for the purpose, or primarily for the purpose of deriving rent and hence are not subject to the rules.

Clients investing or considering investment in business conducted by REITS in the US should consider the potential operation of these rules.

Sector: Property

Date: March 2007

Contact: George Stamoulos - Sydney

USA: Proposed model REIT statute disallows dividend paid deduction

The US Multistate Tax Commission Uniformity Committee recently heard a report regarding the drafting of model statutes on Real Estate Investment Trusts (REIT) featuring a disallowance of the dividends paid deduction otherwise allowed to REITs under federal law. If these models are introduced they could dramatically increase the overall rate of tax paid on REIT dividends subject to a few qualifications.

Sector: Insurance

Date: January 2007

Contact: Neil Toyer - Sydney

Income Tax

ATO Interpretive Decision: ATO ID 2007/41 - Life Insurance Company: Assessment of premiums "paid" to the company

A life insurance risk premium that is due but remains unpaid to a life insurance company at the end of the income year is included in assessable income under paragraph 320-15(1)(a) of the *Income Tax Assessment Act 1997* as an amount that has been "paid to the company".

Paragraph 320-15(1)(a) provides that assessable income of a life insurance company includes the total amount of life insurance premiums paid to the company in the income year.

The Commissioner considered the matching of cash flows with the movements in liabilities under the net risk components of policies in his decision. The net risk component of the life insurance policy was calculated on an accruals basis and hence concluded that the accruals basis should also be applied for insurance premiums receivable.

Sector: Insurance

Date: February 2007

Contact: Neil Toyer - Sydney

Income Tax

ATO Interpretive Decision: ATO ID 2007/27 – Assessability of periodic insurance payments received by an Australian resident from Denmark

The taxpayer and taxpayer's employer were Australian residents and contributed to an insurance policy issued by a Danish pension and insurance company.

The taxpayer received periodic insurance payments when the taxpayer's ability to work was reduced.

The Commissioner found that these foreign insurance payments received by the taxpayer from the Danish pension and insurance company were assessable under s6-5(2) of the *Income Tax Assessment Act 1997*.

Sector: Insurance

Date: March 2007

Contact: Neil Toyer - Sydney

Income Tax

ATO Interpretive Decision: ATO ID 2007/49 – Assessability of certain New Zealand worker's compensation payments made to an Australian resident

While employed in New Zealand, the taxpayer sustained a workplace injury. Subsequent to this, the taxpayer became an Australian resident.

The Commissioner found that the worker's compensation payments that the taxpayer received were assessable to the taxpayer under s6-5(2) of the *Income Tax Assessment Act 1997*.

Sector: Insurance

Date: March 2007

Contact: Neil Toyer - Sydney

Income Tax

Capital Gains Tax

Taxation Determination: TD 2007/4

TD 2007/4, previously issued as TD 2006/D36, sets out the Commissioner's view that the expression "policy of insurance on the life of an individual" in s 118-300 of the *Income Tax Assessment Act 1997 (ITAA97)* includes, but is not limited to, life insurance policies within the common law meaning of the term. The expressions also includes other life insurance policies (as defined in s995-1 of the ITAA97) to the extent that those policies provide for a sum of money to be paid if an event happens that results in the death of an individual.

The key points from the Appendix to TD 2007/4 are:

- The definition of a "life insurance policy" includes a range of policies that are not within the ambit of the common law meaning of the term.
- The term "life insurance policy" in s118-300(1) of the ITAA97 was replaced with the term "policy of insurance on the life of an individual", indicating that Parliament did not intend the terms to have the same meaning.
- A policy of insurance on the life of an individual" includes a life insurance policy to the extent that it provides for the payment of a "terminal illness benefit" (that is, being a benefit which is usually payable upon the diagnosis of an illness which will result in the death of an insured within 12 months)



China

Sector: All

Date: 16 March 2007

Contact: Matthew Wong - Shanghai

China Corporate Income Tax Law

On 16 March 2007 the National People's Congress (NPC), passed the long-awaited China Corporate Income Tax Law (CIT Law). This new regime earmarks the consolidation of two separate enterprise income tax regimes for domestic-invested enterprises (DEs) and foreign-invested enterprises (FIEs) into a single regime. It also provides for a fundamental change in China's tax incentive policy in shaping and directing the future development of the country.

The CIT Law, which contains 8 chapters and 60 articles, will come into effect on 1 January 2008. It mainly provides a framework of general tax provisions. Important details on the definition of numerous terms as well as the interpretation and specific application of various provisions are left to the detailed implementing regulations to be formulated and released by the State Council within this year. The key changes resulted from the new CIT Law are summarised below:

Concept of Tax Resident Enterprise (TRE)

- TRE concept is introduced whereby TREs are subject to China income tax on worldwide income, and non-TREs on China source income
- FIEs registered in China are always TRE
- Foreign Enterprise (FE) whose effective management institute is based in China is regarded as a "TRE". This new concept goes beyond the current "Permanent Establishment" concept which only taxes FEs on their China source income.

Tax Rate – FIEs

- Standardised rate of 25%, with a reduced rate of 20% for qualified small & thin-profit companies.
- 15% for encouraged high/new-tech enterprises.
- FIEs approved before the publication date of the CIT Law and currently taxed at 15% or 24% will be offered a gradual increase to 25% within 5 years.

Tax Rate – FEs

- 20% withholding tax (WHT) rate for passive income derived by Non-TREs.

Tax Incentive Policies

- Tax reduction and exemption treatments are targeted primarily towards (i) agriculture, forestry and animal-husbandry, fishery projects, (ii) basic infrastructure projects; (iii) environment protection projects and energy/water conservative projects; (iv) qualified technology transfer.
- A "Super deduction" is allowed for R&D expenses for new technology, new products, new craftsmanship.
- Taxable income may be reduced by a deemed deduction calculated as a percentage of investment amounts for venture capital business engaged in encouraged industries.

