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Corporate Taxes 2018/19

All information in this book, unless otherwise stated, is up to date as of 1 June 2018.

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Foreword

Welcome to the 2018/19 edition of *Worldwide Tax Summaries – Corporate Taxes*, one of the most comprehensive tax guides available. This year's edition provides detailed information on tax rates and rules in 152 territories worldwide.

As governments across the globe are looking for greater transparency and with the increase of cross-border activities, tax professionals often need access to the current tax rates and other major tax law features in a wide range of territories. The territory summaries, written by our local PwC tax specialists, include recent changes in tax legislation, as well as key information about income taxes, residency, income determination, deductions, group taxation, credits and incentives, withholding taxes, indirect taxes, and tax administration. All information in this book, unless otherwise stated, is up to date as of 1 June 2018.

Our online version of the summaries is available at *www.pwc.com/taxsummaries*. The Worldwide Tax Summaries (WWTS) website also covers the taxation of individuals and is fully mobile compatible, giving you quick and easy access to regularly updated information anytime on your mobile device.

Some of the enhanced features available online include Quick Charts to compare rates across jurisdictions. You may also access WWTS content through Tax Analysts at *www.taxnotes.com*.

If you have any questions, or need more detailed advice on any aspect of tax, please get in touch with us. The PwC tax network has member firms throughout the world, and our specialist networks can provide both domestic and cross-border perspectives on today's critical tax challenges.

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Global Tax &
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Significant developments

The corporate tax rate of 27.5% is extended from the 2017/18 income year to those small business corporate tax entities with an aggregated turnover of less than 25 million Australian dollars (AUD), and from the 2018/19 income year to those with an aggregated turnover of less than AUD 50 million. After the end of the 2023/24 income year, the 27.5% rate for these entities will reduce progressively to 25% by the 2026/27 income year. Under currently enacted law, the corporate tax rate for all other corporate tax entities will remain at 30% (however, there is a proposal to progressively reduce the corporate tax rate for all entities, not just those noted above). *See the Taxes on corporate income section*.

Accelerated depreciation applies to certain depreciating assets with a cost of up to AUD 20,000 acquired and installed ready for use between 12 May 2015 and 30 June 2018 for small business entities. The government has introduced law into Parliament that will extend the measure for a further 12 months, until 30 June 2019. See *the Deductions section for more information*.

From 1 July 2018, the Australian goods and services tax (GST) is payable on certain supplies of low value goods (valued at AUD 1,000 or less) that are purchased and imported by Australian consumers.

The Australian government is seeking to implement the Organisation for Economic Co-operation and Development (OECD) hybrid mismatch rules, which will generally apply to income years commencing on or after 1 January 2019. *See the Group taxation section for more information*.

The Junior Minerals Exploration Incentive (JMEI) replaced the exploration development incentive (EDI) (which ceased to apply on 30 June 2017) and enables eligible minerals exploration companies to generate tax credits for new shareholders by giving up a portion of their tax losses from greenfield mineral exploration expenditure, which can then be distributed to shareholders. The scheme applies from 1 July 2017 until 30 June 2021, with total credits limited to AUD 100 million.

The non-final withholding tax (WHT) rate that applies to foreign residents that dispose of certain taxable Australian property increased to 12.5% from 1 July 2017. *See Capital gains in the Income determination section for more information*.

On 7 June 2017, Australia signed the OECD Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS). *See the Other issues section for more information*.

Australia has implemented a levy (known as the Major Bank Levy) on Australian authorised deposit-taking institutions with total liabilities of greater than AUD 100 billion, with effect from 1 July 2017. *See the Other taxes section for more information.*

Taxes on corporate income

Companies that are residents of Australia are subject to Australian income tax on their worldwide income. Generally, non-resident companies are subject to Australian income tax on Australian-sourced income only. However, where a company is resident in a country with which Australia has concluded a double taxation agreement (DTA), Australia's right to tax business profits is generally limited to profits attributable to a permanent establishment (PE) in Australia.

Under currently enacted law, all companies are subject to a federal tax rate of 30% on their taxable income, except for 'small business' companies, which are subject to a reduced tax rate of 27.5% up to and including the 2023/24 income year, after which the rate will progressively reduce to 25% for the 2026/27 and later income years. The reduced tax rate applies only to those companies who carry on business and who, together with certain 'connected' entities, fall below certain aggregated turnover thresholds. For the 2017/18 year, the aggregated turnover threshold is AUD 25 million, and for the 2018/19 and later income years, it is AUD 50 million. The 27.5% rate for 'small business' entities subsequently will be reduced to:

- 27% for the 2024/25 income year
- 26% for the 2025/26 income year, and
- 25% for the 2026/27 and later income years.

Integrity measures are currently before Parliament to ensure that, from 1 July 2017, a company will not qualify for the reduced rate unless the passive income (including interest, rents, and net capital gains) that it derives represents no more than 80% of its total assessable income for the year.

There is a proposal to progressively reduce the corporate tax rate to 25% for all entities, not just those noted above, by the 2026/27 income year.

Local income taxes

There are no state or municipal taxes on income in Australia.

Corporate residence

A company is a resident of Australia for income tax purposes if it is incorporated in Australia or, if not incorporated in Australia, it carries on business in Australia and either (i) its central management and control are in Australia or (ii) its voting power is controlled by shareholders who are residents of Australia.

Permanent establishment (PE)

The concept of a PE is established in both domestic law and various DTAs that have been concluded with Australia. Where a company is resident in a country with which Australia has a DTA, it is important to have regard to the definition of PE contained therein as this will generally apply in priority to the domestic law.

Broadly, under Australia's domestic law, a PE is a place at or through which a person carries on any business, and includes:

- A place where the person is carrying on business through an agent (except where the agent does not have, or does not habitually exercise, a general authority to negotiate and conclude contracts on behalf of the person).
- A place where the person has, is using, or is installing substantial equipment or substantial machinery.
- A place where the person is engaged in a construction contract.
- Where the person is engaged in selling goods manufactured, assembled, processed, packed, or distributed by another person for, or at or to the order of, the first-mentioned person and either of those persons participates in the management, control, or capital of the other person or another person participates in the management, control, or capital of both of those persons, the place where the goods are manufactured, assembled, processed, packed, or distributed.

Most DTAs contain a definition of PE that is similar, though not identical, to the definition under domestic law.

Other taxes

Goods and services tax (GST)

The federal government levies GST at a rate of 10% and distributes the revenue to state governments. The GST is a value-added tax (VAT) applied at each level in the manufacturing and marketing chain and applies to most goods and services, with registered suppliers getting credits for GST on inputs acquired to make taxable supplies.

Food, with some significant exceptions; exports; most health, medical, and educational supplies; and some other supplies are 'GST-free' (the equivalent of 'zero-rated' in other VAT jurisdictions) and so not subject to GST. A registered supplier of a GST-free supply can recover relevant input tax credits, although the supply is not taxable.

Residential rents, the second or later supply of residential premises, most financial supplies, and some other supplies are 'input-taxed' ('exempt' in other VAT jurisdictions) and are not subject to GST. However, the supplier cannot recover relevant input tax credits, except that financial suppliers may obtain a reduced input tax credit of 75% of the GST on the acquisition of certain services.

Health insurance is GST-free. Life insurance is input-taxed. General insurance is taxed. Reverse charges may apply to services or rights supplied from offshore, where the recipient is registered or required to be registered, and uses the supply solely or partly for a non-creditable supply.

GST is applicable to cross-border supplies of digital products and services imported by Australian consumers from 1 July 2017. This measure ensures that digital products and other imported services supplied to Australian consumers by foreign entities are subject to the GST. Non-resident suppliers are required to register, collect, and remit GST on the digital products and services that they provide to Australian consumers.

The way Australia's GST rules apply to all cross-border supplies that involve non-resident entities operate to ensure that non-resident businesses do not have to engage in Australia's GST system unnecessarily. This includes switching off the GST liability for certain supplies between non-residents and extending the GST-free rules to certain supplies made to non-residents.

Since 1 July 2017, there is no double taxation of digital currencies by ensuring that supplies of digital currency receive equivalent GST treatment to supplies of money.

From 1 July 2018, GST is payable on certain supplies of low-value goods (valued at AUD 1,000 or less) that are purchased by consumers and are imported into Australia.

Wine equalisation tax (WET)

The federal government levies WET at the wholesale level at a rate of 29%, in addition to 10% GST, which is calculated on the price including the WET, and it applies to wine from grapes, fruit and certain vegetables, mead, and sake. Retailers do not receive an input tax credit for WET. A rebate is available to a wine producer of 29% of the wholesale price (excluding WET or GST) for wholesale sales, and of 29% of the notional wholesale selling price for retail sales and applications for own use (up to a maximum rebate of AUD 500,000 before 1 July 2018, and AUD 350,000 from 1 July 2018).

Luxury car tax

The luxury car tax is levied by the federal government at the rate of 33% of the value of the car that exceeds the luxury car tax threshold (AUD 75,526 for fuel-efficient vehicles and AUD 66,331 for other vehicles in the 2018/19 financial year) and is payable on the GST-exclusive value above the threshold. No input tax credit is available for luxury car tax, regardless of whether the car is used for business or private purposes.

Customs duties

Imports into Australia are subject to duties under the Australian Customs Tariff. The top duty rate is 5%.

Australia currently has comprehensive free trade agreements with Chile, China, Japan, Korea, Malaysia, New Zealand, Singapore, Thailand, and the United States. In addition, a regional free trade agreement between Australia, New Zealand, and Southeast Asian nations progressively eliminates all barriers to trade in goods, services, and investments. Australia has also concluded negotiations on a Comprehensive and Progressive Agreement for Trans-Pacific Partnership (TPP-11) between Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, Peru, New Zealand, Singapore, and Vietnam, and a separate free trade agreement with Peru.

Excise duties

Excise duties are imposed at high levels on beer, spirits, liqueurs, tobacco, cigarettes, and petroleum products. Excise rates for tobacco, alcohol, and fuel are indexed bi-annually based on movements in the consumer price index (CPI). Some examples of current excise rates include:

- Beer not exceeding 3% by volume of alcohol packaged in an individual container not exceeding 48 litres: AUD 42.50 per litre of alcohol calculated on that alcohol content by which the percentage by volume of alcohol of the goods exceeds 1.15.
- Tobacco in stick form not exceeding in weight 0.8 grams per stick of actual tobacco content: AUD 0.71046 per stick.
- Petroleum condensate, crude petroleum oil, and diesel: AUD 0.409 per litre.

- Liquefied petroleum gas (LPG), other than LPG exempted from excise duty: AUD 0.133 per litre.

A fuel tax credit system provides a credit for fuel tax (excise or customs duty) that is included in the price of taxable fuel. Broadly, credits are available to entities using fuel in their business and to households using fuel for domestic electricity generation and heating.

Land tax

All states and territories (except the Northern Territory) impose a tax based on the unimproved capital value of land. In general, the principal place of residence and land used for primary production is exempt from land tax.

Stamp duty

All states and territories impose a stamp duty on a wide variety of transactions at different rates. All jurisdictions impose a stamp duty on real estate conveyances, but most exempt conveyances of goods (not associated with other property) from stamp duty. The imposition of duty on share transfers involving unlisted entities differs from state to state. Corporate reconstruction exemptions are available. Advice from a stamp duty specialist should usually be obtained where substantial stamp duty may be imposed because the amount of duty may depend on the form of the transaction.

Fringe benefits tax (FBT)

The federal government levies FBT on employers at the rate of 47% on the 'grossed-up value' of non-salary and wages fringe benefits provided to employees (and/or the employee's associates) by the employer or associates. The grossing-up of the value ensures tax neutrality between providing benefits and cash remuneration. FBT generally is deductible for income tax purposes. There are some exemptions from FBT, including some minor benefits, remote area housing in certain circumstances, and specified relocation costs. In addition, there are some concessional valuation rules, in particular for motor vehicles and certain living-away-from-home benefits.

Payroll tax

States and territories impose a tax on employers' payroll (broadly defined). The various jurisdictions have harmonised their payroll tax legislation, but some differences remain, particularly tax rates and the thresholds for exempting employers whose annual payroll is below a certain level, after taking into account grouping rules. For example, in New South Wales, the rate for the year ended 30 June 2018 is 5.45% with an annual exemption threshold of AUD 750,000. In Victoria, the general rate for the year ended 30 June 2018 is 4.85% (except for regional Victorian employers, where it is 3.65%), and the annual exemption threshold is AUD 625,000. A variety of rates and thresholds apply in other state and territory jurisdictions.

Superannuation guarantee levy

Legislation requires employers to contribute a certain percentage of an employee's earnings base, subject to limited exceptions, to a registered superannuation fund or retirement savings account on behalf of the employee. Failure to make these contributions will result in the employer being liable for a non-deductible superannuation guarantee charge.

Australia

The current superannuation guarantee percentage is 9.5% and will remain so until 30 June 2021. From 1 July 2021, the rate will increase to 10% and will progressively increase up to 12% from 1 July 2025.

No level of Australian government imposes a social security levy.

Major Bank Levy

Australia has implemented a levy (known as the Major Bank Levy) on Australian authorised deposit-taking institutions (ADIs) with total liabilities of greater than AUD 100 billion, with effect from 1 July 2017. The levy is imposed at a rate of 0.015% on certain liabilities of the ADI that are reported to the regulator on a quarterly basis under a reporting standard.

Insurance tax

States impose taxes on insurance premiums, which may be substantial.

Petroleum Resource Rent Tax (PRRT)

PRRT currently applies to all petroleum projects in Australian offshore areas (or Commonwealth adjacent areas) other than production licences derived from the Joint Petroleum Development Area in the Timor Sea. It also applies to all Australian onshore and offshore oil and gas projects, other than the Joint Petroleum Development Area in the Timor Sea.

PRRT is applied to a 'project' or 'production licence area' at a rate of 40% of the taxable profits derived from the recovery of all petroleum in the project, including:

- crude oil
- shale oil
- condensate
- sales gas
- natural gas
- LPG, and
- ethane.

The taxable profit of a project is calculated as follows:

Taxable profit = Assessable receipts - Deductible expenditure

Deductible expenditure broadly includes exploration expenditure, all project development, and operating expenditures.

PRRT is self-assessed by the relevant taxpayer. The taxpayer is, in most cases, required to give the Commissioner of Taxation a PRRT return for each PRRT year. PRRT is generally payable by quarterly instalments.

PRRT applies in addition to normal income tax. PRRT payments (including instalments) are, however, deductible for income tax purposes.

Local municipal taxes

Local taxes, including water, sewerage, and drainage charges, are levied based on the unimproved capital value of land and include a charge for usage (e.g. water usage).

Branch income

Branch profits are subject to ordinary corporate rates of taxation, and there is no withholding on repatriated profits.

Income determination

Inventory valuation

Inventory generally may be valued at cost (full absorption cost), market selling value, or replacement price. Where, because of obsolescence or other special circumstances, inventory should be valued at a lower amount, the lower valuation generally may be chosen, provided it is a reasonable valuation. Special rules apply, however, regarding the valuation of trading stock for certain companies joining a consolidated group. Last in first out (LIFO) is not an acceptable basis of determining cost, nor is direct costing in respect of manufactured goods and work-in-progress.

Conformity is not required between book and tax reporting. For tax purposes, inventory may be valued at cost, market selling value, or replacement price, regardless of how inventory is valued for book purposes. Those who choose to come within the small-business entity measures (broadly defined as taxpayers who carry on business and who, together with certain 'connected' entities, have an aggregated turnover of less than AUD 10 million may ignore the difference between the opening and closing value of inventory if, on a reasonable estimate, this is not more than AUD 5,000.

Capital gains

A capital gains tax (CGT) applies to assets acquired on or after 20 September 1985. Capital gains realised on the disposal of such assets are included in assessable income and are subject to tax at the corporate tax rate. In order to determine the quantum of any gain for any assets acquired before 21 September 1999, the cost base is indexed according to price movements since acquisition, as measured by the official CPI until 30 September 1999. There is no indexation of the cost base for price movements from 1 October 1999. Disposals of plant and equipment are subject to general rules rather than the CGT rules. Capital losses are allowable as deductions only against capital gains and cannot be offset against other income. In calculating capital losses, there is no indexation of the cost base.

Companies that are residents in Australia generally are liable for the tax on gains on the disposal of assets wherever situated, subject to relief from double taxation if the gain is derived and taxed in another country. However, the capital gain or capital loss incurred by a company from a CGT event in relation to shares in a foreign company is reduced by a percentage reflecting the degree to which the foreign company's assets are used in an active business if the company holds a direct voting percentage of 10% or more in the foreign company for a certain period before the CGT event. Attributable income from CGT events happening to shares owned by a controlled foreign company (CFC) are reduced in the same way. Capital gains and capital losses made by a resident company in respect of CGT events happening in respect of 'non-tainted' assets used to produce foreign income in carrying on business through a PE in a foreign country are disregarded in certain circumstances.

Non-resident companies are subject to Australian CGT only where the assets are taxable Australian property (i.e. Australian real property, or the business assets of Australian branches of a non-resident). Australian CGT also applies to indirect Australian real property interests, being non-portfolio interests in interposed entities (including foreign interposed entities), where the value of such an interest is wholly or principally attributable to Australian real property. 'Real property' for these purposes is consistent with Australian treaty practice, extending to other Australian assets with a physical connection with Australia, such as mining rights and other interests related to Australian real property. A 'non-portfolio interest' is an interest held alone or with associates of 10% or more in the interposed entity.

Proceeds from the sale of certain taxable Australian property by a non-resident are subject to a non-final WHT of 12.5% of the proceeds.

Dividend income

A 'gross-up and credit' mechanism applies to franked dividends (dividends paid out of profits that have been subject to Australian tax) received by Australian companies. The corporate shareholder grosses up the dividend received for tax paid by the paying company (i.e. franking credits attaching to the dividend) and is then entitled to a tax offset (i.e. a reduction of tax) equal to the gross-up amount. A company with an excess tax offset entitlement converts the excess into a carryforward tax loss using a special formula.

Dividends paid to another resident company that are unfranked (because they are paid out of profits not subject to Australian tax) are taxable, unless they are paid within a group that has chosen to be consolidated for tax purposes. Dividends paid between companies within a tax consolidated group are ignored for the purposes of determining the taxable income of the group.

Franked dividends paid to non-residents are exempt from dividend WHT.

An exemption from WHT is also available for dividends received by non-resident shareholders (or unitholders) in an Australian corporate tax entity (CTE) to the extent that they are 'unfranked' and are declared to be conduit foreign income (CFI). These rules may also treat the CFI component of an unfranked dividend received by an Australian CTE from another Australian CTE as not taxable to the recipient, provided it is on-paid within a specified timeframe. Broadly, income will qualify as CFI if it is foreign income, including certain dividends, or foreign gains, which are not assessable for Australian income tax purposes or for which a foreign income tax offset has been claimed in Australia.

Non-portfolio dividends repatriated to an Australian resident company from a company resident in a foreign country will be non-assessable, non-exempt income, but only if it is a distribution paid on an equity interest as determined under Australian tax law.

Income of a non-resident entity in which Australian residents hold interests is not assessable when repatriated to Australia where the income has been previously attributed to those residents and taxed in Australia (*see Controlled foreign companies [CFCs] in the Group taxation section for more information*).

Stock dividends

Stock dividends, or the issue of bonus shares, as they are known under Australian law, are, in general, not taxed as a dividend, and the tax treatment is the spreading of the cost base of the original shares across the original shares and the bonus shares.

However, if a company credits its share capital account with profits when issuing bonus shares, this will taint the share capital account (if it is not already a tainted share capital account), causing the bonus share issue to be a dividend. Certain other rules may apply to bonus share issues, depending on the facts.

Financial arrangements

Special rules apply to the taxation of financial arrangements (TOFA). 'Financial arrangement' is widely defined to cover arrangements that involve a cash settlable legal or equitable right to receive, or obligation to provide, something of economic value in the future.

These measures provide six tax-timing methods for determining gains or losses in respect of financial arrangements, along with revenue account treatment of the resulting gains or losses to the extent that the gain or loss is made in earning assessable income or carrying on a business for that purpose. The default methods are the accruals method and the realisation method, one or other of which will apply depending on the relevant facts and circumstances of a particular financial arrangement. In broad terms, the accruals method will apply to spread an overall gain or loss over the life of the financial arrangement where there is sufficient certainty that the expected gain or loss will actually occur. A gain or loss that is not sufficiently certain is dealt with under the realisation method.

Alternatively, a taxpayer may irrevocably choose one or more of four elective methods (i.e. fair value, retranslation, financial reports, and hedging) to determine the tax treatment of financial arrangements covered by the election. Qualification criteria must be met before the elective methods may be used. Generally, these criteria require that the taxpayer prepare a financial report in accordance with Australian (or comparable) accounting standards and be audited in accordance with Australian (or comparable) auditing standards.

Exemptions from this regime may be available having regard to the duration of the arrangement or the nature of the relevant taxpayer and the annual turnover or value of assets of that taxpayer. Certain types of financial arrangements are excluded from these rules, including leasing and hire purchase arrangements. Foreign residents are taxable on gains from financial arrangements under these measures to the extent that the gains have an Australian source.

Royalty income

Royalties are generally subject to taxation as ordinary income.

However, royalties paid to a non-resident (other than where it is received in respect of a PE in Australia of a resident of a treaty country) are subject to a final WHT applied to the gross amount of the royalty. Royalties for WHT purposes covers payments that fall within the ordinary meaning of the term as well as certain specified payments (e.g. payments for the use of, or the right to use, copyright, patent, design or model, plan, secret formula or process, trademark, or any industrial, commercial, or scientific equipment; the supply of scientific, technical, industrial, or commercial knowledge or information; the supply of any assistance that is ancillary and subsidiary to, and is furnished as a means of enabling the application or enjoyment of any of the aforementioned rights, equipment, or information; and the use of, or the right to use, visual images and/or sounds in connection with television or radio broadcasting that are transmitted by satellite, cable, optic fibre, or similar technology), subject to the application of any DTA. Generally, payments for services will not constitute the payment of a royalty. *See the Withholding taxes section for further information*.

Foreign exchange gains and losses

Foreign currency gains and losses are recognised when realised, regardless of whether there is a conversion into Australian dollars, and are included in or deducted from assessable income, subject to limited exceptions. There are exceptions to the timing and characterisation aspects of the realisation approach where the foreign currency gain or loss is closely linked to a capital asset. To reduce compliance costs with foreign currency denominated bank accounts, some taxpayers may elect to disregard gains or losses on certain low balance transaction accounts that satisfy a *de minimis* exemption or may elect for retranslation by annually restating the balance of the account by reference to deposits, withdrawals, and the exchange rates at the beginning and end of each year (or by reference to amounts reported in accordance with applicable accounting standards).

For foreign exchange gains and losses associated with financial arrangements subject to the TOFA measures (*as discussed above*), the compliance impact of the foreign exchange rules will be reduced for those taxpayers who are eligible to and elect the TOFA retranslation or financial reports tax-timing methods.

Entities or parts of entities, satisfying certain requirements, are able to choose to account for their activities in a currency other than Australian dollars for income tax purposes as an intermediate step to translating the result into Australian dollars (known as the 'functional currency' choice).

Foreign income

The current basis upon which the foreign income of corporations resident in Australia is taxed is set out below.

- Foreign dividends or distributions paid on equity interests as defined for Australian income tax purposes (i.e. the exemption does not apply to dividends paid on legal form shares that are treated as debt interests) are exempt from tax when received by a resident corporate tax entity that holds at least a 10% participation interest in the foreign company. The exemption also applies to distributions received indirectly (e.g. via a trust) by resident companies. However, hybrid mismatch rules, which are currently proposed to apply to income years commencing on or after 1 January 2019, may operate to limit the exemption (*see the Group taxation section for more information*).
- Active foreign branch profits of a resident company from carrying on business through a PE in a foreign country and capital gains made by a resident company from the disposal of non-tainted assets used in deriving foreign branch income (except income and capital gains from the operation of ships or aircraft in international traffic) are not assessable for tax.
- Other foreign income of Australian resident corporations is subject to tax; however, in most cases, an offset for foreign income tax paid is allowed to the extent of Australian tax payable on such income.
- Generally, limited partnerships are treated as companies for Australian tax purposes. In certain circumstances, foreign limited partnerships, foreign limited liability partnerships, United States (US) limited liability companies, and United Kingdom (UK) limited liability partnerships will be treated as partnerships (i.e. as a flow-

through entity) rather than as a company for the purposes of Australia's income tax laws.
- Australia also has a comprehensive CFC regime. *See Controlled foreign companies (CFCs) in the Group taxation section for more information*.

Deductions

Depreciation and depletion

A capital allowances regime allows a deduction for the decline in value of depreciating assets held by a taxpayer. The holder of the asset is entitled to the deduction and may be the economic, rather than the legal, owner. A 'depreciating asset' is an asset that has a limited effective life and can reasonably be expected to decline in value over the time it is used, but does not include land, trading stock, or, subject to certain exceptions, intangible assets. Deductions are available for certain other capital expenditure.

Intangible assets that are depreciating assets (if they are not trading stock) are:

- Certain mining, quarrying, or prospecting rights and information.
- Items of intellectual property (IP).
- In-house software.
- Indefeasible rights to use a telecommunications cable system.
- Spectrum licences under radio communications legislation.
- Datacasting transmitter licences.
- Telecommunications site access rights.

Taxpayers that do not qualify as a small business must depreciate the asset over its useful life (known as 'effective life') using either the straight-line (known as the 'prime cost' method) or diminishing-value method (straight-line rate multiplied by 200% for depreciating assets acquired on or after 10 May 2006).

Taxpayers may self-determine the effective life of a unit or plant or may choose the effective life contained in a published determination of the Commissioner of Taxation.

Non-small-business taxpayers are able to choose to write off all items costing less than AUD 1,000 through a low-value pool at a diminishing-value rate of 37.5% *per annum*.

For those who satisfy the small business entity threshold (broadly, those taxpayers who are carrying on business and who, together with certain connected entities, have an aggregated turnover of less than AUD 10 million for the year, a simplified depreciation system applies by taxpayer choice and with more attractive depreciation rates, including an immediate write off for depreciating assets with a cost of less than AUD 20,000 that are first acquired on or after 7.30pm, by legal time in the Australian Capital Territory, on 12 May 2015, and first used or installed ready for use on or before 30 June 2018. The government has introduced law into Parliament that will extend the measure until 30 June 2019.

'Project pool' rules allow expenditures that do not form part of the cost of a depreciating asset to be deductible over the life of a project that is carried on for a taxable purpose. Amongst other things, items that fall within the rules include the following:

- Amounts paid to create or upgrade community infrastructure for a community associated with the project.
- Site preparation costs for depreciating assets (except horticultural plants in certain circumstances).
- Amounts incurred for feasibility studies for a project.
- Environmental assessment costs applicable to the project.
- Amounts incurred to obtain information associated with the project.
- Amounts incurred in seeking to obtain a right to IP.
- Costs of ornamental trees or shrubs.

The so-called 'blackhole' expenditure provisions allow a five-year straight-line write-off for capital expenditure in relation to a past, present, or prospective business, to the extent that the business is, was, or is proposed to be carried on for a taxable purpose. The expenditure is deductible to the extent that it is not elsewhere taken into account (e.g. by inclusion in the cost base of an asset for CGT purposes) and that it is not denied deductibility for the purposes of the income tax law (e.g. by the rules against deducting entertainment expenditure).

Special rules apply for primary producer assets, such as horticultural plants, water and land care assets, and the treatment of expenditure on research and development (R&D) (*see the Tax credits and incentives section for more information*) and expenditure on certain Australian films.

A luxury car cost limit applies for depreciating the cost of certain passenger motor vehicles (AUD 57,581 cost limit for the 2018/19 income year).

Expenditure on the development of in-house software may be allocated to a 'software development pool' and written off over five years (30% in years two, three, and four, and 10% in year five). Amounts spent on acquiring computer software or the right to use it (except where the acquisition is for developing in-house software) generally are treated as incurred on acquiring a depreciating asset, deductible over five years commencing in the year it is first used or installed ready for use.

A loss arising on the sale of a depreciating asset (depreciated value of the asset less sale consideration) is generally an allowable deduction. A gain on the sale of a depreciating asset, to the extent of depreciation recaptured, generally is taxed as ordinary income. Gains exceeding the amount of depreciation recaptured are also taxed as ordinary income.

Subject to exceptions referred to below, capital expenditure incurred after 15 September 1987 in the construction or improvement of non-residential buildings used for producing assessable income is amortised over 40 years at an annual 2.5% rate. Capital expenditure on the construction of buildings used for short-term traveller accommodation (e.g. hotels, motels) and industrial buildings (typically factories) is amortised over 25 years at an annual 4% rate where construction commenced after 26 February 1992. The cost of eligible building construction that commenced after 21 August 1984 and before 16 September 1987 (or construction contracted before 16 September 1987) is amortised over 25 years at an annual 4% rate. There is no recapture of the amortised amount upon disposal of the building, except where the expenditure is incurred after 13 May 1997, in which case recapture will apply, subject to certain transitional rules.

Similar provisions apply in relation to income-producing residential buildings on which construction commenced after 17 July 1985.

The cost of income-producing structural improvements, the construction of which started after 26 February 1992, is eligible for write-off for tax purposes on the same basis as that of income-producing buildings, that is, at a rate of 2.5% *per annum*.

The cost of consumables may be either written off immediately or as used.

The following expenditure attracts an immediate 100% deduction: environmental protection activities, dealing with pollution and waste; landcare operations; exploring or prospecting for minerals, including the cost of mining rights and information acquired from an Australian government agency or government entity; mine site rehabilitation; and capital expenditure incurred by primary producers on fencing and water facilities.

Tax depreciation is not required to conform to book depreciation.

Percentage depletion based on gross income or other non-cost criteria is not available.

Goodwill

Goodwill and trademarks are not depreciating assets, and tax amortisation is not available.

Start-up expenses

Certain start-up expenses, such as costs of company incorporation or costs to raise equity, may qualify for a five-year straight-line write-off to the extent that it is capital expenditure in relation to a current or prospective business that is, or is proposed to be, carried on for a taxable purpose. An immediate deduction is available to a small business entity for a range of professional expenses (e.g. legal and accounting advice) and taxes or charges to an Australian government agency associated with starting a new business.

Interest expenses

Special rules classify financial arrangements as either debt or equity interests. These rules focus on economic substance rather than legal form and take into account related schemes, and extend beyond shares. In this situation, interest expense on non-share equity would be treated as a dividend, which is potentially frankable, and would be non-deductible for the paying company/group.

The law allows companies to claim a deduction for interest expenses incurred in relation to offshore investments that generate non-assessable, non-exempt dividend income.

Thin capitalisation measures apply to the total debt of the Australian operations of multinational groups (including branches of those groups). *See Thin capitalisation in the Group taxation section for more information*.

Bad debts

A deduction may be available for bad debts written off as bad before the end of an income year. Generally, a deduction will only be available where the amount of the debt was previously included in assessable income, or the debt is in respect of money lent in the ordinary course of a money lending business. The ability to claim a deduction for a bad debt is also subject to other integrity measures.

The amount of a commercial debt forgiven (other than an intra-group debt within a tax consolidated group) that is not otherwise assessable or does not otherwise reduce an allowable deduction is applied to reduce the debtor's carryforward tax deductions for revenue tax losses, carryforward capital losses, undeducted capital expenditure, and other capital cost bases in that order. Any amount not so applied, generally, is not assessable to the debtor. Forgiveness includes the release, waiver, or extinguishment of a debt (other than by full payment in cash) and the lapsing of the creditor's recovery right by reason of a statute of limitations.

Charitable contributions

Charitable contributions are generally deductible where they are made to entities that are specifically named in the tax law or endorsed by the Commissioner of Taxation as 'deductible gift recipients'. However, deductions for such gifts cannot generate tax losses. That is, generally the deduction is limited to the amount of assessable income remaining after deducting from the assessable income for the year all other deductions.

Entertainment

Subject to limited exceptions, deductions are denied for expenditure on 'entertainment', which broadly is defined as entertainment by way of food, drink, or recreation, and accommodation or travel to do with providing such entertainment.

Fines and penalties

Fines and penalties imposed under any Australian and foreign law are generally not deductible. This includes fines and penalties imposed in relation to both civil and criminal matters.

The General Interest Charge (GIC) and Shortfall Interest Charge (SIC), which are imposed for failure to pay an outstanding tax debt within the required timeframe or where a tax shortfall arises under an amended assessment, are deductible for Australian tax purposes.

Taxes

In general, GST input tax credits, GST, and adjustments under the GST law are disregarded for income tax purposes. Other taxes, including property, payroll, PRRT, and FBT, as well as other business taxes (excluding income tax and the Diverted Profits Tax [DPT]) are deductible to the extent they are incurred in producing assessable income or necessarily incurred in carrying on a business for this purpose, and are not of a capital or private nature.

Other significant items

Where expenditure for services is incurred in advance, deductibility of that expenditure generally will be prorated over the period during which the services will be provided, up to a maximum of ten years.

General value shifting rules apply to shifts of value, direct or indirect, in respect of loan and equity interests in companies or trusts. Circumstances in which these rules may apply include where there is a direct value shift under a scheme involving equity or loan interests, or where value is shifted out of an asset by the creation of rights in respect of the asset, or where there is a transfer of assets or the provision of services for a consideration other than at market value. The value shifting rules may apply to the head company of a tax consolidated group or multiple entry consolidated (MEC) group for value shifts also involving entities outside the group, but not to value shifting between group members, which the tax consolidation rules address (*see the Group taxation section for more information*).

Net operating losses

Losses may be carried forward indefinitely, subject to compliance with tests of continuity of more than 50% of ultimate voting, dividends, and capital rights or compliance with a same business test. For consolidated group companies, the ability to utilise these losses may be subject to additional rules (*see the Group taxation section for more information*).

Losses may not be carried back.

Payments to foreign affiliates

A corporation can deduct royalties, management service fees, and interest charges paid to non-residents, provided the amounts are referable to activities aimed at producing assessable income, and also having regard to Australia's transfer pricing rules. In the case of royalties and interest payable to non-residents, there is also a requirement that any applicable WHTs are remitted to the Commissioner of Taxation before the deduction can be taken.

Certain payments made to a foreign entity that is an associate of a significant global entity (SGE), broadly an entity that is part of a group with global revenue of AUD 1 billion or more, may be subject to DPT. The DPT aims to ensure that the tax paid by SGEs properly reflects the economic substance of their activities in Australia and aims to prevent the diversion of profits offshore through arrangements involving related parties. Specifically, the DPT applies at a rate of 40% on the Australian tax benefit obtained in connection with a scheme involving a foreign entity that is an associate of the Australian taxpayer where the principal purpose, or one of the principal purposes, of the scheme is to obtain an Australian tax benefit or to obtain both an Australian tax benefit and reduce foreign tax liabilities, subject to certain exceptions (e.g. a 'sufficient economic substance test').

Group taxation

A tax consolidation regime applies for income tax and CGT purposes for companies, partnerships, and trusts ultimately 100% owned by a single head company (or certain entities taxed like a company) resident in Australia. Australian resident companies that are 100% owned (either directly or indirectly) by the same foreign company and have no common Australian head company between them and the non-resident parent are also allowed to consolidate as a multiple entry consolidated (MEC) group. The group that is consolidated for income tax purposes may differ from the group that is consolidated for accounts or for GST purposes.

Groups that choose to consolidate must include all 100%-owned entities under an all-in rule, and the choice to consolidate is irrevocable. However, eligible tier-1 companies (being Australian resident companies that have a non-resident shareholder) that are members of a potential MEC group are not all required to join an MEC group when it forms, but may form two or more separate MEC or consolidated groups, if they so choose, of which the same foreign top company is the 100% owner. If an eligible tier-1 company joins a particular MEC group, all 100% subsidiaries of the company must also join the group. While the rules for forming and joining MEC groups allow more flexibility than with consolidated groups, the ongoing rules for MEC groups are more complex, particularly for tax losses and on the disposal of interests in eligible tier-1 companies, which are subject to cost pooling rules, although for practical purposes these rules are relevant only if the non-resident's interest is (or will become) an indirect Australian real property interest (*see Capital gains in the Income determination section for more information*).

A single entity rule applies to members of a consolidated or MEC group so that for income tax purposes the subsidiary members are taken to be part of the head company, while they continue to be members of the group and intra-group transactions are not recognised. In general, no group relief is available where related companies are not members of the same consolidated or MEC group. Rollover relief from CGT is available on the transfer of unrealised gains on assets, which are taxable Australian property, between companies sharing 100% common ownership where the transfer is between non-resident companies, or between a non-resident company and a member of a consolidated group or MEC group, or between a non-resident company and a resident company that is not able to be a member of a consolidated group.

Consolidated groups file a single tax return and calculate their taxable income or loss ignoring all intra-group transactions.

When a consolidated group acquires 100% of an Australian resident entity, so that it becomes a subsidiary member, the cost base of certain assets (in general, those that are non-monetary) of the joining member are reset for all tax purposes, based on the purchase price plus the entity's liabilities, subject to certain adjustments. In this way, an acquisition of 100% of an Australian resident entity by a consolidated group is broadly the tax equivalent of acquiring its assets. Subject to certain tests being passed, tax losses of the joining member may be transferred to the head company and may be utilised subject to a loss factor, which is broadly the market value of the joining member divided by the market value of the group (including the joining member). The value of the loss factor (referred to as 'the available fraction') that applies for transferred losses may be reduced by capital injections (or the equivalent) into the member before it joined, or into the group after the loss is transferred.

Franking credits and tax losses remain with the group when a member exits, and the cost base of shares in the exiting member is calculated based on the tax value of its assets at the time of exit, less liabilities subject to certain adjustments.

Generally, members of the group are jointly and severally liable for group income tax debts on the default of the head company, unless the group liability is covered by a tax sharing agreement (TSA) that satisfies certain legislative requirements. A member who enters into a TSA generally can achieve a clean exit from the group where a payment is made to the head company in accordance with the TSA.

Transfer pricing

Australia has a comprehensive transfer pricing regime aimed at protecting the tax base by ensuring that dealings between related, international parties are conducted at arm's length. The arm's-length principle, which underpins the transfer pricing regime, uses the behaviour of independent parties as a benchmark for determining the allocation of income and expenses between international related parties. Australia's transfer pricing regime is in line with international best practice as set out by the OECD.

Transfer pricing adjustments operate on a self-assessment basis and apply in respect of certain cross-border dealings between entities and to the allocation of actual income and expenses of an entity between the entity and its PE, using the internationally accepted arm's-length principle, which is to be determined consistently with the relevant OECD Guidance material (and applied to both treaty and non-treaty cases). In addition, companies are required to have transfer pricing documentation in place to support their self-assessed positions before the lodgement of the tax return.