- Shorter tax depreciation life or accelerated depreciation is allowed for particular types of fixed assets due to technology advances.
- A reduction allowance may be available for revenue earned from products manufactured with comprehensive resources pursuant to the State industry policies.
- Investment tax credit will be available on qualifying expenditures on plant and machinery for environmental protection, energy and water conservation and production safety.

Grandfathering of Previous Preferential Tax Treatments

- Unused tax holiday of approved FIEs will be established before CIT Law is grandfathered until expiry. Where the tax holiday has not yet started because of tax losses, it shall be deemed to commence from the first effective year of Unified CIT Law.
- New FIEs which engage in high/new-tech industries are encouraged by the State and located in SEZs, and Pudong may enjoy transitional preferential treatments (to be defined).
- Enterprises in encouraged industries located in Western regions would continue to enjoy the existing tax incentives.

Tax Deductions

- Most rules are similar to current law for FIEs.
- Charitable donation is limited with a cap.
- Non-deductible expenses have been expanded to include sponsorship expenses and unverified provisions and reserves.

Anti-avoidance Rules

- Cost sharing is allowed in respect of intangible assets developed and shared among related parties and for the provision and receipt of common services, so long as the sharing basis is on arm's length.;
- More stringent requirements on filing and submission of related party information for TP enforcement;
- "Controlled Foreign Corporation Rules" (CFC Rules) such that undistributed profits derived by CFCs located in low-tax jurisdictions may be taxed in China as a deemed distribution;
- "Thin-capitalisation Rule" such that excessive interest expense may be disallowed;
- General anti-avoidance provision for making adjustments to taxable revenue or taxable income where business transactions are regarded as arranged without reasonable commercial purpose; and
- Tax adjustments made under the Anti-avoidance Chapter may be subject to interest levy.

Tax Consolidated Filing for Groups of Companies

- Not allowed unless approved by State Council.

Tax Filing Administration

- Filing of annual tax return period is extended to 5 months (from 4 months now) after year end.
- Provisional reporting and payments may be made on monthly basis or quarterly basis.

(Note: Please refer to our China Tax / Business News Flash 2007 Issue 8 for a highlight of the impacts of the new CIT Law on foreign invested financial institutions)

Sector: Banking and Capital Markets

Date: 28 March 2007

Contact: Matthew Wong - Shanghai

Circular Cai Shui [2007] No.45

In response to the unclear tax issues arising from the recent applications by various foreign banks to convert their existing branch network in China into a locally incorporated bank, the PRC State Administration of Taxation (SAT) has issued a new tax circular Cai Shui [2007] No.45 on 28 March 2007 to clarify various taxation treatments on this subject.

In particular, the new circular offers the following preferential tax policies aiming at giving relief on a number of potential tax inefficiencies that may arise in the foreign bank "corporatisation" exercise:

- Neither Business Tax nor Value Added Tax will be levied on asset or equity transfer transactions arising from the branch corporatisation exercise.
- Assets can be transferred from the existing branch network to the newly incorporated bank at net book value, thus resulting in no capital gain to be recognised in the transfer transaction.
- Accumulated tax loss of the existing branch network can be carried forward to the post-corporatisation new bank.
- Unexpired tax holiday of the existing branches can be enjoyed by the new bank after the corporatisation.
- The new bank and its newly registered branches after the corporatisation should be entitled to consolidated corporate income tax filing.
- The existing branches' business contracts and operating capital on which stamp duty has been levied before the corporatisation should not be subject to another level of stamp duty again when the contract and capital are rolled over to the new bank after the corporatisation.
- Deed tax will be exempt on the transfer of legal title of the real estates property from the existing branch network to the new bank.

The tax relief offered is based on the principle that this foreign bank corporatisation exercise is essentially a roll-over of the existing business run by the branch network of the foreign bank to the newly incorporated bank. It is seen to be an important tax development to support foreign banks smoothly going through their local branch corporatisation exercise.

Sector: All

Date: 28 January 2007 and 16 March 2007

Contact: Matthew Wong - Shanghai

Tax residents from Mexico and Korea

The SAT issued the following two tax circulars which express the intention of China to adopt anti-treaty shopping measures when dealing with tax residents from Mexico and Korea:

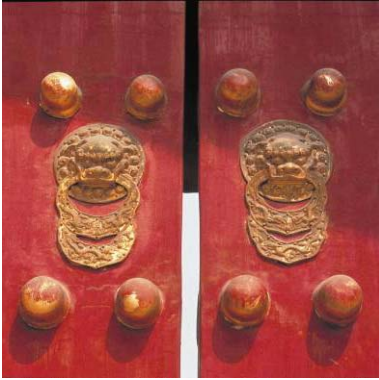
- Circular Guo Shui Han [2007] No.131 (Circular 131) to clarify the interpretation of the Double Tax Treaty and its Protocol between China and Mexico which was effective 1 January 2007
- Circular, Guo Shui Han [2007] No.334 (Circular 334) to clarify the interpretation of a specific article in the 2nd Protocol to the tax treaty between China and Korea which was effective 4 July 2006.

Circular 131 clarifies how Article 6 – Limitation of Benefits (LOB) in the Protocol to the Sino-Mexico Tax Treaty should be interpreted in China. Basically, a Mexico tax resident has to pass two tests in order to enjoy the benefits pertaining to dividend, interest and royalty granted under the Sino-Mexico Tax Treaty.

Circular 334 provides details of SAT's interpretation on Article 1 of the 2nd Protocol to the Sino-Korea Tax Treaty which stipulates who should be the party qualifying for treaty benefits.