Australia implemented the OECD's transfer pricing documentation standards for those companies with global revenue of AUD 1 billion or more. Under these documentation standards, the Australian Taxation Office (ATO) receives the following information on large companies operating in Australia:

- A country-by-country (CbC) report that shows information on the global activities of a multinational, including the location of its income and taxes paid.
- A master file containing an overview of the multinational's global business, its organisational structure, and its transfer pricing policies.
- A local file that provides detail about the local taxpayer's inter-company transactions.

Thin capitalisation

Thin capitalisation measures apply to the total debt of the Australian operations of multinational groups (including branches of those groups). The measures cover investment into Australia of foreign multinationals and outward investment of Australian-based multinationals, and include a safe-harbour debt-to-equity ratio of 1.5:1. Interest deductions are denied to the extent that borrowing exceeds the applicable safe-harbour ratio. Where borrowing exceeds the safe-harbour ratio, multinationals are not affected by the rules if they can satisfy the arm's-length test (that the borrowing could have been borne by an independent entity). A further alternative test is available for certain inward or outward investing entities based on 100% of their worldwide gearing.

As mentioned above, the thin capitalisation rules apply to inward investment into Australia. In particular, they will apply where a foreign entity carries on business through an Australian PE or to an Australian entity in which five or fewer non-residents have at least a 50% control interest, or a single non-resident has at least a 40% control interest, or the Australian entity is controlled by no more than five foreign entities. Separate rules apply to financial institutions. To facilitate their inclusion in the rules, branches are required to prepare financial accounts.

International Financial Reporting Standards (IFRS), equivalents of which currently apply in Australia, make it more difficult for some entities to satisfy thin capitalisation rules because of, for example, the removal of internally generated intangible assets from the balance sheets. Accordingly, thin capitalisation law allows departure from the Australian equivalents to IFRS to exclude deferred tax assets and liabilities and surpluses and deficits in defined benefit superannuation funds from applicable calculations. The law will be amended to require entities to align the value of their assets for thin capitalisation purposes with the value included in their financial statements for income years commencing on or after 1 July 2019. However, a transitional rule will ensure that, in the interim period, only valuations that were made prior to 8 May 2018 may be relied on (this will generally be applicable to the valuation of internally generated intangible assets).

Controlled foreign companies (CFCs)

Under Australia's CFC regime, non-active income of foreign companies controlled by Australian residents (determined by reference to voting rights and dividend and capital entitlements) may be attributed to those residents under rules that distinguish between companies resident in 'listed countries' (e.g. Canada, France, Germany, Japan, New Zealand, the United Kingdom, and the United States) and in other 'unlisted' countries. In general, if the CFC is resident in an unlisted country and it fails the active income test (typically because it earns 5% or more of its income from passive or tainted sources), the CFC's tainted income (very broadly, passive income and gains, and sales and services income that has a connection with Australia) is attributable. If a CFC is resident in a listed country, a narrower range of tainted income is attributed even if the CFC fails the active income test.

When income previously taxed on attribution is repatriated, it is not assessable for tax.

Integrity measures for large multinationals

The following integrity measures seek to address multinational tax avoidance by 'significant global entities' (broadly an entity that is part of a group with global revenue of AUD 1 billion or more):

- Transfer pricing documentation standards (*see above for more information*).
- The doubling of the maximum administrative penalties that can be applied to entities that enter into tax avoidance and profit shifting schemes.
- A targeted anti-avoidance rule aimed at multinationals that enter into arrangements that artificially avoid having a taxable presence in Australia. Specifically, this measure will ensure that profits from Australian sales are taxed in Australia where the activities of an Australian associated entity support the making of those sales, and the profit from the Australian sales is booked overseas and is not attributable to a PE of the foreign entity in Australia. A principal purpose of entering into the arrangement must be to create a tax benefit.
- A requirement to lodge general purpose financial statements with the ATO where such accounts are not already lodged with the Australian Securities and Investment Commission for each income year starting on or after 1 July 2016.
- A Diverted Profits Tax (DPT) that is imposed at a penalty rate of 40% in circumstances where the amount of Australian tax paid is reduced by diverting profits offshore through contrived related-party arrangements. The DPT is extremely broad (for example, both financing and non-financing arrangements are in scope) and applies with respect to tax benefits arising in income years starting on or after 1 July 2017.
- Significantly increased penalties (as great as AUD 525,000) that can be applied for failing to lodge a tax return (or other tax-related document) on time (applicable to documents required to be lodged on or after 1 July 2017).
- Doubling of penalties that can be applied for making a false or misleading statement (applicable to statements made from 1 July 2017).

Hybrid mismatch rules

The government has introduced law into Parliament that seeks to implement the OECD's recommended hybrid mismatch rules. Hybrid mismatches are differences in the tax treatment of an entity or instrument under the laws of two or more tax jurisdictions. If a mismatch arises, the proposed law operates to neutralise the mismatch in Australia by:

- Preventing entities that are liable to income tax in Australia from being able to avoid income taxation, or obtain a double non-taxation benefit, by exploiting differences between the tax treatment of entities and instruments across different countries by disallowing a deduction or including an amount in assessable income.
- Limiting the scope of the exemption for foreign branch income and preventing a deduction from arising for payments made by an Australian branch of a foreign bank to its head office in some circumstances.
- Denying imputation benefits on franked distributions made by an Australian corporate tax entity if all or part of the distribution gives rise to a foreign income tax deduction; and preventing certain foreign equity distributions received, directly or indirectly, by an Australian corporate tax entity from being exempt if all or part of the distribution gives rise to a foreign income tax deduction.

In addition, there is an integrity rule that has the potential to impose additional Australian tax on interest and derivative payments to foreign interposed zero or low-rate entities, irrespective of whether the arrangement involves a hybrid element.

The proposed law will generally apply to assessments for income years starting on or after 1 January 2019.

Tax credits and incentives

Foreign income tax offsets (FITOs)

FITOs are available to avoid double taxation in respect of foreign tax paid on income that is assessable in Australia. Generally, a corporation will be entitled to claim a FITO where it has paid, or is deemed to have paid, an amount of foreign income tax and the income or gain on which the foreign income tax was paid is included in assessable income for Australian tax purposes.

The amount of the FITO available is limited to the greater of AUD 1,000 and the amount of the 'FITO limit'. The FITO limit is broadly calculated as the difference between the corporation's actual tax liability and its tax liability if certain foreign taxed and foreign-sourced income and related deductions were disregarded. Excess FITOs are not able to be carried forward and claimed in later income years.

Inward investment incentives

Depending on the nature and size of the investment project, state governments may give rebates from payroll, stamp, and land taxes on an *ad hoc* basis and for limited periods.

Capital investment incentives

Incentives for capital investment are as follows:

- Accelerated deductions are available for capital expenditures on the exploration for and extraction of petroleum and minerals (other than mining rights and information acquired from a non-government third party that start to be held after 7.30pm [AEST] 14 May 2013, which are claimed over the shorter of 15 years and the life of the asset), the rehabilitation of former mineral extraction sites, certain environmental protection activities, the establishment of certain 'carbon sink' forests, certain expenditure of primary producers, and for certain low cost depreciating assets held by small business entities.

- There are a number of tax concessions aimed at encouraging investments in the venture capital sector. Non-resident pension funds that are tax-exempt in their home jurisdiction and satisfy certain Australian registration requirements are exempt from income tax on the disposal of investments in certain Australian venture capital equity held at risk for at least 12 months. A similar exemption is extended to other tax-exempt non-resident investors, including managed funds and venture capital fund-of-funds vehicles and taxable non-residents holding less than 10% of a venture capital limited partnership. These investors are able to invest in eligible venture capital investments through an Australian resident venture capital limited partnership or through a non-resident venture capital limited partnership. Eligible venture capital investments are limited to specified interests in companies and trusts. Detailed rules in the legislation prescribe the nature of such investments and the characteristics, which such companies and trusts, and their investments, must possess.
- Investors in an Australian Early Stage Innovation Company (ESIC), broadly a company that is at an early stage of establishment to develop new or significantly improved innovations with the purpose of commercialisation to generate an economic return, are provided with a non-refundable carry forward tax offset equal to 20% of the amount paid for the investment, subject to a cap, and a capital gains tax exemption for shares that have been held for between one and ten years.
- There is a venture capital tax concession applicable to an 'early stage venture capital limited partnership' (ESVCLP). The thresholds for qualification include requirements that, amongst other things, the committed capital of the ESVCLP must be at least AUD 10 million but not exceed AUD 200 million, the investments made must fall within prescribed parameters as to size and proportion of total capital, and the ESVCLP must have an investment plan approved by Innovation Australia. Where the thresholds for their application are met, the ESVCLP provisions provide flow-through tax treatment to domestic and foreign partners, with the income and capital received by the partners exempt from taxation. As the income is tax exempt, the investor is not able to deduct investment losses.
- The taxable income derived from offshore banking transactions by an authorised offshore banking unit in Australia is taxed at the rate of 10%.
- Refundable tax offsets are available to companies for certain expenditure incurred in Australia in producing specified classes of film or undertaking specified post, digital, or special effects production activities in respect of specified classes of films. The concessions are only available to a company that is either an Australian resident or a non-resident carrying on business through an Australian PE and which has been issued with an Australian Business Number (ABN). The availability of the offsets is subject to a number of conditions, including meeting registration and minimum spend requirements. The rate of the offset varies from 16.5% to 40%, depending upon the nature of the relevant film and activities undertaken.
- The Junior Minerals Exploration Incentive (JMEI), which replaced the exploration development incentive (EDI) (which ceased to apply on 30 June 2017), enables eligible minerals exploration companies to generate tax credits for new shareholders by giving up a portion of their tax losses from greenfield mineral exploration expenditure, which can then be distributed to shareholders. The scheme applies from 1 July 2017 until 30 June 2021, with total credits limited to AUD 100 million.

R&D tax credit

For income years commencing before 1 July 2018, companies with an annual turnover of less than AUD 20 million can access a 43.5% refundable R&D tax credit. Companies with a turnover of at least AUD 20 million have access to a non-refundable 38.5% tax credit.

Changes are currently proposed to the R&D incentive for income years commencing on or after 1 July 2018. For companies with aggregated annual turnover below AUD 20 million, the refundable R&D offset will be a premium of 13.5% above a claimant's company tax rate. Cash refunds from the refundable R&D tax offset will be capped at AUD 4 million *per annum*, with any R&D tax offsets that cannot be refunded to be carried forward as non-refundable tax offsets to future income years. For companies with aggregated annual turnover of at least AUD 20 million, the government will introduce an R&D premium that ties the rates of the non-refundable R&D tax offset to the incremental intensity of R&D expenditure as a proportion of total expenditure for the year. The marginal R&D premium will be the claimant's company tax rate plus:

- 4% for R&D expenditure between 0% and 2% R&D intensity.
- 6.5% for R&D expenditure above 2% to 5% R&D intensity.
- 9% for R&D expenditure above 5% to 10% R&D intensity.
- 12.5% for R&D expenditure above 10% R&D intensity.

Generally, only genuine R&D activities undertaken in Australia qualify for the R&D tax incentive. However, R&D activities conducted overseas also qualify in limited circumstances where the activities cannot be undertaken in Australia. Special grant programmes also may be available to assist corporations in the conduct of certain R&D in Australia. These grants are awarded on a discretionary basis.

Other incentives

Cash grants for export-market development expenditure are available to eligible businesses seeking to export Australian-source goods and services.

Withholding taxes

WHT rates are shown in the following table.

	WHT (%)		
Recipient	**Dividends (1)**	**Interest (2)**	**Royalties (3)**
Resident corporations or individuals (35)	0	0	0
Non-resident corporations or individuals:			
Non-treaty	30	10	30
Treaty:			
Argentina	10/15 (4)	12	10/15 (4)
Austria (5)	15	10	10
Belgium	15	10	10
Canada	5/15 (6)	10	10
Chile (7)	5/15 (7)	5/10/15 (7)	5/10 (7)
China, People's Republic of (8)	15	10	10
Czech Republic	5/15 (9)	10	10
Denmark	15	10	10
East Timor (Timor Sea Treaty) (10)	15	10	10

Recipient	WHT (%) Dividends (1)	Interest (2)	Royalties (3)
Fiji	20	10	15
Finland	0/5/15 (11)	0/10 (11)	5 (11)
France	0/5/15 (12)	0/10 (12)	5 (12)
Germany (34)	5/15 (34)	0/10 (34)	5
Hungary	15	10	10
India	15	15	10/15 (13)
Indonesia	15	10	10/15 (14)
Ireland, Republic of	15	10	10
Italy	15	10	10
Japan	0/5/10/15 (15)	0/10 (15)	5 (15)
Kiribati	20	10	15
Korea, Republic of	15	15	15
Malaysia	0/15 (16)	15	15
Malta	15 (17)	15	10
Mexico	0/15 (18)	10/15 (18)	10
Netherlands	15	10	10
New Zealand	0/5/15 (19)	0/10 (19)	5
Norway	0/5/15 (20)	0/10 (20)	5
Papua New Guinea	15/20 (21)	10	10
Philippines	15/25 (22)	10/15 (22)	15/25 (22)
Poland	15	10	10
Romania	5/15 (23)	10	10
Russian Federation	5/15 (24)	10	10
Singapore	0/15	10	10
Slovak Republic	15	10	10
South Africa	5/15 (25)	0/10 (25)	5
Spain	15	10	10
Sri Lanka	15	10	10
Sweden	15	10	10
Switzerland (26)	0/5/15 (26)	0/10 (26)	5/10 (26)
Taipei/Taiwan	10/15 (27)	10	12.5
Thailand	15/20 (28)	10/25 (28)	15
Turkey (29)	5/15 (29)	0/10 (29)	10
United Kingdom (30)	0/5/15 (31)	0/10 (31)	5
United States	0/5/15/30 (32)	0/10/15 (32)	5 (32)
Vietnam	10/15 (33)	10	10

Notes

1. Dividends paid to non-residents are exempt from dividend WHT except when paid out of profits of a company that have not borne Australian tax (i.e. unfranked dividends). Dividends include those stock dividends that are taxable. The rates shown apply to dividends on both portfolio investments and substantial holdings other than dividends paid in connection with an Australian PE of the non-resident. Unfranked dividends paid to non-residents are exempt from dividend WHT to the extent that the dividends are declared by the company to be conduit foreign income. There is also a deduction in certain cases to compensate for the company tax on inter-entity distributions where these are on-paid by holding companies to a 100% parent that is a non-resident (*see Dividend income in the Income determination section*). Dividends paid to a non-resident in connection with an Australian PE are taxable to the non-resident on a net assessment basis (i.e. the dividend and associated deductions will need to be included in the determination of the non-resident's taxable income, the dividend is not subject to dividend WHT), and a franking tax offset is allowable to the non-resident company for franked dividends received.

2. Australia's interest WHT rate is limited to 10% of gross interest, although the treaty may allow for a higher maximum limit. An exemption from Australian WHT can be obtained for interest on certain public issues or widely held issues of debentures. Provisions exist to ensure that discounts and other pecuniary benefits derived by non-residents on various forms of financings are subject to interest WHT. Interest paid to non-residents by offshore banking units is exempt from interest WHT where offshore borrowings are used in offshore banking activities (including lending to non-residents). An offshore borrowing is defined as a borrowing from (i) an unrelated non-resident in any currency or (ii) a resident or a related person in a currency other than Australian currency. The interest WHT rates listed above for residents in a treaty country are those that generally apply. It is common for Australia's tax treaties to include a reduced limit for interest derived by certain government entities and/or financial institutions. One should refer to the relevant treaty for these limits.
3. Royalties paid to non-residents (except in respect of a PE in Australia of a resident of a treaty country) are subject to 30% WHT (on the gross amount of the royalty), unless a DTA provides for a lesser rate. Tax is generally limited to the indicated percentage of the gross royalty.
4. For Australian-sourced dividends that are franked under Australia's dividend imputation provisions and paid to a person who directly holds at least 10% of the voting power of the company, the limit is 10% (although note that Australia does not impose WHT on franked dividends). For Argentinean-sourced dividends paid to a person who holds at least 25% of the capital in the company, the limit is 10%. A 15% limit applies to other dividends. Source-country tax is limited to 10% of the gross amount of royalties in relation to copyright of literary, dramatic, musical, or other artistic work; the use of industrial or scientific equipment; the supply of scientific, technical, or industrial knowledge; assistance ancillary to the above; or certain forbearances in respect of the above. Source-country tax is limited to 10% of the net amount of royalties for certain technical assistance. In all other cases, it is limited to 15% of the gross amount of royalties.
5. The government announced on 4 February 2010 that negotiations to update Australia's tax treaty with Austria would take place in March 2010. No further announcements have been made in relation to the progress of treaty negotiations.
6. A 5% dividend WHT rate applies to franked dividends paid by an Australian resident company and, in the case of dividends paid by a Canadian resident company (other than a non-resident owned investment corporation), to a company that directly holds at least 10% of the voting power in the dividend company (although note that Australia does not impose WHT on franked dividends). Otherwise, the maximum WHT rate on dividends is 15%.
7. A 5% dividend WHT rate applies to dividends paid to a company that directly holds at least 10% of the voting power in the company paying the dividends. Otherwise, the maximum WHT rate on dividends is 15%. In respect of interest, a 5% WHT rate applies to interest derived by a financial institution that is unrelated to and dealing wholly independently with the payer. Where the 5% rate does not apply, a 15% WHT rate applies to interest arising in Chile, and a 10% WHT rate applies to interest in all other cases. A 5% royalty WHT rate applies to royalties for the use of, or right to use, any industrial, commercial, or scientific equipment, and a 10% royalty WHT rate applies in all other cases.
8. Except Hong Kong and Macau.
9. The treaty between Australia and the Czech Republic allows Australia to impose a 5% WHT on the franked part of a dividend in certain circumstances (although note that Australia does not impose WHT on franked dividends). In the Czech Republic, a rate of 15% applies to the gross amount of dividends if the dividends are paid to a company that directly holds at least 20% of the capital of the company paying the dividend.
10. East Timor does not have a comprehensive DTA with Australia. However, the Timor Sea Treaty governs the taxation rights between the two countries for petroleum-related activities conducted in the Joint Petroleum Development Area of the Timor Sea by any person or entity, irrespective of the residency status of that person or entity. Where the Timor Sea Treaty applies to third-country resident payees, only 10% of the total gross interest, dividend, or royalty payment is subject to Australian WHT, as follows:
    - Interest: 10% of total gross interest paid is subject to WHT at a rate of 10%.
    - Dividends: 10% of total gross unfranked dividends paid are subject to WHT at a rate of 15%, or at the relevant DTA rate of the recipient.
    - Royalties: 10% of total gross royalties paid is subject to WHT at a rate of 10%, or at the relevant DTA rate of the recipient. However, the other 90% of each such amount is subject to East Timorese WHT at the same rates.
11. A zero WHT rate applies to inter-corporate dividends where the recipient directly holds 80% or more of the voting power of the company paying the dividend. A 5% rate limit applies on all other inter-corporate dividends where the recipient directly holds 10% or more of the voting power of the company paying the dividend. A 15% rate applies to all other dividends. A rate limit of 10% applies to interest, except no tax is chargeable in the source country on interest derived by a financial institution resident in the other country or a government or political or administrative subdivision or local authority or central bank of the other country. Amounts derived from equipment leasing (including certain container leasing) are excluded from the royalty definition and treated either as international transport operations or business profits.
12. The source country exempts inter-corporate non-portfolio (i.e. minimum 10% shareholding) dividends paid out of profits that have borne the normal rate of company tax. There is a 5% rate limit for all other non-portfolio dividends. A rate limit of 15% applies for all other dividends. A rate limit of 10% applies to interest, except no tax is chargeable in the source country on interest derived by a financial institution resident in the other country or a government or political or administrative subdivision or local authority or central bank of the other country. Amounts derived from equipment leasing (including

certain container leasing) are excluded from the royalty definition and treated either as international transport operations or business profits.

13. The source-country limit under the Indian agreement is 10% for royalties paid in respect of the use of or rights to use industrial, commercial, or scientific equipment or for the provision of consulting services related to such equipment. In other cases, the limit is 15%.
14. The source-country limit under the Indonesian agreement is 10% for royalties paid in respect of the use of or the right to use any industrial, commercial, or scientific equipment or for the supply of scientific, technical, industrial, or commercial knowledge or information, and it is 15% in other cases.
15. The source country exempts inter-corporate dividends where the recipient directly holds 80% or more of the voting power of the company paying the dividend and certain limitation of benefit thresholds are met. A 5% rate limit applies on all other inter-corporate dividends where the recipient directly holds 10% or more of the voting power of the company paying the dividend. A rate limit of 10% otherwise applies for dividends. However, where the dividends are paid by a company that is a resident of Japan, which is entitled to a deduction for the dividends in Japan, the rate limit is 15% where more than 50% of the assets of the paying company consist, directly or indirectly, of real property situated in Japan and 10% in all other cases. Special rules apply to distributions to Japanese residents by real estate investment trusts (REITs). A rate limit of 10% applies to interest, except no tax is chargeable in the source country on interest derived by a financial institution resident in the other country or a government or political subdivision or local authority or central bank or other specified entity of the other country. Amounts derived from equipment leasing (including certain container leasing) are excluded from the royalty definition and treated either as international transport operations or business profits.
16. A zero dividend WHT rate applies to franked dividends paid by an Australian resident company to an entity that directly holds at least 10% of the voting power in the dividend paying company'; otherwise, a 15% WHT rate applies. In relation to dividends paid by a company resident of Malaysia, no WHT applies.
17. Source-country tax in Malta is limited to the tax chargeable on the profits out of which the dividends are paid.
18. A zero dividend WHT rate applies to franked dividends paid (in Mexico, those dividends that have been paid from the net profit account) to a company that directly holds at least 10% of the voting power in the dividend paying company. In all other cases, a 15% WHT rate will apply to dividends. Source-country tax is limited to 10% when interest is paid to a bank or an insurance company, derived from bonds and securities that are regularly and substantially traded on a recognised securities market, paid by banks (except where the prior two criteria apply), or paid by the purchaser to the seller of machinery and equipment in connection with a sale on credit. It is 15% in all other cases.
19. A zero WHT rate applies in certain cases to inter-corporate dividends where the recipient directly holds at least 80% of the voting power in the dividend paying company. A rate of 5% applies on all other inter-corporate dividends where the recipient directly holds 10% or more of the voting power of the company paying the dividend. A general limit of 15% applies for all other dividends. Source-country tax on interest is limited to 10%. However, no tax is chargeable in the source country on interest derived by a government or a political subdivision or local authority of the other country (including a government investment fund or a bank performing central banking functions) or on interest derived by a financial institution that is unrelated to and dealing wholly independently of the payer (excluding interest paid as part of a back-to-back loan arrangement and, for New Zealand payers, where that person has not paid approved issuer levy).
20. A zero WHT rate applies in certain cases to inter-corporate dividends where the recipient directly holds at least 80% of the voting power in the dividend paying company for the 12-month period prior to payment. A rate of 5% applies to all other inter-corporate dividends where the recipient directly holds 10% or more of the voting power of the company paying the dividend. A general limit of 15% applies to all other dividends. A general rate limit of 10% applies to interest. However, no tax is chargeable in the source country on interest derived by a government of the other country (including its money institutions or a bank performing central banking functions) from the investment of official reserve assets and on interest derived by a financial institution resident in the other country (excluding interest paid as part of a back-to-back loan arrangement).
21. For Australian-source dividends, the limit is 15%. Where dividends are sourced in Papua New Guinea, the limit is 20%.
22. Source-country tax is limited to 15% where relief by way of rebate or credit is given to the beneficial owner of the dividend. In any other case, source-country tax is limited to 25%. Source-country tax generally is limited to 15% of gross royalties if paid by an approved Philippines enterprise. In all other cases, the rate is limited to 25% of the gross royalties.
23. Source-country tax (Australia) is limited to 5% where a dividend is paid to a Romanian resident company that directly holds at least 10% of the capital of the Australian company paying the dividend to the extent that the dividend is fully franked. Source-country tax (Romania) is limited to 5% where a dividend is paid to an Australian resident company that directly holds at least 10% of the capital of the Romanian company paying the dividend if the dividend is paid out of profits that have been subject to Romanian profits tax. In other cases, it is limited to 15%.
24. Source-country tax generally is limited to 15%. However, a rate of 5% applies where the dividends have been fully taxed at the corporate level, the recipient is a company that has a minimum direct holding in the paying company, and the recipient has invested a minimum of AUD 700,000 or the Russian ruble equivalent in the paying company. Where the dividends are paid by a company that is a resident in Russia, the dividends are exempt from Australian tax.

25. A 5% rate limit applies on all inter-corporate dividends where the recipient directly holds 10% or more of the voting power of the company paying the dividend. A rate limit of 15% otherwise applies for dividends. A general rate limit of 10% applies to interest. However, no tax is chargeable in the source country on interest derived by a government of the other country (including a bank performing central banking functions) and on interest derived by a financial institution resident in the other country (excluding interest paid as part of a back-to-back loan arrangement).
26. The DTA applies a 5% WHT rate to dividends paid to companies that hold directly 10% or more of the voting power of the paying company. Dividends paid to publicly listed companies, or subsidiaries thereof, or to unlisted companies in certain circumstances, that hold 80% or more of the voting power of the paying company will be exempt from dividend WHT. Dividends paid to government or a political subdivision or local authority (including a government investment fund), a central bank, complying Australian superannuation funds, and tax exempt Swiss pension schemes will also be exempt from dividend WHT. In all other cases, a 15% WHT rate will apply. A general rate limit of 10% applies to interest. However, interest paid to bodies exercising governmental functions, banks performing central banking functions, banks that are unrelated to and dealing independently with the payer, complying Australian superannuation funds, and tax exempt Swiss pension schemes are exempt from interest WHT. The DTA applies a 5% WHT on royalties.
27. Source-country tax (Taiwan) is limited to 10% of the gross amount of the dividends paid to a company that holds at least 25% of the capital of the company paying the dividends. A rate of 15% applies in all other cases. To the extent that dividends are franked because they are paid out of profits that have borne Australian tax, they are exempt from dividend WHT (*See Note 1 above*). The treaty allows Australia to impose a 10% WHT on the franked part of a dividend.
28. The source-country limit on dividends where the recipient has a minimum 25% direct holding in the paying company is 15% if the paying company engages in an industrial undertaking; 20% in other cases. The source-country limit on interest is 10% when interest is paid to a financial institution.
29. A 5% WHT rate applies to inter-corporate dividends where the recipient directly owns 10% of the voting power of an Australian resident company or directly owns 25% of the capital of a Turkish resident company where the profits out of which the dividend is paid has been subject to the full rate of corporation tax in Turkey. In all other cases, a 15% WHT rate will apply. The DTA applies a general limit of 10% WHT on interest. However, interest derived from the investment of official reserve assets by the either the Australian or Turkish government, the Australian or Turkish central bank, or a bank performing central banking functions in either Australia or Turkey shall be exempt from interest WHT.
30. On 28 October 2008, it was announced that the Australian and the United Kingdom governments would commence negotiations on a revised tax treaty. No further announcements have been made in relation to the progress of treaty negotiations.
31. Source-country tax on dividends is generally limited to 15%. However, an exemption applies for dividends paid to a listed company that satisfies certain public listing requirements and controls 80% or more of the voting power in the company paying the dividend, and a 5% limit applies to dividends paid to other companies with voting power of 10% or greater in the dividend paying company. Source-country tax on interest is generally limited to 10%. However, generally zero interest WHT is payable where interest is paid to a financial institution or a government body exercising governmental functions.
32. Source-country tax on dividends is generally limited to 15%. No source country tax is chargeable on dividends to a beneficially entitled company that satisfies certain public listing requirements and holds 80% or more of the voting power in the company paying the dividend. A 5% limit applies to dividends paid to other companies with voting power of 10% or greater in the dividend paying company. No limit applies to US tax on dividends paid on certain substantial holdings of Australian residents in US REITs. In practical terms, US tax on these dividends is increased from 15% to the current US domestic law rate of 30%. The 15% rate applies to REIT investments made by certain listed Australian property trusts subject to the underlying ownership requirements not exceeding certain levels. Investments in REITs by listed Australian property trusts acquired before 26 March 2001 are protected from the increased rate. Source-country tax on interest generally is limited to 10%. However, generally zero interest WHT is payable where interest is paid to a financial institution or a government body exercising governmental functions. Rules consistent with US tax treaty policy and practice will allow interest to be taxed at a higher 15% rate (the rate that generally applies to dividends) and for tax to be charged on intra-entity interest payments between a branch and its head office. Amounts derived from equipment leasing (including container leasing) are excluded from the royalty definition.
33. Source-country tax is limited to 15% (Australia) and 10% (Vietnam).
34. Germany and Australia signed a new tax treaty, which took effect in relation to WHTs from 1 January 2017. Source-country tax on dividends will be generally limited to 15%, subject to an exemption for dividends paid to a beneficially entitled company that satisfies certain public listing requirements and holds 80% or more of the voting power in the company paying the dividend and a 5% limit that will apply to dividends paid to companies with voting power of 10% or greater in the dividend paying company. Source-country tax on interest is generally limited to 10%. However, zero interest WHT will be payable where interest is paid to a financial institution or a government body exercising governmental functions.
35. Where the recipient does not quote a Tax File Number (or Australian Business Number), the payer is obligated to withhold tax at the rate of 47% from 1 July 2017 (previously 49%) under the Pay-As-You-Go (PAYG) withholding regime. No withholding is required in relation to franked dividends.

Other payments

A PAYG withholding regime applies to require the deduction and remittance of taxes on behalf of foreign resident individuals and entities that are in receipt of the following types of payments:

Type of payment	Rate of withholding (%)
Payments for promoting or organising casino gaming junket arrangements	3
Payments for performing artists and sportspersons, including payments to support staff such as art directors, bodyguards, coaches, hairdressers, and personal trainers:	
if recipient is a company	30
if recipient is an individual	the applicable non-resident marginal tax rate
Payments under contracts entered into for the construction, installation, and upgrading of buildings, plant, and fixtures, and for associated activities	5

Managed investment trust (MIT) distributions

For MIT fund payments to a non-resident investor, a WHT regime applies, with divergent outcomes, depending upon whether or not the recipient of such fund payments is resident of a country identified as being one with which Australia has an effective exchange of information (EEOI) arrangement and which is regulated as such for purposes of these rules. For a resident of a regulated EEOI country, a final WHT at a 15% rate applies for distributions. For residents of non-EEOI regulated countries, a final WHT at a 30% rate applies.

There are also proposals to limit access to tax concessions for foreign investors by increasing the MIT withholding rate on income attributable to a trading business or amounts from certain cross-staple arrangements to a rate equal to the top corporate tax rate (currently 30%), rather than 15%. This is proposed to apply to a fund payment made by an MIT on or after 1 July 2019, subject to transitional relief for certain pre-existing arrangements held immediately before 27 March 2018.

Distributions from an MIT that holds only certified ‘clean buildings’ is eligible for a reduced rate of WHT of 10% where the recipient of the fund payment is a resident of a regulated EEOI country.

EEOI countries that have been identified by regulation are Anguilla, Antigua and Barbuda, Aruba, the Bahamas, Belize, Bermuda, the British Virgin Islands, the Cayman Islands, the Cook Islands, Gibraltar, Guernsey, Isle of Man, Jersey, Macau, Mauritius, Monaco, the Netherlands Antilles, San Marino, St. Christopher and Nevis, St. Vincent and the Grenadines, and the Turks and Caicos Islands, as well as countries with which Australia has concluded DTAs, other than Austria, Chile, Greece, the Philippines, Switzerland, and Turkey. Australia has entered into EEOI agreements with Andorra, Bahrain, Brunei (not yet in force), Chile, Costa Rica, Dominica, Grenada, Guatemala (not yet in force), Liberia, Liechtenstein, the Marshall Islands, Montserrat, Saint Lucia, Samoa, Switzerland, Turkey, Uruguay, and Vanuatu; however, these countries have not yet been identified in regulations to be EEOI countries.

Australia has an attribution tax regime that certain MITs (known as attribution managed investment trusts or AMITs) can choose to adopt to apply. The allocation of trust components to the members of an AMIT will be based on an 'attribution' rather than based on present entitlement to distributable income. Members of an AMIT will be taxed on the parts of the AMIT's trust components that are attributed to them as if they derived those amounts in their own right and in the same circumstances as the AMIT.

Tax administration

Taxable period

The Australian tax year runs from 1 July to 30 June. However, a corporation may apply to adopt a substitute year of income, for example, 1 January to 31 December.

Tax returns

A corporation (including the head company of a tax consolidated group) lodges/files a tax return under a self-assessment system that allows the ATO to rely on the information stated on the return. Where a corporation is in doubt as to its tax liability regarding a specific item, it can ask the ATO to consider the matter and obtain a binding private ruling.

Generally, the tax return for a corporation is due to be lodged/filed with the ATO by the 15th day of the seventh month following the end of the relevant income year or such later date as the Commissioner of Taxation allows. Additional time may apply where the tax return is lodged/filed by a registered tax agent.

Payment of tax

A PAYG instalment system applies to companies other than those whose annual tax is less than AUD 8,000 that are not registered for GST. Most companies are obligated to pay instalments of tax for their current income year on a monthly or quarterly basis. All companies with turnover of AUD 20 million or more pay instalments on a monthly basis.

Instalments are calculated by applying an instalment rate to the amount of the company's actual ordinary income (ignoring deductions) for the previous quarter. The instalment rate is notified to the taxpayer by the ATO and determined by reference to the tax payable for the most recent assessment. The ATO may notify a new rate during the year on which subsequent instalments must be based. Taxpayers can determine their own instalment rate, but there may be penalty tax if the taxpayer's rate is less than 85% of the rate that should have been selected.

Final assessed tax is payable on the first day of the sixth month following the end of that income year or such later date as the Commissioner of Taxation allows by a published notice.

Tax audit process

The Australian tax system for companies is based on self-assessment; however, the ATO undertakes ongoing compliance activity to ensure corporations are meeting their tax obligations. The ATO takes a risk-based approach to compliance and audit activities, with efforts generally focused on taxpayers with a higher likelihood of non-compliance and/or higher consequences (generally in dollar terms) of non-compliance. Compliance activities take various forms, including general risk reviews, questionnaires, reviews of specific issues, and audits.

Statute of limitations

Generally, the Commissioner of Taxation may amend an assessment within four years after the day of which an assessment is given to a company. Under the self-assessment system, an assessment is deemed to have been given to the company on the day on which it lodges its tax return. The four-year time limit does not apply where the Commissioner is of the opinion there has been fraud or evasion, or to give effect to a decision on a review or appeal, or as a result of an objection made by the company, or pending a review or appeal. An unlimited period of review of an assessment to give effect to a transfer pricing adjustment was changed to a seven-year period of review in respect of assessments raised for an income year commencing on or after 29 June 2013.

Topics of focus for tax authorities

The ATO periodically releases during the year its compliance focus areas that are attracting its attention. The following are current areas of focus by the ATO for large and multinational businesses:

- A strong focus on shifting of profits to lower tax jurisdictions and the cessation of Australian operations, including a focus on cross-border transactions (in particular, related-party financing).
- Structuring and business events, such as mergers and acquisitions, divestment of major assets and demergers, share buy backs, capital raisings and returns of capital, private equity entries and exits, and initial public offerings.
- Capital gains tax, losses (capital and revenue), tax consolidation, infrastructure investments, and financial arrangements.
- GST and property transactions, cross-border issues, and financial supply transactions.
- Sharing data and intelligence on risks and opportunities, sharing capabilities and strategies, and joint compliance action with other jurisdictions.
- R&D tax incentive.

Other issues

Intergovernmental agreement (IGA) on the Foreign Account Tax Compliance Act (FATCA)

In April 2014, the Australian government signed an IGA with the United States in relation to the implementation of FATCA. The agreement is intended to establish a framework to assist Australian financial institutions in meeting their obligations under FATCA.

Australia has enacted legislation to give effect to the IGA requiring Australian financial institutions to collect information about their customers that are likely to be taxpayers in the United States, and report that information to the ATO. The Australian Commissioner of Taxation will then pass this information on to the US Internal Revenue Service (IRS). Australia's obligations under the agreement apply to FATCA 'reportable accounts' maintained on or after 1 July 2014.

OECD Multilateral Convention

Australia signed the OECD Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS on 7 June 2017. The Multilateral Instrument (MLI) provides participating jurisdictions with a means to swiftly modify its bilateral treaties to implement measures developed as part of the OECD/G20 BEPS Project without having to negotiate changes on a treaty-by-treaty basis. The government has introduced law into Parliament to give effect to the Convention.

Transparency

The Commissioner of Taxation is required to publish limited information about the tax affairs of public and foreign-owned companies with 'total income' of AUD 100 million or more for an income year, and Australian-owned private companies with total income of at least AUD 200 million for an income year, as reported in the entity's tax return, and those with a liability to pay the PRRT. The published information discloses the entity's name, Australian Business Number, total income, taxable income, and tax payable.

The Australian government has encouraged all companies (annual turnover of AUD 100 million or more) to adopt a Voluntary Tax Transparency Code (TTC) for increased public disclosure of their tax information.

Australia has also adopted the OECD's Common Reporting Standard (CRS), which applies to financial institutions in Australia from 1 July 2017, with a first reporting deadline of 31 July 2018. Financial Institutions, including banks and other deposit-taking institutions, custodial institutions, or entities that hold financial assets for the account of others, are required to report information in the form of a statement to the Commissioner of Taxation about financial accounts held by foreign tax residents. In turn, the Commissioner of Taxation will provide this information to the foreign residents' tax authorities and will receive information on Australian tax residents with financial accounts held overseas.

Foreign investment tax conditions

Foreign investors that invest in Australia are now subject to additional criteria as part of the clearance process for proposed foreign investment in Australia. Tax conditions are now formally applied and will be considered in making an assessment of Australia's national interest, a key criterion in the foreign investment clearance process. These tax conditions may include requirements relating to the settlement of outstanding debts, ongoing compliance with tax laws, and annual reporting to the ATO.

Cambodia

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Significant developments

Cambodia introduces transfer pricing rules

On 10 October 2017, the Ministry of Economy and Finance (MEF) issued Prakas No. 986 to provide 'rules and procedures on income and expense allocation among related parties' (known as the 'Local Transfer Pricing Rules'), which is effective immediately. The Prakas represents one of the most important developments in the Cambodian tax regulations in the last 20 years. In addition to being in line with Cambodia's tax reform plans, this regulation also demonstrates Cambodia's commitment to aligning with global tax frameworks on transparency and combatting tax avoidance. *See Transfer pricing in the Group taxation section for more information*.

Revised tax base for tax for public lighting (TPL)

The MEF has issued Prakas No. 976 to revise the current tax base for the TPL on the supplies of alcohol and tobacco products for each supply transaction. This Prakas applies to the supplies of alcohol and tobacco products after the products are imported or produced in Cambodia.