The new requirements/restrictions imposed by the above notice mainly include the following:

- Each foreign individual can purchase **only** one household property in Beijing.
- When performing registrations for purchase and ownership, foreign individuals have to submit certificates regarding their residency status in China issued by the Beijing immigration bureau; foreign institutions have to present the business registration certificates of their representative offices in Beijing.
- The foreign institutions and individuals have to commit, in writing, that properties are purchased for self-use purpose. In addition, the properties purchased are not to be leased out or disposed at the institution's own discretion.
- A foreign institution is not allowed to dispose of the acquired properties until it closes its representative office in Beijing. In all other situations, foreign institutions and individuals have to establish legal enterprises in China to own the purchased property in order to lease out and dispose of the properties.



Hong Kong

Sector: All

Date: March 2007

Contact: Peter Yu
Florence Yip - Hong Kong

Revised Departmental and Interpretation Practice Notes 44 on China-Hong Kong Double Tax Agreement

The Inland Revenue Department (IRD) issued a Departmental Interpretation and Practice Notes (DIPN) No. 44 on 29 December 2006 to provide some guidance on the interpretation and implementation of the revised double tax agreement (DTA) signed between the Mainland China and Hong Kong. The revised DTA takes effect on 1 January 2007 in the Mainland and 1 April 2007 in Hong Kong.

A revised DIPN 44 was published on 26 April 2007. The following summarised the major different views currently taken by the Mainland China tax authorities (SAT) and the Hong Kong IRD on the revised DTA:

1. Whether a Hong Kong branch of an overseas bank is a Hong Kong resident

The IRD takes the view that such a branch is a Hong Kong resident if it is managed in Hong Kong. However, the SAT takes the view that the management or control of the bank instead of the Hong Kong branch only should be considered. The two tax authorities will continue to liaise on this point with a view to reaching a consensus.

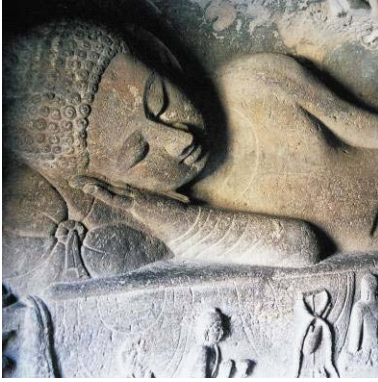
2. Method of counting the "6-month" period

The IRD and the SAT adopt different methods in counting the "6-month" period in deciding whether an enterprise has established a permanent establishment as a result of provision of services. Hong Kong treats a "month" as 30 days so a "6-month" period means 180 days. The Mainland takes the view that physical presence of 1 day in a month can constitute 1 month, and if no service was provided for a period of 30 consecutive days, 1 month can be deducted from the relevant period in which the services were performed. The IRD will continue to discuss with the SAT on this point with a view to reaching a consensus.

3. 25% Threshold for Capital Gain Exemption

An exemption is available for capital gain on disposal of shares if the shareholding is less than 25%. This capital gain exemption however does not apply to a land rich company, that is, a company with assets comprising mainly of immovable properties.

The IRD interprets the threshold to apply to the portion of shares disposed of, ie the disposal gain may be taxed only when the "shares disposed of" are not less than 25% of the total shareholding at the time of disposal. SAT interprets the 25% threshold to apply at any one point, ie the disposal gain may be taxable if the seller has 25% or more shareholding at any time. According to the revised DIPN, the SAT may consider to set a time frame for the purpose of deciding whether the seller has "once held" at least 25% of the shareholding. Hopefully, it will be something similar to the Mauritius/China DTA.



India

Sector: Capital Market

Date: February 2007

Contact: Jairaj Purandare / Radhakishan Rawal - PwC Mumbai

Budget 2007 - Policy proposals

- To promote a world class financial centre in Mumbai and realize the objective of making “financial services” the next growth engine for India.
- To allow institutions short selling of securities. Securities lending and borrowing to be introduced.
- To allow Indian companies to issue Exchangeable Bonds to facilitate unlocking of value in group companies.
- Regulations are proposed to be put in place to allow the creation of mortgage guarantee companies.

A detailed notification /guidelines in this regard are awaited.

Sector: Real Estate / Mutual Funds

Date: February 2007

Contact: Gautam Mehra / Radhakishan Rawal - PwC Mumbai

Budget 2007 - Tax proposals

Venture Capital Funds

Under the existing provisions Venture Capital Company or Venture Capital Fund (VCFs) making investment in a Venture Capital Undertakings (VCU) are given pass through status. Accordingly, VCF are not subject to tax but the investors in such VCFs are liable to tax. Investments in Indian real estate sector have been structured based on a VCF route.

As per the Budget 2007 proposal, the definition of VCU is restricted to undertakings engaged in certain specified activities. Consequently, the tax exemption claimed by VCFs investing in VCUs engaged in the real estate sector is withdrawn.

Mutual Funds

In the Budget proposal 2007, the dividend distribution tax is proposed to be increased to 25% (excluding surcharge and education cess) in the case of dividend distributed by money market mutual fund or liquid mutual funds.

A money market mutual fund means a mutual fund which has been set up with the objective of investing exclusively in money market instruments.

“Money market instruments” include commercial papers, commercial bills; treasury bills; Government securities with an unexpired maturity up to one year; call or notice money; certificates of deposit, usance bills; and any other similar instruments as specified by the Reserve Bank of India.

Sector: Real Estate

Date: March 2007

Contact: Gautam Mehra / Radhakishan Rawal - PwC Mumbai

CIT v. Neha Builders (P) Ltd. [2007] 207 CTR 231 (Guj)

Any income derived from a property held as 'stock in trade' would be subject to tax as 'income from business' and not 'income from house property'.

Rental income from property is generally subject to tax under the head 'income from house property', but where the property is held as stock in trade, rental income derived from the property will not be assessed as 'income from house property' but as 'business income'.