The revised TPL base shall be determined as follows:

- For producers and importers, the TPL base is the price recorded on the invoice inclusive of all taxes, except value-added tax (VAT) and TPL itself.
- For further supply of the products to distributors/consumers, the TPL base is equal to 20% of the price recorded on the invoice inclusive of all taxes, except VAT and TPL itself.

Please note that before this Prakas, TPL was imposed at 3% on the invoice price at every supply of alcohol and tobacco products. TPL is due and payable at the time of supply. The rules of supply for TPL purposes shall be the same as the rules of VAT supply as stated in Article 62 of the Law on Taxation. Taxpayers who supply TPL products shall have their obligations to submit tax returns and make monthly payments of TPL no later than the 20th day of the following month. Prakas 976 is now effective.

Double taxation agreements (DTAs)

At the time of writing, the Kingdom of Cambodia had signed DTAs with the Republic of Singapore, the People's Republic of China, Brunei Darussalam, the Kingdom of Thailand, and the Socialist Republic of Vietnam for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income.

The agreements between the Kingdom of Cambodia and the Republic of Singapore and between the Kingdom of Cambodia and the Kingdom of Thailand have been effective from 1 January 2018. However, the agreements with the People's Republic of China, Brunei Darussalam, and the Socialist Republic of Vietnam are not yet effective.

The Kingdom of Cambodia is in the process of negotiating DTAs with other countries.

Deadline for submission of banks, insurance enterprises, and financial institutions' reportable accounts for 2014-2016 to the General Department of Taxation (GDT)

The GDT of the MEF has issued a Notification informing banks, insurance enterprises, and financial institutions that are subject to reporting obligations under the Agreement between the Cambodian Government and the Government of the United States of America to improve International Tax Compliance and to implement the Foreign Account Tax Compliance Act (FATCA) to submit their reportable accounts for 2014-2016 to the GDT no later than 30 June 2017.

Banks, insurance enterprises, and financial institutions that are subject to FATCA may incur penalties if they failed to submit their reportable accounts by the deadline.

Amendment to Article 7 of the Sub-Decree on the Establishment of a Social Security Scheme on Healthcare for Persons Defined by the Provisions of the Labour Law

The Royal Government of Cambodia has issued Sub-Decree No. 140 dated 26 August 2017), which amends Article 7 of Sub-Decree No. 1 (dated 6 January 2016) on the Establishment of a Social Security Scheme on Healthcare for Persons Defined by the Provisions of the Labour Law.

Previously, an employer and employee who are under the provisions of the Law on Social Security Schemes for persons defined by provisions of the Labour Law were required to continue paying healthcare benefits based on a 50% split between the employer and employee (i.e. 1.3% of average monthly wage each) to the National Social Security Fund (NSSF) until 31 December 2017.

Under the amended Sub-Decree, which is effective from 1 January 2018, the obligation to pay the contribution of healthcare as stated in the above paragraph is the full burden (100%) of the employer.

Guidelines on implementation of withholding tax (WHT) on dividend distributions

The MEF has issued Prakas No. 518 to provide guidelines on the implementation of WHT on dividend distributions as stated in the new Articles 26 and 33 of the Law on Taxation.

This Prakas intends to set out rules for implementation of WHT on dividend distributions that resident taxpayers pay to non-resident taxpayers. This Prakas is applicable to self-declaration taxpayers carrying out their businesses in Cambodia. The key points are:

- WHT on dividend distributions: Distribution of dividends, as defined in Article 10 of the Law on Financial Management for 2017, by resident taxpayers to non-resident taxpayers is subject to WHT at 14% (Article 26).
- Conversion of retained earnings into capital: Conversion of retained earnings, in part or in full, into registered capital of enterprise isn't considered as dividend

distribution and it's not subject to WHT. Enterprises making the conversion are required to have a resolution of their board of directors, and the revised capital must be recognised by the competent authorities.
- Sale of shares or distribution of capital from conversion of retained earnings: If an enterprise sells its shares or distributes its capital during the on-going business operations or during liquidation or dissolution of the enterprise, the capital portion that is converted from the retained earnings is subject to WHT (Article 26).
- Obligations of withholding agents: An enterprise that makes any dividend payment to non-resident taxpayers must submit a tax return and pay the WHT to the tax authorities by the 20th day of the following month.

For WHT purposes, if the dividend distribution is recorded in the accounting books, it will be considered as a dividend payment and so will trigger WHT obligations.

Taxes on corporate income

Cambodia's taxation rules vary according to the taxpayer's regime, the classification of taxpayers under different tax collection and control procedures of the GDT. The self-declaration regime is the only tax regime in Cambodia. Under the self-declaration regime, taxpayers are classified into three categories (e.g. large, medium, and small taxpayers) based on their turnover, legal form, and other criteria (*see table below*).

Type of taxpayer	Criteria (turnover is in approximate United States dollars [USD])
Small	Sole proprietorship or partnership: • annual turnover from USD 62,500 to USD 175,000 • total turnover for any three consecutive months in calendar year from USD 15,000 • total expected turnover for next three consecutive months from USD 15,000, or • participating in bidding, price consultation, or surveys for the supply of goods or services.
Medium	• annual turnover from USD 175,000 to USD 1 million • registered as a legal person or representative office • national or sub-national state institutions, associations, and non-government organisations (NGOs), or • foreign diplomatic and consular missions, international organisations, and technical cooperation agencies of other governments.
Large	• annual turnover from USD 1 million • Subsidiary of multi-national company, branch of a foreign company, or • Qualified Investment Projects (QIPs).

Resident taxpayers are subject to tax on worldwide income while non-residents are taxed on Cambodian-sourced income only. A permanent establishment (PE) is taxable on its Cambodian-source income only.

Corporate tax rate

The standard rate of corporate income tax (CIT), previously known as tax on profit, for companies and PEs who are classified as medium and large taxpayers is 20%.

For companies and PEs who are classified as small taxpayers, the CIT rates are progressive rates from 0% to 20%.

Industry-specific tax rates

Oil and gas and certain mineral exploitation activities are subject to CIT at the rate of 30%.

Insurance companies are taxable at a rate of 5% on the gross premium income and at the rate of 20% on other income derived from non-insurance/reinsurance activities. Net interest income of insurance companies received after 4% or 6% WHT is not taxable income.

The small taxpayer is subject to CIT at the progressive rates as stated in Article 20 of the Law on Taxation.

Minimum tax (MT)

Self-declaration regime taxpayers are subject to a separate MT. The MT is an annual tax with a liability equal to 1% of annual turnover inclusive of all taxes except VAT. However, an exemption has been provided for QIPs (*see the Tax credits and incentives section for more information*).

As a separate tax to the CIT, the MT is due irrespective of the taxpayer's profit or loss position (i.e. the MT will be liable if the 1% of total annual turnover exceeds the 20% CIT liability).

According to the Law on Financial Management 2017, the MT is no longer applicable to enterprises that maintain proper accounting records from 1 January 2017. However, there is still no definition of what constitutes 'maintaining proper accounting records'.

Additional CIT on dividend distribution

A dividend-paying taxpayer is required to pay an additional CIT at the time of dividend distribution if the profit was previously subject to a 9% or 0% CIT. The rates of additional CIT vary depending on the profits to be distributed. For profit that has been subject to CIT at the rate of 20%, 9%, or 0%, that profit will be subject to additional CIT at the following rates, respectively:

CIT	Additional CIT
20% (standard rate)	0%
9% (preferential rate, which is no longer applicable after 31 December 2010)	11/91 (approximately 12.09%)
0% (during tax holiday)	20%

A shareholder is entitled to establish a special dividend account from which the relevant dividend that was already subject to 20% CIT may be on-paid without further additional CIT obligations.

A dividend will be exempt from tax in the hands of the shareholder if additional CIT and WHT for non-resident shareholders has been paid.

Local income taxes

Provincial and local income taxes are not applicable in Cambodia.

Corporate residence

Resident taxpayers include companies organised, managed, or having their principal place of business in Cambodia.

Permanent establishment (PE)

A non-resident company may be deemed to have a PE in Cambodia if (i) there is a permanent place or entity through which the non-resident persons carry on their business, (ii) there is an exercise of the authority to conclude a contract on behalf of a foreign entity, or (iii) business activities exceed certain time periods in Cambodia.

Factors to be considered in determining a PE include a place of management, an agent or office, a warehouse or factory, a workshop, any place of extraction of natural resources, a plantation, etc. Carrying out projects (e.g. supervisory activities of a construction project, provision of services) exceeding a time period of six months in any 12-month period may also be considered as having a PE.

Other taxes

Value-added tax (VAT)

VAT is applicable to self-declaration regime entities and is charged at 10% on the value of the supply of most goods and services.

Exported goods and services rendered outside Cambodia are zero-rated. In addition, 0% VAT applies to the supporting industries or contractors who directly supply goods (including milled rice) or services (including milled rice production services) to export-oriented garment, textile, footwear, bag, handbag, and headwear manufacturers, milled rice exporters, and domestic supplies of paddy rice.

Some supplies are VAT exempt, the main categories being public postal services, medical and dental services, electricity, water, transportation of passengers by wholly state-owned public transport systems, insurance services, primary financial services, and land. Some are exempt supplies under the Law on Financial Management 2017.

VAT returns and payments are due within 20 days of the following month. Note that strict record-keeping requirements do exist.

Import and export duties

Import duties are levied on a wide range of products. Rates vary from 0% to 35%. Following Cambodia's entry into the Association of South-East Asia Nations (ASEAN) during 1999, the government is required to reduce import duties in accordance with the Common Effective Preferential Tariffs programme.

Export duties are levied on a limited number of items, such as timber and certain animal products (including most seafood).

Specific tax on certain merchandise and services (SPT)

SPT is a form of excise tax that applies to the importation or domestic production and supply of certain goods and services. SPT on domestically produced goods is generally applied to the SPT base, which is 90% of the invoice price before VAT and SPT itself. For imported goods, SPT is due on the cost, insurance, and freight (CIF) value inclusive of customs duty. For hotel and telecommunication services, SPT is payable based on the invoice prices.

For local and international air transportation of passengers, SPT is 10%, payable based on the air ticket value issued in Cambodia for travel within and outside Cambodia. The SPT base is inclusive of all taxes other than SPT and VAT. For example, for return air tickets from Phnom Penh to Singapore costing 2 million Cambodian riel (KHR), exclusive of airport tax, the SPT payable is KHR 181,818 (KHR 2 million/1.1 x 10%).

Accommodation tax

Accommodation tax is calculated at 2% of the accommodation fee, inclusive of all taxes and other services except accommodation tax and VAT.

Tax for public lighting (TPL)

TPL is imposed on the distribution in Cambodia of both foreign made and locally produced alcoholic and tobacco products.

The TPL base for calculation of 3% shall be determined as follows:

- For producers and importers, the TPL base is the price recorded on the invoice inclusive of all taxes, except VAT and TPL itself.
- For further supply of the products to distributors/consumers, the TPL base is equal to 20% of the price recorded on the invoice inclusive of all taxes, except VAT and TPL itself.

Tax on immovable property (ToIP)

ToIP is levied at 0.1% *per annum* of the ToIP base. The tax base is 80% of the market value of the immovable properties stated in Appendix 1 of Prakas No. 371 less the threshold of KHR 100 million. The immovable property valued below the threshold is not subject to ToIP. The Prakas also determines that ToIP is effectively collected on immovable properties located in Phnom Penh and other cities of the provinces.

Immovable property is defined to include land, buildings, and other constructions on land (e.g. infrastructures built on land, regardless of having a wall or roof). Certain exemptions exist for government-owned property, agricultural land, property owned and used for cultural and religious purposes, property of foreign embassies and NGOs, and property in the special economic zones.

The owners, possessors, and final beneficiaries of immovable property are required to register and obtain a Tax Identification Number for each immovable property valued above the threshold from the tax administration where the immovable property is located. Any changes in relation to the registered immovable property (e.g. a change of title) are also required to be reported.

The owners, possessors, and final beneficiaries hold responsibility for calculating ToIP, preparing and filing a ToIP return, as well as remitting the ToIP liability to the tax administration once per year by 30 September. A ToIP return is required for every single immovable property and must be completed and filed separately. Since this is a self-assessment tax, the tax administration will perform a tax audit on ToIP in the subsequent years.

Tax on unused land

Land in towns and other specified areas without any construction, or with construction that is not in use, and even certain built-upon land, is subject to the tax on unused land. The tax is calculated at 2% of the market value of the land per square metre as determined by the Commission for Valuation of Unused Land on 30 June each year. The owner of the land is required to pay the tax on 30 September each year. The tax is paid by the owner on land that doesn't fall under the scope of ToIP.

Stamp tax

Property

The transfer of title in certain assets (e.g. land, building, vehicles) and transfer of company shares (whether partial or full) are subject to stamp tax. The tax is imposed on the transfer values at the following rates:

- Transfer of assets: 4%.
- Transfer of shares: 0.1%.

The tax base for stamp tax on the soft and hard title transfer of immovable property (i.e. land) is the higher of:

- the property's value set by the appendix of the MEF's Prakas No. 962, or
- the property's value stated in a title transfer contract or other related legal documents if the transferred value is equal to or higher than the value set by the appendix of the Prakas.

Government contract

Stamp tax is imposed at the rate of 0.1% on the contract value of the public procurement contract for goods or services.

Document/signage

Stamp tax is to be paid on certain documents relating to the establishment, dissolution, or merger of a business, other official documents (perhaps more importantly for foreign investors), and certain advertising postings and signage. Amounts vary according to such factors as the type of documents, the location of the signage, illumination, and nationality of any scripted words. For certain documents, the tax amount is fixed up to KHR 1 million.

Cigarettes

Domestic producers or importers of cigarettes have the obligation to buy and affix tax stamps on packets of cigarettes. No person is allowed to sell or display packaged cigarettes for sale without a tax stamp.

Patent tax

Registered businesses must pay a (relatively nominal) patent tax on initial business registration and annually thereafter. Patent tax is levied with reference to turnover or estimated turnover.

Type of taxpayers	Patent tax (approximate USD amount)
Small	USD 100 per year
Medium	USD 300 per year

Type of taxpayers	Patent tax (approximate USD amount)
Large	• USD 750 for turnover from USD 500,000 to USD 2,500,000. • USD 1,250 for turnover of over USD 2,500,000.
	Additional tax of USD 750 if the taxpayer has a branch, warehouse, factory, or workshop for a business activity in a different city or province.

The annual patent tax return and payment are to be filed annually, within three months of calendar year-end.

Tax on means of transportation

The tax on means of transportation imposes a number of statutory fees on the registration of certain vehicles, including trucks, buses, and ships.

Tax on Salary (ToS) and Tax on Fringe Benefits (ToFB)

Cambodia's ToS rules follow internationally familiar residency and source principles. A Cambodian resident taxpayer's worldwide salary will be subject to Cambodian ToS. For non-residents, only the Cambodian-sourced salary will be subject to ToS. The place of salary payment is not considered relevant in determining source.

A distinction is made between cash and fringe benefit salary components. Different tax scales also apply.

ToS or ToFB is a tax on employees' income, but employers are held liable to these taxes if the employers fail to withhold.

The tax tables applicable to individuals (e.g. ToS, ToFB) are provided in the Taxes on personal income section of Cambodia's Individual tax summary at www.pwc.com/taxsummaries.

Social security contributions

Employers are currently required to make the Occupational Risks Contribution (ORC) and the payment for healthcare to the National Social Security Fund (NSSF).

Payment for ORC

An employer with at least eight employees must register itself and all its employees with the NSSF.

The employer is required to contribute ORC equal to 0.8% of the monthly average wage of an employee to the NSSF's designated bank account.

Payment for healthcare

In addition to the NSSF payment for ORC, the employer is also required to contribute, collect, and remit the contribution for healthcare to the NSSF on a monthly basis. According to Sub-Decree No. 140, dated 26 August 2017, from 1 January 2018, the obligation to pay the contribution of healthcare is the full burden (100%) of the employer at 2.6% of the monthly average wage of employees. Previously, the healthcare contribution was required from both employers and employees, each equal to 1.3% of the monthly average wage of employees.

Branch income

Branches of foreign corporations are subject to CIT on Cambodian-source income only.

If any branch of a foreign company transfers its Cambodian-sourced income to foreign countries, the income shall be subject to the WHT as stated in paragraph 10 of Article 33 of the Law on Taxation.

Income determination

Inventory valuation

Inventory can be valued at weighted-average cost, first in first out (FIFO), or current value at the close of the period, where this value is lower than the purchase price or production cost. Work-in-progress should be valued at production costs.

Capital gain

Capital gains form part of taxable profit.

Dividend income

Dividend means any distribution of money or property that a legal person distributes to a shareholder with respect to the shareholder's equity interest in such legal person, with the exception of stock dividends and distributions in complete liquidation of the company. Whether or not a distribution is a dividend shall be determined under the preceding condition without regard to whether or not the legal person has current or accumulated income or profit or earnings.

Inter-company dividends

Inter-company dividends between residents are exempt from CIT (*see the Withholding taxes section for more information*).

Gross dividend income received by a resident company from a non-resident enterprise is subject to CIT. A foreign tax credit for taxes paid on these dividends is allowed for deduction from the CIT. The maximum amount of the foreign tax credit is the CIT liability with respect to that dividend income.

Passive income

Designated passive income (such as interest, royalties, and rent) forms part of taxable profit.

Foreign income

Resident entities are taxed on their worldwide income, and tax credits are available for foreign taxes incurred. Foreign income is taxable in the period it is earned; there is no provision allowing tax to be deferred on the income earned overseas.

Deductions

Depreciation and amortisation

Property should be depreciated at rates according to four classes of assets as specified in the tax legislation. Land is not considered a depreciable asset. The straight-line or the declining-balance method is specifically required to be used for each class of assets.

Assets	Method	Rate (%)
Building and structures	Straight line	5
Computers, electronic information systems, software, and data handling equipment	Declining balance	50
Automobiles, trucks, office furniture, and equipment	Declining balance	25
All other tangible property	Declining balance	20

Expenditures on intangible property are amortisable over the life of the property or at 10% *per annum*.

Special depreciation

A QIP will be entitled to a 40% special depreciation in the first year of purchase or, if later, the first year the assets are used. However, the special depreciation will only apply to assets used in 'manufacturing and processing' (still to be defined) and only if the taxpayer has elected not to use a tax holiday. A clawback provision exists for assets held for less than four years.

Goodwill

Purchased goodwill is a depreciable intangible fixed asset for CIT purposes. If the useful life of the intangible fixed assets can be determined, the annual depreciation charges shall be calculated on the useful life by using the straight-line method. If the useful life cannot be determined, the annual depreciation rate of 10% shall be used.

Start-up expenses

Preliminary and formation expenses are allowed to be fully deducted in the period in which the expenses arise, or they can be amortised over two years.

Interest expenses

Interest deductibility in any year is limited to the amount of interest income plus 50% of the net profits excluding interest income and interest expense. The excess non-deductible interest expense can be carried forward to the following tax years indefinitely.

Based on the GDT's internal instruction, the tax authorities set maximum interest rates for loans from third parties (i.e. 120% of the market interest rate at the time of obtaining the loan) and loans from related persons (i.e. the market interest rate at the time of obtaining the loan). If the interest rate is higher than the maximum interest rate, the surplus interest expense is not deductible.

Bad debt

A loss on a claim (i.e. bad debt) is deductible where the impossibility to recover the loss can be clearly shown and that claim has been written off from the accounting books, except where the giving up of the claim is an 'abnormal act of management' (still to be defined).

Charitable contributions

The charitable contribution expense is deductible to the extent the amount does not exceed 5% of taxable profit. The taxpayer must have proper evidence supporting the payments.

Fines and penalties

Additional tax, late tax payment interest, and fines of all types incurred for the violation of various legal provisions are not deductible.

Taxes

Taxes that are not a charge to the enterprise (e.g. WHT, ToS, ToFB, CIT, and additional CIT on dividend distribution) are not deductible.

Loss between related parties

No deduction is available for certain losses incurred on dealings between 51% commonly owned parties.

Net operating losses

Taxpayers may carry forward their losses for five years. The carryback of losses is not permitted. There is no provision for any form of consolidated filing or group loss relief.

To be eligible to carry forward tax losses, a taxpayer must not change its activities or ownership.

If a taxpayer received a unilateral tax reassessment from the GDT, a taxpayer will not be able to utilise the tax losses brought forward in the year of reassessment.

Payments to foreign affiliates

An expense payable to a related party that is not paid within 180 days of the year-end will not be deductible. A deduction can be claimed in the year in which the payments are made. This rule is not applicable for an outlay or expense for inventory, capital property, and depreciable property.

Group taxation

There is no specific provision for group taxation in Cambodia.

Transfer pricing

On 10 October 2017, the MEF issued Prakas No. 986 to provide ‘rules and procedures on income and expense allocation among related parties’ (known as the ‘Local Transfer Pricing Rules’), which is effective immediately.

The Prakas defines the transfer price as ‘the price of goods, services, or property charged between related parties’. Transfer pricing refers to setting the value of transactions (e.g. the sale or purchase of goods or services, royalties, or interest) between related parties using the most appropriate transfer pricing methodology. If the transactions aren’t at arm’s length, the tax authority may adjust the value and impose taxes accordingly.

Cambodia

The purpose of transfer pricing rules is typically to make sure related entities compensate each other appropriately in an amount that is commensurate with the value of property transferred or services provided and to prevent entities from manipulating profits between related parties to minimise tax exposure.

We've summarised key information from the Prakas, including the definition of related party, acceptable transfer pricing methodologies, and the required documentation, below.

Related party definition

The Prakas defines 'related party' as a relative of the taxpayer or an enterprise that controls, is controlled by, or is under common control with the taxpayer. The term 'control' means ownership of 20% or more of the equity interest in the enterprise or voting power of the board of directors.

Transfer pricing methodologies

The acceptable methodologies for determining arm's-length pricing under the Prakas are those endorsed by the Organisation for Economic Co-operation and Development (OECD) in the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. The five methodologies are described below:

Transfer pricing method	How it works	When to use it
Comparable Uncontrolled Price (CUP)	The CUP method compares the price charged for goods or services transferred in a controlled transaction to the price charged for property or services transferred in a comparable uncontrolled transaction.	The CUP method is generally the most direct and reliable way to measure an arm's-length result for the same property in substantially the same circumstances as the controlled transaction. But it can be difficult to find a transaction that is similar enough that no differences have a material effect on the price.
Resale Price (RP)	The RP method determines the arm's-length price by deducting an appropriate gross margin for the activities of the reseller from the actual resale price.	RP is the easiest method to use if the distributors do not add significant value to the product transferred.
Cost Plus (CP)	The arm's length price is determined by adding an appropriate mark-up to the cost of the product or service.	The CP method is most useful for sales of semi-finished goods, joint facility agreements, long-term buy-and-supply arrangements, and the provision of services.
Transactional Net Margin Method (TNMM)	The TNMM compares the net profit margin relative to an appropriate base (e.g. costs, sales, or assets) that a taxpayer realises from a controlled transaction to an appropriate base. It is similar to the CP and RP methods but at the net profit margin level.	The TNMM applies to cases where one of the parties contributes unique intangibles, while the other party does not make any unique contribution.

Transfer pricing method	How it works	When to use it
Profit Split Method (PSM)	The PSM establishes transfer pricing by dividing the profits of a multinational company in a way that would be expected of independent companies in a joint-venture relationship. Independent companies would split the combined profit in proportion to the value of their respective contributions to the generation of profit in the transaction.	The PSM is the most appropriate method in cases where both parties to a transaction make unique and valuable contributions to the transactions.

Transfer pricing documentation

Entities that transact with related parties must prepare and maintain transfer pricing documentation setting out related-party transactions and the transfer pricing methodologies used to justify an arm's-length value. Documents related to the transactions, such as invoices, must also be kept for ten years from the tax year end.

Entities must also disclose related-party transactions when filing their annual CIT return and provide relevant transfer pricing documents if required by the tax authority.

Thin capitalisation

There is no provision for thin capitalisation in Cambodia.

Controlled foreign companies (CFCs)

There is no provision for CFCs in Cambodia.

Tax credits and incentives

Foreign tax credit

Residents earning foreign-sourced income can receive credits for foreign taxes paid.

Inbound investment

The Council for the Development of Cambodia (CDC) may be approached for a one-stop service to register a project and obtain approval for a QIP status. CDC licensing is, however, not mandatory (except for certain large, politically sensitive projects) and is applicable to those projects that do not fall within the 'negative list'. Some of the projects in the 'negative list' include the following:

- All kinds of commercial activities, import and export activities, and transportation services (except the railway sector).
- Currency and financial services.
- Activities that relate to newspapers and media.
- Production of tobacco products.
- Provision of value-added services of all kinds of telecommunication services.
- Real estate development.

The current investment incentives that are applicable to the QIP registered with the CDC include a CIT exemption period of up to six years or special depreciation (*see Special depreciation in the Deductions section*), import duty exemptions, and exemption from MT. Not all QIPs will be entitled to all incentives.

Annually, a QIP is required to obtain a Certificate of Compliance (CoC) from the CDC to guarantee its investment incentives. The CoC is intended to provide confirmation that the QIP has acted in compliance with the relevant tax regulations.

Additional tax incentives for rice farming, paddy rice purchase, and export of milled rice

The MEF has issued Prakas to provide additional tax incentives to any enterprises in the business of rice farming, paddy rice purchase, and export of milled rice, as follows:

VAT:

- Domestic supplies of paddy rice: 0%.
- Domestic supplies of milled rice: 10%.
- Export of milled rice: 0%.
- Supplies of milled rice or milled rice production services to rice exporters (subject to specific conditions): 0%.
- Supplies of milled rice or milled rice production services to the local market: 10%.
- Input VAT related to rice farming, paddy rice purchase, and export of milled rice is creditable or refundable.
- Input VAT related to import of production inputs and equipment to produce milled rice for export is borne by the government (subject to specific conditions).
- Local purchases of production inputs, except for paddy rice: 10%.

CIT and MT:

- Exempt from 1% MT.
- Entitled to tax holiday period (i.e. trigger period plus three years plus three year priority period).
- Exempt from 1% prepayment of CIT during the tax holiday period.

Withholding taxes

WHT needs to be withheld on payments made by residents (and it seems only to those who fall under the self-declaration regime). The withheld tax constitutes a final tax when withheld in respect of resident and non-residents.

The types of payments caught are as follows.

WHT on payment to residents

- Interest: 15% (except payment to a Cambodian bank).
- Royalties: 15%.
- Rental: 10%.
- Services: 15% (except payments to a registered taxpayer and supported by a valid VAT invoice).

WHT on payment to non-residents

Under the Law on Financial Management 2017, which is effective from 1 January 2017 onwards, any resident taxpayer carrying on a business, including a PE of a non-resident person, who pays any Cambodian-source income as defined under Article 33 of the Law on Taxation to a non-resident taxpayer must withhold tax at 14% of the amount paid. WHT does not apply to property or risk reinsurance premiums in Cambodia.

According to Article 33 of the Law on Taxation, Cambodian-source income includes:

- Interest paid by a resident enterprise, resident pass-through, or a governmental institution of Cambodia.
- Dividends distributed by a resident enterprise.
- Income from services performed in Cambodia.
- Compensation for management and technical services paid by a resident person.
- Income from movable or immovable property, if the property is situated in Cambodia.
- Royalties from the use, or right to use, intangible property paid by a resident person or paid by a non-resident person through a PE maintained in Cambodia.
- Gain from the sale of immovable property located in Cambodia or from the transfer of any interest in immovable property situated in Cambodia.
- Premiums from the insurance or reinsurance of risks in Cambodia.
- Gain from the sale of movable property that is part of a PE's business property maintained by a non-resident taxpayer in Cambodia.
- Income from business activities conducted by a non-resident through a PE in Cambodia.

WHT is due when the amount is paid. An expense is considered 'paid' when it is recorded in the accounting records.

Except WHT on the rental of movable and immovable properties as stated in Article 25 and 26 of the Law on Taxation, small taxpayers are exempted from being the WHT agents for other WHT implications.

Tax administration

Taxable period

The standard tax year is the calendar year, although different accounting year-ends may be granted upon application.

Tax returns

The return for annual tax (i.e. CIT or MT) is to be filed annually, within three months of tax year-end.

Returns for monthly taxes (e.g. 1% prepayments of CIT, WHT, ToS or ToFB, SPT, and accommodation tax) are to be filed monthly, within 20 days of the following month. The deadline will be extended to the next working day if the 20th day falls on a Saturday, Sunday, or public holiday.

Payment of tax

CIT or MT is due for payment three months after tax year-end. The CIT or MT liability can be reduced by prepayment of CIT payments.

Monthly taxes are due for payment by the 20th day of the succeeding month. The deadline will be extended to the next working day if the 20th day falls on a Saturday, Sunday, or public holiday.

Prepayment of CIT

A prepayment of CIT equal to 1% of monthly turnover inclusive of all taxes, except VAT, is required to be paid on a monthly basis. The prepayment can be offset against the annual CIT liability and the MT.

Where a taxpayer is in the period of CIT holiday, the taxpayer is also exempted from the prepayment obligations. However, a nil monthly return will need to be lodged.

Where a taxpayer is not subject to MT, a monthly prepayment of CIT must still be made. However, unutilised prepayments from a prior year can be used to offset the current amount due, and no physical payment may be required.

Tax audit process

There are two types of tax audit in Cambodia (i.e. limited and comprehensive tax audits). Initially, the tax authorities will send a notification letter to the taxpayer informing them of a tax audit. During the tax audit process, tax auditors visit the taxpayers' office to review the documents and discuss any potential tax issues with the taxpayers and may request supporting evidence. After the visit to the taxpayer's office, the tax auditors issue a notice of tax reassessment (NoTR), which indicates the reassessed tax liabilities and the basis of their tax reassessment. If the taxpayers agree with the reassessed tax liabilities, they can proceed with the payment. If not, the taxpayers have to submit an objection letter to the tax authorities within 30 days of the receipt of the NoTR.

Statute of limitations

The tax audit period (i.e. the limitation of the period within which the tax authorities can perform tax audits) is as follows:

- Within three years of the date of submission of the tax returns.
- Within ten years of the date of submission of the tax returns if there is any evidence of 'obstruction of the implementation of laws'.
- Any time with the written consent of the taxpayers.

In practice, the GDT regularly extends the time limit for tax audit up to ten years.

Topics of focus for tax authorities

In practice, the tax authorities focus the tax reassessment on various matters, including payment to third parties overseas, fringe benefits provided to employees, and related party transactions (e.g. payment of management fee to head office, loans from shareholder).

Other issues

Statutory financial audit requirement

All enterprises (whether physical or legal persons) that meet two of the following criteria are required to have their financial statements audited by an independent external auditor registered with the Kampuchea Institute of Certified Public Accountants and Auditors (KICPAA):

- Annual turnover above KHR 3 billion.
- Total assets above KHR 2 billion.

- More than 100 employees.

QIPs registered with the CDC are required to have their financial statements audited by independent external auditors registered with the KICPAA.

The law does not state the deadline for the enterprises to submit their audited financial statements. However, the deadline for audited financial statements to be completed is six months after the accounting year-end (i.e. for the financial year ended 31 December 2017, the deadline is 30 June 2018).

United States (US) Foreign Account Tax Compliance Act (FATCA)

The intergovernmental agreement (IGA) between the United States and Cambodia regarding the US FATCA was signed on 14 September 2015. This agreement shall enter into force on the date of Cambodia's written notification to the United States that Cambodia has completed its necessary internal procedures for entry into force of this agreement.

China, People's Republic of

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Significant developments

In 2017 and 2018, the Ministry of Finance (MoF) and State Administration of Taxation (SAT) issued several circulars to deepen the value-added tax (VAT) reform in China. The VAT rate of 13% was abolished from 1 July 2017. The VAT rates of 17%, 11%, and 6% were reduced to 16%, 10%, and 6%, respectively, from 1 May 2018.

In May 2017, China's relevant authorities jointly issued the Administrative Measure on Due Diligence Procedures for Non-residents' Financial Account Information in Tax Matters (the Measures) to implement the Common Reporting Standard (CRS) in China. Financial institutions established in China are required to carry out due diligence procedures on financial accounts starting from 1 July 2017. China is committed to exchange the first round of financial account information by September 2018.

Taxes on corporate income

Tax resident enterprises (TREs) are subject to corporate income tax (CIT) on their worldwide income. A non-TRE that has no establishment or place in China is taxed only on its China-source income. A non-TRE with an establishment or place in China shall pay CIT on income derived by such establishment or place from sources in China as well as income derived from outside China that effectively is connected with such establishment or place.

Under the CIT law, the standard tax rate is 25%.

A lower CIT rate is available for the following sectors/industries:

- Qualified new/high tech enterprises are eligible for a reduced CIT rate of 15%. An enterprise has to fulfil a set of prescribed criteria and be subject to an assessment in order to qualify as a new/high tech enterprise.
- Key software production enterprises and IC design enterprises are eligible for a reduced CIT rate of 10%. An enterprise has to fulfil a set of prescribed criteria and be subject to an assessment in order to qualify as a key software production enterprise or key IC design enterprise.
- Qualified technology-advanced service enterprises are eligible for a reduced CIT rate of 15%. An enterprise has to fulfil a set of prescribed criteria and be subject to an assessment in order to qualify as a technology-advanced service enterprise.

- Enterprises established in the Qianhai Shenzhen-Hong Kong Modern Services Industry Cooperation Zone are eligible for a reduced CIT rate of 15%, provided that the enterprise is engaged in projects that fall within the Catalogue for CIT Preferential Treatments of the zone.
- Enterprises established in Zhuhai's Hengqin New Area are eligible for a reduced CIT rate of 15%, provided that the enterprise is engaged in projects that fall within the Catalogue for CIT Preferential Treatments of the area.
- Enterprises established in the Pingtan Comprehensive Experimental Zone are eligible for a reduced CIT rate of 15%, provided that the enterprise is engaged in projects that fall within the Catalogue for CIT Preferential Treatments of the zone.
- For qualified small and thin-profit enterprises with annual taxable income of less than 1 million renminbi (CNY), the CIT rate is reduced to 10% from 1 January 2018 to 31 December 2020.
- From 1 January 2011 to 31 December 2020, encouraged enterprises in the Western Regions are eligible for a reduced preferential CIT rate of 15%.

Local income taxes

There is no local or provincial income tax in China.

Corporate residence

Enterprises established in China are always TREs. A foreign enterprise with a place of effective management in China is also regarded as a TRE.

Permanent establishment (PE)

An 'establishment or place' is defined in the CIT regulations as an establishment or place in China engaging in production and business operations, including the following:

- Management organisations, business organisations, and representative offices.
- Factories, farms, and places where natural resources are exploited.
- Places where labour services are provided.
- Places where contractor projects, such as construction, installation, assembly, repair, and exploration are undertaken.
- Other establishments or places where production and business activities are undertaken.
- Business agents who regularly sign contracts, store and deliver goods, etc. on behalf of the non-TRE.

Other taxes

Value-added tax (VAT)

The sales or importation of goods, the provision of services, and the sales of intangible properties and immovable properties are subject to VAT. For general VAT payers, input VAT can be credited against output VAT.

The applicable VAT rate for general VAT payers from 1 May 2018 are set out in the following table, and the rate for small-scale VAT payers is 3%.

Industries	Applicable VAT rate (%)
Sales or importation of goods	16
Sales or importation of necessity goods (e.g. agricultural products, water, gas)	10
Provision of repairs, replacement, and processing services	16
Tangible movable property leasing services	16
Transportation services, postal services, basic telecommunications services, construction services, immovable property leasing services, sales of immovable properties, transfer of land-use right	10
Value-added telecommunications services, financial services, modern services (except for leasing services), consumer services, sales of intangible properties (except for land-use right)	6
Exportation of goods; exportation of repair, replacement, and processing services; international transportation services and spacecraft transportation services; exported services that are completely consumed outside China, including: • Research and development (R&D) services. • Energy performance contracting services. • Design services. • Production and distribution services for radio, film, and television programs. • Software services. • Circuit design and testing services. • Information system services. • Process management services. • Offshore outsourcing services. • Transfer of technology.	0

For taxpayers that are eligible for the above zero rate, generally they may be entitled to a credit or refund of the input VAT incurred.

The VAT refund rate for exported services is the same as the applicable VAT rate. For exported goods, the VAT refund rates range from 0% to 16%. There is a prescribed formula for determining the amount of refund, under which full refund of input VAT is not available to many exported goods and the exporter will suffer different degrees of export VAT costs.

In addition, a few types of qualified exported services may be applicable to the VAT exemption treatment. In that respect, the relevant input VAT incurred cannot be credited or refunded.

Customs duties

Import and export customs duty is levied on goods that are allowed to be imported into or exported based on the relevant customs regulations. The Consignee of imported goods, consignor of export goods, and owner of entry articles are parties held liable for paying customs duties.

The customs classification of import and export goods is the base for the customs supervision, customs taxation, and customs statistics. In 2017, along with the revisions of the classified catalogue in 'International Convention for Harmonized Commodity Description and Coding System' made by World Customs Organisation (WCO), large scale adjustments have been made to China's import and export tariff system.

Import duty is charged in ad valorem, specific, compound, or sliding terms, etc. Ad valorem duty is charged based on the customs valuation of the goods. The dutiable value of the goods is multiplied by an ad valorem duty rate to arrive at the amount of duty payable. Duty collection on an ad valorem basis is the main taxation measure used by most countries, including China. The dutiable value of import and export goods is the taxable value determined by the Customs to levy ad valorem duties on the import and export goods, which is the base to value and levy customs duties payable of import and export goods and import links taxes payable of the import goods.

Import duties are categorised as normal tariff rate, Most Favoured Nation (MFN) tariff rate, contractual tariff rate, preferential tariff rate, tariff-rate quota (TRQ) rate, and temporary tariff rate.

The Country of Origin of imported goods also plays a part in determining the applicability of a number of other trade policies, such as TRQ, preferential tariffs, anti-dumping duty, anti-subsidy duty, etc.

Import and export goods are reduced with or exempted from customs duties, import VAT, and consumption tax according to state regulations.

The importation of raw materials under processing trade is bonded, and customs duty, import VAT, and consumption tax exemption is allowed on the part to be re-exported after processing.

For goods that enter into and exit from the customs special supervision zone, import duties, import VAT, and consumption tax are held over at the time of importation, which are to be exempted for exportation and to be paid for sales from the customs special supervision zone to domestic markets.

Consumption tax

A consumption tax is imposed on specified categories of luxury and environmental unfriendly goods, including cigarettes, alcoholic beverages, high-end cosmetics, jewellery, gasoline, automobiles, battery and coating, etc. The tax liability is computed based on the sales amount and/or the sales volume, depending on the goods concerned. Consumption tax is not recoverable but is deductible as an expense for CIT purposes.

Real estate tax

A real estate tax, which is based on the value of the property or rental received, is assessed annually on land and buildings used for business purpose or leased. The tax rate is 1.2% of the original value of buildings. A tax reduction of 10% to 30% is commonly offered by local governments. Alternatively, tax may be assessed at 12% of the rental value. Real estate tax is deductible for CIT purposes.

Urban and township land-use tax

An urban and township land-use tax is levied on taxpayers who utilise land within the area of city, country, township, and mining districts. It is computed annually based on the space of area actually occupied by a taxpayer multiplied by a fixed amount per square metre that is determined by the local governments.

Arable land occupation tax

Arable land occupation tax is levied on companies and individuals who build houses or carry out non-agricultural construction on arable lands. It is computed based on the space of area actually occupied by a taxpayer multiplied by a fixed amount per square metre that is determined by the local governments and is settled in a lump sum.

Land appreciation tax

A land appreciation tax is levied on the gain from the disposal of properties at progressive rates from 30% to 60%. Land appreciation tax is deductible for CIT purposes.

Stamp tax

All enterprises and individuals who execute or receive 'specified documentation', including 11 types of contracts and a few specified documents, are subject to stamp tax. The stamp tax rates vary between 0.005% on loan contracts to 0.1% for property leasing and property insurance contracts.

Deed tax

A deed tax, generally at rates from 3% to 5%, may be levied on the purchase, sale, gift, or exchange of ownership of land-use rights or real properties. The transferee/assignee is the taxpayer.

Payroll taxes

For employment income, an employer is obligated to withhold individual income tax from an employee's salary and settle the payment with the tax authorities on a monthly basis.

Social security contributions

Social security contributions to pension funds, medical funds, etc. are mandatory for both employers and employees in China. Employers are normally required to make social security contributions in relation to pension, medical, unemployment, maternity, and work-related injury for their employees. The percentage of social security benefits borne by employers and employees, as well as the contribution base, vary from city to city.

Urban construction and maintenance tax

Urban construction and maintenance tax is imposed at a certain rate on the amount of China's indirect taxes (i.e. VAT and consumption tax) payable by the taxpayer. Effectively, the taxpayers of indirect taxes are also the taxpayers of urban construction and maintenance tax. It is charged at three different rates depending on the taxpayer's location: 7% for urban areas, 5% for county areas, and 1% for other areas.

Educational surtax

Educational surtax is imposed at 3% on the amount of China's indirect taxes (i.e. VAT and consumption tax) payable by the taxpayer. Effectively, the taxpayers of indirect taxes are also the taxpayers of educational surtax.

Local educational surtax

Local educational surtax is levied at 2% on the amount of China's indirect taxes (i.e. VAT and consumption tax) payable by the taxpayer. Effectively, the taxpayers of indirect taxes are also the taxpayers of local educational surtax.

Motor vehicle acquisition tax

A motor vehicle acquisition tax at a rate of 10% of the taxable consideration will be levied on any purchase and importation of cars, motorcycles, trams, trailers, carts, and certain types of trucks.

Vehicle and vessel tax

A vehicle and vessel tax is a tax that is levied on all vehicles and vessels within China. A fixed amount is levied on a yearly basis. Transport vehicles generally are taxed on a fixed amount according to their own weight, with passenger cars, buses, and motorcycles being taxed on a fixed unit amount. Vessels are taxed on a fixed amount, according to the deadweight tonnage.

Vessel tonnage tax

Vessel tonnage tax is levied on any vessel entering into a port inside the territory of China from overseas and is collected by the General Customs. The tax payable is computed based on the net tonnage multiplied by the applicable tax rate that is determined based on the net tonnage and the term of the tonnage tax licence.

Resource tax

The exploitation of natural resources, including crude oil, natural gas, coal, salt, raw metallic metals, and non-metallic metals, etc., is subject to resource tax on a sales turnover or tonnage/volume basis. The range of tax rates are specified by the State Council.

Resource tax is collected on the usage of water in 10 provinces on a trial basis.

Environmental protection tax (EPT)

China's legislative body passed the Environmental Protection Tax Law (EPT Law) at the end of 2016. The EPT Law became effective on 1 January 2018 and replaced the previous pollutant discharge fees. EPT is collected from enterprises that directly discharge taxable pollutants (i.e. air pollutants, water pollutants, solid waste, and noise pollution) within the territory of China. EPT is calculated based on the volume of pollutants discharged, multiplied by the specific EPT amount.

Tobacco tax

Tobacco tax is levied on taxpayers who purchase tobacco leaves within the territory of China. The tax is assessed at the rate of 20% on the purchasing value and shall be settled with the local tax bureau at the place of the purchase.

Cultural business development levy

Companies and individuals engaged in entertainment and advertising businesses shall pay cultural business development levy at 3% on the relevant income.

Branch income

Under the CIT law, a branch of a non-TRE in China is taxed at the branch level. If there is more than one branch, they may elect to file their tax at the main office in China on a consolidated basis. There is no further tax upon remittance of branch profits.

Income determination

Taxable income is defined as 'gross income in a tax year after deduction of non-taxable income, tax exempt income, various deductions, and allowable losses brought forward from previous years'. The accrual method of accounting should be used.

Gross income refers to monetary and non-monetary income derived by an enterprise from various sources, including, but not limited to, the sales of goods, provision of services, transfer of property, dividends, interest, rentals, royalties, and donations.

Non-taxable income refers to fiscal appropriation, governmental administration charges, governmental funds, and other income specified by the central government.

Inventory valuation

Inventory must be valued according to costs. In computing the cost of inventories, the enterprise may choose one of the following methods: first in first out (FIFO), weighted average, or specific identification.

Unrealised gain or loss due to changes in fair value

An unrealised gain or loss due to changes in the fair value of financial assets, financial liabilities, and investment properties held by an enterprise is not taxable/deductible for CIT purpose. The gain/loss is taxable/deductible only when the asset/liability actually is disposed of or realised.

Capital gains

Capital gains are treated in the same way as ordinary income of a revenue-nature for a TRE.

Dividend income

An exemption exists for CIT on dividend derived by a TRE from the direct investment into another TRE except for where the dividend is from stocks publicly traded on the stock exchanges and the holding period is less than 12 months.

Interest income

Interest income is treated as ordinary income.

Rental income

Rental income is treated as ordinary income.

Royalty income

Royalty income is treated as ordinary income.

Partnership income

Partnerships registered in China are not subject to CIT. The income of a partnership is taxable at the partners' level.

Unrealised exchange gains

Unrealised exchange gain (loss) from the year-end translation of assets (liabilities) denominated in foreign currency generally is taxable (deductible).

Foreign income

The worldwide income of a TRE and its branches both within and outside China is taxable. There are no provisions in the CIT law that allow foreign income directly earned by the TRE to be deferred for tax purposes. The CIT law contains a controlled foreign company (CFC) rule under which the unremitted earnings of a foreign company controlled by Chinese enterprises may be taxable in China (*see the Group* *taxation section for more information*). A foreign tax credit is allowed for foreign income taxes paid on foreign-source income.

Deductions

Generally, an enterprise is allowed to deduct reasonable expenditures that actually have been incurred and are related to the generation of income.

Depreciation of fixed assets

Fixed assets with useful lives of more than 12 months must be capitalised and depreciated in accordance with the CIT regulations. Generally, depreciation is calculated by the straight-line method. Shorter tax depreciation life or accelerated depreciation may be allowed due to advancement of technology or suffering from constant vibration or severe corrosion. Production-nature biological assets, such as livestock held for breeding and commercial timber, also have to be capitalised and depreciated using the straight-line method.

Under the straight-line method, the cost of an item, less its residual value, is depreciated over the useful life of the asset. Residual value should be reasonably determined based on the nature and usage of the asset. The CIT law provides minimum useful lives for the following assets:

Assets	Years
Buildings and structures	20
Aircraft, trains, vessels, machinery, mechanisms, and other production equipment	10
Appliances, tools, and furniture etc. related to production and business operations	5
Means of transport other than aircraft, trains, and vessels	4
Electronic equipment	3
Production-nature biological assets in the nature of forestry	10
Production-nature biological assets in the nature of livestock	3

From 1 January 2018 to 31 December 2020, newly acquired fixed assets, other than real estate properties, with unit value not exceeding CNY 5 million are allowed to be expensed-off in one lump sum in the year of acquisition.

Accelerated depreciation

Shorter tax depreciation life or accelerated depreciation is allowed for particular types of fixed assets (e.g. fixed assets that need to be replaced more frequently due to advancement of technology, fixed assets that suffer from constant vibration or severe corrosion).

From 1 January 2018 to 31 December 2020, new fixed assets and equipment, other than real estate properties, with unit value exceeding CNY 5 million acquired by companies in certain specified industries may be depreciated over a shorter depreciation life or under an accelerated depreciation method.

Where a shorter depreciation period method is applied, the minimum depreciation period cannot be less than 60% of the minimum depreciation period as prescribed in the CIT Law; where an accelerated depreciation method is applied, the double-declining-balance method or sum-of-years-digits method can be used.

Amortisation of intangibles and goodwill

A deduction is allowed for amortisation of intangible assets, such as, but not limited to, patents, trademarks, copyrights, and land-use rights. Generally, intangible assets have to be amortised over a period of not less than ten years. For an intangible asset obtained through capital contribution or assignment, it can be amortised according to the useful life prescribed in the laws or agreed in the contracts, if any. However, acquired goodwill is not deductible until the invested enterprise is entirely transferred or liquidated.

Organisational and start-up expenses

Organisational and start-up expenses are tax deductible fully in the first year of operation.

Research and development (R&D) expense

For R&D expenses incurred for new technology, new products, or new craftsmanship, an extra 50% of the actual expenses incurred are also tax-deductible as an incentive.

From 1 January 2017 to 31 December 2019, the extra 50% deduction is increased to 75% for qualified small and medium-sized technology enterprises.

Asset loss

Asset loss (including bad debt loss) may be deductible in the tax year during which such loss is incurred, provided that supporting documents are maintained for inspection by the in-charge tax bureau.

Interest expenses

Interest on loans generally is tax-deductible. For interest expenses on borrowings from non-financial institutions by a non-financial institution, the portion that does not exceed the commercial rate is deductible. The tax deduction of interest paid to related parties is subject to the thin capitalisation rule under the CIT law (*see the Group taxation section for more information*).

Reserves and provisions

Provisions for asset impairment reserves (e.g. bad debt provisions) and risk reserves generally are not tax-deductible unless otherwise prescribed in the tax rules. Financial institutions and insurance companies may deduct certain provisions and reserves, subject to the caps specified in the relevant tax circulars.

Contingent liabilities

The CIT law does not specifically address the deductibility of contingent liabilities. According to the general principle of the CIT law, contingent liabilities are liabilities that an enterprise has not actually incurred and thus shall not be tax-deductible.

Charitable donations

Charitable donations are tax-deductible at up to 12% of the annual accounting profit, and any excess amount in the current year can be carried forward and deductible in the following three years. Non-charitable donations, as well as sponsorship expenditures that are non-advertising and non-charitable in nature, are not deductible.

Wages and staff welfare expenses

Reasonable wages and salaries of employees incurred by an enterprise are tax-deductible. Directors' fees are also tax-deductible. As an incentive to encourage the hiring of handicapped people, 200% of the actual salary expenses paid to handicapped staff are deductible.

Basic social security contributions, including basic pension insurance, basic medical insurance, unemployment insurance, injury insurance, maternity insurance, and housing funds, that are made by an enterprise in accordance with the scope and criteria as prescribed by the state or provincial governments are deductible.

Commercial insurance premiums paid for investors or employees shall not be tax-deductible unless they are paid for safety insurance for workers conducting special types of work.

Staff welfare expenses, labour union fees, and staff education expenses are tax-deductible at up to 14%, 2%, and 8% of the total salary expenses, respectively.

Entertainment expenses

Entertainment expenses are tax-deductible up to the lesser of 60% of the costs actually incurred and 0.5% of the sales or business income of that year. The excess amount must not be carried forward to and deducted in the following tax years.

Advertising expenses and business promotion expenses

Advertising expenses and business promotion expenses are deductible at up to 15% (30% for certain enterprises in the cosmetics, medicine, and beverage industries) of the sales (business) income of that year unless otherwise prescribed in the tax regulations. Any excess amount is allowed to be carried forward and deductible in the following tax years. Advertising expenses and business promotion expenses incurred by the tobacco industry are entirely not tax-deductible.

Fines and penalties

Fines, penalties, and losses arising from confiscation of property are not deductible for CIT purposes.

Taxes

CIT payments and surcharges that are imposed on overdue taxes are not deductible for CIT purposes.

Net operating losses

Generally, tax losses can be carried forward for no longer than five years starting from the year subsequent to the year in which the loss was incurred. For new/high tech enterprises and small and medium sized technology enterprises, tax loss can be carried forward for ten years. Carryback of losses is not permitted.

Payments to affiliates

Management fees for stewardship are not deductible, but services fees paid for genuine services provided by affiliates in China or overseas and charged at arm's length should be deductible. Other payments to affiliates, such as royalties, are also tax-deductible, provided that the charges are at arm's length.

Group taxation

Group taxation is not permitted under the CIT law unless otherwise prescribed by the State Council.

Transfer pricing

All enterprises are required to conduct transactions with related parties on an arm's-length basis. The Chinese tax authorities are empowered to make adjustments to transactions between related parties that are not conducted at arm's length and result in the reduction of taxable income of the enterprise or its related parties using the following appropriate methods: comparable uncontrolled price method, resale price method, cost plus method, transactional net margin method, profit split method, and other methods (e.g. cost approach, market approach, income approach) that are consistent with the arm's-length principle. In June 2016, the SAT issued a circular that imposed new transfer pricing compliance requirements in China, including annual reporting forms for related-party transactions (RPT forms), country-by-country (CbC) reporting, and transfer pricing documentation, all of which contain substantial changes to the previous rules. Specifically, the transfer pricing documentation requirement has adopted a three-tiered approach, including a master file, local file, and special issue file (i.e. cost sharing agreement special issue file and thin capitalisation special issue file).

The SAT also issued a revised circular on advance pricing arrangements (APAs) in October 2016, which provides process and requirements for an enterprise to apply for an APA as well as the situations where an APA application will be prioritised or declined.

The SAT issued a circular in March 2017 to renew the Chinese rules on the procedures of transfer pricing investigation and mutual agreement procedures (MAPs). This circular empowers the Chinese tax authorities to collect financial information of overseas related parties under the transfer pricing audit for value chain purpose. In addition, this circular reiterates and reinforces the Chinese tax authorities' focus on outbound related-party remittance, such as service fees and royalty payments (*see Recent focus of Chinese tax authorities in the Tax administration section for details*).

The CIT law also contains a few tax avoidance rules, such as a thin capitalisation rule (*see below*), a CFC rule (*see below*), and general anti-avoidance rules (GAAR) (*see the Tax administration section*).

Thin capitalisation

The CIT law has a thin capitalisation rule disallowing interest expense arising from excessive related-party loans. The safe harbour debt/equity ratio for enterprises in the financial industry is 5:1 and for enterprises in other industries is 2:1. However, if there is sufficient evidence (e.g. a thin capitalisation special issue file) to show that the financing arrangement is at arm's length, these interests may still be fully deductible even if the ratios are exceeded.

Controlled foreign companies (CFCs)

Under the CFC rule, the undistributed profits of CFCs located in low-tax jurisdictions with an effective income tax rate of less than 12.5% may be taxed as a deemed distribution to the TRE shareholders. The Chinese tax authorities have published a list of countries (i.e. a 'white list') that they do not regard to be low-tax jurisdictions.

Tax credits and incentives

The CIT law adopts the 'Predominantly Industry-oriented, Limited Geography-based' tax incentive policy. Key emphasis is placed on 'industry-oriented' incentives aiming at directing investments into those industry sectors and projects encouraged and supported by the state. The tax incentive policies mainly include the following and are applicable to both domestic and foreign investments.

Tax reduction and exemption

CIT may be reduced or exempted on income derived from the following projects:

Projects/industries	CIT incentive	Valid period
Agriculture, forestry, animal-husbandry, and fishery projects	Exemption or 50% reduction	All years, as long as it is engaged in these projects
Specified basic infrastructure projects	3 + 3 years tax holiday (2)	Starting from the first income-generating year
Environment protection projects and energy/water conservative projects	3 + 3 years tax holiday (2)	Starting from the first income-generating year
Qualified new/high tech enterprises established in Shenzhen, Zhuhai, Shantou, Xiamen, Hainan, and Pudong New Area of Shanghai after 1 January 2008	2 + 3 years tax holiday (1)	Starting from the first income-generating year
Software enterprises established before 31 December 2017	2 + 3 years tax holiday (1)	Starting from the first profit-making year or 2017, whichever is earlier
Integrated circuits design enterprises established before 31 December 2017	2 + 3 years tax holiday (1)	Starting from the first profit-making year or 2017, whichever is earlier
Integrated circuits production enterprises established before 31 December 2017 with a total investment exceeding CNY 8 billion or that produce integrated circuits with a line-width of less than 0.25um, provided that its operation period exceeds 15 years	5 + 5 years tax holiday (3)	Starting from the first profit-making year
Integrated circuits production enterprises established before 31 December 2017 that produce integrated circuits with a line-width of less than 0.8um	2 + 3 years tax holiday (1)	Starting from the first profit-making year
Integrated circuits production enterprises or projects invested after 1 January 2018 that produce integrated circuits with a line-with of less than 130nm, provided that its operation period exceeds 10 years	2 + 3 years tax holiday (1)	Starting from the first profit-making year for enterprises; Starting from the first income-generating year for projects
Integrated circuits production enterprises or projects invested after 1 January 2018 with a total investment exceeding CNY 15 billion or that produce integrated circuits with a line-with of less than 65nm, provided that its operation period exceeds 15 years	5 + 5 years tax holiday (3)	Starting from the first profit-making year for enterprises; Starting from the first income-generating year for projects
Qualified integrated circuits packaging/testing enterprises established before 31 December 2017	2 + 3 years tax holiday (1)	Starting from the first profit-making year or 2017, whichever is earlier
Qualified enterprises that manufacture key parts or equipment used for the production of integrated circuits established before 31 December 2017	2 + 3 years tax holiday (1)	Starting from the first profit-making year or 2017, whichever is earlier

Projects/industries	CIT incentive	Valid period
Qualified energy-saving service enterprises	3 + 3 years tax holiday (2)	Starting from the first income-generating year
Encouraged enterprises in underprivileged areas of Xinjiang	2 + 3 years tax holiday (1)	Starting from the first income-generating year
Projects involving a clean development mechanism (CDM)	3 + 3 years tax holiday	Starting from the first year during which the first disposal of certified emission reduction units takes place
Certified animation enterprises that produce self-developed animation products established before 31 December 2017	2 + 3 years tax holiday (1)	Starting from the first profit-making year or 2017, whichever is earlier

Notes

1. '2 + 3 years tax holiday' refers to two years of exemption from CIT followed by three years of 50% reduction of CIT.
2. '3 + 3 years tax holiday' refers to three years of exemption plus three years of 50% reduction of CIT.
3. '5 + 5 years tax holiday' refers to five years of exemption plus five years of 50% reduction of CIT.

For income derived from the transfer of technology in a tax year, the portion that does not exceed CNY 5 million shall be exempted from CIT and the portion that exceeds CNY 5 million shall be allowed a 50% reduction of CIT.

A CIT exemption applies to the dividend derived by a TRE from the direct investment into another TRE, except where the dividend is from stocks publicly traded on the stock exchanges and the holding period is less than 12 months.

A CIT exemption also applies to the income derived by recognised non-profit-making organisations engaging in non-profit-making activities.

Reduced tax rate

The CIT rate may be reduced under certain conditions for different industries (*see the Taxes on corporate income section for more information*).

Reduction of revenue

Where an enterprise uses resources specified by the state as its major raw materials to produce non-restricted and non-prohibited products, only 90% of the income derived is taxable.

Offset of certain venture capital investment

For a venture capital enterprise that makes an equity investment in a non-listed small to medium-sized new/high tech enterprise or a start-up technology enterprise for more than two years, 70% of its investment amount may be used to offset against the taxable income of the venture capital enterprise in the year after the holding period has reached two years. Any portion that is not utilised in that year can be carried forward and deducted in the following years. A Chinese corporate partner of a venture capital in the form of a limited partnership is also eligible for such incentive.

Investment tax credit

Enterprises purchasing and using equipment specified by the state for environmental protection, energy and water conservation, or production safety purposes are eligible for a tax credit of 10% of the investment in such equipment. Any unutilised amount can be carried forward and creditable in the following five years.

Other incentives

There are also tax incentives in relation to the deduction of expenses and cost (e.g. 50% additional R&D deduction, shorter tax depreciation period, and accelerated depreciation). *See the Deductions section for more information*.

Foreign tax credit

A TRE is allowed to claim foreign tax credit in relation to foreign income tax already paid overseas in respect of income derived from sources outside China on a country-basket basis or under the comprehensive method. The creditable foreign tax also includes foreign income tax paid by qualified CFCs. However, the creditable amount may not exceed the amount of income tax otherwise payable in China in respect of the foreign-sourced income. In addition, there is a five-year carryforward period for any unutilised foreign tax.

Withholding taxes

Foreign enterprises without establishments or places of business in China shall be subject to a unilateral concessionary rate of withholding tax (WHT) at 10% on gross income from dividends, interest, lease of property, royalties, and other China-source passive income unless reduced under a tax treaty. Nevertheless, dividends distributed by a foreign investment enterprise out of its pre-2008 profit are still exempted from WHT.

WHT rates under China's tax treaties with other countries/nations are as follows (as of 31 May 2018):

	WHT (%)		
Recipient	**Dividends**	**Interest (1)**	**Royalties (2)**
Non-treaty	10	10	10
Treaty:			
Albania	10	10	10
Algeria	5/10 (3a)	7	10
Armenia	5/10 (3a)	10	10
Australia	15	10	10
Austria	7/10 (3b)	7/10 (4a)	6/10
Azerbaijan	10	10	10
Bahrain	10	10	10
Bangladesh	10	10	10
Barbados	5/10 (3a)	10	10
Belarus	10	10	10
Belgium	5/10 (3i)	10	7
Bosnia and Herzegovina (7)	10	10	10
Botswana (9)	5	7.5	5
Brazil	15	15	15/25 (5a)
Brunei	5	10	10
Bulgaria	10	10	7/10
Cambodia	10	10	10
Canada	10/15 (3f)	10	10
Chile	10	4/10/15 (4b)	2/10
Croatia	5	10	10

Recipient	WHT (%) Dividends	Interest (1)	Royalties (2)
Cuba	5/10 (3a)	7.5	5
Cyprus	10	10	10
Czech Republic	5/10 (3a)	7.5	10
Denmark	5/10 (3a)	10	7/10
Ecuador (6)	3/5 (6)	8/10 (6)	8/10 (6)
Egypt	8	10	8
Estonia	5/10 (3a)	10	10
Ethiopia	5	7	5
Finland	5/10 (3a)	10	7/10
France	0/5/10 (3q)	10	6/10
Georgia	0/5/10 (3c)	10	5
Germany	5/10/15 (3o)	10	6/10
Greece	5/10 (3a)	10	10
Hong Kong Special Administrative Region	5/10 (3d)	7	5/7 (5d)
Hungary	10	10	10
Iceland	5/10 (3a)	10	7/10
India	10	10	10
Indonesia	10	10	10
Iran	10	10	10
Ireland, Republic of	5/10 (3b)	10	6/10
Israel	10	7/10 (4a)	7/10
Italy	10	10	7/10
Jamaica	5	7.5	10
Japan	10	10	10
Kazakhstan	10	10	10
Kenya (9)	5	10	10
Korea, Republic of	5/10 (3a)	10	10
Kuwait	0/5 (3l)	5	10
Kyrgyzstan	10	10	10
Laos	5	5 (in Laos) 10 (in Mainland China)	5 (in Laos) 10 (in Mainland China)
Latvia	5/10 (3a)	10	7
Lithuania	5/10 (3a)	10	10
Luxembourg	5/10 (3a)	10	6/10
Macao Special Administrative Region	5/10 (3a)	7	5/7 (5d)
Macedonia	5	10	10
Malaysia	10	10	10/15 (5b)
Malta	5/10 (3a)	10	7/10
Mauritius	5	10	10
Mexico	5	10	10
Moldova	5/10 (3a)	10	10
Mongolia	5	10	10
Morocco	10	10	10
Nepal	10	10	15
Netherlands	0/5/10 (3j)	10	6/10
New Zealand	15	10	10
Nigeria	7.5	7.5	7.5

China, People's Republic of

	WHT (%)		
Recipient	**Dividends**	**Interest (1)**	**Royalties (2)**
Norway	15	10	10
Oman	5	10	10
Pakistan	10	10	12.5
Papua New Guinea	15 (3n)	10	10
Philippines	10/15 (3g)	10	10/15 (5b)
Poland	10	10	7/10
Portugal	10	10	10
Qatar	10	10	10
Romania	0/3 (3r)	0/3 (4c)	3
Russia	5/10 (3p)	0	6
Saudi Arabia	0/5 (3m)	10	10
Seychelles	5	10	10
Singapore	5/10 (3a)	7/10 (4a)	6/10
Slovak Republic	10	10	10
Slovenia	5	10	10
South Africa	5	10	7/10
Spain	10	10	6/10
Sri Lanka	10	10	10
Sudan	5	10	10
Sweden	5/10 (3a)	10	6/10
Switzerland	0/5/10 (3j)	10	9
Syria	5/10 (3a)	10	10
Taiwan (9)	5/10 (3d)	7	7
Tajikistan	5/10 (3a)	8	8
Thailand	15/20 (3d)	10	15
Trinidad and Tobago	5/10 (3e)	10	10
Tunisia	8	10	5/10 (5c)
Turkey	10	10	10
Turkmenistan	5/10 (3a)	10	10
Uganda (9)	7.5	10	7/10
Ukraine	5/10 (3a)	10	10
United Arab Emirates	0/7 (3l)	7	10
United Kingdom	5/10/15 (3k)	10	6/10
United States	10	10	7/10
Uzbekistan	10	10	10
Venezuela	5/10 (3h)	5/10 (4a)	10
Vietnam	10	10	10
Yugoslavia (8)	5	10	10
Zambia	5	10	5
Zimbabwe	2.5/7.5 (3e)	7.5	7.5

Source: State Administration of Taxation, China

Notes

This table is a summary only and does not reproduce all the provisions relevant in determining the application of WHT in each tax treaty/arrangement.

1. 0% is due on interest paid to government bodies, except for Australia, Bosnia and Herzegovina, Brunei, Chile, Cyprus, Israel, Slovenia, and Spain. Reference should be made to the individual tax treaties.

2. The lower rate on royalties applies for the use of or right to use any industrial, commercial, or scientific equipment.
3. The following notes apply to dividend WHT:
    a. The lower rate applies where the beneficial owner of the dividend is a company (not a partnership) that directly owns at least 25% of the capital of the paying company.
    b. The lower rate applies where the beneficial owner of the dividend is a company that directly owns at least 25% of the voting shares of the paying company.
    c. The lowest rate (i.e. 0%) applies where the beneficial owner is a company that directly or indirectly owns at least 50% of the capital of the paying company and the investment exceeding 2 million euros (EUR). The lower rate (i.e. 5%) applies where the beneficial owner is a company that directly or indirectly owns at least 10% of the capital of the paying company and the investment exceeding EUR 100,000.
    d. The lower rate applies where the beneficial owner of the dividend is a company that directly owns at least 25% of the capital of the paying company.
    e. The lower rate applies where the beneficial owner of the dividend is a company that directly or indirectly owns at least 25% of the capital of the paying company.
    f. The lower rate applies where the beneficial owner of the dividend is a company that owns at least 10% of the voting stock of the paying company.
    g. The lower rate applies where the beneficial owner of the dividend is a company that directly owns at least 10% of the capital of the paying company.
    h. The lower rate applies where the beneficial owner is a company (other than a partnership) that directly owns at least 10% of the capital of the paying company.
    i. The lower rate applies where the beneficial owner of the dividend is a company (not a partnership) that directly owns at least 25% of the capital of the paying company within at least 12 consecutive months before the payment takes place.
    j. The lowest rate (i.e. 0%) applies if the beneficial owner of the dividends is the governmental bodies specified in the treaty, any of its institutions, or other entity the capital of which is wholly owned, directly or indirectly, by that contracting state. The lower rate (i.e. 5%) applies if the beneficial owner is a company (other than a partnership) that directly holds at least 25% of the capital of the company paying the dividends. The 10% rate applies in all other cases.
    k. The 0% rate applies if the beneficial owner of the dividends is the government of the other contracting state. The 5% rate applies if the beneficial owner of the dividends is a company that directly holds at least 25% of the capital of the company paying the dividends. The 15% rate applies where those dividends are paid out of income or gains derived directly or indirectly from immovable property within the meaning of Article 6 by an investment vehicle that distributes most of this income or gains annually and whose income or gains from such immovable property is exempted from tax. The 10% rate applies in all other cases.
    l. The lower rate (i.e. 0%) applies where the beneficial owner of the dividend is (i) the government of the other contracting state or any of its institutions or other entity wholly owned, directly or indirectly, by the government of the other contracting state or (ii) a company that is a resident of the other contracting state whose shares are at least 20% owned, directly or indirectly, by the government of the other contracting state.
    m. The lowest rate (i.e. 0%) applies where the beneficial owner of the dividend is the government of the other contracting state or any of its institutions or other entity wholly owned, directly or indirectly, by the government of the other contracting state.
    n. In the case of Papua New Guinea, the WHT shall be limited to 10% of the dividend while the Chinese tax law existing on the date of the signing of the tax treaty regarding dividends still applies; otherwise, the tax rate shall be 15%.
    o. The lowest rate (i.e. 5%) applies if the beneficial owner of the dividends is a company (other than a partnership) that directly holds at least 25% of the capital of the company paying the dividends. The highest rate (i.e. 15%) applies where those dividends are paid out of income or gains derived directly or indirectly from immovable property within the meaning of Article 6 by an investment vehicle that distributes most of this income or gains annually and whose income or gains from such immovable property is exempted from tax. The 10% rate applies in all other cases.
    p. The lower rate (i.e. 5%) applies if the beneficial owner of the dividends is a company (other than a partnership) that directly holds at least 25% of the capital of the company paying the dividends and this holding amounts to at least EUR 80,000 or its equivalent in any other currency.
    q. The lowest rate (i.e. 0%) applies if the dividends are derived by a sovereign wealth fund specified in the treaty. The lower rate (i.e. 5%) applies if the beneficial owner of the dividends is a company (other than a partnership) that directly holds at least 25% of the capital of the company paying the dividends. The 10% rate applies in all other cases. However, the dividends may be taxed at the rate under the domestic law if the dividends are paid out of income or gains derived from immovable property within the meaning of Article 6 by an investment vehicle that distributes most of this income or gains annually, whose income or gains from such immovable property is exempted from tax, and where the beneficial owner of those dividends holds, directly or indirectly, 10% or more of the capital of the vehicle paying the dividends.
    r. The lower rate (i.e. 0%) applies if the dividends arise in a contracting state and are paid to the other contracting state or a political subdivision, local authority, or administrative - territorial unit thereof, or any entity wholly or mainly owned by the other contracting state.
4. The following notes apply to interest WHT:
    a. The lower rate applies to interest payable to banks or financial institutions.

   b. The lowest rate (i.e. 4%) applies to interest payable to banks or financial institutions. The highest rate (i.e. 15%) will be applied for a period of two years from the date on which the treaty takes effect, and the 10% rate will be applied afterwards. In the event that Chile agrees to a lower rate of tax with another country (in particular with reference to financial institutions wholly owned by the government), such new rate shall automatically apply under the China/Chile tax treaty under the same conditions.
   c. The lower rate applies to the interest that is paid (i) in respect of indebtedness arising as a consequence of the sales on credit of any equipment, merchandise, or service; (ii) on any loan granted by a financial institute of that contracting state; or (iii) to that other state or a political subdivision, local authority, or administrative – territorial unit thereof, or any entity wholly or mainly owned by that other state.
5. The following notes apply to royalties WHT:
   a. The higher rate applies to trademarks.
   b. The higher rate applies to copyright of literary, artistic, or scientific work, including cinematograph films or tapes for television or broadcasting.
   c. The lower rate applies to royalties paid for technical or economic studies or for technical assistance.
   d. The lower rate applies to royalties paid to an aircraft and ship leasing business.
6. The lower rates apply in cases where the dividend, interest, or royalty paid from Ecuador to China is applicable to the Foreign Exchange Control Tax in Ecuador.
7. The tax treaty with the former Socialist Federal Republic of Yugoslavia is now applicable to Bosnia and Herzegovina.
8. The tax treaty with the former Federal Republic of Yugoslavia is now applicable to the nations of Serbia and Montenegro.
9. These tax treaties have not yet entered into force as of 31 May 2018.

In addition to the above tax treaties, China has also entered into tax information exchange agreements (TIEAs) with a few countries. For example:

- Argentina.
- Bahamas.
- Bermuda.
- British Virgin Islands (BVI).
- Cayman Islands.
- Guernsey.
- Isle of Man.
- Jersey.
- Liechtenstein.
- San Marino.

Tax administration

Taxable period

The tax year commences on 1 January and ends on 31 December.

Tax returns

Enterprises are required to file their annual income tax return within five months after the end of the tax year, together with an audit certificate of a registered public accountant in China. Information on related-party transactions must be filed with the annual income tax return.

Payment of tax

Enterprises are required to file and pay provisional income taxes on a monthly or quarterly basis within 15 days following the end of each month/quarter. Three options are available to the taxpayer in computing the provisional tax: (i) actual profits of the month/quarter, (ii) average monthly or quarterly taxable income of the preceding year, or (iii) other formulas approved by the local tax authorities.

Settlement of tax payment is due, in conjunction with the annual income tax return, within five months after the end of the tax year.

Tax audit process

There is no fixed audit cycle in China. Tax audit targets are selected pursuant to certain criteria.

Statute of limitations

For unintentional errors (e.g. calculation errors) committed by the taxpayer in its tax filing, the statute of limitation is three years and extended to five years if the amount of tax underpaid is CNY 100,000 or more. For transfer pricing adjustments, the statute of limitation is ten years. There is no statute of limitation for tax evasion, refusal to pay tax, or defrauding of tax payment.

Recent focus of Chinese tax authorities

Since 2009, the Chinese tax authorities have strengthened their tax administration on transfer pricing and income derived by non-TREs. The SAT has released a number of tax circulars addressing the tax administration of transfer pricing, foreign contractors and service providers, WHT on passive income, etc.

Under the CIT Law, non-TREs are subject to CIT on the capital gain derived from the disposal of equity investment in Chinese companies. In addition, the transfer has to be effected at fair value so that any gain shall be recognised for tax purpose at the time when the transaction takes places (unless the transaction qualifies for deferral tax treatment provided under the tax regulations). The Chinese tax authorities have, in recent years, challenged and clawed back CIT on several equity transfer cases whereby non-TREs disposed of their equity investment in China to related parties at cost or below 'fair value'. In addition, they have become more knowledgeable on valuation theories and methodologies and are applying them in reviewing valuation reports in order to ascertain the fair value of equity transfer transactions for tax purposes.

In addition, the Chinese tax authorities have geared up their efforts in recent years to scrutinise investment structures involving intermediate holding companies incorporated in low-tax jurisdictions. One of their focuses is on the indirect equity transfer of Chinese companies by non-TREs. The income derived by a non-TRE from the disposal of a non-Chinese company is not taxable under China's domestic income tax law. However, if the Chinese tax authorities are of the view that the non-TRE transferor has used an abusive arrangement to indirectly transfer the equity of the Chinese company (i.e. interposing and disposing of the special purpose vehicle for no reasonable commercial purpose, but just for avoidance of China withholding income tax), it may re-characterise the equity transfer based on the 'substance over form' principle and disregard the existence of the special purpose vehicle. Once the special purpose vehicle is disregarded, the transfer would be effectively a transfer of the underlying Chinese company's equity, and the transfer gain would be China source and subject to China withholding income tax. In early 2015, the SAT issued a circular that sets out new guidance on the assessment of indirect transfer of China taxable properties by non-TREs. The new guidance extends the scope to capture all 'China taxable properties', including not only equity investment in Chinese companies but also immovable properties located in China and assets of an establishment or place of a foreign company in China. It also provides clearer criteria on how to assess 'reasonable commercial purpose' and introduces 'safe harbour' scenarios.

The SAT has also released circulars relating to the claiming of treaty benefits by non-TREs and interpretation of certain articles and terms in the tax treaties, such as dividends, royalties, beneficial ownership, etc. Aggressive tax planning (including, but not limited to, tax-avoidance and treaty-abusive arrangements) not supported by reasonable commercial purposes and substance will be subject to scrutiny by the Chinese tax authorities. Non-residents and their withholding agents are required to file certain prescribed forms and other supporting documents when performing tax filing to justify their claims for the tax treaty benefits. The tax position taken by the non-residents or withholding agents are subject to examination by the Chinese tax authorities after the tax filing.

The SAT issued a Departmental Interpretation Note (DIN) in 2010 for the tax treaty concluded between China and Singapore. It is the first time the SAT has introduced a set of technical views, interpretation, and practice guidelines for the implementation of a tax treaty in such a comprehensive manner. More importantly, this set of interpretation is also applicable to other tax treaties concluded by China if the provisions of the relevant articles in those tax treaties are the same as those in the China/Singapore tax treaty. Thus, it is likely to have a wide impact to tax residents of other countries/regions that have entered into tax treaties with China.

For transfer pricing investigation, increasing scrutiny has been imposed on outbound related-party remittance, such as service fees and royalty payments. Specifically, in addition to the arm's-length nature of the service fees and royalty transactions, the Chinese tax authorities may also require taxpayers to demonstrate the commercial substance of the overseas service provider or intangible property owner. The Chinese tax authorities are also stringent on activities for the decision-making, monitoring, control, and compliance purposes of the group, and may challenge the service remittance for group finance, tax, human resources, and legal activities, which is different from common positions taken by Organisation for Economic Co-operation and Development (OECD) countries. Another focus of the Chinese tax authorities in transfer pricing investigation is location-specific advantages (e.g. location saving of Chinese low-cost resources, market premium of Chinese market). As such, the Chinese tax authorities often expect a different transfer pricing policy in China, which will pose difficulties on multinational groups who implement a consistent transfer pricing policy around the world.

General anti-avoidance rules (GAAR)

There is a GAAR provision in the CIT law allowing the Chinese tax authorities to make adjustments to taxable revenue or taxable income where business arrangements, structures, or transactions are entered into without reasonable commercial purpose and result in a reduction, exemption, or deferral of tax payment. The Chinese tax authorities may initiate a GAAR investigation if they suspect that an enterprise undertakes any of the following arrangements: abuse of preferential tax treatments, abuse of tax treaties, abuse of corporate structure, use of tax havens for tax avoidance purposes, or other arrangements that do not have a reasonable commercial purpose.

The SAT released the Administrative Measures on GAAR in late 2014. The Administrative Measures provides comprehensive guidance on the implementation of GAAR, including elaboration on certain principles, adjustment methods, procedures throughout the GAAR life cycle, and relevant documentation requirements.