Sector: Investment Management

Date: February 2007

Contact: Gautam Mehra / Radhakishan Rawal - PwC Mumbai

Pre-IPO realty offers in FDI loop

In a move that has major ramifications for foreign institutional investors (FIIs) and real estate companies, the finance ministry has concluded that all pre-IPO placements to FIIs by realty players should adhere to foreign direct investment (FDI) regulations applicable to the sector. This means that all such investments would be subject to three-year lock-in, minimum capitalisation of \$5 million and development of at least 10 hectares of land.

A detailed proposal to this effect has been sent by the finance ministry for the consideration of the Cabinet Committee on Economic Affairs (CCEA). The Finance Ministry stand—based on inputs provided by the Reserve Bank of India (RBI)—has the potential to slow down FII investment in realty companies.

A detailed notification /guidelines in this regard are awaited.

Sector: Investment Management

Date: March 2007

Contact: Gautam Mehra / Radhakishan Rawal - PwC Mumbai

Protocol to the Indo-UAE DTAA

The Governments of UAE and India concluded a protocol to amend the double taxation avoidance agreement (DTAA) entered between the two countries. The protocol forms an integral part of the agreement. Some of the important amendments related to capital gains taxation are summarised in the following paragraphs.

- Prior to the amendment, the gains from the alienation of any immovable property or movable property forming part of the business property of a permanent establishment or pertaining to a fixed base was taxed in the source country.
- However, post amendment, where the property of a company consists directly or indirectly principally of immovable property situated in a country, the gains from the alienation of shares of the capital stock of such company would be taxed in the country in which the property is situated.
- Prior to the amendment, gains from sale of shares other than the above were taxable only in the resident country. However, based on the amendment, gains from alienation of such shares would be taxed in the country of source.

Any other gains from the alienation of any property other than movable, immovable or that referred to above shall be taxable only in the country of residence.



Indonesia

Sector: Banking

Date: January 2007

Contact: Christian Pellone
Margie Margaret
Tomy Harsono - Jakarta

Evaluation system of healthiness for commercial banks

Regulation *No.9/1/PBI/2007* regarding the evaluation system of healthiness for commercial banks based on Syariah principles. This regulation evaluates based on the following factors below:

1. Capital
2. Assets quality
3. Management
4. Earning
5. Liquidity
6. Sensitivity to market risk.

Sector: Banking

Date: March 2007

Contact: Christian Pellone
Margie Margaret
Tomy Harsono - Jakarta

Regulation of money markets

Regulation *No.9/5/PBI/2007* regards the regulation of money markets in banking as based on Syariah principles. This regulation is to develop and enhance the money market transactions based on the Syariah principle to improve the liquidity of the Syariah Bank

Sector: Banking

Date: March 2007

Contact: Christian Pellone
Margie Margaret
Tomy Harsono - Jakarta

Mudharabah Investment Certificate

Regulation *No.9/8/DPM/2007* regards the Mudharabah Investment Certificate amongst banks. This regulation provides the guidelines regarding the mechanisms of transactions related to the Mudharabah Certificate such as:

1. A general explanation related to the Mudharabah Certificate;
2. Characteristics and Conditions related to the Mudharabah Certificate;
3. The mechanism of the transaction;
4. Transaction settlement and;
5. Reporting.

Sector: Banking

Date: March 2007

Contact: Christian Pellone
Margie Margaret
Tomy Harsono - Jakarta

Second Amendment to the Bank Indonesia Regulation Number 8/2/PBI/2006

Bank Indonesia issued regulation *No.9/6/PBI/2007* on the Second Amendment to the Bank Indonesia Regulation Number 8/2/PBI/2006 on the Evaluation of the Quality of the Commercial Banks' Assets. In this regulation, several changes were made to the evaluation of the quality of the commercial bank's assets in the framework of facilitating the acceleration of the financing. Financing continues to take into account the application of the principles of prudence and risk management in banks.

Several rules relating to the perfection of the previous PBI (Bank Indonesia Regulation) including:

- Establishing the quality of the productive assets shall be based only on timely payment of the principal and/or interest to be applied for:
 - the bank shall establish the uniform classification system (UCS) for the provision of productive assets
 - the bank may not establish the UCS if the debtor has different projects
 - dispensation of the establishment of the quality of Placement in the form of credits for the Rural Credit Bank (BPR)
- The type of collateral that may be calculated as a subtractor for the Assets Elimination (PPA)

Sector: Banking

Date: February 2007

Contact: Christian Pellone
Margie Margaret
Tomy Harsono - Jakarta

Bank Offshore-Loans

Bank Indonesia issued regulation *No.9/1/DInt/2007* regarding the Bank's offshore-loan. This regulation is to provide guidance in relation to generating loans from offshore. This regulation also provides for the general principle of the offshore loan and describes the different types of offshore loan.

Sector: Capital Market

Date: February 2007

Contact: Christian Pellone
Margie Margaret
Tomy Harsono - Jakarta

Statement of Registration

In an effort to improve the accessibility of information in the capital market, the Capital Market and Financial Institution Supervisory Board issued Circular Letter *No SE-01/BL/2007* to accommodate previous regulations in relation to the Statement of Registration. In addition to the registration form, a registering entity is to submit consolidated Financial Statement and stand alone Financial Statements of the company and its subsidiaries to the Capital Market and Financial Institution Supervisory Board. In the case when the issuing entity is a public company with subsidiaries, the financial statement must be consolidated and audited by a reputable accounting firm.



Japan

Sector: Banking and Capital
Markets
Insurance
Investment Management
Real Estate

Date: March 2007

Contact: Sachihiko Fujimoto
Katsuyo Oishi
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Akemi Kitou - Tokyo

Revision of depreciation method of fixed assets in 2007 Japanese Tax Reforms

The Japanese Tax Reforms were approved by the Diet on 23 March 2007 and were promulgated on 30 March 2007. On the same date, the Cabinet Orders relating to the revised tax laws were also public.