Other issues

Choice of business entity

Foreign companies, enterprises, or individuals may establish equity joint ventures, contractual joint ventures, wholly foreign-owned enterprises, or representative offices in China. Certain foreign financial institutions, including banks and insurance companies, may, subject to approval, set up branches in China. Foreign investors are allowed to establish foreign invested partnerships in China. For certain foreign invested industries and projects, approval is needed from the relevant Chinese government authorities.

Exchange controls

Foreign exchange transactions are administered by the State Administration of Foreign Exchange (SAFE) and its branches. The regulatory administration on foreign exchange transactions of an enterprise depends on whether the transaction is a current account item or a capital account item. Current account items refer to ordinary transactions within the context of international receipts and payments, including, but not limited to, balance of payments from trade, labour services, and unilateral transfers. Capital account items refer to items of increase or decrease in debt and equity due to inflow or outflow of capital within the context of international receipts and payments, including, but not limited to, direct investment, all forms of loans, and investment in securities. Generally, a payment that falls under the category of a current account may be remitted overseas if supported with proper contracts, invoices, and tax payment/exemption certificates. In the past, most of the transactions under the category of capital account items had to be approved by the SAFE. Since the end of 2012, the SAFE has relaxed the administration of certain capital account items so that approval is no longer needed for a few types of transactions.

Intellectual properties

Patents, trademarks, and copyrights are governed by separate laws and administered by separate governmental bodies. The government encourages the development and transfer of intellectual properties. The transfer of qualified technology and qualified technical services are exempted from VAT.

Mergers and acquisitions (M&A) activities

Both Chinese domestic and foreign investors increasingly are using M&A transactions to establish or expand their Chinese operations.

The MoF and the SAT jointly released several circulars that address the CIT treatment for six forms of restructuring transactions, namely, change in legal form, debt restructuring, equity acquisition, assets acquisition, merger, and spin-off. The general principle is that enterprises undergoing corporate restructuring should recognise the gain/loss from the transfer of relevant assets/equity at fair value when the transaction takes place. However, if certain prescribed conditions are satisfied, the parties involved could opt for special tax treatments, which are essentially tax deferral tax treatment. In other words, recognition of gain/loss of the transferor from transfer of assets/equity can be deferred with respect to the equity-payment portion; and the transferee may take over the transferor's tax basis of the acquired assets/equity. Such special tax treatments are only available to a very few specific types of cross-border transactions.

China, People's Republic of

Development of the Foreign Account Tax Compliance Act (FATCA) in China

In late June 2014, the Chinese government reached an agreement in substance with the United States (US) on the terms of a Model 1 Intergovernmental Agreement (IGA). However, as of 31 May 2018, the China-US IGA has not been signed, and the financial institutions in China have not started implementing FATCA.

Base Erosion and Profit Shifting (BEPS) and the Multilateral Instrument (MLI)

China has been actively involved in the BEPS project as a partner of the OECD and one of the G20 members. After the final reports on all the 15 action plans were endorsed in 2015, China has implemented and localised the BEPS action plans on a needed basis.

China imposed new transfer pricing compliance requirements, including annual reporting forms for related-party transactions (RPT forms), country-by-country (CbC) reporting, and transfer pricing documentation, all of which contain substantial changes to the previous rules.

China entered into the Multilateral Competent Authority Agreement (MCAA) for the Automatic Exchange of Country-by-Country Reports in 2016. Out of the 68 signatories to the CbC MCAA, China has activated CbC report bilateral exchange relationships with France, Germany, and the United Kingdom on 31 July 2017 (effective for taxable periods starting on or after 1 January 2017).

China also entered into the Multilateral Instrument (MLI) in June 2017. Some important positions of China in relation to the articles in the MLI are as follows:

- Covered tax agreement: China puts all of its existing tax treaties (excluding China's three tax arrangements with Hong Kong, Macau, and Taiwan) into the covered agreement, except for the one with Chile and the one with India.
- Treaty abuse: China adopts the principle purpose test (PPT) provision but does not adopt the simplified limitation of benefits (LOB) test. The threshold period for enjoying treaty benefit on capital gain from the transfer of property-rich companies is three years instead of the one-year period provided in the MLI.
- China opts out of all the provisions in the avoidance of PE section and the arbitration clause for MAPs.

Common Reporting Standard (CRS)

China entered into the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information. In May 2017, the relevant Chinese authorities jointly issued the Administrative Measures on Due Diligence Procedures for Non-residents' Financial Account Information in Tax Matters (the Measures) to implement CRS in China. Financial institutions established in China are required to carry out due diligence procedures on financial accounts starting from 1 July 2017. China is committed to exchange the first round of financial account information by September 2018.

Fiji

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Significant developments

Corporate income tax (CIT)

The following amendments to the Fiji Income Tax Act (FITA) 2015 are effective from 1 August 2017:

- The tax on dividends has been repealed (i.e. dividends shall no longer be subject to any tax in the hands of the shareholder).
- The export income deduction of 50% has been extended until 2017.
- Pre-2014 profits not distributed as dividends by 30 June 2017 shall be subject to 1% transitional tax.
- Health insurance benefits provided to employees who are Fiji citizens shall be exempt from fringe benefits tax (FBT).
- All Tax Free Region (TFR), commercial agriculture, and agro-processing incentives have been extended from 2018 to 2028.
- The bio-fuel incentive has been restructured and extended from 2018 to 2028.
- The minimum capital to qualify for the electric vehicle charging station incentive has been reduced from 3 million Fijian dollars (FJD) to FJD 500,000.

Tax Administration Act

Effective 1 August 2017, the tax authority may issue amended notices of assessment at any time. Previously, there was a six-year limitation except in certain cases (e.g. fraud).

Value-added tax (VAT)

Effective 1 August 2017, fish supplied to the Pacific Fishing Company Limited (PAFCO) shall be a zero-rated supply.

Service turnover tax (STT) and environment and climate adaptation levy (ECAL)

The following amendments to the STT Act and Environmental Levy (EL) Act are effective from 1 August 2017:

- The EL has been renamed the ECAL.
- The ECAL rate on prescribed services increases from 6% to 10%, and the STT rate decreases from 10% to 6%.
- ECAL shall be applicable on the following:
  - Prescribed plastic bags at 10 cents per bag.
  - 10% on the import of new or re-conditioned luxury vehicles with engine capacity exceeding 3000cc, subject to certain exemptions.

- The 12.5% superyacht charter fee shall be replaced with the ECAL at the rate of 10%.
- The STT and ECAL shall only be charged once for the same service.

Water Resource Tax (WRT) Promulgation

Effective 1 August 2017, the WRT has been amended as follows:

Current threshold (litres per month)	Previous threshold (litres per month)	WRT (cents per litre)
0 to 9,999,999	0 to 3,499,999	1.00
10,000,000 and above	3,500,000 and above	18.00

Pending legislation

Please note that this summary is current as of 1 June 2018. Typically, pending legislation is announced and/or enacted in June or July. Please visit the Worldwide Tax Summaries website at *www.pwc.com/taxsummaries* to see any significant corporate tax developments that occurred after 1 June 2018.

Taxes on corporate income

Resident corporations are taxed on their worldwide income. Non-resident corporations may only be taxed on their Fiji-sourced income.

CIT is payable and assessed on the chargeable income of the business calculated by subtracting deductible expenses from all assessable income specified under the FITA.

CIT is payable on taxable income at the following rates:

Type of company	CIT rate (%)
Non-resident shipping companies in respect of outgoing business from carriage of passengers, livestock, mail, merchandise, or goods embarked or loaded in Fiji	2
Non-resident company that establishes its regional or global headquarters in Fiji (subject to certain conditions)	17
Company listed on the South Pacific Stock Exchange (SPSE)	10
All other companies, including non-resident companies carrying on business in Fiji (e.g. branch profits)	20

Corporate residence

A company incorporated, formed, or settled in Fiji is considered a 'resident' in Fiji. A company not incorporated in Fiji is resident in Fiji if it has any part of its central management and control located in Fiji.

Permanent establishment (PE)

PE is determined based on the applicable tax treaty. The FITA also defines 'permanent establishment' as a fixed place of business through which the business of a person is wholly or partly carried on and includes the following:

- A place of management, branch, office, factory, warehouse, or workshop, but not a liaison office.

- A mine site, oil or gas well, quarry, or other place of exploration for, or extraction of, natural resources.
- A building site, or a construction, assembly, or installation project, or supervisory activities connected with such site or project, but only if the site, project, or activities continue for more than six months.
- The furnishing of services by the person, including consultancy services, including through employees or other personnel engaged by the person for such purpose, but only if activities of that nature continue for the same or a connected project by the person or an associate for a period or periods aggregating more than six months in any 12-month period.
- A person, referred to as an ‘agent’, acting on behalf of another person, referred to as the ‘principal’, if the agent:
  - regularly negotiates contracts on behalf of the principal, or
  - habitually maintains a stock of trading stock from which the agent regularly delivers trading stock on behalf of the principal but does not include an agent of independent status.
- Substantial equipment used for more than six months within a 12-month period or installed by, for, or under contract with the person.
- The carrying on of activities, including the operation of substantial equipment in the exploration for, or exploitation of, natural resources or standing timber for the period or periods exceeding in aggregate of 90 days in any 12-month period, for or under contract with a person.

However, PE excludes the business of a person that enters into a contractual arrangement solely with the government or persons in which the government has an interest, subject to certain conditions.

Other taxes

Value-added tax (VAT)

VAT of 9% generally applies on the supply of goods and services in Fiji by a registered person in the course or furtherance of a taxable activity carried on by that person. The threshold amount for VAT registration is FJD 100,000 for the supply of goods and/or services.

The supply of financial services (except for certain insurance services), residential accommodation (subject to certain conditions), and education by an approved institution is exempt.

Exports of goods and services and international transportation are zero-rated under certain conditions.

The due date for lodgement of VAT returns and payment of any VAT payable is the end of the month following the taxable period, which is normally a month. However, where an entity’s supplies do not exceed FJD 300,000, it may opt to lodge VAT returns and pay any VAT payable on an annual basis.

Under certain conditions, directors of companies with insufficient funds may be held liable for any outstanding VAT or CIT liability of the company and may be sued in their personal capacity.

Customs duties/import excise taxes

Import excise tax (from 5% to 15%) applies to selected goods (in addition to the fiscal duties imposed on importation), including:

- Alcohol and tobacco.
- Used or second-hand liquefied petroleum gas (LPG) powered motor vehicles.
- New or used licensed mini buses.
- Some goods that are also locally manufactured.
- Certain white goods and luxury items.

Excise taxes

Excise tax is payable on tobacco, alcohol products, and carbonated soft drinks manufactured in Fiji, based on quantities produced.

Property taxes

There are no property taxes at the national level. However, the municipalities may charge property rates in their respective areas.

Stamp duties

Under the Fiji Stamp Duties Act, stamp duty is payable in respect of instruments, including, but not limited to, declaration of trusts, leases, loans, mortgages, transfer of property (or interest therein), and shares.

Capital gains tax (CGT)

Capital gains made from the following assets (excluding trading stock, depreciable assets, or business intangibles) may be subject to CGT of 10%:

- Land or an interest therein.
- Ships or boats.
- Yachts.
- Shares, securities, equities, or other financial assets (except shares listed on the SPSE).
- Intangible assets.
- Interest in a partnership or trust.
- Aircraft.
- Option, right, or other interest in an asset referred to above.

A capital gain made on disposal of an asset that is used solely to derive income that is exempt from tax under the FITA shall be exempt from CGT.

Foreign tax paid in respect of the disposal of a capital asset may be allowed as a tax credit against the CGT payable.

There is no carryforward of capital losses in calculating CGT.

Any gain on the disposal of shares listed on the SPSE shall be exempt from CGT.

Any gain on the disposal of shares in any Unit Trust in Fiji shall be exempt from CGT, subject to certain conditions.

Any gain on the disposal of shares by a Fiji resident shall be exempt from CGT where a private company goes through reorganisation, restructure, or amalgamation for the purpose of listing on the SPSE, subject to certain conditions.

Transfer of shares due to corporate reorganisation shall not be subject to CGT, subject to certain conditions.

Service turnover tax (STT) and environment and climate adaptation levy (ECAL)

STT at the rate of 6% (effective 1 August 2017; previously 10%) is imposed on the turnover of a person conducting a business involving the provision of a prescribed service, which includes the following:

- Provision of accommodation, refreshments, and any other services by a hotel.
- Any services provided in a vessel that is principally or wholly engaged in the carriage of tourists in Fiji.
- Provision of meals, beverages, and any other services in a bar.
- Provision of services in a nightclub.
- Provision of in-bound tour services.
- Live entertainment provided by artists for a fee.
- Provision of services for recreational activity for gain.
- Provision of services relating to exhibition of films to the public or section thereof by an exhibitor where a charge is made for admission, including services provided by cinema operators.
- Provision of services by hired or rental car operators and chartered transport services to tourists by omnibus or mini-bus operators.
- Provision of meals, beverages, and any other services by bistros or coffee shops with an annual gross turnover over FJD 1.5 million.
- Provision of meals, beverages, and any other services on sale by restaurants with annual gross turnover over FJD 1.25 million.
- Provision of charter flight services by an aircraft or helicopter, excluding such services for medical or natural disaster relief evacuation.
- Provision of all water sports, including underwater activities and river safaris.
- Provision of accommodation in a private residence or property that accommodates tourists, international students, or overseas visitors who are paying guests.

The above-prescribed services are also subject to ECAL at the rate of 10% (effective 1 August 2017; previously 6%). However, non-consumption services by hotel properties are no longer subject to STT (or ECAL). STT and ECAL shall only be imposed once for the same service. The following shall also be subject to ECAL:

- Prescribed plastic bags at 10 cents per bag.
- Import of new or re-conditioned luxury vehicles with engine capacity exceeding 3000cc, subject to certain exemptions.
- Charter of superyachts.

The due date for payment of STT and ECAL is aligned with the VAT Act requirements (i.e. end of the month following the taxable period).

Water Resource Tax (WRT)

The WRT, at the following rates, shall be levied upon the extraction of water in its natural state for sale:

Litres extracted monthly	Cents per litre
0 to 9,999,999	1.00
10,000,000 and above	18.00

Fringe benefits tax (FBT)

FBT of 20% is payable by the employer on the grossed-up value of certain fringe benefits provided to employees (the effective tax rate is 25%).

Payroll taxes

Employers are required to deduct and remit monthly to the tax authority appropriate Pay-As-You-Earn (PAYE) tax, social responsibility tax (SRT), and ECAL from employee gross cash emoluments.

If appropriate PAYE taxes, SRT, and ECAL are not deducted and remitted, the tax authority may recover the taxes from the employer or the employee and/or disallow a tax deduction for the expenditure.

Contributions to the Fiji National Provident Fund (FNPF)

The FNPF is a compulsory superannuation scheme for local employees. Under the FNPF Act, employers and employees are required to contribute 10% and 8%, respectively, of cash emoluments of employees to the Fund.

Employers are not required to contribute to the FNPF for expatriate employees.

Telecommunication levy

Telecommunication levy of 1% is imposed on all voice call charges.

Third party insurance levy

Third party insurance levy of 20% is imposed on the total third party insurance premium collected in a month.

Gambling turnover tax (GTT)

GTT is imposed on the value of consideration paid or payable in respect of the provision of prescribed gambling services (i.e. acceptance of bets and provision of tickets for any lottery) at the rate of 15%.

Branch income

The profits of a foreign company's branch operating in Fiji are subject to the same tax rate as the tax rate levied on profits of a resident corporation (i.e. 20%).

Income determination

CIT is payable and assessed on taxable income of the business. Taxable income is calculated by subtracting allowable deductions from all assessable income (i.e. all sources of income).

Inventory valuation

Inventories are normally valued at the lower of cost and net realisable value. While the first in first out (FIFO) method is acceptable, the last in first out (LIFO) method is not, for either book or tax purposes. Conformity between book and tax reporting is not required, and there are no special provisions for valuing inventories or determining inventory flows.

Capital gains

Any profit or gain accrued or derived from the sale or disposal of real or personal property, or any interest therein, shall be subject to income tax when:

- the business of the company comprises dealing in such property
- the property is acquired for the purpose of selling or otherwise disposing thereof, or
- any profit or gain is derived from the carrying on or carrying out of any undertaking or scheme entered into or devised for the purpose of making a profit.

Otherwise, the capital gain may be subject to CGT of 10% (*see Capital gains tax [CGT] in the Other taxes section for more information*).

Dividend income

Transfers of property by private companies to shareholders and associates may be deemed to be a dividend paid by that company.

Effective 1 August 2017, dividends are no longer subject to tax in the hands of the shareholders.

Interest income

Interest income over FJD 200 derived by a resident from a company shall be appropriately subject to resident interest withholding tax (WHT) of 10%, which may be claimed as a tax credit against income tax payable on income. Exempt income shall not be subject to WHT.

Royalty income

Royalty income derived by a resident company or PE may be appropriately subject to contractors' WHT of 5%, which may be claimed as a tax credit against income tax payable on income.

Royalty income derived by a non-resident company without a PE in Fiji should be appropriately subject to WHT at the rate of 15%.

Partnership income

The income of the partners from a partnership for any income year is equal to each partners' respective share of income from that partnership. Each partner declares income separately and is individually liable for filing a tax return for each applicable year.

Liability of directors/shareholders

Directors/shareholders of companies in liquidation or with insufficient assets to satisfy tax liabilities may be held liable for any outstanding tax liability of the company, under certain conditions.

Other significant items

Where a foreign-controlled business in Fiji produces less income than might be expected, the revenue authorities may determine the income for tax purposes.

Foreign income

Resident corporations are taxed on their worldwide income. Foreign income derived from a treaty country is taxed according to the treaty. Foreign income sourced from a non-treaty country by a Fiji tax resident is subject to income tax in Fiji. A credit is allowed in Fiji for foreign tax paid on foreign income. The tax credit is limited to the lesser of the Fiji tax payable or the foreign tax paid on such income. There are no special provisions for taxing undistributed income of foreign subsidiaries.

Deductions

Generally, expenses wholly and exclusively incurred in deriving assessable income are allowable deductions. Expenditures that are capital or domestic in nature are generally not deductible.

Depreciation and depletion

Depreciation may be calculated on the cost of a business asset on a straight-line or diminishing-value basis. The prescribed rates of depreciation are based on the estimated life of the asset. Upon disposal of a business asset, either recoupment of depreciation claimed is taxable or the excess of tax written-down value over sale proceeds is deductible. The taxpayer has an option to set-off recoupment of depreciation against the cost of replacement assets. Conformity between book and tax depreciation is not required.

There are three broad bands of depreciation rates for assets (other than buildings). The three broad bands and the depreciation rates are as follows:

Band	Kind of asset	Diminishing value (%)	Straight line (%)
1	Motor vehicles; buses and minibuses with a seating capacity of less than 30 passengers; goods vehicles with a load capacity of less than seven tonnes; computers and data handling equipment; and construction equipment and earthmoving equipment	40	25
2	Buses with a seating capacity of 30 or more passengers; goods vehicles designed to carry or pull loads of more than seven or more tonnes; specialised trucks; tractors; trailers and trailer-mounted containers; and plant and machinery used in manufacturing, mining, or farming operations	30	20
3	Vessels, barges, tugs, and similar water transportation equipment; aircraft; specialised public utility plant, equipment, and machinery; office furniture, fixtures, and equipment; and any depreciable asset not included in another category	20	12.5

Certain renewable energy plant and water storage facilities also qualify for a 100% write-off.

Capital expenditure aimed at economising on the consumption of fuel, electricity, or its derivatives, or on an asset using energy sources indigenous to Fiji, may be eligible for accelerated depreciation at varying rates.

The cost of the acquisition of a mining lease or tenement and the cost of development of mines may be written off in equal instalments in any five of the first eight years, commencing with the year in which the expenditure was incurred.

A deduction for depletion of other natural resources is not available.

Goodwill

Goodwill, and the amortisation thereof, may be deductible for income tax purposes.

Start-up expenses

Start-up expenses are deductible for income tax purposes.

Interest expenses

Interest expenses that are revenue expenditure wholly and exclusively incurred in deriving taxable income are generally deductible in calculating taxable income, subject to the thin capitalisation rules (*see Thin capitalisation in the Group taxation section for more information*).

Provisions

Provisions for expenses not yet incurred (e.g. bad debts) are not tax-deductible. Deductions are generally permitted in respect to amounts that are actually paid or incurred.

Charitable and other contributions

Contributions to approved academic and charitable organisations of up to FJD 100,000 are deductible.

There are certain other specific donations that qualify for varying levels of deductions, including:

- Donations to the Fiji Heritage Foundation, which qualify for a deduction of 150%.
- Donations to Tourism Fiji, which qualify for a deduction of 150%.
- Cash donations exceeding FJD 50,000 to the Poverty Relief Fund for Education, which qualify for a deduction of 200%.
- Cash donations exceeding FJD 50,000 to a Sports Fund (as approved by the CEO of the Fiji Revenue and Customs Service [FRCS]) for purposes of sports development in Fiji, which qualify for a deduction of 150%.
- Total cost of new computers, laptops, and tablets of not less than FJD 10,000 but not exceeding FJD 100,000 that are donated to urban and rural schools registered with the Ministry of Education, which qualify for a deduction of 150% and 200%, respectively.
- The following payments qualify for a deduction of 150%:
  - Cash donations of not less than FJD 10,000 but not exceeding FJD 100,000 to the Disaster Rehabilitation Fund.
  - Cash sponsorships of more than FJD 100,000 but not exceeding FJD 200,000 towards the hiring of international sporting coaches.
  - Cash donations not exceeding FJD 50,000 towards any approved housing project for squatters by the Fiji government.

- Cash donations of not less than FJD 10,000 to the Farmers Disaster Relief Emergency Fund Account, which qualify for a 200% deduction.

Fines and penalties

Generally, fines and penalties are not deductible for income tax purposes.

Taxes

Taxes levied on income are not deductible. Only 50% of the employer's statutory FNPF contribution paid by the employer is allowed as a deduction for tax purposes in the year the contribution was paid (*see Contributions to the FNPF in the Other taxes section for more information*).

Employee cost not appropriately subject to Pay-As-You-Earn (PAYE) final WHT is not allowed as a deduction for tax purposes.

FBT is not allowed as a deduction for tax purposes.

Net operating losses

Tax losses may be carried forward for four consecutive years, provided the company can demonstrate a minimum 51% continuity of shareholding between the year of loss and the year of claim. Notwithstanding the change in ownership, losses may also be carried forward where a company carries on the same business in the carried forward year as it did in the loss year (subject to certain conditions).

In relation to certain private hospitals and medical services businesses, tax losses may be carried forward for eight years. *Please refer to the Medical industry incentives in the Tax credits and incentives section*.

Loss carrybacks are permitted, but only in very limited circumstances.

Payments to foreign affiliates

Subject to the normal rules of deductibility, a deduction may be claimed for royalties, management service fees, and interest charges paid to foreign affiliates.

Group taxation

Group taxation is not available in Fiji.

Transfer pricing

Transfer pricing provisions state that the tax authority may allocate income and expenses between associates (related entities) to reflect income and expenses on an arm's-length basis.

The Income Tax (Transfer Pricing) Regulations provide that the Organisation for Economic Co-operation and Development (OECD) Transfer Pricing guidelines may be used in interpreting the provisions of the Regulations in determining income or expenses on an arm's-length basis.

Thin capitalisation

If a foreign controlled resident company, other than a financial institution, has a debt to equity ratio in excess of 2:1 at any time during a tax year, interest expense in relation to that part of the debt that exceeds the ratio is not allowed as a tax deduction unless the company can properly substantiate the arm's-length nature of the debt.

Controlled foreign companies (CFCs)

Fiji does not have specific rules in relation to CFCs.

Tax credits and incentives

The tax incentives in Fiji are designed primarily to promote export sales and to encourage the development of industries that are considered of benefit to the economic development of Fiji.

Export income deduction

A deduction for export income is allowed in accordance with the following:

Year of assessment	Percentage of export income to be deducted (%)
2017	50

'Export income' means net profit derived by a taxpayer from the business of exporting goods and services; and the CEO of the FRCS may, where separate records for export income are not maintained, determine what this income should be.

Information and communication technology (ICT) tax incentives

The income of an ICT operator may be exempt from CIT for a period of 13 years from the date of issue of the licence, provided that the business employs 50 employees or more for six months within the income year and 60% or more of the total value of its services in that income year is exported.

The income of the following may be exempt from CIT for a period of 13 years from the date of approval:

- ICT start-ups involved in application design or software development.
- Accredited ICT training institutions.

The expenses incurred by the following entities shall qualify for a 150% deduction:

- ICT start-ups involved in application design or software development.
- Accredited ICT training institutions.

Employment incentives

Salary and wages paid to first-time employees (including apprentices and trainees) for the first 12 months of employment qualify for a 200% deduction, subject to certain conditions. This deduction is available until 31 December 2020.

Salary and wages paid to students qualify for a 200% deduction, subject to certain conditions. This deduction is available until 31 December 2020.

Salary and wages paid to disabled persons qualify for a 300% deduction, subject to certain conditions. This deduction is available until 31 December 2022.

Employees' education fees qualify for a 150% deduction, subject to certain conditions.

Hotel industry incentives

The following incentives are currently available only to new hotels.

Approved capital expenditure incurred in building, renovating, or expanding a hotel is subject to an investment allowance of 25% of the approved expenditure, in addition to normal depreciation.

Under the Short Life Investment Package (SLIP), the following concessions are available to a company:

- Exemption from CIT for a period of four years (previously ten years), provided that the capital investment in the hotel is more than FJD 7 million.
- Duty-free entry of certain capital equipment, plant, and machinery, upon receiving provisional approval from the Minister.
- Permission to generate one's own electricity, the excess to be sold to the Fiji Electricity Authority.

Any tax losses incurred by an entity granted approval for the investment allowance or SLIP may be carried forward for four years, but may only be set off against income of the hotel business or from the hotel premises.

The recipients of provisional approval for hotel investment tax incentives are required to complete the hotel projects within two years from the date provisional approval is granted.

The incentives are also available for new apartments, subject to certain conditions.

Medical industry incentives

Approved capital expenditure incurred in building, renovating, or expanding a private hospital (minimum capital investment of FJD 1 million) or ancillary medical centre (minimum capital investment of FJD 500,000) is allowed an investment allowance of 60% of the approved expenditure, in addition to normal depreciation.

Under the Medical Investment Package (MIP), the following concessions are available to a company:

- Exemption from CIT for a period of ten years, provided that the capital investment in the private hospital or ancillary medical centre is more than FJD 7 million or FJD 2 million, respectively.
- Duty-free entry of certain capital equipment, plant, and machinery, upon receiving provisional approval from the Minister.

Any tax losses incurred by an entity granted approval for the investment allowance or MIP may be carried forward for eight years, but may only be set off against income of the medical business or from the hospital premises.

The recipients of provisional approval are required to complete the projects within two years from the date provisional approval is granted.

Residential housing incentives

The following concessions are available to a company developing buildings for residential purposes with a capital investment of more than FJD 2 million and at least 20 residential housing units:

- Subsidy of 5% or 7% (depending on capital investment) of the total approved capital expenditure incurred, in addition to normal depreciation.
- Duty-free and VAT-free entry of certain capital equipment, plant, and machinery, upon receiving provisional approval from the Minister.

The recipients of provisional approval are required to complete the projects within two years from the date provisional approval is granted.

Electric vehicle charging station incentives

The following concessions are available to a company developing electric vehicle charging stations with a capital investment of more than FJD 500,000:

- Subsidy of 5% of the total approved capital expenditure incurred, in addition to normal depreciation.
- Exemption from CIT for a period of seven years.
- Duty-free entry of certain capital equipment, plant, and machinery, upon receiving provisional approval from the Minister.

The recipients of provisional approval are required to complete the projects within two years from the date provisional approval is granted.

Filmmaking and audio-visual incentives

A tax exemption or reduced tax rate is available on the income of non-resident employees of an approved non-resident company engaged or intending to be engaged in making a film in Fiji.

A resident entity (excluding an entity holding a broadcast licence in television or radio in Fiji or with substantial shareholdings in the same) may deduct up to 150% of expenditure on audio-visual production in respect of income in the year of the expenditure. 'Audio-visual productions' include production for exhibition or sale of theatrical films, broadcast television, direct-to-video and video disk programme, audio recording, computer software, and interactive websites.

A tax exemption is available on the income derived by a taxpayer from the commercial exploitation of a copyright until the taxpayer has received from the commercial exploitation a return of up to 60% of the expenditure. The expenditure must be of capital nature and in relation to the audio-visual production costs in respect of a qualifying audio-visual production.

Tax concessions are also available for residents of areas declared as studio city zones by the appropriate government minister.

Tax Free Regions (TFRs)

The following concessions may be available to a newly incorporated entity engaged in trade, business, or manufacture in the TFRs:

- Exemption from CIT for a period of 5 to 20 consecutive fiscal years for a new activity established between 1 January 2009 to 31 December 2028, depending on the level of investment and the equity held by an iTaukei landowner.
- Duty-free entry of raw materials, machinery, and equipment (including parts and materials) required for the establishment of the business.

The areas declared TFRs are Vanua Levu, Rotuma, Kadavu, Lomaiviti, Lau, and the airport side of the Rewa Bridge, excluding the town of Nausori up to the Ba side of the Matawalu River (previously Korovou to Tavua).

CIT exemption of 5, 7, or 13 years (depending on the amount of capital investment) is available to a taxpayer engaged in any new activity established in the TFR from the airport side of the Rewa Bridge, excluding the town of Nausori up to the Ba side of the Matawalu River, subject to certain conditions.

Other tax incentives

An investment allowance of 55% is available for the construction or refurbishment and renovation of a vessel, in addition to normal depreciation, subject to certain conditions.

An approved mining company may, for a specified period, be exempt from CIT or taxed at a lower rate. The holder of a valid prospecting licence may write off approved expenditure on prospecting for minerals against income from all sources.

A 150% deduction is available for direct capital expenditure incurred by commercial banks in rural banking programmes.

Investors engaged in value adding processes in the food processing, agricultural processing, fisheries, or forestry business may be able to claim a 100% deduction with respect to amounts invested or re-invested (for expansion), provided that the businesses meet the 50% local content rule.

A CIT exemption may be available to a taxpayer engaged in the following commercial agricultural farming and agro-processing activities, subject to certain conditions:

- Any new activity approved between 1 January 2009 and 31 December 2028, for a period of 5 to 13 consecutive fiscal years, depending on the level of capital investment.

Income derived by a taxpayer from a new activity in processing agricultural commodities into bio-fuels established between 1 January 2009 and 31 December 2028 may be exempt from CIT for a period of 5 to 13 consecutive tax years (depending on the level of capital investment), under certain conditions.

An exemption from CIT for a period of five years may be available to a taxpayer engaging in renewable energy projects and power cogeneration.

Entities in the agriculture, fisheries, and tourism industries, with a maximum turnover threshold of FJD 500,000, may also be exempt from CIT.

A 150% deduction is available on expenses incurred in reorganising a company for the purpose of listing on the SPSE.

Any gain derived from the following sale of shares shall be exempt from CIT:

- For the purpose of listing on the SPSE, subject to certain conditions.
- By a resident of shares in an SPSE-listed company.

40% of capital expenditure of not less than FJD 50,000 incurred by any existing business located in Vanua Levu is allowed as a deduction for tax purposes, subject to certain conditions.

A 150% deduction is available on expenditure not exceeding FJD 250,000 incurred in marketing goods and services for export to any of the South Pacific countries, excluding Australia and New Zealand.

The income of a shipping company derived from servicing Rotuma and the Lau Group shall be exempt from CIT for a period of seven years, subject to certain conditions.

A 50% deduction is available on expenditure incurred for uniforms made in Fiji and supplied to an employee, provided that the cost is not recovered from the employees.

A 150% deduction is available for foreign companies for capital expenditure incurred for the relocation to Fiji of its regional or global headquarters, which provides management, technical, or other supporting services to its offices or associated companies, subject to certain conditions.

Foreign tax credit

A credit is allowed in Fiji for foreign tax paid on foreign income, limited to the lesser of the Fiji tax payable or the foreign tax paid on such income.

Withholding taxes

WHTs are levied as follows:

	WHT (%)				
Recipient	**Dividends**	**Interest**	**Royalties**	**Know-how, management fees**	**Professional fees**
Resident corporations	0	10 (1)	5 (2)	5 (2)	5 (2)
Resident individuals	0	10 (1)	5 (2)	5 (2)	5 (2)
Non-resident corporations:					
Non-treaty	0	10	15	15	15
Treaty:					
Australia	0	10	15	15	0/15 (3)
India	0	10	10	10	0/10 (3)
Japan	0	10	10	10	0/10 (3)
Korea, Republic of	0	10	10	10	0/10 (3)
Malaysia	0	10	15	15	0/15 (3)
New Zealand	0	10	15	15	0/15 (3)
Papua New Guinea	0	10	15	15	0/15 (3)
Qatar	0	0	5	5	0/5 (3)
Singapore	0	10	10	10	0/10 (3)
United Arab Emirates	0	0	10	10	0/10 (3)
United Kingdom	0	10	15	15	0/15 (3)

Notes

1. Applies to interest (over FJD 200) but is not applicable if income is exempt.
2. This WHT only applies where there is a formal written contract.
3. Depending on the provisions of the applicable double taxation agreement.

Tax administration

The Tax Administration Act (TAA) was promulgated with the stated intention of harmonising the administration of the various tax laws, including CIT and VAT. CGT, FBT, STT, and ECAL are also covered by the provisions of the TAA.

If a due date falls on a Saturday, Sunday, or holiday, the due date is the last working day before the due date.

Taxable period

Tax is assessed on income derived during the calendar year preceding the year of assessment. Returns are therefore generally accepted on a calendar-year basis, although approval is also given to use an alternative fiscal-year basis. For purposes of assessment of returns completed on a fiscal-year basis, the calendar year in which more than one-half of the fiscal year falls is deemed to be the calendar year in which the income is derived.

Tax returns

The Fiji tax system is not based on self-assessment. Returns of income contain information on the basis of which assessments are raised by the tax authorities.

The due date for lodgement of CIT returns is three months after the end of the income year. However, under the Tax Agent Lodgement Programme, an extension of time may be granted to lodge the CIT returns.

Payment of tax

Final payment of CIT (i.e. the balance of actual tax payable) is generally due by the tax return lodgement due date.

Advance tax payments are required to be made in three instalments, as follows:

- First advance: Due on the last day of the sixth month of the current fiscal year (33⅓% of the preceding income year's tax payable or estimated tax liability).
- Second advance: Due on the last day of the ninth month of the current fiscal year (33⅓% of the preceding income year's tax payable or estimated tax liability).
- Third advance: Due on the last day of the fiscal year (33⅓% of the preceding income year's tax payable or estimated tax liability).

The TAA provides for various ways to ensure the collection of taxes, including, but not limited to, the following:

- Departure prohibition order: A departure prohibition order may be used by the tax office to prevent taxpayers from leaving the country without settling outstanding taxes.
- Garnishee orders: The tax office may garnish bank accounts for outstanding taxes.
- Registration of charges on personal and real properties of the taxpayer.
- Distress and sale of personal property.

- Temporary closure of business.

Penalties

Administrative penalty provisions have been amended and increased under the TAA. Some of the penalties are as follows:

- Failure to register: Every person who fails to apply for registration as required pursuant to the Act commits an offence against the Act and will, on conviction, be liable to a fine not exceeding 50% of the tax payable where the delay does not exceed six months, or a fine not exceeding the tax payable where the delay exceeds six months.
- Late filing of a return: A registered person who fails to lodge a tax return is liable for a penalty of 20% of the tax payable in the case where tax is payable and a penalty of 5% of the tax payable for every month of default.
- Late payment of tax payable: Where any tax remains unpaid on the expiry of the due date, a penalty of 25% of the tax payable in respect of that taxable period will apply.
- Failure to comply with the late payment penalty: Every person who fails to comply with the late payment penalty is liable for penalty of 5% of the unpaid tax for each month of default.
- Failure to maintain proper records: A registered person who fails to keep, retain, or maintain account, documents, or records is liable for a penalty of 75% (knowingly or recklessly made) or 20% (in other cases).
- Insufficient payment of advance taxes: A taxpayer who makes advance payment of taxes less than the required amount per instalment is liable for a penalty of 40%.

Tax audit process

The FRCS undertakes ongoing compliance activities to ensure corporations are meeting their tax obligations. Compliance activities take various forms, including questionnaires, reviews of specific issues, and audits.

Statute of limitations

Generally, the tax authority may issue amended notices of assessment at any time. Previously, there was a six-year limitation except in certain cases (e.g. fraud).

Topics of focus for tax authorities

The FRCS has recently been focusing on transfer pricing issues, the implementation of PAYE tax as a final tax, FBT, WHT, and excise and fiscal duties.

Hong Kong

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Significant developments

New legislation enacted

The following pieces of legislation were enacted in the past 12 months:

- Two-tier profits tax rates: Inland Revenue (Amendment) (No.3) Ordinance 2018, which implements the two-tier profits tax rates in Hong Kong, was gazetted on 29 March 2018. Effective from the year of assessment 2018/19, the first 2 million Hong Kong dollars (HKD) of assessable profits of corporations and unincorporated businesses will generally be taxed at 8.25% and 7.5%, respectively. The remaining assessable profits will be subject to the normal tax rate at 16.5% and 15% for corporations and unincorporated business, respectively. As an anti-avoidance measure, a group of 'connected entities' can only nominate one entity within the group to enjoy the reduced tax rate for a given year of assessment.
- Concessionary tax regime for aircraft leasing and management operations: Inland Revenue (Amendment) (No. 3) Ordinance 2017 was enacted on 7 July 2017. The Ordinance introduced, among others, a concessionary tax regime for the aircraft financing and leasing businesses in Hong Kong by (i) offering a concessionary profits tax rate of 8.25% for the assessable profits derived from qualifying aircraft leasing activities and qualifying aircraft leasing management activities carried out in Hong Kong and (ii) deeming the taxable net lease payments derived by a qualifying aircraft lessor from leasing of aircraft to an aircraft operator as 20% of the gross lease payments less deductible expenses, excluding tax depreciation allowance, when certain specified conditions are met. The concessionary tax regime applies to sums received or accrued on or after 1 April 2017.
- Increase in stamp duty on certain transactions: Stamp Duty (Amendment) Ordinance 2018 was gazetted on 19 January 2018. It increases the stamp duty rate on transfer of Hong Kong residential properties to a flat rate of 15%, with certain exemptions. One common exemption is the acquisition of residential property by a Hong Kong permanent resident who does not own any residential property at the time of acquisition. In this case, the applicable stamp duty ranges from a fixed amount of HKD 100 (for property consideration of up to HKD 2 million) to 4.25% of the consideration (for property consideration exceeding HKD 20 million). The 15% flat rate applies retrospectively from 5 November 2016, unless specifically exempted or provided otherwise.
- Close the loophole in stamp duty: Stamp Duty (Amendment) (No. 2) Ordinance 2018 was gazetted on 20 April 2018. It tightens the situation where the 15% flat rate is not applicable. Pursuant to the Ordinance, unless specifically exempted or otherwise provided, any instrument executed on or after 12 April 2017 for acquisition of more than one residential property under that instrument will be subject to stamp duty at a flat rate of 15%, even if the acquirer is a Hong Kong

permanent resident who does not own any residential property in Hong Kong at the time of acquiring the multiple residential properties.

Taxes on corporate income

Hong Kong adopts a territorial basis of taxation. Profits tax is payable by every person (defined to include corporation, partnership, and sole proprietorship) carrying on a trade, profession, or business in Hong Kong on profits arising in or derived from Hong Kong from that trade, profession, or business. However, capital gains and receipts that are capital in nature are not subject to tax. Dividends from local companies chargeable to tax are exempt, whereas dividends from overseas companies are generally offshore in nature and not subject to tax in Hong Kong. The tax residence of a person is generally irrelevant for profits tax purposes. The tax treatments of public and private companies are the same.

Certain income that would not otherwise be subject to Hong Kong profits tax is deemed to arise in or be derived from Hong Kong from a trade, profession, or business carried on in Hong Kong and thus becomes taxable in Hong Kong. This includes royalties received by a non-resident for the use of or right to use a patent, design, trademark, copyright material, secret process or formula, or other property of a similar nature in Hong Kong, or for the use of such intellectual properties outside Hong Kong, but the royalties paid can be claimed as a deduction by a person for profits tax purposes.

Effective from the year of assessment 2018/19, a two-tiered profits tax rate is introduced in Hong Kong. The following table shows the applicable tax rates for companies and unincorporated businesses:

<table>
<tr><th>Rates of tax</th><th>Where the two-tiered rate applies * (%)</th><th>Where the two-tiered rate does not apply (%)</th></tr>
<tr><td>Companies:</td><td></td><td></td></tr>
<tr><td>First HKD 2 million</td><td>8.25</td><td rowspan="2">16.50</td></tr>
<tr><td>On the remainder</td><td>16.50</td></tr>
<tr><td>Unincorporated businesses:</td><td></td><td></td></tr>
<tr><td>First HKD 2 million</td><td>7.50</td><td rowspan="2">15.00</td></tr>
<tr><td>On the remainder</td><td>15.00</td></tr>
</table>

* As an anti-avoidance measure, a ‘group of connected entities’ can only nominate one entity within the group to enjoy the two-tiered tax rate for a given year of assessment.

There are special rules for determining the tax liabilities of certain industries, such as shipping, air services, and financial services. There is also a special tax framework for Islamic bonds (i.e. *sukuk*) that provides for the same tax treatments for *sukuk* vis-à-vis their conventional counterparts.

Incomes from certain qualifying debt instruments (QDIs) are either tax exempt or subject to a concessionary tax rate (i.e. 50% of the regular profits tax rate). However, there is a specific anti-avoidance provision under which the concessionary tax rate/ tax exemption does not apply to incomes derived from QDIs by a person who is an associate of the issuer of the QDIs.

Offshore investment funds (i.e. funds with central management and control outside Hong Kong) having fund managers and investment advisors with full discretion for making investment decisions in Hong Kong can be exempt from Hong Kong profits tax on profits derived in Hong Kong, provided the specified conditions are met. The offshore funds tax exemption covers different types of offshore funds (e.g. hedge funds and private equity funds), but the qualifying conditions are different for different types of funds. There are also specific anti-avoidance provisions in the Inland Revenue Ordinance (IRO) deeming certain resident persons to be subject to profits tax on their share of the non-resident person's tax-exempt profits.

Profits derived from the business of reinsurance of offshore risks and qualifying offshore captive insurance business are subject to profits tax at a concessionary tax rate (i.e. 50% of the regular profits tax rate).

Qualifying profits derived by a qualifying corporate treasury centre are subject to profits tax at a concessionary tax rate (i.e. 50% of the regular profits tax rate) under specified conditions.

Effective from 1 April 2017, qualifying profits derived from qualifying aircraft leasing activities and qualifying aircraft leasing management activities carried out in Hong Kong are subject to profits tax at a concessionary tax rate (i.e. 50% of the regular profits tax rate) under specified conditions. In addition, the taxable net lease payments derived by a qualifying aircraft lessor from leasing of aircraft to an aircraft operator will be deemed as 20% of the gross lease payments less deductible expenses, excluding tax depreciation allowance.

Corporate residence

In general, for Hong Kong profits tax purposes, corporate residency is not important in determining taxability of an entity. The decisive factors for taxability are (i) whether a corporation is carrying on a trade, profession, or business in Hong Kong, and (ii) whether the profits are arising in or derived from Hong Kong.

However, where it is necessary to determine the corporate residence, such as for the purpose of a comprehensive double tax agreement (CDTA), companies incorporated in Hong Kong and companies that are normally managed or controlled/centrally managed and controlled (depending on the provisions of the relevant CDTA) in Hong Kong are generally considered as a Hong Kong tax resident.

Permanent establishment (PE)

For Hong Kong profits tax purposes, whether a foreign corporation is carrying on a trade, profession, or business in Hong Kong and the source of profits, rather than whether there is a PE in Hong Kong, are the decisive factors in determining taxability. The existence of a PE is generally irrelevant for Hong Kong profits tax purposes except in the situation where a CDTA of Hong Kong is applicable.

Other taxes

Value-added tax (VAT)

Hong Kong does not have a VAT, goods and services tax, or sales tax.

Customs duties

There is no tariff on general imports in Hong Kong.

Excise tax

Duties are levied on limited categories of dutiable commodities (i.e. tobacco, liquor, methyl alcohol, and hydrocarbons), regardless of whether they are imported or locally manufactured.

Property tax

Property tax is charged annually to the owner of any land or buildings (except government and consular properties) in Hong Kong at the standard rate of 15% on the net assessable value of such land or buildings. Net assessable value of a property is the consideration payable to the owner for the right to use the land or buildings less rates paid by the owner and a 20% notional allowance.

Rental income derived by a company from a Hong Kong property is subject to profits tax. The company that is subject to profits tax may apply for an exemption from property tax in respect of the property. If no exemption is applied, the property tax paid can be used to offset against the profits tax payable by the company.

Stamp duty

Stamp duty is charged on transfer of Hong Kong stock by way of sale and purchase at 0.2% of the consideration (or the market value if it is higher) per transaction. Hong Kong stock is defined as stock the transfer of which must be registered in Hong Kong.

For conveyance on sale of immovable property in Hong Kong, the stamp duty payable depends on the type of property transferred (i.e. residential property vs. non-residential property) and the property consideration. Currently, stamp duty on transfer of properties is charged as follows:

1. Transfer of residential property: A flat rate of 15%, with certain exemptions. One common exemption is acquisition of a single residential property by a Hong Kong permanent resident who does not own any other residential property in Hong Kong at the time of acquisition (*see 2 below*).
2. Acquisition of a single residential property by a Hong Kong permanent resident who does not own any other residential property in Hong Kong at the time of acquisition and some other specified circumstances: Scale 2 rates ranging from HKD 100 (for property consideration of up to HKD 2 million) to 4.25% (for property consideration exceeding HKD 20 million).
3. Transfer of non-residential property: Scale 1 rates ranging from 1.5% (for property consideration of up to HKD 2 million) to 8.5% (for property consideration exceeding HKD 20 million).

The stamp duty payable is computed by applying the relevant rate to the consideration or market value of the property (whichever is higher). When Scale 1 or Scale 2 rates are applicable, marginal relief is available for transfer where the consideration is marginally above the lower bound of each rate band.

For lease of immovable property in Hong Kong, stamp duty is calculated at a specified rate of the annual rental that varies with the term of the lease. Currently, the applicable rate ranges from 0.25% (for lease period of not more than one year) to 1% (for lease period of more than three years).

Exemption is available for certain transactions, such as transfer of shares between associated corporate bodies, transfer of shares or units of exchange traded funds listed in Hong Kong, and certain stock borrowing and lending transactions, provided that the specified conditions for exemption (if any) are satisfied.

Special Stamp Duty (SSD)

There is an SSD on resale of residential property within 36 months from the date of acquisition. The SSD is imposed on top of the stamp duty payable on conveyance on sale or agreement for sale of residential property, with a few exemptions. The SSD payable will be calculated based on the stated consideration or the market value (whichever is higher) of the resold property at the regressive rates indicated below.

- 20% for residential properties held for six months or less.
- 15% for residential properties held for more than six months but for 12 months or less.
- 10% for residential properties held for more than 12 months but for 36 months or less.

Buyer's Stamp Duty (BSD)

A BSD is payable on acquisition of Hong Kong residential properties by any person (including Hong Kong and foreign companies) other than a Hong Kong permanent resident. The BSD is charged at a flat rate of 15% on the stated consideration or the market value of the property acquired, whichever is higher. The BSD is imposed on top of the stamp duty and the SSD (if applicable), with exemptions in certain situations.

Business registration fees

Every person who carries on a business in Hong Kong is required to apply for business registration with a fee within one month from the date of commencement of the business. The business registration certificate has to be renewed either on an annual basis or every three years with a payment of a business registration (renewal) fee. Special registration and licence fees are applicable to banks and deposit-taking companies.

Capital duty

There is currently no capital duty in Hong Kong.

Government rates and rent

Rates are an indirect tax levied on properties in Hong Kong. Rates are charged at 5% of the rateable value, which is the estimated annual rental value of a property at the designated valuation reference date of 1 October.

Privately owned land in Hong Kong is normally held by way of a government lease under which rent is payable to the Hong Kong Special Administrative Region (SAR) Government in return for the right to hold and occupy the land for the term (i.e. the duration) specified in the lease document. Currently, government rent is calculated at 3% of the rateable value of the property and is adjusted in step with any subsequent changes in the rateable value.

Payroll taxes

In Hong Kong, there are no payroll taxes other than the Mandatory Provident Fund (MPF) contribution (*see below*).

Mandatory Provident Fund (MPF) contribution

Under the MPF scheme, an employer is required to make a mandatory contribution for an employee in the amount equal to 5% of the monthly income of that employee. The maximum level of income for contribution purpose is HKD 30,000 per month. An employer may make voluntary contributions in addition to the mandatory contribution required.

Branch income

The tax rate for branches is the same as that for corporations. The Hong Kong profit of a foreign corporation with a branch in Hong Kong is determined according to the accounts maintained for the Hong Kong operation (or business). If the Hong Kong accounts do not disclose the true profits arising in or derived from Hong Kong attributable to the Hong Kong operation, the Hong Kong profit of the branch for profits tax purposes will be computed according to the ratio of turnover in Hong Kong to total turnover (or the proportion of Hong Kong assets over total assets) on the worldwide profits. Alternatively, the Hong Kong Inland Revenue Department (HKIRD) tax assessor may estimate the profits of the Hong Kong branch. In certain situations, the profits of the Hong Kong branch can be estimated based on a fair percentage of the turnover in Hong Kong.

Income determination

Inventory valuation

Inventory may be stated at the lower of cost or market value. Last in first out (LIFO) may not be used for tax purposes. First in first out (FIFO) must be consistently applied.

The prevailing accounting standards require financial assets and liabilities held for trading purpose (e.g. shares and securities held as trading stock) to be carried at market value, with fluctuations in values of such assets and liabilities taken to the profit and loss accounts, irrespective of whether the profits or losses are realised. Following the court decision in the *Nice Cheer* case, the increases (unrealised gains) in the market values of trading securities are not taxable while the decreases (unrealised losses) may be deductible when they are recorded in the financial statements.

There are special tax provisions for valuation upon cessation of a business under which inventory is valued at market value, unless it is sold to a person carrying on business in Hong Kong, who may deduct a corresponding amount as the cost of the inventory in computing the assessable profits.

Capital gains

Gains from realisation of capital assets or receipts that are capital in nature are not taxed.

Dividend income

Dividends from local companies chargeable to tax are exempt, whereas dividends from overseas companies are generally offshore in nature and not subject to Hong Kong profits tax. Hong Kong corporations may declare bonus issues (i.e. stock dividends), which are not taxable in the hands of the recipients.

Interest income

Hong Kong sourced interest income received by or accrued to a corporation carrying on a trade or business in Hong Kong is subject to profits tax. Exemption is provided to interest income derived from any deposit placed in Hong Kong with a financial institution, unless the deposit secures a borrowing where the interest expense is deductible. This exemption, however, does not apply to interest accruing to a financial institution.

Interest accruing to a bank or financial institution will be deemed to be sourced and taxable in Hong Kong if the interest arises through or from the carrying on of business in Hong Kong by the bank or financial institution.

Interest income arising through or from the carrying on of an intra-group financing business in Hong Kong by a corporation (other than a financial institution) will be deemed to be sourced and taxable in Hong Kong.

Royalties

Royalties paid or accrued to a non-resident for the use of or right to use in Hong Kong or outside Hong Kong (if the royalties are deductible in ascertaining the assessable profits of a person for Hong Kong profits tax purposes) a trademark, patent, design, copyright material, secret process, or other property of a similar nature, or for the use in Hong Kong of cinema or television tape or any sound recording, are deemed to be taxable in Hong Kong.

A total of 30% of the sum receivable is deemed to constitute profits subject to tax in normal situations. Where such royalties are received by or accrued to an associated corporation, however, 100% of the sum is deemed to constitute profits under certain circumstances.

Partnership income

Partnership business is taxed as a single entity, although an individual partner can use its share of losses incurred by a partnership to offset against the assessable profits of its other business. In general, there is no special registration requirement other than business registration for a partnership. The assessable profits of a partnership are basically determined in the same way as those of a corporation, with certain special rules (e.g. salaries or other remunerations paid to a partner or a partner's spouse are not deductible).

Unrealised exchange gains/losses

In general, unrealised exchange gains/losses are taxable/deductible if they are recognised in the profit and loss accounts in accordance with Generally Accepted Accounting Principles (GAAP), provided that they are revenue in nature and with a Hong Kong source. The nature and source of exchange gains/losses are determined by the nature and source of the underlying transactions. Exchange gains/losses arising from ordinary business transactions (e.g. trade receivables or payables) are taxable/deductible whereas exchange gains/losses arising from capital transactions (e.g. sale of capital assets) are non-taxable/non-deductible.

Foreign income

Hong Kong resident corporations are not taxed on their worldwide income. Foreign-sourced income, whether or not remitted to Hong Kong, is not taxed. As such, there is no specific tax provision dealing with deferral or non-remittance of foreign earnings. Nor does Hong Kong have any controlled foreign company (CFC) legislation.

Deductions

Expenses that are incurred for producing profits chargeable to tax and that are not capital in nature are generally tax deductible. In addition, special tax relief is available for certain capital expenditure. There are special rules for deduction of certain expenses (e.g. interest expenses).

Accounting treatments are usually followed in determining the assessable profits, except when there is an explicit rule in the IRO. Accrued expenses recognised in the profit and loss accounts in accordance with GAAP are usually deductible if they are incurred for producing profits chargeable/subject to Hong Kong profits tax and are not capital in nature.

Expense items for which a tax adjustment is necessary in determining the amount of taxable profits from the accounting profits include: tax depreciation allowance vs. accounting depreciation, expenses that are capital in nature, general provisions that are non-deductible, and non-deductible interest expenses on borrowings used to finance non-income producing assets.

Set out below are the Hong Kong profits tax treatments of some common expense items.

Tax depreciation of fixed assets

Tax depreciation allowances/deductions are available for capital expenditure incurred on the construction of buildings or structures and in the provision of machinery and plant for trade or business purposes, as follows:

- Industrial buildings and structures: An initial allowance of 20%, in addition to an annual allowance of 4%, of the cost of construction or cost of purchase from a developer is granted for an industrial building or structure occupied for the purpose of a qualifying trade. Provision is made for balancing allowance or charge in the year of assessment in which the building is disposed of to adjust the written-down value of the building to the disposal price. Balancing charges are restricted to the total of initial and annual allowances previously given.
- Commercial buildings and structures: An annual allowance of 4% of the capital expenditure incurred on the construction is applicable. A balancing allowance or charge applies upon disposal. Balancing charges are restricted to the total annual allowances previously given.
- Plant and machinery: An initial allowance of 60% of the capital expenditure on plant and machinery is given for the year of assessment during the basis period in which the expenditure is incurred. An annual allowance is also given for depreciation at three prescribed rates on the reducing value of each of the three depreciation rate 'pools'. The three prescribed rates are 10%, 20%, and 30%, and the reducing value of each of the three depreciation rate pools is original cost less initial and annual allowances and sales proceeds. Provision is made for balancing charges when plant and machinery within one of the three depreciation rate pools is sold or disposed of and the reducing value of that pool is less than the sale price, which is capped at the original amount incurred in the pool. In addition, balancing allowances or charges may be applicable upon cessation of business. Otherwise,

sales proceeds are deducted in calculating the reducing value on which the annual allowance is calculated.

Book depreciation is adjusted for tax purposes in accordance with the above depreciation allowances granted under the IRO.

Goodwill

Cost of acquisition of goodwill/amortisation of goodwill is not deductible as it is capital in nature.

Organisational and start-up expenses

In general, company formation/start-up expenses that are incurred before the commencement of a trade, profession, or business and that are for the establishment of the overall income producing structure are capital in nature and not tax deductible.

Research & development (R&D)

There is a specific provision allowing the deduction of expenditure incurred on R&D (including payments made to an approved research institute and in-house expenditure), provided that certain specified conditions are met.

Interest expenses

There is no thin capitalisation rule in Hong Kong. However, except in some specified circumstances (e.g. interest expenses paid to an overseas associated corporation by a corporation carrying on an intra-group financing business in Hong Kong where certain conditions are met), interest expenses paid to an overseas recipient (whether a related or unrelated party) are generally not deductible if the overseas recipient is not subject to Hong Kong profits tax on the interest income. In addition, deduction of interest expense is subject to stringent and complicated rules that are designed to guard against loan arrangements with an intention to avoid Hong Kong profits taxes.

Bad debts

A bad or doubtful debt incurred in any trade, business, or profession, proved to the satisfaction of the HKIRD to have become bad during the basis period for a year of assessment, is deductible. The deduction is limited to debts that were included as a trading receipt in ascertaining the taxpayer’s assessable profits or debts in respect of money lent in the ordinary course of a money-lending business in Hong Kong.

If any bad or doubtful debt that has previously been allowed as a deduction is ultimately recovered, it will be treated as taxable profits of the basis period in which it is recovered.

Charitable contributions

A deduction is allowed for cash donations to approved charities made in the basis period for a year of assessment if the aggregate of such donations is not less than HKD 100. The deduction is limited to 35% of the assessable profits of the year of assessment.

Pension expenses

A deduction is allowed for regular/ordinary contributions to a mandatory provident fund scheme or recognised occupational retirement scheme made by an employer in respect of an employee to the extent that the contributions do not exceed 15% of the employee’s total emoluments for the period to which the contributions relate.

Special payments, other than the ordinary contributions to a mandatory provident fund scheme or recognised occupational retirement scheme, are capital in nature but can be deducted evenly over a five-year period under a specific provision of the IRO.

There are also specific rules for deduction of provisions for contributions to a mandatory provident fund scheme or recognised occupational retirement scheme.

Payments for directors

Director fees or other remunerations paid by a corporation to its directors are generally deductible under the normal deduction rule. Nevertheless, no deduction is allowed on salaries or other remunerations paid to a sole proprietor or any partners or partners' spouses of a partnership business.

Contingent liabilities

Generally speaking, general provisions for expenses are not deductible, whereas specific provisions are deductible if the HKIRD is satisfied that the amount has been incurred (i.e. the taxpayer has a legal/contractual obligation to pay such amount in the future) and that the provision represents a reasonably accurate estimate of the future liability.

Special deductions

There are special deduction rules for expenditures incurred:

- for refurbishment of a building or structure, other than a domestic building or structure
- on environmental protection installation and machinery
- on environment-friendly vehicles
- on machinery or plant used specifically and directly for any manufacturing process, computer hardware (other than that which is an integral part of machinery or plant), computer software, and computer systems (collectively known as prescribed fixed assets)
- for registering trademarks, designs, or patents used in the production of taxable profits, and
- on the purchase of patent/know-how rights and specified intellectual property (IP) rights (i.e. copyrights, registered trademarks, or registered designs), provided certain specified conditions are met.

Fines and penalties

Fines and penalties are generally not deductible, as the HKIRD does not consider them to be expenses incurred for producing profits chargeable/subject to tax.

Taxes

Taxes paid on corporate profits are generally not deductible for the purpose of calculating the assessable profits. However, the HKIRD generally accepts that a foreign tax that is an expense that must be borne regardless of whether or not a profit is derived (e.g. a foreign withholding tax [WHT] levied on the gross amount of interest or royalties received), as opposed to a charge on the profits themselves, is deductible under the general deduction provision. Where interest income or gains from the sale of a certificate of deposit or bill of exchange are deemed to be subject to profits tax, a deduction is allowed for foreign taxes of substantially the same nature of Hong Kong profits tax paid in respect of the same income, provided that the taxpayer is not eligible for double taxation relief under a CDTA.

Net operating and capital losses

Net operating losses incurred in an accounting year can be carried forward indefinitely to offset future profits of the business. A corporation carrying on more than one business may have losses in one business offset profits of the others, with any balance being carried forward. Net operating losses cannot be carried backward.

Capital losses are not tax deductible.

Payments to foreign affiliates

Royalties and service fees paid/payable by a Hong Kong corporation to foreign affiliates are deductible, provided they are incurred for the production of profits chargeable/subject to tax. There is no special restriction on the deductibility of these payments.

In general, interest payable by a Hong Kong corporation to a foreign affiliate is not deductible if the recipient is not chargeable/subject to Hong Kong profits tax on the interest income received (except where either the payer or the recipient is a financial institution as defined in the tax law). Interest expenses on money borrowed from a non-Hong Kong associated corporation by a corporation in the ordinary course of its intra-group financing business carried on in Hong Kong are deductible, provided that certain specified conditions are met.

Group taxation

Hong Kong does not have a consolidated or group taxation regime.

Transfer pricing

Currently, there is no specific and comprehensive transfer pricing legislation in Hong Kong. While a few existing provisions in the IRO may be employed by the tax authority to tackle non-arm's-length transactions, such provisions are primarily aimed at transactions with closely connected non-residents or tax avoidance transactions rather than specific legislation on transfer pricing.

There are two Departmental Interpretation and Practice Notes (DIPNs) issued by the HKIRD to address the transfer pricing issues in Hong Kong. DIPN 45 focuses on the administrative/procedural issues involved in providing double tax relief in a treaty context, such as when such relief is available and what are the procedures for claiming such relief. DIPN 46 outlines the HKIRD's view on the legislative framework for transfer pricing in Hong Kong (including the statutory provisions in the IRO and the articles in a CDTA that are relevant to transfer pricing) and provides guidance on numerous transfer pricing related issues, such as the application of the arm's-length principle and the acceptable transfer pricing methodologies, which are largely in line with the Organisation for Economic Co-operation and Development (OECD) transfer pricing guidelines. The DIPN also spells out the documentation that taxpayers should consider retaining to support their transfer pricing arrangements and explains the interaction between the transfer pricing and sourcing rules in Hong Kong.

In general, the HKIRD currently adopts the arm's-length principle and will seek to apply the OECD transfer pricing guidelines except where they are incompatible with the express provisions in the IRO. Transfer pricing rules will be implemented by the Hong Kong SAR Government through the enactment of Inland Revenue (Amendment) (No. 6) Bill 2017, which was gazetted on 29 December 2017. The proposed transfer pricing rules follow the OECD guidelines and adopt the arm's-length principle. Domestic transactions without any Hong Kong tax advantage are excluded from the application of the transfer pricing rules. The Bill also introduces rules for transfer pricing documentation and advance pricing arrangement (APA) application. Once enacted, the transfer pricing rules and the APA statutory regime, as provided in the Bill, will have retrospective effect from 1 April 2018.

An APA programme is available in Hong Kong. The objectives of the APA programme are to help taxpayers obtain tax certainty on their complex or significant transfer pricing arrangements and reduce the risk of double taxation arising from related-party transactions. Resident enterprises or non-resident enterprises with a PE in Hong Kong may apply for an APA in respect of their transactions with associated enterprises under a CDTA, provided that certain conditions (including the threshold for an APA application) are met.

Currently, the HKIRD is primarily focused on bilateral APA or multilateral APA applications in respect of cross-border, related-party transactions involving countries that are CDTA partners with Hong Kong.

DIPN 48, issued by the IRD, provides guidance on various aspects of the APA regime, such as the timeframe and threshold for an APA application, the various stages involved in the APA process, an audit involving years covered by a concluded APA, and possible rollback of the transfer pricing methodology agreed under an APA to prior years. The appendices of the DIPN include various sample documents for use in an APA application.

Country-by-country (CbC) reporting regime

To implement the minimum standard under Action 13 of the OECD's Base Erosion and Profit Shifting (BEPS) Action Plan, the Hong Kong SAR Government has proposed to introduce CbC report filing requirements in Hong Kong in the Inland Revenue (Amendment) (No. 6) Bill 2017, gazetted on 29 December 2017. The Bill seeks to, among others, introduce a transfer pricing regulatory regime and mandatory three-tiered transfer pricing documentation requirement (including CbC report) in Hong Kong. The Bill has not yet been enacted into law as of the end of May 2018.

Key features of the proposed CbC reporting regime are summarised as follows:

- The Hong Kong ultimate parent entity of a multinational enterprise group with annual consolidated group revenues of 750 million euros (EUR) (i.e. about HKD 6.8 billion) or above (i.e. a reportable group) will be required to file a CbC return in Hong Kong.
- A Hong Kong entity of a reportable group that is not the group's ultimate parent entity will also be required to file a CbC return in Hong Kong if the ultimate parent entity is not required to file a CbC report in its own jurisdiction of tax residence or if Hong Kong is not able to obtain the CbC report from that jurisdiction.
- The CbC report filing requirement will apply retrospectively to accounting periods beginning on or after 1 January 2018.

- Generally speaking, the deadline for filing a CbC return is within 12 months after the end of the accounting period to which the return relates. Where surrogate parent filing applies and a later deadline for filing CbC reports is prescribed in the laws or regulations of the jurisdiction of tax residence of the surrogate parent entity, the later deadline will be taken as the filing deadline in relation to the CbC return concerned.

Thin capitalisation

Hong Kong does not have thin capitalisation rules. *For restrictions on deduction of interest expenses, see Interest expenses in the Deductions section*.

Controlled foreign companies (CFCs)

Hong Kong does not have a CFC regime.

Tax credits and incentives

Foreign tax credits

Foreign tax credits are available if foreign taxes are payable/paid on income derived from a jurisdiction that has entered into a CDTA with Hong Kong and the same income is subject to tax in Hong Kong. *See the Withholding taxes section for a list of jurisdictions that have entered into a CDTA with Hong Kong*.

Foreign investment incentives

Hong Kong does not have any specific incentives for foreign investment, except that offshore funds may be exempt from profits tax under certain circumstances.

Other tax incentives

Please refer to the Taxes on corporate income *section for other tax incentives that can be enjoyed by both foreign and Hong Kong companies*.

Withholding taxes

There is no WHT on dividends and interest. Royalties received by non-residents (*see Royalties in the Income determination section*) are subject to a WHT (*see the applicable WHT rates for corporations below*).

Resident consignees are required to furnish quarterly returns to the HKIRD showing the gross proceeds from sales on behalf of their non-resident consignors and to pay to the Commissioner of Inland Revenue (CIR) a sum equal to 0.5% of such proceeds. The HKIRD normally accepts this as satisfying the Hong Kong tax obligations of the non-resident.

Hong Kong has so far entered into 40 treaties with different jurisdictions. The following table shows the applicable WHT rates for payments made from Hong Kong payers to non-treaty and treaty country corporate recipients. The rates shown in the table are the lower of the domestic and treaty rates. For WHT rates on payments received by Hong Kong recipients from treaty country payers, please refer to the summaries of the respective treaty countries.

Hong Kong

Recipient	WHT (%) Dividends (1)	Interest (1)	Royalties (2)
Non-treaty	0	0	2.475 to 4.95 (2)
Treaty:			
Austria	0	0	2.475 to 3 (3)
Belarus	0	0	2.475 to 3 (4)/2.475 to 4.95 (5)
Belgium	0	0	2.475 to 4.95 (5)
Brunei	0	0	2.475 to 4.95 (5)
Canada	0	0	2.475 to 4.95 (5)
China, the People's Republic of	0	0	2.475 to 4.95 (5)
Czech Republic	0	0	2.475 to 4.95 (5)
Finland (8)	0	0	2.475 to 3 (3)
France	0	0	2.475 to 4.95 (5)
Guernsey	0	0	2.475 to 4 (6)
Hungary	0	0	2.475 to 4.95 (5)
India (8)	0	0	2.475 to 4.95 (5)
Indonesia	0	0	2.475 to 4.95 (5)
Ireland	0	0	2.475 to 3 (3)
Italy	0	0	2.475 to 4.95 (5)
Japan	0	0	2.475 to 4.95 (5)
Jersey	0	0	2.475 to 4 (6)
Korea	0	0	2.475 to 4.95 (5)
Kuwait	0	0	2.475 to 4.95 (5)
Latvia	0	0	0/2.475 to 3 (7)
Liechtenstein	0	0	2.475 to 3 (3)
Luxembourg	0	0	2.475 to 3 (3)
Malaysia	0	0	2.475 to 4.95 (5)
Malta	0	0	2.475 to 3 (3)
Mexico	0	0	2.475 to 4.95 (5)
The Netherlands	0	0	2.475 to 3 (3)
New Zealand	0	0	2.475 to 4.95 (5)
Pakistan	0	0	2.475 to 4.95 (5)
Portugal	0	0	2.475 to 4.95 (5)
Qatar	0	0	2.475 to 4.95 (5)
Romania	0	0	2.475 to 3 (3)
Russia	0	0	2.475 to 3 (3)
Saudi Arabia (8)	0	0	2.475 to 4.95 (5)
South Africa	0	0	2.475 to 4.95 (5)
Spain	0	0	2.475 to 4.95 (5)
Switzerland	0	0	2.475 to 3 (3)
Thailand	0	0	2.475 to 4.95 (5)
United Arab Emirates	0	0	2.475 to 4.95 (5)
United Kingdom	0	0	2.475 to 3 (3)
Vietnam	0	0	2.475 to 4.95 (5)

Notes

1. Hong Kong does not impose WHT on dividends and interest currently. However, the treaties provide for a maximum WHT rate on dividends and interest should Hong Kong impose such WHT in the future. Some of the treaties also provide for a reduced WHT rate on dividends and interest if conditions specified in the treaties are met.
2. With the introduction of two-tier profits tax rates, there are two possible sets of domestic WHT rates on royalties paid to non-resident corporations:

i. If the two-tier tax rates apply, the WHT rates are 2.475% for the first HKD 2 million of assessable profits and 4.95% for the remaining amount.
ii. If the two-tier tax rates do not apply, the WHT rate for the whole amount of assessable profits is 4.95%.

The 2.475% and 4.95% rates are determined by applying the relevant two-tier rates, which are 8.25% and 16.5%, respectively, on the deemed assessable profits of the royalties. In the normal situation, the deemed assessable profits are 30% of the royalties received by or accrued to a non-resident corporation. Hence, the effective WHT rate ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (applies to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two-tier rates are not applicable).

In the situation where a person carrying on a trade or business in Hong Kong has, at any time, wholly or partly owned the IP in respect of which the royalties are paid and the non-resident corporation is an associate of the Hong Kong payer, the deemed assessable profits are 100% of the royalties received by or accrued to a non-resident corporation. Hence, the applicable WHT rates are 8.25% for the first HKD 2 million of assessable profits and 16.5% for the remaining amount if the two-tier rates are applicable.

3. The domestic WHT rate ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (applies to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable), capped at 3% according to the treaty.
4. For payments for the use of, or the right to use, aircraft, the effective WHT rate ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 3% (applies to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable). For other cases, the effective WHT rate ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (applies to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable).
5. Since a rate specified in the treaty is higher than the domestic WHT rates, the effective WHT rate ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (applies to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable).
6. The domestic WHT rate ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (applies to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable), capped at 4% according to the treaty.
7. The 0% rate applies to payments for the use of, or the right to use, industrial, commercial, or scientific equipment or for information concerning industrial, commercial, or scientific experience. For other cases, the WHT rate ranges from 2.475% (when the assessable profits are HKD 2 million or less and the two-tier rates are applicable) to 4.95% (applies to the assessable profits in excess of HKD 2 million when the two-tier rates are applicable or when the two tier-rates are not applicable), capped at 3% according to the treaty.
8. Not yet ratified.

Tax administration

Taxable period

A year of assessment (or tax year) begins on 1 April of a year and ends on 31 March of the following year. The period that is used to compute the taxable profits for a year of assessment is called the basis period, which is normally the financial year ended in the year of assessment.

Tax returns

Tax returns are issued on the first working day of April each year. The filing deadline is usually within a month from the date of issue. However, corporations whose financial year ended after 30 November and are represented by a tax representative are normally granted with an extension for filing their returns. The exact filing due date depends on the accounting year-end date of the taxpayer.

The basis of assessment is the accounting profits of the financial year ending within the year of assessment, with appropriate adjustments for tax purposes. A tax return is usually filed together with a tax computation showing the tax adjustments to the accounting profits in arriving at the taxable profits or allowable tax losses for a given year of assessment.

Corporate taxpayers are also required to attach their audited accounts as supporting documents when filing a profits tax return, unless they qualify as a small corporation as defined by the HKIRD (i.e. mainly those with gross income for a basis period of not exceeding HKD 2 million plus a few other conditions). Small corporations are not required to attach supporting documents with their profits tax returns but are still required to keep those documents and submit them upon request. A branch of a foreign corporation doing business in Hong Kong is required to file a profits tax return annually, and the HKIRD may require audited accounts of the foreign corporation to support the Hong Kong branch's profits tax return.

Notice of assessment will be issued after the tax return has been examined by the HKIRD. Taxpayers may be subject to post-assessment investigation or field audit under the computerised random selection procedures of the HKIRD at a later date.

Payment of tax

Tax is usually payable in two instalments. The dates of payment of tax, which generally fall between November of the year in which the return is issued and April of the following year, are determined by the CIR and specified in an assessment notice. A system of provisional tax payments applies whereby estimated tax payments are made during the current year. The provisional profits tax payable is normally estimated based on the previous year's profits tax liability. The provisional profits tax already paid is credited against the final profits tax assessed for a year of assessment, which is determined after filing of the return.

Taking a company with an accounting year end date of 31 December as an example, the final tax payment for the company for a given tax year is usually due in November of the year in which the return is issued, whereas the provisional tax payments (to be paid in two instalments) are usually due in November of the current year and January of the next year.

Tax audit process

There is no specific tax audit cycle in Hong Kong. Tax audit targets are selected with reference to certain criteria determined by the HKIRD.

Statute of limitations

An additional assessment may be made by an HKIRD tax assessor if a taxpayer chargeable to tax has not been assessed to tax or has been assessed at less than the proper amount. The assessment must be made within the relevant year of assessment or within six years after the end of that year of assessment. The time limit for making additional assessments is extended when a taxpayer either has not been assessed, or is under-assessed, due to fraud or wilful evasion. In that case, an additional assessment may be made up to ten years after the end of the relevant assessment year.

A statement of loss is not an assessment, and the above six-year time limit does not apply to issue or revision of a statement of loss. A tax loss year remains technically open until the sixth year after the first year in which the taxpayer has an assessable profit after utilising all the tax losses brought forward.

Topics of focus for tax authorities

Profits tax issues that are often subject to close scrutiny of the tax authority include offshore claim of profits, capital claims of income, transactions with related parties and closely connected non-residents, and deductibility of expenses (e.g. interest expenses, share-based payments, intra-group management/service fees).

General anti-avoidance rules (GAARs)

The IRO includes a GAAR (i.e. section 61A) allowing the HKIRD to disregard a transaction or counteract the tax benefit conferred by a transaction if the sole or dominant purpose of entering into such a transaction is to obtain a tax benefit. Whether the sole or dominant purpose of entering into a transaction is for obtaining a tax benefit will be assessed according to a set of factors stipulated in section 61A. Another GAAR in the IRO is section 61, which empowers the HKIRD to disregard a transaction that reduces or would reduce the amount of tax payable by any person if that transaction is considered artificial or fictitious. Although both GAARs could be used, in practice, section 61A is more often invoked by the HKIRD in tackling tax avoidance schemes.

Specific anti-avoidance provision for related-party transactions

In addition to the general anti-avoidance provisions described above, there is a specific anti-avoidance provision dealing with transactions with closely connected non-residents. Under the specific provision, if a resident person carries on a business with a closely connected non-resident person such that no profits or less than the ordinary profits are derived by the resident person in the course of such business, the non-resident person can be assessable and chargeable to tax in respect of profits derived from such business in the name of the resident person.

Other issues

Base Erosion and Profit Shifting (BEPS)

The Inland Revenue (Amendment) (No. 6) Bill 2017 was gazetted on 29 December 2017. The Bill seeks to, among others, (i) introduce a transfer pricing regulatory regime and a mandatory three-tiered transfer pricing documentation requirement in Hong Kong, (ii) implement a statutory APA regime, and (iii) remove the ring-fencing features in certain concessionary tax regimes in Hong Kong. The Bill was introduced into the Legislative Council for scrutiny in January 2018 and has not yet been passed as of May 2018.

Multilateral Instrument (MLI)

Hong Kong, as represented by mainland China, was one of the signatories to the MLI. In implementing the MLI, Hong Kong has taken a pragmatic approach by (i) opting in the provisions of the MLI that represent the BEPS minimum standards (e.g. the principal purpose test for preventing treaty abuse and the requirement for allowing a minimum three-year period for a person to prevent its case for Mutual Agreement Procedure) and (ii) opting out of the other provisions that are not mandatory, for instance, those provisions addressing hybrid mismatches and artificial avoidance of PE.

Hong Kong is currently going through the necessary domestic legislative process to implement the MLI as domestic legislation, and the MLI is not yet effective for Hong Kong.

Automatic exchange of financial account information (AEOI) / Common Reporting Standard (CRS) regime

The Inland Revenue (Amendment) (No. 3) Ordinance 2016, which commenced operation on 30 June 2016, put in place a legislative framework for Hong Kong to implement the AEOI/CRS regime. Reportable financial institutions are required to identify the reportable financial accounts held by tax residents of reportable jurisdictions or held by passive non-financial entities whose controlling persons are tax residents of reportable jurisdictions in accordance with the specified due diligence procedures, collect the required information of those reportable accounts, and furnish such information to the HKIRD. Such information will be exchanged on an annual basis. Hong Kong will only conduct AEOI with a reportable jurisdiction when an arrangement is in place with the reportable jurisdiction concerned to provide the basis for exchange. There are currently 75 reportable jurisdictions. As of May 2018, Hong Kong has signed bilateral Competent Authority Agreements for AEOI with 15 jurisdictions.