Outline on Revision of the Depreciation Method

1. With regard to depreciable assets acquired on or after 1 April 2007, the concept of residual value will be abolished such that after the useful life has expired, depreciable assets can be depreciated until their book value is JPY 1.
2. An accelerated depreciation rule, the so called "250% declining balance method" is introduced.
3. With regard to depreciable assets acquired on or before 31 March 2007, the residual value of 5% can be depreciable using a straight line method over 5 years starting from the next fiscal year following the fiscal year in which the available limit for depreciation applied to the assets (being 95% of the acquisition cost) is depreciated (5 Years Average Depreciation).
4. The valuation method is maintained with regard to depreciable assets for fixed asset tax purposes.

Calculation Method

1. The Old Straight Line Method is calculated by taking the acquisition price of an asset less its residual value (10% of the acquisition price) and multiplied by the depreciation rate. The New Straight Line Method will be calculated by multiplying the acquisition price by the depreciation rate, now that the residual value has been abolished.
2. The Old Declining Balance Method is calculated by multiplying the book value as of the beginning of the fiscal year by a predetermined depreciation rate. The New Declining Balance Method will be calculated by multiplying the book value as of the beginning of the fiscal year by the depreciation rate, which is 2.5 times the depreciation rate under the straight line method. If the amount calculated using the New Declining Balance Method is less than the "amount calculated by dividing the book value as of the beginning of the fiscal year by the remaining years (useful life less the elapsed year)", then the calculation method will be changed from the declining balance method to the straight line method when calculating the depreciation limit.
3. For depreciable assets acquired on or before 31 March 2007, the residual value of 5% will be depreciable over 5 years starting from the fiscal year after the fiscal year in which the available limit for depreciation (95% of the acquisition cost) is depreciated. The decision whether the available limit has been depreciated will be made on a fiscal year basis. Therefore, 5 Years average depreciation will apply from the next fiscal year when the available limit is depreciated.

Sector: Banking and Capital Markets
Insurance
Investment Management
Real Estate

Date: March 2007

Contact: Sachihiko Fujimoto
Katsuyo Oishi
Yuka Matsuda
Tetsuo Imura
Akemi Kitou - Tokyo

Accounting treatment for depreciation

In the “Audit treatment for depreciation” released by the Japanese Institute of Certificate Public Accountants on 25 April 2007, the relationship between the 2007 tax reforms and treatments in the audit process were discussed. According to this treatment, when depreciating new or existing assets, although any of the Old Straight Line Method, the New Straight Line Method, the Old Declining Balance Method or the New Declining Balance Method can be applied, care should be taken when changing depreciation methods as it should be a reasonable change in accounting policy.

Sector: Banking and Capital Markets
Insurance
Investment Management
Real Estate

Date: March 2007

Contact: Sachihiko Fujimoto
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Consideration paid to shareholders in a corporate reorganization

The new Corporation Law rules relating to corporate reorganizations will become effective as of 1 May 2007. These rules allow more flexibility for corporations carrying out merger and acquisition transactions and will enable acquiring companies to acquire a target corporation in Japan via the so-called “triangular merger”. In a triangular merger, a corporation exchanges the stock of its parent company for the shares of a target company.

The 2007 Tax Reform provides that a corporate reorganization in which shares of the parent corporation (domestic or foreign) are exchanged by a Japanese acquiring corporation solely for the shares of a Japanese target corporation will be treated as tax qualified only if (1) the parent directly owns, and will continue to own, 100% of the shares of the Japanese acquiring corporation prior to, and after, the reorganization and (2) any one of the other requirements for a tax qualified reorganization are met (eg, the continuity of business test – see other articles regarding the requirements for a tax qualified reorganization).

The above amendments will be applicable to corporate reorganizations carried out on or after 1 May 2007.



Korea

Sector: Insurance **Date:** February 2007 **Contact:** J. Y. Lee - Seoul

Under the amendment to the Presidential Decree of the Corporate Income Tax Act (CITA), statutory reserves of IBNR for personal insurance will be gradually allowed for tax purposes. Reserves subject to deduction are reserves recorded after the effective date.

Sector: Banking & Capital
Markets
Investment Management
Insurance **Date:** February 2007 **Contact:** J. Y. Lee - Seoul

Under the amendment to the Presidential Decree of the CITA, valuation gain or loss arising from currency related derivatives held by a corporation to hedge currency fluctuation risk will be recognized for tax purposes. For financial institutions, valuation gain or loss from currency related derivatives will be recognized even if there is no hedging purpose.

Sector: Banking & Capital
Markets
Insurance **Date:** February 2007 **Contact:** J. Y. Lee - Seoul

Under the amendment to CITA, bad debt reserve for a financial institution is deductible up to the greater of 2%, the actual write off ratio (ie actual write off divided by total receivable) and the amount approved by the Financial Supervisory Service in the case of qualified financial institutions.

Sector: Capital Markets &
Investment Management **Date:** February 2007 **Contact:** J. Y. Lee - Seoul

Under the amendment to the Special Tax Treatment Control Act, Securities Transaction Tax exemption has been abolished for private funds and extended for 2 years up to 31 December 2008 for public funds.



Malaysia

Sector: Banking and Capital Markets
Insurance
Investment Management
Real Estate

Date: January 2007

Contact: Khoo Chuan Keat
Frances Po
Jennifer Chang
Lim Phaik Hoon - Kuala Lumpur

Deduction on Expenditure for Establishment of an Islamic Stock Broking Business

The Income Tax (Deduction for Expenditure for Establishment of an Islamic Stock Broking Business) Rules 2007 provides for tax deduction on establishment expenditure (ie consultancy and legal fees, cost of feasibility study, cost of market research, and cost of obtaining license and business approval for the purpose of establishing an Islamic stock broking business) incurred by an Islamic stock broking company resident in Malaysia.

In order to qualify for the tax incentive, the application for approval for the Islamic stock broking business must be made to Bursa Malaysia from 2 September 2006 until 31 December 2009. Further, Islamic stock broking business must commence within 2 years from the date of approval by the Bursa Malaysia.

The Rules became effective from 2 September 2006.

Sector: Banking and Capital Markets
Insurance
Investment Management
Real Estate

Date: February 2007

Contact: Khoo Chuan Keat
Frances Po
Jennifer Chang
Lim Phaik Hoon - Kuala Lumpur

Exemption from income tax on qualifying professional services rendered in Labuan

Under this Order, 65% of statutory income from the provision of qualifying professional services (ie legal, accounting, financial or secretarial services and includes services provided by a trust company) rendered by a person in Labuan to an offshore company is exempted from the Year of Assessment (YA) 2005 until YA 2010.

Where the person referred to above is a company, the amount of income exempted shall be credited into a 2-tier exempt income account from which 2 tier tax exempt dividends can be distributed.

Sector: Banking and Capital
Markets
Insurance
Investment Management

Date: March 2007

Contact: Khoo Chuan Keat
Frances Po
Jennifer Chang
Lim Phaik Hoon - Kuala Lumpur

Stamp Duty and Real Property Gains Tax Exemption - merger of the whole or any part of the business and operations of a licensed discount house, licensed merchant bank or dealer

Stamp duty that is ordinarily payable on all instruments for any scheme of merger of the whole or any part of the business and operations of a licensed discount house, licensed merchant bank or dealer where the merger would result in the establishment of an investment bank between 1 July 2005 until 30 June 2007 are exempted.

In addition, real property gains tax arising from the abovementioned scheme of merger is also exempted.

Sector: Banking and Capital
Markets
Insurance
Investment Management

Date: March 2007

Contact: Khoo Chuan Keat
Frances Po
Jennifer Chang
Lim Phaik Hoon - Kuala Lumpur

New package of incentives

The Government is offering a new package of incentives, starting with certain zones within the Iskandar Development Region (IDR). The following first incentives package was announced and these incentives apply to qualifying companies in 6 targeted sectors, namely creative industries, educational services, financial advisory and consulting, healthcare, logistic and tourism related services:-

- Corporate income tax exemption for activities within these zones and outside Malaysia for 10 years, upon commencement of operations; and
- Withholding tax exemption on certain payments for 10 years upon commencement of operations;
- Exemption from Foreign Investment Committee (FIC) rules;
- Freedom to source capital globally; and
- Unrestricted employment of foreign employees within the approved zones.

provided such operations commenced before the end of **2015**.

Further details of the incentives and support package will be announced by the one-stop centre Iskandar Regional Development Authority (IRDA) in due course.

Sector: Banking and Capital
Markets
Insurance
Investment Management

Date: March 2007

Contact: Khoo Chuan Keat
Frances Po
Jennifer Chang
Lim Phaik Hoon - Kuala Lumpur

Real Property Gains Tax (Exemption)(No. 2) Order 2007 was gazetted 1 April 2007

Under this Order, the Minister exempts any person from all provisions of the Real Property Gains Tax Act, 1976 in respect of any disposal of chargeable assets after 31 March 2007.



New Zealand

Sector: All

Date: March 2007

Contact: Vincent Sue
Rajul Makan - Wellington

International Financial Reporting Standards ('IFRS')

The Government is proposing tax changes relating to the adoption of IFRS.

Under the proposals, taxpayers who prepare IFRS accounts will generally be required to calculate tax gains and losses on financial arrangements in line with the IFRS treatment used for accounting purposes. Gains and losses included in the statement of changes in equity will also need to be taken into account for tax purposes. Exceptions will be made for taxpayers who have adopted IFRS but who elect to use the expected value method for foreign currency loans, forward contracts and swaps.

The rules will apply to the spreading of income and expenditure only. Determining the debt / equity portion of hybrid instruments will not follow the IFRS treatment.

If enacted, the tax changes will apply from the year a taxpayer adopts IFRS. Early adopters of IFRS will be able to use the existing financial arrangement rules and pre-IFRS accounting practice for the relevant years but must adopt the IFRS treatment for financial arrangements from the 2007-08 income year.

Sector: All

Date: March 2007

Contact: Geof Nightingale
Hadleigh Brock - Wellington

Associated Persons Reforms

The Government has released an Officials' Issues Paper that discusses potential changes to the current definitions of "associated persons" in the Income Tax Act 2004. One proposal is to replace the current multiple definitions with a single standard definition that would be subject to limited modification for certain provisions. The Issues Paper also proposes expanding the definition significantly for applications to trusts (including tests to associate settler and beneficiaries, trustees and beneficiaries, and two trustees with a common settler), the aggregation of associated interests and the introduction of a universal tripartite test.

Submissions on the paper are due on 11 May 2007.

Sector: Insurance

Date: March 2007

Contact: Paul Mersi
Ian Rowe - Wellington

Life Insurance

Following on from the Government's release of its first Officials paper entitled "Life insurance tax reform - Officials' paper No. 1 - scope of the review" in October 2006, the second consultation document has been issued entitled: "Life insurance tax reform: Officials' paper No. 2 – suggestions for reform".

The paper suggests a new model for taxing life insurance products, based on the way that general insurance products are taxed and incorporating aspects of the portfolio investment entity rules. The paper states that Officials would prefer to split a life insurance company's taxable income calculation into shareholders' income (reflecting the return on assets effectively owned by the shareholders in the life insurance company) and policyholders' income (reflecting the return on assets that are attributed to policyholders in the life insurer).

Feedback on the proposals is open until 2 May 2007 with any potential changes expected to be included in a tax bill to be released towards the end of 2007.