Tax information exchange agreements (TIEAs)

Currently, Hong Kong has entered into seven TIEAs with different jurisdictions as shown in the following table.

- Denmark
- Faroes
- Greenland
- Iceland
- Norway
- Sweden
- United States

All of the above TIEAs are ratified and effective.

In addition to the signing of the HK-US TIEA, Hong Kong signed a Model 2 intergovernmental agreement (IGA) with the United States in November 2014 to facilitate financial institutions in Hong Kong to comply with the Foreign Account Tax Compliance Act (FATCA).

Foreign investment restrictions

In general, Hong Kong does not impose restriction to foreign investors to make investments in Hong Kong, and wholly foreign owned companies are allowed. The only exception is the restriction on foreign ownership of Hong Kong's licensed television/sound broadcasters, of which the collective foreign ownership ceiling is 49% of the voting power. In addition, an approval from the Broadcasting Authority must be obtained for holding, acquisition, or exercise of voting control by a foreign investor of more than 2% of a licensee.

Exchange controls

Hong Kong does not have any foreign exchange control. There is no restriction on entry or repatriation of capital or remittance of profits from investments. Funds can be freely remitted to persons outside Hong Kong by various means (e.g. dividends, interest, royalties, service fees, branch profits).

Choice of business entity

The principal forms through which a business can be conducted in Hong Kong are as follows:

- Company incorporated in Hong Kong (either private or public via listing on the Stock Exchange of Hong Kong).
- Branch of a foreign company.
- Representative or liaison office of a foreign company.
- Joint venture (can be set up either as a company or partnership).
- Partnership.
- Sole proprietorship.

Of the above, privately incorporated companies and branches of foreign companies are most commonly used by foreign investors, as limited liability is usually desirable.

Intellectual property (IP) regulations

The Intellectual Property Department is responsible for monitoring the IP regime and ensuring the protection and enforcement of IP rights in Hong Kong. The Department is also responsible for investigating complaints against infringements and has extensive powers of search and seizure. Registration and protection of patents, copyrights, trademarks, and registered designs are each governed by a separate ordinance.

Merger and acquisition (M&A) activities

There are no specific restrictions on M&A activities in Hong Kong. The following tax considerations are relevant in the M&A context:

- Dividends or other forms of distribution of profits (e.g. distribution of branch profits to the head office) are generally not taxable.
- Capital gains arising from an M&A transaction are not taxable in the hands of the transferor, whereas amortisation of the goodwill in the transferee's accounts is not tax deductible due to its capital nature.
- Gains derived from transfer of revenue items (e.g. trade receivables) in an asset deal will be subject to profits tax.
- For a share deal, stamp duty is payable on the transfer of Hong Kong shares at 0.2%, unless an exemption applies; for an asset deal, stamp duty is payable on conveyance of immovable property in Hong Kong at various rates up to 15%, depending on the type of immovable property transferred and the date of the transfer (*see Stamp duty in the Other taxes section*).
- There is no special tax concession/incentive relating to M&A transactions.
- Tax losses in the acquired company can generally be carried forward indefinitely to set off against future assessable profits. However, there are specific anti-avoidance provisions in the IRO that prevent the transfer of shares of a company with accumulated tax losses to owners of a profitable company for the sole or dominant purpose of utilising the tax losses (i.e. offsetting the tax losses against the profits generated from other trade, profession, or business of the transferee).
- Pending the enactment of specific tax legislation dealing with corporate amalgamation, the HKIRD has issued some guidance on the profits tax treatment of various issues arising from corporate amalgamation on its website. In addition to the utilisation of tax losses, the guidance also covers issues such as the profits tax treatment of fixed assets and trading stocks transferred, and the profits tax return filing positions of the amalgamating and the amalgamated companies in the year of amalgamation, etc.

India

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Significant developments

Expanded scope of 'dependent agent'

The Finance Act, 2018 has expanded the scope of 'dependent agent'. In line with Base Erosion and Profit Shifting (BEPS) Action Plans 7 and 1, the term 'dependent agent' will now include persons who play a principal role in conclusion of contracts leading to the conclusion of contracts.

Concept of 'significant economic presence' introduced

The Finance Act, 2018 has introduced the concept of 'significant economic presence' in domestic tax law. By virtue of this, the income of non-residents is deemed to accrue or arise in India if they have a significant economic presence in India.

The term 'significant economic presence' has been defined to include: (i) transactions carried out by a non-resident in India, including provision of download of data or software in India, if the aggregate payment arising from such transactions exceeds such amount as may be prescribed later, and (ii) systematic and continuous soliciting of business activities or engaging in interaction with such number of users as may be prescribed in India through digital means.

Further, such transactions or activities shall constitute significant economic presence in India whether or not (i) the agreement is entered into in India, (ii) the non-resident has a residence or place of business in India, or (iii) services are rendered in India.

Though the above amendments are applicable from tax year 2018/19, the same would be in force post amendments made to Indian tax treaties on implementation of the Multilateral Instrument (MLI).

Income computation and disclosure standards (ICDS)

For the purposes of computation of income chargeable to income tax under the head 'profits and gains of business or profession' or 'income from other sources', ICDS were introduced by the government of India. There has been debate on applicability of these standards. The government of India, through the Finance Act, 2018, in order to bring certainty in the light of debate, has amended the provisions of the tax laws and made certain retrospective amendments.

Taxes on corporate income

A resident company is taxed on its worldwide income. A non-resident company is taxed only on income that is received in India, or that accrues or arises, or is deemed to accrue or arise, in India.

India

The corporate income tax (CIT) rate applicable to an Indian company and a foreign company for the tax year 2018/19 is as follows:

	Rate of CIT (%)					
	Turnover not greater than INR 2.5 billion in tax year 2016/17		Other domestic companies		Foreign companies	
Income *	**Basic**	**Effective****	**Basic**	**Effective****	**Basic**	**Effective ****
Less than 10 million Indian rupees (INR)	25	26.00	30	31.20	40	41.60
More than INR 10 million but less than INR 100 million	25	27.82	30	33.38	40	42.43
More than INR 100 million	25	29.12	30	34.94	40	43.68

* Surcharge is payable only where total taxable income exceeds INR 10 million.

** Effective tax rates include surcharge and health and education cess.

Minimum alternative tax (MAT)

Companies are liable to pay MAT on their adjusted book profits (other than income from life insurance business) where the tax liability under the normal provisions (excluding surcharge and health and education cess) of the Income Tax Act, 1961 ('the Act') for the tax year is not more than 18.5% (excluding surcharge and health and education cess) of such book profits. MAT credit is the amount paid over and above the normal tax liability, which can be carried forward and can be utilised for 15 years. However, MAT credit to the extent of difference between the foreign tax credits allowed against MAT over such credit allowable against the tax under the other provisions of the Act shall not be eligible to be carried forward.

Further, due to implementation of Indian Accounting Standards (Ind AS) by the government, which are converged with the International Financial Reporting Standards (IFRS), the government amended the MAT provisions of the Act, so as to provide the framework for the computation of book profit for the purpose of levying MAT in the case of companies required to comply with Ind AS in the year of adoption and thereafter. This framework was specified on the basis of the recommendations of the MAT Ind AS Committee constituted for this purpose.

MAT provisions are not applicable to foreign companies that do not have a permanent establishment (PE) in India. However, the Finance Act, 2018 has provided that MAT provisions shall not apply to foreign companies where their total income is solely derived from shipping business, exploration of mineral oils, business of aircraft, or civil construction in turnkey projects, and income thereon is offered to tax as per specific provisions provided under the Act.

Capital gains from transfer of securities, interest, royalties, and fees for technical services accruing or arising to a foreign company (which has a PE in India) have been excluded from chargeability of MAT if tax payable on such income is less than 18.5% (exclusive of surcharge, education cess, etc.). Further, expenditure, if any, debited to the profit and loss account corresponding to such income shall be added back to the book profit for the purpose of computation of MAT.

	Rate of MAT (%)			
	Indian company		Foreign company (other than exempted)	
Income *	Basic **	Including surcharge and health and education cess (effective tax rate)	Basic	Including surcharge and health and education cess (effective tax rate)
Less than INR 10 million	18.5	19.240	18.5	19.240
More than INR 10 million but less than INR 100 million	18.5	20.586	18.5	19.240
More than INR 100 million	18.5	21.548	18.5	20.202

* Surcharge is payable only where total taxable income exceeds INR 10 million.

** Basic rate of MAT is 9% in case of a company located in an International Financial Services Centre and deriving income solely in convertible foreign exchange.

Sick companies (i.e. companies whose losses have wiped out their net worth and that are doubtful of being revived and nursed back to profitability) are not subject to MAT.

A Special Economic Zone (SEZ) developer and a unit in an SEZ are also liable to pay MAT.

Tonnage tax scheme

The tonnage tax scheme, a presumptive tax provision, can be chosen by a non-resident company that has a place of effective management (PoEM) in India, owns at least one qualifying ship, and whose main objective is to carry on the business of operating 'qualifying ships'. The tonnage tax scheme is in place of CIT and is levied on the basis of tonnage of vessels owned, operated, or chartered by it instead of on net income generated by commercial operations. Under a presumptive tax system, taxpayers can opt to be taxed at a pre-designated tax rate on its revenues.

Under this scheme, deemed income shall be assessed at 7.5% of the amount paid or payable (whether in or out of India) for carriage of passengers, livestock, mail, or goods shipped from any port in India, and the amount received or deemed to be received in India on account of carriage of passengers, livestock, mail, or goods shipped to any port outside India shall be treated as profits and gains of business.

Treaty rates will apply to non-resident shipping companies if they are lower than the rates under the tonnage tax scheme.

A government company, or a public company formed and registered in India with the main object of operating ships, is eligible for a deduction not exceeding the lower of 50% of its profits and the sum transferred to a special reserve to be utilised in accordance with the provisions of the Act.

Local income taxes

There are no local, state, or provincial taxes on income in India at present.

Corporate residence

A company is treated as a resident of India in any previous year if:

- it is an Indian company, or
- its PoEM in that year is in India (*see below*).

A partnership firm, a limited liability partnership (LLP), and other non-individual entities are treated as resident in India if any portion of their control and management is in India. They are non-resident if their control and management is situated wholly outside India.

Place of effective management (PoEM)

Presently, a foreign company is considered resident in India if the control and management of its affairs is situated wholly in India.

To bring to tax those companies that are incorporated outside India but controlled from India, the condition of PoEM has been introduced. PoEM is an internationally recognised concept accepted by the Organisation for Economic Co-operation and Development (OECD).

A foreign company will be regarded as a resident in India if its PoEM is in India in that year. Since residency is determined for each year, PoEM is also required to be determined on a year-to-year basis. The concept of PoEM is one of substance over form. The term PoEM has been explained to mean a place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance, made. To provide clarity and address certain concerns with regard to implementation of determination of residency of a foreign company on the basis of PoEM, the Central Board of Direct Taxes (CBDT) has issued a circular laying down guidelines. The guidelines laid down the concept of determination of PoEM based on bifurcation of companies engaged in active business outside India and other companies. The circulars clarify that the PoEM provisions shall not apply to a foreign company having turnover or gross receipts of INR 500 million or less in a tax year.

Permanent establishment (PE)

A PE is defined in India as a fixed place of business through which the business of an enterprise is wholly or partly carried on.

Business connection

The Finance Act, 2018 has modified the scope of 'business connection' to align with the modified PE Rule as per the MLI.

'Business connection' includes business activities carried on by a non-resident through dependent agents. The scope of business connection under the Act is similar to the provisions relating to Dependent Agent Permanent Establishment (DAPE) in India's Double Taxation Avoidance Agreements (DTAAs). The amendment provides that business connection shall also include any business activities carried through a person who, acting on behalf of the non-resident, habitually concludes contracts or habitually plays the principal role leading to conclusion of contracts by the non-resident. It further states that the contracts should be:

- in the name of the non-resident

- for the transfer of the ownership of, or for the granting of the right to use, property owned by that non-resident or that the non-resident has the right to use, or
- for the provision of services by that non-resident.

Further, as per the provisions of the Act, 'significant economic presence' would also constitute a business connection in India.

'Significant economic presence' means:

- any transaction in respect of any goods, services, or property carried out by a non-resident in India, including provision of download of data or software in India if the aggregate of payments arising from such transaction or transactions during the previous year exceeds the amount as may be prescribed, or
- systematic and continuous soliciting of its business activities or engaging in interaction with such number of users as may be prescribed in India through digital means.

However, only so much of income as is attributable to such transactions or activities shall be deemed to accrue or arise in India. It is also proposed that the transactions or activities shall constitute significant economic presence in India whether or not the non-resident has a residence or place of business in India or renders services in India.

Other taxes

Goods and services tax (GST)

The government of India took a landmark step and implemented the GST with effect from 1 July 2017. GST is an indirect tax, which is a transaction-based taxation regime.

For smooth GST implementation, the government has formed a GST Council. The Council consists of the State Finance Ministers representing their states. The GST Council provides recommendations to the government on various aspects of GST law, such as rate revisions and amendments in GST rules, etc.

Prior to GST, there were multiple indirect taxes leviable on various transactions at each stage separately by the Union Government and the states at varying rates. Such taxes included excise duty, service tax, value added tax (VAT)/central sales tax (CST), entertainment tax, luxury tax, lottery taxes, state cesses and surcharges, etc. All such taxes (except customs duty) have been subsumed under GST, and there is one single tax applicable on supply of goods and services. However, there are a few products that continue to be outside the ambit of GST, like petrol, diesel, aviation turbine fuel (ATF), natural gas, and crude oil.

GST regime

GST is a comprehensive 'consumption tax' levied on the supply of all goods and services. Indian GST is a dual model:

- Central GST (CGST), levied by the Central Government.
- State GST (SGST)/Union Territory GST (UTGST), levied by the State Government/ Union Territories.

In case of intra-state supply of goods and services, CGST+SGST/UTGST would become applicable, and in case of inter-state supply of goods and services, Integrated

GST (IGST) would become applicable. IGST is a sum of CGST and SGST/UTGST. The rate of GST varies from 5% to 28% depending upon the category of goods and services, the general rate of tax being 18%. Additionally, some categories of goods/services, like vehicles, aerated beverages, etc., notified by the government are subject to Compensation Cess under GST.

The threshold limit for the purpose of obtaining GST registration is INR 2 million aggregate turnover in a tax year (INR 1 million for some special category states, like the North Eastern states). For the purpose of the threshold, aggregate turnover shall be computed on an all India basis. For some specific categories of supplies and suppliers, the registration requirement is mandatory.

Similar to previous VAT laws, there is a concept of composition scheme under GST for small traders. Small traders having turnover of INR 10 million have an option to avail a composition scheme. Under the said scheme, GST at a lower rate (1% of the taxable turnover for manufacturers/traders and 5% in case of restaurants) would apply. The concept of composition scheme is not applicable for services, except restaurant services.

Import of goods and services

The import of goods under the GST regime will be subject to IGST and Compensation Cess (if applicable), along with Basic Custom Duty (BCD) and Social Welfare Surcharge (at 10% levied on the BCD). BCD and Social Welfare Surcharge paid at the time of imports are not available as credit under GST; consequently, they will always be a cost to the importer.

Similar to erstwhile service tax laws, on import of service, service recipient would be liable to pay IGST under reverse charge. Also, there are specified categories of goods and services notified by the government on which GST needs to be paid by the recipient under reverse charge.

Zero-rated supplies/Export of goods and services

Export of goods and services are zero rated under GST. Exporters can claim refund of input tax credit of inputs/input services used in export of goods/services, subject to fulfilment of prescribed conditions. Per GST laws, exporters will be provided provisional refund within seven days from the date of acknowledgement.

For claiming the zero rate on exports, there is a requirement to file a bond/Letter of Undertaking (LUT) to the jurisdictional tax authorities. Alternatively, the exporter can pay tax on output and claim refund of the same.

Also, the supplies to an SEZ for authorised operations have been made zero rated under GST. Unlike the erstwhile indirect tax regime, which involved a lot of paperwork for claiming export refund claims, a simplified online process for claiming refund of exports has been specified under GST. However, presently along with online refund application, documents need to be filed manually to claim refund claim.

To facilitate trade for small exporters, the concept of 'merchant exporter' has been introduced under GST. Accordingly, the merchant exporters will now have to pay nominal GST of 0.1% for procuring goods from domestic suppliers for export, subject to conditions specified in the notification.

Input tax credit

Per input tax credit provisions stipulated under GST law, a registered taxable person is eligible to claim input credit of such goods and services that are used or intended to be used in the course or furtherance of business. However, there is a specified list of goods and services mentioned below where credit will not be available under GST:

- Personal use of goods and services procured.
- Goods and services being used for effecting exempt supplies.
- Supply of the following goods and services:
  - Motor vehicles (credit available in certain cases where used for transportation business).
  - Food and beverages, outdoor catering, beauty treatment, health services, cosmetic and plastic surgery, except where such inward supply of goods or services of a particular category is used by a registered taxable person for making an outward taxable supply of the same category of goods or services.
  - Membership of a club, health, and fitness centre.
  - Rent-a-cab, life insurance, health insurance, except where the government notifies the services that are obligatory for an employer to provide to its employees under any law for the time being in force.
  - Travel benefits extended to employees on vacation, such as leave or home travel concession.
  - Works contract services when supplied for construction of immovable property, other than plant and machinery, except where it is an input service for further supply of works contract service.
  - Goods or services received by a taxable person for construction of an immovable property on one's own account, other than plant and machinery, even when used in the course or furtherance of business to the extend capitalised.
  - Goods lost, stolen, destroyed, written off, or disposed of by way of gift or free samples.

Under GST, taxpayers are allowed to take credit of taxes paid on inputs (input tax credit) and utilise the same for payment of output tax liability. However, no input tax credit on account of CGST can be utilised towards payment of SGST/UTGST and vice versa. The credit of IGST is permitted to be utilised for payment of IGST, CGST, and SGST/UTGST in that order. Also, it is pertinent to note that the credit pool is state-specific (i.e. IGST, CGST, and SGST of one state cannot be used to offset output of IGST, CGST, and SGST liability of another state).

Compliances

There are three monthly returns for a normal taxpayer under GST *viz.* GSTR 1 for output (to be filed by the tenth day of the succeeding month), GSTR 2 for input tax credit (by the 15th day of the succeeding month), and GSTR 3 a monthly tax return (by the 20th day of the succeeding month), and one annual return (by 31 December of the succeeding tax year). The government has also issued a requirement to file monthly GSTR 3B (to be filed by the 20th day of the succeeding month), and such monthly return needs to be filed till December 2018.

Further, filing of GSTR 2 and 3 continues to be suspended. Recently, in a GST Council meeting, a new return design has been proposed. The highlights of the new design structure has been mentioned in the ensuing paragraphs.

Latest update

Recently, in the 27th GST Council meeting, the GST Council has approved the revised design of GST returns. The GST Council has also decided to make GSTN a 100% government-owned company by buying out the shares. The major decisions taken by the GST Council are mentioned below:

- All taxpayers shall file one simplified monthly return with due dates being staggered based on the taxpayer's turnover.
- Composition dealers and dealers having nil transaction will have facility to file returns on a quarterly basis.
- On the matching principle of GST, the supplier will continue to be required to upload the invoices in the system. For all business-to-business (B2B) supplies, the Harmonised System of Nomenclature (HSN) at the four-digit level will need to be used. The invoices can be uploaded any time. The system will automatically calculate tax liability, based on the details of invoices.
- The input tax credit will also be calculated automatically by the system based on invoices uploaded by suppliers, and the buyer will not be required to upload any invoices for claiming credits.
- To incentivise digital payment, 2% concession in the GST rate on business-to-consumer (B2C) supplies is proposed if payment is made through cheque or digital mode, subject to a ceiling of INR 100 per transaction.

Customs duty

Customs duty is levied by the Central Government on goods imported into, and exported from, India. The rate of customs duty applicable to a product imported or exported depends upon its classification under the Customs Tariff Act, 1975. With regard to exports from India, customs duty is levied only on a very limited list of goods.

The Customs Tariff is aligned with the internationally recognised HSN provided by the World Customs Organisation (WCO).

Customs duty is levied on the transaction value of the imported or exported goods. According to section 14 of the Customs Act, 1962 (CA), the concept of transaction value is the sole basis for valuation for the purpose of import and export of goods. While the general principles adopted for valuation of goods in India are in conformity with the World Trade Organisation (WTO) agreement on customs valuation, the Central Government has framed independent Customs Valuation Rules that apply to the export and import of goods.

The customs duty applicable to any product is composed of a number of components, which are as follows:

- The import of goods under the GST regime will be subject to IGST and Compensation Cess (if applicable)
- BCD is the basic component of customs duty levied at the effective rate under the First Schedule to the Customs Tariff Act (CTA) and applied to the landed value of the goods (i.e. the cost, insurance, and freight [CIF] value of the goods). The peak rate of BCD is 10%.
- BCD and Social Welfare Surcharge (at 10% levied on the BCD). BCD and Social Welfare Surcharge paid at the time of imports are not available as credit under GST; consequently, they will always be a cost to the importer.

The duty incidence arising on account of the IGST may be set off or refunded, subject to prescribed conditions. Where goods are imported, the Indian supplier may take credit of the IGST paid at the time of import for offset against the output IGST, CGST, and SGST liability. Also, the Central Government provides exemption from payment of BCD and IGST on import of certain specified goods, subject to fulfilment of prescribed conditions. For example, goods imported for petroleum operations are exempt from BCD.

Recently, during April 2018, the Central Board of Indirect Taxes and Customs (CBIC) notified the Pre-Consultation Regulations under customs law. Under the said regulations, before issuance of notice, importer will be informed in writing along with grounds for the intention of issuing the notice. The importer, within 15 days, is expected to respond in writing, including the option to be heard in person. In absence of response within the time period specified, the officer will proceed with issuance of notice.

E-way bills

The e-way bill is an electronic bill that will be required for the movement of goods in case the value of the consignment is above INR 50,000. The movement of goods may be (i) in relation to supply, (ii) for reasons other than supply, or (iii) due to inward supply from unregistered persons.

The bill can be generated from the GSTN portal, and every GST-registered taxpayer is required to comply with the requirement to issue an e-way bill.

Recently, with effect from 1 April 2018, the Central Government has notified the requirement to generate an e-way bill for inter-state goods movement. For intra-state goods movement, the government has provided that the e-way bill system will be introduced with effect from a date to be announced in a phased manner, but not later than 1 June 2018.

However, majority states like Maharashtra, Assam, Madhya Pradesh, and Himachal Pradesh, etc. have already started issuing notifications for issuance of an e-way bill for intra-state goods movement.

Advance rulings for customs and GST

To enable foreign investors to ascertain their indirect tax liabilities arising from proposed business ventures in India, the Central Government has constituted the Authority for Advance Rulings (AAR) as a high-level, quasi-judicial body. The functions of the AAR consist of giving advance rulings on a specific set of facts relating to specified matters under customs and GST.

Advance rulings may be sought by any resident/non-resident investor entering into a joint venture in India in collaboration with another non-resident or resident of India, or by a resident setting up a joint venture in India in collaboration with a non-resident. Through the Finance Act, 2005, this facility has also been made available to existing joint ventures in India. The Central Government is also empowered to include any other class or category of persons as eligible for the benefit of an advance ruling. Under the customs law, the Central Government has allowed a 'resident public limited company' to be eligible for an advance ruling. Under the erstwhile excise and service tax regime, advance rulings could be given only on a proposed transaction, whereas under GST, advance rulings can be obtained on a proposed transaction as well as a transaction being undertaken by the appellant.

In terms of GST provisions, the following matters/questions specified can be sought before the AAR:

- Classification of any goods or services, or both.
- Applicability of a notification issued under the provisions of the CGST Act.
- Determination of time and value of supply of goods or services, or both.
- Admissibility of input tax credit of tax paid or deemed to have been paid.
- Determination of the liability to pay tax on any goods or services, or both.
- Whether applicant is required to be registered.
- Whether any particular thing done by the applicant with respect to any goods or services, or both, amounts to or results in a supply of goods or services, or both, within the meaning of that term.

The comprehensive provision for advance rulings is provided under GST to ensure that disputes are minimal. Timelines are also given within which the ruling is to be given by the concerned authority. The aim is to provide certainty to the taxpayer with respect to one's obligations under the GST Act and an expeditious ruling, so that the relationship between the taxpayer and administration is smooth and transparent and avoids unnecessary litigation.

Property taxes

Property tax is levied by the governing authority of the jurisdiction in which the property is located. The rate of tax levied varies from city to city in India, and is generally related to the prevailing market prices for property in each locality.

Stamp duties

Stamp duty is a government tax that is levied on all legal property transactions. Stamp duty is a tax that is paid as evidence for any purchase or sale of a property between two or more parties. Stamp papers, which are bought either in the name of the buyer or seller, are valid for six months, provided the stamp duty is paid without any delay. No document that has not been duly stamped can be introduced as evidence in any court proceedings. Stamp duty is charged at both central and state levels. State level stamp duties vary from state to state, and on the document type. Stamp duty should be paid in full without any delay, failing which, a penalty is levied. Stamp duty has to be paid prior to execution (signature by an individual's party) of a given document, the next day, or on the day of document execution. Stamp duty is paid by a buyer in most cases. However, both the seller and the buyer have to bear the burden of stamp duty for property exchange cases. Stamp duty rates differ in various states across the country, as stamp duty in India is a state subject. However, the Central Government fixes the stamp duty rates of specific instruments.

Dividend distribution tax (DDT)

Indian companies distributing or declaring dividends are liable to pay DDT at 15% (*plus* surcharge [12%] and health and education cess [4%]). This rate is required to be grossed up; consequently, the effective rate of DDT is 20.56%. This tax is payable on declaration, distribution, or payment, whichever is earlier, and it is in addition to the CIT payable on business profits.

Further, the Finance Act, 2018 has introduced the levy of DDT on companies (not being a company in which the public are substantially interested) for making payment of:

- any sum by way of advance or loan to a shareholder who is the beneficial owner of shares holding not less than 10% of the voting power
- any sum by way of advance or loan to any concern in which such shareholder is a member or a partner and in which one has a substantial interest, or
- any sum by any such company on behalf, or for the individual benefit, of any such shareholder.

In those cases, the advance or loan or the sum of money will be treated as deemed dividend and on which 30% DDT (without gross up) shall be payable. The effective tax rate, including surcharge at 12% and health and education cess at 4%, is 34.944%.

Dividend income on which DDT is paid by the Indian company is exempt from tax in the hands of the recipient. However, non-corporate resident taxpayers earning more than INR 1 million of dividend are to pay tax at 10% (*plus* applicable surcharge and education cess) on the dividend income earned over and above INR 1 million in addition to the DDT paid by the company. However, the 'dividend income' in this paragraph does not include the 'deemed dividend income' as mentioned in the preceding paragraph.

A holding company does not have to pay DDT on dividends paid to its shareholders to the extent that it has received dividends from its Indian or foreign subsidiary company on which DDT has been paid by the respective subsidiary, subject to fulfilment of certain conditions.

Further, no tax will be chargeable/payable by a company located in an International Financial Service Centre, deriving income solely in convertible foreign exchange on profits distributed from the total profits, for any tax year on any amount declared, distributed, or paid by such company, by way of dividends (whether interim or otherwise) on or after 1 April 2017 out of its current income, either in the hands of the company or person receiving such dividend.

Securities transaction tax (STT)

STT is applicable to transactions involving the purchase/sale of equity shares, derivatives, units of equity-oriented funds through a recognised stock exchange, or the purchase/sale of a unit of an equity-oriented fund to any mutual fund. The STT leviable in respect of such transactions varies for each kind of instrument, whether delivery based or non-delivery based. Rate of STT varies from 0.001% to 0.125%, depending upon the nature of securities. However, securities transacted by any person on a recognised stock exchange located in an International Financial Services Centre where the consideration for such transaction is paid or payable in foreign currency are not subject to STT.

Payroll taxes and social security payments

Contributions representing 8.33% of the employees' pay needs to be remitted by the employer to the Employees' Pension Fund in respect of all Indian nationals working in an establishment covered under the Employees' Provident Fund and Miscellaneous Provisions Act, 1952, within 15 days of the close of every month. A 'foreign worker' holding a passport of a country with which India has signed a social security agreement is required to contribute to the social security system 12% of one's salary. A similar

12% of salary is contributed by resident employees' for the Employees' Provident Fund and Employees' Pension Fund. However, foreign workers can detach themselves from the scheme under a special provision on obtaining a 'detachment/coverage certificate' issued by an appropriate social security institution indicating the period of employment in India being less than the maximum period of detachment agreed in the agreement.

Branch income

Branches of foreign companies are taxed on income that is received in India, or which accrues or arises in India, at the rates applicable to foreign companies. There is no withholding tax (WHT) on remittance of profits by the branch to its head office.

Income determination

Income computation and disclosure standards (ICDS)

The CBDT has notified ten ICDS to be followed by all taxpayers that follow the mercantile system of accounting for the purpose of computation of income chargeable to income tax under the head 'profits and gains of business or profession' or 'income from other sources' and not for the purpose of maintenance of books of accounts. In case of conflict between the provisions of the Indian Income Tax Act and the ICDS, the provisions of the Act shall prevail to that extent. These standards have been implemented from tax year 2016/17.

The list of certain important points on implementation of ICDS is given below:

- Inventory has to be valued at lower of cost or net realisable value. Further, cost of inventory is to include taxes paid, irrespective of recoverable or not.
- Interest on compensation or enhanced compensation is to be offered to tax in the year of receipt.
- Any subsidy or grant received from the government, which is not adjusted to cost of asset, shall be offered to tax in year of receipt of such subsidy/grant even if the conditions attached to it are not yet fulfilled.
- Marked-to-market loss computed in accordance with ICDS shall only be allowed.
- Gain/loss on account of foreign currency fluctuation for monetary and non-monetary items shall be computed and allowed as per provisions of ICDS.
- Profits from construction contracts and/or service contracts shall be calculated based on the percentage of completion method. For service contracts with less than a 90-days period, the project completion method can be used. Further, for service contracts with indeterminate number of acts over a specific period of time, the straight-line method can be used. Retention money shall be included while computing contract revenue.
- It may be noted that ICDS does not recognise the concept of materiality and the concept of prudence.

Inventory valuation

Inventories are generally valued at cost or net realisable value, whichever is lower. Generally, there is conformity between book and tax reporting. The first in first out (FIFO) and weighted average cost methods are acceptable, provided that they are consistently applied.

Capital gains

Capital gains refer to the gains made on the transfer of a capital asset. Transfer includes sale, exchange, relinquishment, or extinguishment of rights in an asset. Capital assets are either short-term capital assets or long-term capital assets. Long-term capital gains are eligible for a concessional rate of tax and indexation of cost of purchase and cost of improvement (*discussed below*).

Short-term capital assets are capital assets held for a period of not more than 36 months. In case of listed shares, listed securities, or units of specified mutual funds or zero-coupon bonds, the short-term holding period is not more than 12 months, and in case of unlisted shares is not more than 24 months. Capital assets that do not qualify as short-term capital assets are considered as long-term capital assets.

Normally, long-term capital gains are determined after increasing the cost by a prescribed multiplier that varies with the period of holding, to adjust for inflation. In case of non-residents, capital gains on transfer of shares or debentures in Indian companies are computed in the foreign currency in which the shares or debentures were acquired, and the capital gains are then reconverted into Indian currency to compute the tax liability thereon.

Capital gains are taxed as follows:

- Long-term capital gains on the transfer of equity shares in a company acquired on or after 1 October 2004 shall be exempted only if STT was paid at the time of acquisition. This exemption stands withdrawn from 1 April 2018. Post such withdrawal, the long-term capital gains exceeding INR 100,000 will be taxed at the rate of 10% (plus surcharge and health and education cess). The said amendment will be applicable to units of equity oriented funds as well. The benefit of adjustment of cost of inflation index will not be available. In addition, the benefit of computation of long-term capital gains in foreign currency in the case of a non-resident will not be allowed.
- Other long-term capital gains are subject to taxation at 20% (plus the surcharge and health and education cess). However, long-term capital gains arising from the transfer of listed securities, units, or zero-coupon bonds on which STT is not paid are taxed at 10% (without adjusting the cost for inflation) or at 20% (after adjusting the cost for inflation), whichever is more beneficial to the taxpayer. These rates exclude surcharge and health and education cess.
- Long-term capital gains arising to a non-resident (not being a company) or a foreign company from transfer of unlisted securities, shares, debentures, etc. are taxable at 10% (plus surcharge and health and education cess) without any indexation benefit.
- Short-term capital gains on the transfer of listed shares in a company or units of an equity-oriented fund that are subject to STT are taxed at 15% (plus surcharge and health and education cess).
- Other short-term capital gains are subject to taxation at the normal rates.
- In the case of certain overseas financial organisations (e.g. off-shore funds and foreign institutional investors), long-term capital gains arising on the transfer of units purchased in foreign currency are taxable at 10% (plus surcharge and health and education cess) on the gross amount.
- Transfer of rupee-denominated bonds (issued by an Indian company outside India) held by a non-resident to another non-resident will be exempt from long-term capital gains. Further, the benefit of excluding the forex appreciation of rupee-denominated bonds in the capital gains computation at the time of redemption will

also be extended to secondary holders of such bonds. This is effective from tax year 2018/19 onwards.
- The indexation benefit is available on cost of acquisition and cost of improvement for assets classified as long-term while computing capital gains. The taxpayer shall have the option to consider the fair market value of the asset on 1 April 2001 as the cost of acquisition where date of acquisition is before 1 April 2001. This is effective from the tax year 2018/19.

The rules of carryforward and set off of loss for capital gains are as follows:

- Capital losses arising from the transfer of a short-term capital asset can be set off against capital gains arising from any other asset in the same tax year.
- Capital losses arising from the transfer of a long-term capital asset can be set off only against capital gains arising from the transfer of any other long-term capital asset.
- Capital losses that cannot be set off in the tax year in which they are incurred can be carried forward and set off against future capital gains at any time within a period of eight years after the year of loss.
- When depreciable assets forming part of a block of assets for tax purposes are transferred, as a result of which the value of the block becomes negative, or all the assets forming part of the block cease to exist, the difference between the transfer price and the value of the block is treated as short-term capital gain or loss.

Taxability of shares issued at a price less than fair market value of shares

Where a closely held unlisted company receives any consideration from a resident towards issue of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value will be deemed to be the income of the recipient-company. The 'fair market value' is computed according to the formulas per the prescribed mechanism. Further, the said provision has been amended and, accordingly, the scope has been widened. From tax year 2018/19, entities are liable to pay taxes on the following receipt that they have received without consideration or for a consideration that is less than the fair market value:

- Any sum of money.
- Any immovable property being land or building, or both.
- Any property, other than immovable property, being shares and securities, jewellery, archaeological collections, drawings, paintings, sculptures, any work of art, and bullion.

Taxability of transfer of property for nil or inadequate consideration

Where a person is in receipt of the following property for nil consideration or for an inadequate consideration, then the difference between the fair value of the property and the consideration paid shall be considered as deemed income in the hands of recipient of the property:

- Any sum of money.
- Any immovable property being land or building, or both.
- Any property, other than immovable property, being shares and securities, jewellery, archaeological collections, drawings, paintings, sculptures, any work of art, and bullion.

In a case where the difference between the fair value of property and consideration paid does not exceed INR 50,000, the same shall be ignored from this taxation. However, the Finance Act, 2018 has liberalised the limit of INR 50,000 in case of immovable property. It is now provided that no adjustments shall be made in a cases where the variation between stamp duty value and the sale consideration is not more than 5% of the sale consideration.

Dividend income

Dividend income received from Indian companies is not taxable in the hands of all shareholders. This applies to resident as well as non-resident shareholders. However, tax is payable at the rate of 10% on income earned by way of dividend in excess of INR 1 million by a taxpayer resident in India other than domestic companies and certain funds, trusts, and institutions. This tax is in addition to the tax payable by a company on dividend distribution.

Income received by overseas financial organisations (offshore funds) from units of specified mutual funds, or from the Unit Trust of India, that are purchased in foreign currency is taxable at 10% on the gross amount of income. Any income distributed by a mutual fund being an equity-oriented fund, the mutual fund shall be liable to pay additional income tax at 10% on the income so distributed. Dividends received from a foreign subsidiary company in which the Indian company holds 26% or more in the nominal value of the equity share capital, then the applicable tax rate would be 15% of the gross amount of the dividend.

Income received from units of specified mutual funds is not taxable in the hands of the recipient. The distributing mutual fund is liable to pay a distribution tax of 25% or 30% (plus surcharge and health and education cess at applicable rates). The above tax is not chargeable in respect of income distributed by an equity-oriented fund in respect of distribution under such scheme.

Stock dividends (bonus shares) distributed are not taxed at the time of receipt in the hands of the recipient shareholders, but capital gains provisions are applicable to the sale of these stock dividends.

Buyback of shares

An additional tax is payable on transactions involving buyback of shares by unlisted companies from its shareholders. A tax at 20% is payable by the company on the difference of consideration paid on buyback and the issue price of shares. The CBDT has prescribed the methodology for determination of amount received for issue of shares under 12 different situations, being a subject matter of tax on buyback. The buyback consideration received will be tax exempt in the hands of the receiver. No tax credit will be allowed in case of such taxes paid either to the company or to the shareholder.

Interest income

Interest income received by an Indian company is taxable at normal CIT rates. Interest income received by a foreign company is taxed at a concessional rate of withholding at 5%/20%, subject to conditions.

Royalty income

The domestic tax law defines the term ‘royalty’ to include consideration from the transfer of all or any rights (including the granting of a licence), imparting of any information, or use or right to use of any right in respect of a patent, invention, model, design, secret formula or process, trademark, or similar property. The definition also includes imparting of any information concerning technical, industrial, commercial, or scientific knowledge, experience, or skill; use or right to use any industrial, commercial, or scientific equipment; the transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic, or scientific work, including films or video tapes for use in connection with television, or tapes for use in connection with radio broadcasting, but not including consideration for the sale, distribution, or exhibition of cinematographic films; or rendering of any services in connection thereto.

Royalty income received by a non-resident taxpayer is taxed at 10%, 15%, or 20% (subject to treaty benefits and furnishing of prescribed documentation). Surcharge and health and education cess as applicable will be levied in addition to the basic tax rates mentioned above. However, surcharge and health and education cess would not apply on the tax rate specified in the tax treaties.

Partnership/LLP income

A partnership firm and an LLP are taxed as separate legal entities. The share of income of partners from a partnership firm or an LLP is exempt from tax. Partnerships and LLPs are taxed at 31.2% (inclusive of surcharge and health and education cess) if the income is less than INR 10 million and 34.944% (inclusive of surcharge and health and education cess) if the income exceeds INR 10 million.