Sector: All

Date: March 2007

Contact: Ian Fay
Hadleigh Brock - Wellington

Use of Money Interest ('UOMI') rates increase

The Inland Revenue Department ('IRD') UOMI rates on unpaid and overpaid tax have increased from 8 March 2007.

The rate charged by the IRD on unpaid tax will rise from 13.08% to 14.24% and the rate paid by the IRD on overpaid tax will rise from 5.71% to 6.66%.

Sector: All

Date: March 2007

Contact: Ian Fay
Hadleigh Brock - Wellington

Netherlands Antilles /New Zealand Information exchange agreement

New Zealand has signed a tax information exchange agreement with the Netherlands Antilles.



Philippines

Sector: Banking and Capital
Markets
Insurance
Investment Management
Real Estate

Date: January 2007

Contact: George Lavadia
Malou Lim - Manila

Extension of Twin Collection Programs of the Bureau of Internal Revenue (BIR)

The deadline for availment of the Improved Voluntary Assessment Program (IVAP) and One-Time Abatement Program (OTAP) of the BIR has been extended until March 30, 2007 (previous deadline was December 2006). In addition, the coverage of the OTAP was expanded to cover taxpayer's delinquent accounts or assessment, preliminary or final, disputed or not, as of November 30, 2006 (previously as of June 30, 2006).

(Revenue Regulations No. 3-2007 dated January 16, 2007, Revenue Memorandum Circular No. 6-2007 dated January 31, 2007 and Revenue Memorandum Circular No. 7-2007 dated January 31, 2007)

Sector: Banking and Capital
Markets
Insurance
Investment Management
Real Estate

Date: January 2007

Contact: George Lavadia
Malou Lim - Manila

Amendment of the Consolidated Value-Added Tax Regulations of 2005

Revenue Regulations No. 16-2005, otherwise known as the Consolidated VAT Regulations of 2005, has been amended to clarify and update certain provisions pursuant to Republic Act Nos. 9337 and 9361 which amended the VAT law under the Philippine Tax Code. The more salient clarifications/amendments are as follows:

- 12% VAT rate is effective starting February 1, 2006
- Output tax on the sale of real property on installment plan shall be due on the instalment payments received, including interest and penalties for late payment. The corresponding input tax can be claimed by the buyer in the same period as the output tax recognition by the seller.
- Output and input tax related to the sale of real property on a deferred payment basis not on instalment plan (treated as a cash sale) shall be recognized at the time of the execution of the instrument of sale
- Tax-free exchanges where real property is exchanged for shares appears to be limited to transactions where the transferor and transferee of real property are both real estate dealers and the transferor gains control of the transferee-corporation.
- Non-life reinsurance premiums are not subject to VAT since these have already been subjected to VAT upon receipt of the insurance premiums.
- The term "gross receipts" excludes amounts earmarked for payment to un-related third parties or received as reimbursement for advance payment on behalf of another which do not redound to the benefit of the payor.
- Construction in Progress (CIP) is considered as purchase of service which is not a capital good until completed and not depreciated until put in service. Hence, not subject to the rules on input VAT amortization. Once construction is completed and asset is reclassified as a depreciable capital asset, no additional input tax can be claimed.

(Revenue Regulations 4-2007, dated February 7, 2007)

Sector: Insurance

Date: March 2007

Contact: Yip Yoke Har
Nur Adila - Singapore

The Income Tax (Concessionary Rate of Tax for Provision of Processing Services to Financial Institutions) (Amendment) Regulations 2007 was issued to amend the Schedule to the Income Tax (Concessionary Rate of Tax for Provision of Processing Services to Financial Institutions) Regulations 2005 to extend the list of prescribed processing services to include services supporting the insurance industry, which includes the following:

- claims management and processing services;
- loss adjusting services;
- policy issuance, processing, administration, renewal and collection services;
- risk modeling and related services; and
- run-off management and related services.

Sector: Insurance

Date: February 2007

Contact: Yip Yoke Har
Nur Adila - Singapore

The Income Tax (Amendment) Act 2007, published on 13 February 2007, sets out the changes to the relevant sections of the Income Tax Act as a result of the implementation of the Risk Based Capital Framework by insurance companies.

Sector: Investment management

Date: February 2007

Contact: Shefali Deshmukh - Singapore

2007 Budget key changes to tax incentive schemes for fund management

Key changes proposed in the 2007 Budget on enhancements to tax incentive schemes for fund management include the following:

1. Removal of the 80:20 rule

Currently, funds meeting certain criteria are protected from Singapore tax even if their discretionary management is carried out in Singapore. To qualify for an exemption, the fund must not have more than 20% of the total number of its issued shares (where it is a company) owned by Singapore residents or citizens, either directly or indirectly. This is known as the 80:20 rule. The Budget 2007 proposed a removal of the 80:20 rule in relation to "foreign investors" for non-resident funds. However, no details on the proposed removal are currently available and as such the 80:20 rule continues to apply until details are available.

2. Modification to the definition of designated investments

The incentive regime exempting funds from Singapore tax applies only to a specific list of investments (designated investments). The Budget 2007 announced that with effect from 15 February 2007, the list of designated investments will be expanded to include "qualifying loans", "commodity derivatives (both over-the-counter and exchange traded) and physical commodities". The definition of 'qualifying loans' has not yet been provided.

3. Investment advisory fees

Currently, fund management and/or advisory fees derived under a direct advisory agreement (not under a sub-advisory agreement) from offshore funds and qualifying onshore funds by a company which is granted the Financial Sector Incentive (FSI) for fund management are taxable at the rate of 10%. The Budget 2007 clarified that with effect from 15 February 2007, fees earned by an FSI company from providing investment advisory services to a foreign investor or to an offshore fund manager under a delegation arrangement would be taxable at 10%.



Taiwan

Sector: Banking and Capital
Markets
Insurance
Investment Management
Real Estate

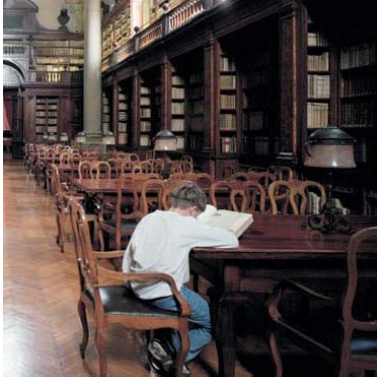
Date: February 2007

Contact: Richard Watanabe - Taipei

Tax treatment on merger and acquisition transactions

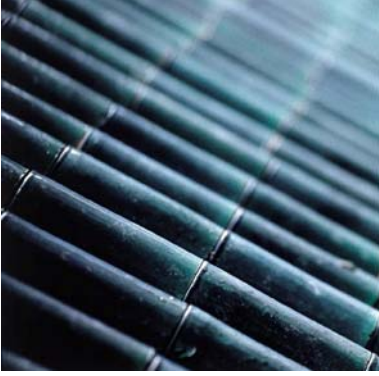
The Ministry of Finance (MOF) released its official view regarding tax treatment on merger and acquisition transactions involving share swaps and redemption of preference shares within a specified period.

In a share swap scenario, any excess of the fair value of preference shares issued on swap date over the original acquisition cost of ordinary shares of a Target company is viewed as gains from security transaction. When the preference shares are redeemed, any redemption in excess of the fair value of preference shares is regarded as dividend income and income tax will be levied.



Glossary

ABI	Approved Bond Intermediaries	J-REIT	Japan Real Estate Investment Trust
ACU	Asian Currency Unit	LLC	Limited Liability Company
ADR	American Depository Receipt	LRA	Land Registration Authority
ADT	Approved Derivative Traders of entity profit distribution	NRP	Non- resident Professional
AFM	Approved Fund Managers	O	Other
AMLC	Anti-money Laundering Council	OH	Operational Headquarters
BCM	Banking & Capital Markets	PD	Change in rules on taxation
CAR	Certificate Authorising Registration	QDI	Qualifying Debt Instrument
CSEZ	Clark Special Economic Zone	QDS	Qualifying Debt Securities AUD Issues arising from tax audit
CTR	Changes in domestic corporate	QFII	Qualified Foreign Institutional Investor
CWT	Creditable Withholding Tax	R&D	Research & Development
DES	Debt-to-equity swap	RAMO	Revenue Memorandum Order
DST	Documentary Stamp Tax	RBU	Regular Banking Unit Register of Deeds
ECB	External Commercial Borrowing owned and acquired	RD	tax rate
ECMI	Equity Capital Market	RDO	Revenue District Office
EFCDU	Expanded Foreign Currency Commission Deposit Unit	RE	Real Estate
EFPS	Electronic Filing and Purchases Payment System	RMC	Revenue Memorandum Circular
ELS	Equity Linked Securities	ROPOA	Real and Other Properties
FCDU	Foreign Currency Deposit Unit	RR	Revenue Regulation Intermediaries
GDR	Global Depository Receipt	SEC	Securities and Exchange
IAET	Improperly Accumulated Abatement Program Earnings Tax	SLSP	Summary Lists of Sales and
IM	Investment Management	SME	Small Medium Enterprises
INS	Insurance	SPC	Special Purpose Companies
IT	Information Technology	TT	Tax Treaty Change
ITR	Income Tax Return	VAAP	Voluntary Assessment and
		VAT	Value Added Tax
		WHT	Withholding Tax



Notes



Recent PwC Asia Publications

Future of foreign banks in Australia 2006

This survey is the first comprehensive report on foreign banks in Australia to be released by PricewaterhouseCoopers since 1997 and builds on comparable surveys in Canada, China, India, Japan and South Africa.

Future of foreign banks in China 2006

This survey includes observations on the changes in China's financial markets, the development of the regulatory environment, banking risks in China, future opportunities and the results of the peer review.

Future of foreign banks in India 2006

This survey includes overall performance of foreign banks, new opportunities in wholesale and retail segments, the range of regulatory issues and results of peer review.

Asia Pacific Insurance Digest

This publication is dedicated to providing thought-provoking insights into some of the key strategic issues facing the insurance industry in Asia. (April 2004)

IM Asia Pacific Newsletter

China's fund market opens up; Japanese real estate investments on the rise; Singapore reforms for growth, and Hedge Funds: scale vs capacity. (March 2004)

Role of Auditors and Tax Advisers in the Hedge Fund Industry

Includes taxation considerations in Hong Kong, Singapore, Japan, Taiwan, Korea and Australia. (March 2004)

Asia Banking and Capital Markets Handbook – 2nd edition

Outlines the regulatory, supervisory, financial reporting and taxation environment faced by financial institutions operating in, or seeking to enter, the Banking and Capital Markets of 15 Asian territories. (March 2004)

The Financial Jungle – International Taxation of Equity Finance - Asia

An analysis of the taxation of equity financing – stock lending, repurchase agreements, equity swaps in 15 Asian territories. (November 2003)

Asia Pacific Insurance Handbook 2003 – 3rd edition

In CD-Rom format, the handbook contains a brief overview of the insurance industry in the Asia Pacific region, as well as a comprehensive guide on the industry in 27 Asian territories. (October 2003)

Asia Pacific Private Banking/Wealth Management Survey 2002-2003

An Asia Pacific private banking/wealth management survey based on responses to detailed questionnaires by private banks/wealth management organisations from Australia, Hong Kong and Singapore. (July 2003)

The Financial Jungle – Taxation of Derivative Financial Instruments in Asia

This publication provides an overview of derivative financial instruments and an analysis of the tax implications of using them in 14 Asian countries. (February 2003)