The interest payment to partners on capital or current account is allowed as tax-deductible expenditure. However, the maximum interest rate allowable for tax purposes is 12% *per annum*. A working partner can be paid salary, bonus, commission, or remuneration. The maximum permissible deduction in respect of remuneration payable collectively to all working partners is based on the book profit of the firm, at slab rates for different levels of book profit.

Unrealised exchange gains/losses

Principles for classification of foreign exchange gains or losses (post amendments made by the Finance Act, 2018) are as follows:

- Unrealised foreign exchange profit/loss is considered to be of a capital nature if a foreign currency loan is taken for a capital asset or fixed asset purchased outside India.
- Any other unrealised foreign exchange profit/loss (not covered above) is considered as revenue in nature.

Foreign income

An Indian company is taxed on its worldwide income. A foreign company is taxed only on income that is received in India, or that accrues or arises, or is deemed to accrue or arise, in India. This income is subject to any favourable tax treaty provisions. According to the current tax law, payments for allowing/transferring the right to use software, customised data, or transmission of any signal by satellite, cable, optic fibre, or similar technology are taxable as royalty income deemed to accrue or arise in India, whether or not the location of such right or property is in India. The CBDT has notified the rules for granting foreign tax credit to resident taxpayers in respect of taxes paid in overseas countries. The rules lay down broad principles and conditions for computation and claim of foreign tax credit, respectively. In cases where the taxpayer has not been given credit of certain taxes paid outside India since the tax was under dispute, the taxpayer can approach the tax officer within six months from the end of the month in which the dispute was settled with prescribed documents. The tax officer has been empowered to pass an order granting consequential relief. This has been made effective from tax year 2018/19 onwards.

Double taxation of foreign income for residents is avoided through treaties that generally provide for the deduction of the lower of foreign tax or Indian tax on the doubly taxed income from tax payable in India. Similar relief is allowed unilaterally where no treaty exists, in which case a resident would be taxed under the Indian tax law but would be allowed a deduction from the Indian income tax payable of a sum being the lower of the Indian tax rate on the doubly taxed income or the rate of tax prevailing in the other country in which income is already taxed.

Deductions

Expenses that are revenue in nature are, by and large, allowed as a deduction to businesses and professionals if they are:

- incurred wholly and exclusively for the purpose of the business or profession
- not in the nature of a personal expense, and
- not in the nature of a capital expense.

Depreciation

Depreciable assets are grouped in blocks, and each block is eligible for depreciation at a prescribed rate. The CBDT has issued a notification clarifying that with effect from 1 April 2017 the block of assets that are entitled to more than 40% depreciation shall now be restricted to 40%. Hence, the depreciation available in case of different block of assets ranges from 0% to 40% as summarised below:

Block	Rate (%)
Residential building	5
Office building	10
Furniture and fittings	10
Plant and machinery	15 to 40
Computers	40
Intangible assets	25

Where the asset is used for less than 180 days in a tax year, the depreciation is restricted to 50% of the prescribed rate. If money receivable on the transfer of a depreciable asset exceeds the opening written-down value plus cost of acquisitions of assets falling within the block concerned, the excess is taxed as a short-term capital gain at the same tax rate as that applicable to business income.

Additional depreciation of 20% is allowed on the cost of new plant and machinery (other than ships or aircraft) acquired and installed to companies engaged in the business of manufacture of articles or things. This benefit is extended to power generating, transmission, or distributing business. Also, the benefit of initial depreciation to companies engaged in transmission of power is available. Power-generating or power-distributing companies have the option to either apply the reducing-balance method provided under the normal schedule or to charge depreciation on a straight-line basis. The straight-line rates are aligned with power companies' book depreciation rates.

Know-how, patents, licences, franchises, and similar intangible assets can form part of a block of depreciable assets, provided they are owned and put to use in the course of their business and are eligible for depreciation at the prescribed rate, which is 25%.

Additional depreciation of 35% (as against the current rate of 20%) has been made available on new plant and machinery acquired and installed between 1 April 2015 and 31 March 2020, in the year of installation in the states of Andhra Pradesh, Bihar, Telangana, and West Bengal. In line with the existing provisions, such incentive is not available to specified assets (e.g. office appliances, computer software).

Tax depreciation is not required to conform to book depreciation. However, an Accounting Standard mandates companies to reconcile both and provide for deferred tax assets, liabilities, expenses, and incomes.

Investment allowance

An investment allowance benefit is allowed for companies engaged in the business of manufacture of articles or things. Taxpayers who have acquired and installed new plant and machinery (other than a ship or aircraft) on or after 1 April 2015 but before 1 April 2020 in the states of Andhra Pradesh, Bihar, Telengana, and West Bengal can avail of an allowance of 15% of the actual cost of investment made in plant and machinery. Further, the acquisition of the plant and machinery can be made in any tax year.

In case installation of the new asset is in a year other than the year of acquisition, then the investment allowance shall be allowed in the year in which the new asset is actually installed. The assets have to be held for more than five years, and, if the asset is sold before this period, the investment benefit claimed will be reversed in the year of sale.

Investment in new plant and machinery will not include assets like plant or machinery used earlier in or outside India, any plant or machinery installed in any office premises or in residential accommodation (or guest house), any office appliances (including computers or computer software), vehicle, ship, or aircraft, the cost of which has been allowed as a deduction under any other provision.

Goodwill

Goodwill and commercial brand equity that are acquired in the course of amalgamation are intangible assets entitled to depreciation. The amalgamated/ demerged company and the resulting company shall not be entitled to claim deduction for depreciation exceeding the amount calculated in any previous year. The deduction shall be apportioned between the amalgamating/demerging company and the amalgamated/demerged company in the ratio of the number of days for which the assets were used by them during any tax year. However, the issue of whether goodwill is eligible for tax depreciation or not is the subject of litigation, and there are divergent views of courts on this.

Start-up expenses

Certain expenses are incurred by taxpayers either before the start-up of a business or after start-up of a business, in connection with extension of the industrial undertaking, or in connection with setting-up a new unit. One-fifth of such expenditure is allowed as a deduction each year, over a period of five years.

Tax framework for start-ups in India

With a view to providing an impetus to start-ups and to facilitate their growth in the initial phase of their business, a deduction of 100% of the profits and gains derived by an eligible start-up from a business involving innovation development, improvement of products, processes, or services, or a scalable business model with a high potential of employment generation or wealth creation will be available.

The benefit of 100% deduction of the profits derived from such business shall be available for a period of three consecutive years out of seven years beginning from the year the start-up is incorporated.

Eligible start-up companies can carry forward losses and set off against income of the previous year only if all the shareholders holding shares in the prior year in which such loss was incurred continued to hold those shares in the year of the set off as well. Further, only the losses incurred during the period of seven years beginning from the year in which such company was incorporated may be used for set off.

'Eligible start-up' means a company or an LLP engaged in the business mentioned above and which fulfils the following conditions, namely:

- it is incorporated on or after 1 April 2016 but before 1 April 2021
- the total turnover of its business does not exceed INR 250 million in any tax year(s) prior to which the deduction was claimed, and
- it holds a certificate of eligible business from the Inter-Ministerial Board of Certification as notified in the Official Gazette by the Central Government.

Reduced rate of tax for newly set-up companies

To provide relief to newly set-up Indian companies, a beneficial CIT rate of 25% (plus applicable surcharge and health and education cess) has been announced with effect from tax year 2016/17. This beneficial rate is at the option of the company and is applicable on satisfaction of the following conditions, cumulatively:

i. The company is registered and set up on or after 1 March 2016.
ii. The company is engaged in any business other than the business of manufacture or production of any article or thing and research or distribution of such article or thing manufactured or produced.
iii. The company has not claimed a benefit for establishing its unit in an SEZ, benefit of accelerated depreciation, or benefit of additional depreciation, investment allowances, expenditure on scientific research, and any deduction in respect of certain income.
iv. The company has not claimed set off of loss carried forward from any earlier years following the tax years, provided such loss is attributable to the deductions referred to in (iii) above.
v. The option of seeking the benefit of a reduced CIT rate of 25% is furnished in the prescribed manner before the due date of furnishing of income.

For companies other than Indian companies, the rate of CIT (plus applicable surcharge and education cess) shall remain unchanged.

Interest expenses

Any interest paid by a taxpayer on capital borrowed for the purposes of the taxpayer's business or profession is tax-deductible without any limit. However, if such interest is paid to certain related persons, then the interest expense will be restricted to 30% of earnings before interest, taxes, depreciation, and amortisation (EBITDA). Excess interest expenditure disallowed in that year can be carried forward for eight years and would be available for set-off. If the capital is borrowed for acquiring a capital asset, then interest liability pertaining to the period until the time the asset is put to use cannot be allowed as a tax-deductible expense and will have to be added to the cost of such asset. *See Expenses allowable on actual payment basis below*.

There are some specific guidelines for interest deduction being prescribed in ICDS.

Bad debts

The amount of any bad debt, or part thereof, that has been written off as irrecoverable in the accounts of the taxpayer for the year is allowed as a tax-deductible write-off. If any part of the sum written off is subsequently recovered, the recovered sum is taxable in the year of recovery.

Charitable contributions

Any charitable contribution made by a company to any charity is allowed as a tax-deductible expense, subject to certain conditions. The tax deductibility ranges from 50% to 100% of the charitable contribution, depending upon the nature of charity.

Expenditure incurred on corporate social responsibility (CSR) activities

Expenditure incurred by a taxpayer on CSR activities mandated under the Companies Act, 2013 is not allowed as a deduction for tax purposes under the Income Tax Act. However, if contributions are made to any charitable institutions, then deduction may be claimed from the total income, subject to conditions. *See charitable contributions above.*

Expenses allowable on actual payment basis

Certain expenses, such as, but not limited to, employees' provident fund dues (i.e. retirement benefit funds), bonus to employees, and interest payable to financial institutions and banks, are allowed as tax-deductible expenses only on actual payment. Tax disallowances are attracted if certain payments are delayed beyond their due dates under the respective laws.

Bribes, kickbacks, illegal payments

Expenditure incurred by a taxpayer that is illegal is deemed not to have been incurred for the purposes of the business or profession, and no deduction of such expenditure will be allowed.

Fines and penalties

Under the tax law, there are various procedural compliances (*viz.*, audit of books of accounts, submission of tax returns, disclosure of particulars of income, etc.) that need to be complied with by taxpayers by the respective due dates prescribed therein. Non-compliance/delayed compliances of these procedures attract interest and penal consequences. There are prosecution provisions as well for certain offences. Penalties and fines paid for infraction of, or non-compliance with, any law are not deductible as business expenditure. Prosecution proceedings are criminal proceedings, and, in such proceedings, courts presume a culpable mental state on the taxpayer's part. The burden of proving beyond all reasonable doubt (and not merely by preponderance of probability) the absence of such a state is on the taxpayer. Prosecution shall lie against companies that fail to file their return, whether or not tax is payable.

Further, a penalty of INR 10,000 on specified persons (i.e. accountants, registered valuers, or merchant valuers) for furnishing incorrect information in any report or certificate furnished by them under any provision of the Act or the Rules. The aforesaid penalty will not be imposable if there is reasonable cause for failure. Further, a new provision has been included to levy a penalty of INR 5,000 where the taxpayer has filed one's return of income after the due date but on or before the 31st day of December of the tax year and INR 10,000 where the taxpayer has filed one's return of income after the 31st day of December or has not filed one's return of income. Failure to furnish statement of financial transaction or reportable account within the prescribed time is liable to pay a penalty of INR 500 for each day of continuing default. Further, INR 1,000 shall be charged for each day of continuing default in case of failure to furnish statement of financial transaction or reportable account within the period specified in the notice issued by the revenue authority.

Taxes

All taxes (tax, duty, cess, or fees by whatever name called) relating to business (other than income tax) incurred during the tax year are usually deductible only in the year of payment.

Net operating losses

Losses can be carried forward and set off against income from subsequent year(s) for periods set out in the following table:

Types of losses	Time limit
Unabsorbed depreciation	Perpetually
Business losses (other than speculation business losses)	8 years
Speculation business losses	4 years
Capital losses	8 years

There are no provisions in India for carrying losses back to earlier years.

Payments to foreign affiliates

Indian companies can claim deduction for payments on account of royalties, and for interest and fees for technical or management service provided by foreign affiliates, as long as they are not capital in nature. Such payments are deductible in the year the requisite WHT is paid into the government treasury.

Group taxation

Group taxation is not permitted under the Indian tax law.

Transfer pricing

Transfer pricing on international transactions

The Indian transfer pricing regulations (ITPR) stipulate that income arising from 'international transactions' between 'associated enterprises' should be computed having regard to the 'arm's-length price'. Furthermore, any allowance for expenses or interest arising from any international transaction is also to be determined having regard to the arm's-length price. The expressions 'international transactions' and 'associated enterprises' have been defined in the ITPR.

The ITPR also contain the concept of 'deemed international transaction' whereby a transaction between an enterprise and a third party (whether based in India or overseas) would be subjected to transfer pricing regulations in case there exists a prior agreement in relation to such a transaction between the third party and the associated enterprise of the transacting enterprise or if the terms of such a transaction are determined in substance between the third party and the associated enterprise of the transacting enterprise.

The ITPR also define a certain class of transactions undertaken by a taxpayer with its domestic related parties and whose aggregate value exceeds INR 200 million as specified domestic transactions to which the transfer pricing provisions apply.

Initially, the ITPR prescribed five methods for computation of arm's-length price. These are broadly in line with OECD Guidelines. A sixth method, termed as the 'other method', was notified in 2012. Taxpayers are required to adopt the most appropriate method for determining the arm's-length price.

Taxpayers are also required to maintain a comprehensive set of prescribed information and documents relating to international transactions and specified domestic transactions that are undertaken between associated enterprises, on an annual basis, within the prescribed timelines (due date of filing the income tax return). Taxpayers being a constituent entity of an international group shall also keep and maintain such information and documents (essentially master file and country-by-country [CbC] report) in respect of the international group. Further, taxpayers are required to obtain an Accountant's Report from an independent accountant certifying the nature and amount of international transactions. The certificate needs to be filed along with the income tax return. The burden of proving the arm's-length character of the transaction is primarily on the taxpayer.

The taxpayer is required to comply with the above requirements on an annual basis.

The ITPR adopt an arithmetic mean of comparable prices as the arm's-length price, with a flexibility of deviation from the percentage that is notified by the Central Government as +/- 1% for wholesalers and +/- 3% for others. The CBDT has also prescribed rules for use of range for determining arm's-length price, which is discussed subsequently. Where the transfer pricing officer is of the opinion that the arm's-length price was not applied, the officer may re-compute the taxable income after giving the taxpayer an opportunity to be heard. Stringent penalties are prescribed in cases of failure to comply with the provisions of the ITPR.

Notified Jurisdictional Area (NJA)

The Indian government is empowered to declare a country/territory with which there does not exist an effective mechanism for exchange of information as an NJA.

Any transaction between a taxpayer and a person located in an NJA or a transaction entered into by a taxpayer wherein one of the parties is located in an NJA will be covered under the ITPR. However, the benefit of the +/- 3% range and the option to be covered under the Safe Harbour Rules would not be available in this case.

Safe Harbour Rules

Safe Harbour Rules were notified in 2013. These rules prescribe who the eligible taxpayers are, which are the eligible international transactions, the target operating margin, procedural aspects, timeline for audit, etc. Thereafter, these Safe Harbour Rules were also extended to certain domestic transactions.

The Safe Harbour Rules were initially applicable for a maximum of five tax years beginning with tax year 2013/14.

Thereafter, in June 2017, the CBDT made amendments to the Safe Harbour Rules reducing the target operating margins for most of the eligible international transactions. Further, the revised Safe Harbour Rules introduced receipt of low value-adding intra-group services to the list of eligible transactions subject to certain thresholds. Also, there were certain modifications made to the definitions of certain terms *vis-à-vis* in the original Safe Harbour Rules. The revised Safe Harbour Rules are applicable for a maximum of three tax years beginning with tax year 2017/18 with the taxpayers having an option to apply the original Safe Harbour Rules or the revised Safe Harbour Rules for the tax year 2017/18, whichever is more beneficial.

Where a taxpayer has opted to be covered under the Safe Harbour Rules and the transfer price declared has been accepted by the tax authorities, then such a taxpayer cannot invoke proceedings under a Mutual Agreement Procedure (MAP).

Advance pricing agreements (APAs)

An APA is an arrangement between the taxpayer and the tax authorities covering transactions, with a view to pre-empt potential transfer pricing disputes. The CBDT has notified detailed rules providing the procedures and necessary forms for application/ administration of APAs.

The rules provide for constitution of an APA team, which shall consist of an income tax authority and experts from economics, statistics, law, and other necessary fields. APAs can be applied to existing, as well as proposed, transactions.

The rules have provided for both unilateral and bilateral/multilateral APAs. In cases where a bilateral APA negotiated between competent authorities is not acceptable to the taxpayer, the taxpayer may, at its option, continue with the process of entering into a unilateral APA without benefit of an MAP.

The salient features of the procedure laid down for APAs are application for APA, withdrawal of APA, defective application, procedure, compliances post-APA, cancellations of APA, and revisions and renewal of APA.

The legislation has provisions of roll-back of APAs for four years prior to the first year covered under the APA.

Rules prescribing the use of 'range' and multiple year data

The CBDT has notified the rules prescribing the scheme for the usage of the 'range' concept and multiple year financial data for determining the arm's-length price. These rules are applicable to international transactions and specified domestic transactions.

The rules envisage the applicability of the 'range' concept and multiple year data only where the arm's-length price determination is done using either the transactional net margin method, resale price method, cost plus method, or comparable uncontrolled price method. Furthermore, the rules in connection with the applicability of the 'range' concept, *inter alia*, prescribe the adequate number of external comparables and the methodology for computing the upper and lower percentile. In case the number of external comparables identified is not adequate, the 'range' concept will not apply and the concept of arithmetic mean will continue to apply.

The multiple year data can only be used if the most appropriate method selected of benchmarking purposes is either transactional net margin method, resale price method, or cost plus method. Further, multiple year data entails use of data for the year under consideration (current year) and data for up to two preceding tax years. Data for the current year is compulsorily to be considered. If the data for the current year is available and is not comparable on account of either qualitative or quantile reasons, the comparable cannot be considered.

Master file and country-by-country (CbC) reporting documentation as per BEPS

The government has introduced three-layered transfer pricing documentation requirements in line with the international standard as per the BEPS Action Plan 13. Taxpayers are required to prepare a master file, local file, and CbC report from tax year 2016/17. The CBDT has notified the final rules for maintaining and furnishing of transfer pricing documentation in the master file and CbC report.

As per the rules, the master file shall be applicable to every Indian taxpayer (called as a constituent entity or CE) part of an international group (whether inbound or outbound) having an annual consolidated turnover of over INR 5 billion in the preceding accounting year of the parent company and meeting certain other thresholds of the quantum of aggregate value of international transactions. Again, the Indian taxpayer must furnish the master file with the prescribed authority (Director General of Income Tax [Risk Assessment]). For Indian subsidiaries with parent companies resident outside India, the master file must be furnished even if it is filed by the parent entity in its home country or by a designated entity in its home country. The documentation prescribed by the rules in respect of the master file is largely in line with OECD's final BEPS Action Plan 13 report; however, there are certain additional information requirements, like the description of the functions, assets, and risks (FAR) analysis of all CEs within the group that contribute at least 10% of revenues or assets or profits of the group; detailed description of the financial arrangements of the group, including the names and address of the top ten unrelated lenders; and a list of all entities of the international group engaged in development and management of intangible property, along with their addresses.

The CbC report is applicable only for taxpayers having an annual consolidated group turnover of over INR 55 billion in the preceding accounting year of the parent company. A parent entity of an outbound international group or an alternate reporting entity of an inbound international group, resident in India, must file the CbC report with the prescribed authority. For Indian subsidiaries with parent companies resident outside India, the CbC report must ordinarily be filed by the parent entity in its home country or by an alternate reporting entity/a designated entity in its home country. The Indian tax authorities will access the CbC report through mutual exchange of information agreements with such country, failing which the Indian subsidiary will be required to furnish the report. However, if the parent entity is not obligated to file the CbC report in its home country or if there is no mutual exchange of information agreement signed between India and the parent entity's country or territory, then the Indian subsidiary will be required to furnish the report.

In case there are multiple entities of the same international group resident in India, one of the entities will have to be identified as the designated entity for filing the master file as well as for other communication in respect of the master file and the CbC report. Further, the rules have prescribed various forms for intimations to be filed with the prescribed authority and filing of the master file and CbC report with the prescribed authority at various dates. The due date for filing the master file and CbC report is the specified due date for filing the annual tax returns. In case of CbC report, every parent entity or the alternate reporting entity resident in India will have to file the report within a period of 12 months from the end of the said reporting accounting year. No specific timelines have been prescribed for filing of the CbC report by Indian subsidiaries with parent companies resident outside India.

Significant penalty provisions will apply for non-compliance and furnishing inaccurate information.

Restrictions on interest deduction

The BEPS Action Plan 4 recommends alternate approaches for countries to limit tax base erosion through interest deductions and other financial payments. Provisions have been introduced in the Income Tax Act, 1961, which seek to limit the interest deduction of Indian companies or PEs of foreign companies in India. Taxpayers engaged in banking or insurance business are specifically excluded.

The provision will apply to interest or similar expenses paid (including those paid on existing debt) to (i) overseas associated enterprises or (ii) third-party lenders for whom the underlying debt is backed by an implicit or explicit guarantee or equivalent deposit from overseas associated enterprises.

Any interest paid for the year under consideration in excess of 30% of the EBITDA of the taxpayer will be treated as excess interest. Excess interest disallowed in a year will be eligible for carry forward up to eight consecutive years, subject to the above limits. The provision will, however, not apply to interest paid or payable up to INR 10 million.

The proposed provisions that limit the interest deductions have largely adopted the 'Fixed Ratio Rule' proposed as a best practice approach under BEPS Action Plan 4, however, with some differences. It is relevant to note that the provisions do not correspondingly limit the WHT liability or taxability of the non-resident associated enterprise on the interest income. The provisions apply from tax year 2017/18 onwards.

Secondary adjustment

To align the ITPR with the OECD Guidelines and international practices, provisions have been introduced in the ITPR for a secondary adjustment. The secondary adjustment is an adjustment in the books of account of the taxpayer and its associated enterprise to reflect that the actual allocation of profits between the Indian taxpayer and its associated enterprise are consistent with the transfer price determined as a result of primary adjustment. This is intended to remove the imbalance between the cash account and actual profit of the Indian taxpayer.

The secondary adjustment is required only where a primary adjustment to the transfer price occurs in one of the following circumstances:

- Where adjustment has been made on one's own by the taxpayer in one's income tax return.
- Adjustment made by the Assessing Officer has been accepted by the taxpayer.
- Arising due to the APA signed.
- Application of Safe Harbour Rules.
- Settlement arrived at under the MAP route.

However, an exception has been made according to which such secondary adjustments shall not be carried out by the taxpayer if the amount of the primary adjustment made in the case of a taxpayer does not exceed INR 10 million.

According to this provision, excess money arising from primary transfer pricing adjustments not repatriated into India within the prescribed time limit will be deemed as an advance made by the Indian taxpayer to its associated enterprise. Time limits have been prescribed having regard to the circumstance leading to the primary transfer pricing adjustment. The effect of the advance is given by way of an imputation of interest on such advance. The imputed *per annum* interest on such advance will be computed at the one year marginal cost of fund lending rate of the State Bank of India as on 1 April of the relevant previous year plus a spread of 325 basis points in cases where the international transaction in denominated in Indian rupees. In cases where the international transaction is denominated in foreign currency, the interest will be computed at six month London Interbank Offered Rate (LIBOR) as of 30 September of the relevant previous year plus a spread of 300 basis points. This interest will be imputed till such time as the excess money arising due to primary transfer pricing adjustments is repatriated into India.

The provisions relating to secondary transfer pricing adjustment are generally applicable for primary transfer pricing adjustments made from tax year 2016/17 onwards.

Thin capitalisation

No prescribed debt-to-equity ratios or thin capitalisation rules exist under Indian taxation law. However, interest paid to related parties at rates or on terms that are considered unreasonably high are disallowable by the tax officer.

Controlled foreign companies (CFCs)

India currently has no CFC rules, so there will be no Indian tax on foreign profits that remain unremitted from offshore subsidiaries.

Tax credits and incentives

Tax incentive provisions normally have conditions applicable for the period within which the preferred activity should be undertaken and the period for which the tax incentive is available. It may also be necessary to fulfil certain other conditions, such as 'forming' of a 'new' undertaking.

Real Estate Investment Trusts (REITs)/Infrastructure Investment Trusts (InvITs)

The Securities and Exchange Board of India (SEBI) has enacted regulations relating to two categories of investment vehicles, namely REITs and InvITs.

Pass-through status is provided to REITs in respect of income earned from renting, leasing, or letting out any real estate asset owned directly by the REITs. Thus, rental income is exempt in the hands of REITs. On distribution of rental income, REITs are not required to withhold taxes. Tax is not required to be withheld by tenants on payment of rent to the REITs.

The interest paid by special purpose vehicles (SPVs) to business trusts (BTs) is taxable at the investor level (as against the BT itself) when the BT distributes such amounts. Interest income to non-resident investors is taxable at a lower rate of 5% (plus applicable surcharge and cess), whereas residents are taxable at the applicable tax rates.

Dividends distributed by SPVs to the BTs are exempt from levy of DDT in the hands of the SPV. Such dividends are also exempt in the hands of BTs and investors if 100% of the equity shares of the SPV are held by BTs, except in case of shares mandatorily held by another entity as per law, and the dividends are distributed out of profits made after the acquisition of the SPV by BTs. Capital gains (e.g. on sale of shares of SPVs) are taxable in the hands of BTs at the applicable capital gains tax treaty rates. Any other income (including rental income) is taxable at the maximum marginal rate. Onward distributions of such income are exempt in the hands of the investors.

Transfer of units of BTs through stock exchanges are liable to STT, and gains earned by investors on such sale of units are exempt from tax if the units qualify as long-term capital assets. A lower rate of 15% (plus applicable surcharge and cess) is applicable to short-term capital assets. Taxability of capital gains arising to sponsors on exchange of shares in SPVs with units of BTs is deferred to the time of disposal of such units by the sponsor. The applicability of MAT on gains arising from the swap of shares of the SPV for units of BT is deferred to the stage when the units are transferred by the BT. No capital gains tax exemption is available on the swap of other assets with units of BTs.

Tax incentives for undertakings other than infrastructure development undertakings

If certain conditions are met, a tax holiday is permitted on the profits earned by an undertaking engaged in any of the following:

- Integrated business of handling, storage, and transportation of food grains.
- Commercial production or refining of mineral oils.
- Processing, preservation, and packaging of fruits or vegetables.
- Operating and maintaining a hospital in a rural area.

The tax holiday periods range from five to ten years, and the percentage of the rebate is 30%, 50%, or 100% in initial years and 30% in the later years. The number of years constituting ‘initial’ and ‘later’ years varies from sector to sector.

A relaxation of 100% shall be provided under certain conditions to avail of profit-linked deduction in the business of developing qualifying affordable housing projects. The conditions are as follows:

- Size of residential until will be measured as ‘carpeted area’ and not a ‘built-up area’.
- Completion of project for claiming deduction will be increased from three years to five years from receipt of approval.
- Size restriction of 30 square metres for residential units shall apply only to metro cities (i.e. municipal limits of Chennai, Delhi, Kolkata, and Mumbai).

Tax incentives for infrastructure development undertakings

Enterprises engaged in the business of power generation, transmission, or distribution; developing or operating and maintaining a notified infrastructure facility, industrial park, or SEZ; substantially renovating and modernising the existing network of transmission or distribution lines (between specified periods); or laying and operating a cross-country natural gas distribution network are eligible for a tax exemption of 100% of profits for any ten consecutive years falling within the first 15 years of operation (first 20 years in the case of infrastructure projects, except for ports, airports, inland waterways, water supply projects, and navigational channels to the sea).

An investment-linked deduction will be available to Indian companies or their consortium engaged in the business of developing or operating and maintaining of a new infrastructure facility. The taxpayers should have entered into an agreement with the Central or State Government or local authorities in respect of such activities relating to specified infrastructure facilities.

Since now there are investment-linked deductions, the profit-linked deduction available for infrastructure facilities have a sunset clause of 31 March 2017 for commencement of the operations. Thereafter, deduction of 100% of capital expenditure incurred on setting up of the said infrastructure facility is available with effect from 1 April 2017. Investment-linked deductions in respect of specified capital expenditure shall not be allowed if incurred for the purpose of acquisition of asset for payment (individual or aggregate) exceeding INR 10,000 per day unless such payment was made:

- by an account payee cheque/draft, or
- through electronic clearing system through a bank account.

‘Infrastructure facility’ means roads, including toll roads, bridges, rail systems, highway projects, water supply projects, water treatment systems, irrigation projects, sanitation and sewerage systems or solid waste management systems, ports, airports, inland waterways, inland ports, or navigational channels to the sea.

Tax incentives for exports

Export profit from a new undertaking, satisfying prescribed conditions and set up in an SEZ, is eligible for tax exemption of 100% for the first five years, from the year in which manufacturing commences, followed by a partial tax exemption of 50% for the next five years. A further tax exemption of 50% of the export profit for five years is also available after that, subject to an equal amount of profit being retained and transferred to a special reserve in the books of account. The said exemption is available on commencement of eligible business between 1 April 2006 and 31 March 2021.

Tax incentives for units in the North Eastern Region of India

Measures are in place to facilitate the development of the North Eastern Region of India and of the state of Sikkim. Undertakings located in these states that (i) begin to manufacture or produce any eligible article, (ii) undertake substantial expansion, or

(iii) commence an eligible business between 1 April 2007 and 1 April 2017 are eligible for a 100% deduction of profits for ten consecutive years.

A list of eligible businesses has been provided by the Indian government. The eligible businesses include hotels (not below two-star category), adventure and leisure sports including ropeways, the provision of medical and health services in nursing homes with a minimum capacity of 25 beds, operating a vocational training institute for hotel management, catering and food crafts, entrepreneurship development, nursing and para-medical training, civil aviation related training, fashion design and industrial training, running an information technology-related training centre, manufacturing of information technology hardware, and bio-technology. Businesses other than the above-listed eligible businesses are not entitled to claim the tax holiday.

Tax incentives for certain income relating to offshore banking units and International Financial Services Centres

A scheduled bank, or any bank incorporated by or under the laws of a country outside India, that has an offshore banking unit in an SEZ or an International Financial Services Centre with a specified income that is subject to prescribed conditions is eligible for a tax exemption of 100% of the specified income for five consecutive years beginning from the year in which the permission under the Indian Banking Regulation Act, 1949 was obtained and of 50% of the specified income for five consecutive years.

To encourage the location of offshore fund managers in India, a specific regime has been laid down. In the case of an eligible investment fund, fund management activity carried out through an eligible fund manager acting on behalf of such fund will not constitute a business connection in India. An eligible investment fund will not be treated as resident in India merely because the eligible fund manager undertakes fund management activities in India. Offshore funds and fund managers are required to satisfy certain conditions to be eligible for the regime. The conditions are not applicable to funds set up by the government of a foreign state or the Central Bank of a foreign state, a sovereign fund, or such other funds as may be notified by the government of India and subject to fulfilment of conditions as may be specified. Further, the special regime shall be applied in accordance with guidelines and in such manner as the administrative board may prescribe.

However, in order to minimise economic distortions and curb erosion of the tax base, the long-term capital gains on sale of equity shares undertaken on a recognised stock exchange located in any International Financial Services Centre and where the consideration for such transfer is received or receivable in foreign currency will not be taxable. Further, the requirement of payment of STT at the time of transfer of long-term capital asset shall not apply. *See the description of Capital gains in the Income determination section.*

Tax incentive for hiring new workmen

With a view to encouraging generation of employment, the benefit of deduction on hiring of new workmen has been extended to all taxpayers who are subjected to tax audit, instead of the earlier provision, which was applicable only to manufacturing units. Further, to enable smaller units to claim this deduction, the benefit has been extended to units employing 50 regular workmen.

To increase employment generation incentive to taxpayers across all sectors (who are subject to tax audit), where emoluments paid to an employee are less than or equal to

INR 25,000 per month, the taxpayer will be eligible for deduction of 30% of additional wages paid to new regular workmen in a factory for a period of three years wherein the workmen are employed for not less than 240 days in a year (150 days in case of apparel, footwear, and leather industry). The benefits of this incentive would also be available in the first year of business, on emoluments paid to all employees. From the tax year 2018/19 (i.e. from 1 April 2018), the deduction shall be allowed in the succeeding tax year if an employee is employed for a period less than the minimum period (i.e. 150 days or 240 days) in the tax year and continues to remain employed for the minimum period in the succeeding tax year.

However, no deduction shall be allowed in respect of cost incurred on employees for whom the government has paid the entire contribution under the Employees' Pension Scheme, and for employees who do not participate in a recognised provident fund.

Amortisation of cost of spectrum fee for Telecom operators

Amortisation of capital expenditure incurred and actually paid by the taxpayer for acquiring the right to use spectrum for telecommunication services, in equal instalments over the period of useful life of the spectrum licence, is permitted.

Patent Box Regime

In order to encourage companies to locate high-value jobs associated with the development, manufacture, and exploitation of patents in India, the government has introduced a concessional taxation regime for income from patents. Accordingly, income by way of royalty in respect of a patent developed and registered in India earned by an eligible taxpayer shall be subject to tax at the rate of 10% (plus surcharge and cess) on a gross basis.

An eligible taxpayer means a person resident in India, who is the true and first inventor of the invention, and whose name is entered on the patent register as the patentee.

Tax incentive of capital expenditure on certain specified businesses

Deduction of capital expenditure is allowed at 100% in the year when the commercial operations begin in respect of the following specified businesses:

- Setting up and operating cold chain facilities.
- Setting up and operating warehousing facilities for storage of agriculture produce.
- Setting up and operating an inland container depot, freight station, or warehousing facility for storage of sugar, beekeeping, and honey and beeswax production.
- Laying and operating a cross-country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such a network.
- Building and operating a hotel of two-star or above category in India.
- Building and operating a hospital with at least 100 beds.
- Developing and building a housing project under a scheme for slum redevelopment or rehabilitation framed by the government.
- Developing and building specified housing projects under an affordable scheme of the central/state government.
- Investing in a new plant or newly installed capacity in an existing plant for production of fertiliser.
- Developing, or operating and maintaining, or developing, operating and maintaining any infrastructure facility.

The following characteristics and conditions may be noted:

- Any sum received or receivable in cash or in kind on transfer, etc. of the capital asset shall be considered as business income if expenditure on such an asset has been allowed as a deduction under this section.
- Any loss computed in respect of the above specified businesses shall be allowed to be offset or carried forward and offset only against the profits and gains of specified businesses.
- The specified business should:
  - not be set up by splitting up or reconstruction of a business already in existence
  - not be set up by transfer of used machinery or plant exceeding 20% of the total value of the machinery or plant used in such business, and
  - have been approved by the prescribed authority (i.e. the government).

Besides the above, capital expenditure incurred on acquisition of asset (individual or aggregate) exceeding INR 10,000 per day shall be ignored for the purposes of computing the actual cost unless such payment was made:

- by an account payee bank cheque/draft, or
- through the electronic clearing system through a bank account.

Research and development (R&D) expenditure

A weighted deduction of 150% of expenditure is available in respect of expenditure incurred on scientific research in an in-house R&D facility approved by the prescribed authority for companies engaged in specified businesses and in research associations, universities, etc., respectively. Such weighted deduction will be restricted to 100% of the expenditure from tax year 2019/20 onwards.

A payment made to an approved research association undertaking research in the social sciences or in statistical research, or to an Indian company to be used by it for scientific research, is eligible for a deduction of 100% of the payment made.

Contributions made to any National Laboratory, approved scientific research associations, universities, and the Indian Institute of Technology are eligible for a weighted deduction of 150% of the contributions made up to 31 March 2021. Thereafter, the deduction will be restricted to 100% of the contribution.

Foreign tax credit

See Foreign income in the Income determination section for a description of the foreign tax credit regime.

Withholding taxes

There is an obligation on the payer (either resident or non-resident) of income to withhold tax when certain specified payments are credited and/or paid. Some of the expenses that require tax withholding are as follows.

Payments to resident companies

Nature of payment	Payment threshold for WHT (INR) (1)	WHT rate (%)
Specified type of interest	None	10 (3)
Non-specified type of interest	5,000 (2)	10

Nature of payment	Payment threshold for WHT (INR) (1)	WHT rate (%)
Professional or technical service	30,000	10
Commission and brokerage	5,000	5
Rent of plant, machinery, or equipment	180,000	2
Rent of land, building, or furniture	180,000	10
Contractual payment (except for individual/HUF)	30,000 (single payment) 100,000 (aggregate payment)	2
Contractual payment to individual/HUF	30,000 (single payment) 100,000 (aggregate payment)	1
Royalty or fees for technical services	30,000	10
Deemed dividend	2,500	10

Notes

1. Payments have different threshold limits. The payer is only required to withhold tax if the total payment within a tax year to a single person (except where specified otherwise) is above the limits specified above.
2. The threshold limit for WHT for non-specified type of interest is INR 5,000, except in the case of interest received from a bank, co-operative society, or deposit with post office, for which it is INR 10,000.
3. 2% in case the company is engaged in business of operation of call centres.

If the Permanent Account Number (PAN) of the deductee is not quoted, the rate of WHT will be the rate specified in relevant provisions of the Income Tax Act, the rates in force, or the rate of 20%, whichever is higher.

The definition of 'royalty' also includes consideration for use of, or right to use, computer software. Transfer of all or any rights in respect of any right, property, or information includes transfer of all or any right to use computer software (including granting of a licence), irrespective of the medium through which such a right is transferred and irrespective of whether any right or property is located in India. Hence, while applying WHT on such payments in the nature of royalty, one needs to consider the definition of royalty as amended by the Budget 2012 with retrospective effect from 1 June 1976.

Payment to non-resident companies

Nature of payment	WHT rate (%)
Interest on foreign currency (subject to conditions)	5
Interest on money borrowed in foreign currency under a loan agreement or by way of long-term infrastructure bonds (or rupee denominated bonds)	5
Interest on investment in long-term infrastructure bonds issued by Indian company (rupee denominated bonds or government security)	5
Non-specified type of interest	20
Royalty and technical fees	10
Long-term capital gains other than equity shares of a company or units of an equity-oriented fund/business trust on which STT is paid	20
Long-term capital gains on equity shares of a company or units of an equity-oriented fund/business trust on which STT is paid	10
Income by way of winning from horse races	30
Other income	40

Notes

- Percentage to be increased by a surcharge and health and education cess to compute the effective rate of tax withholding.

- Income from units of specified mutual funds is exempt from tax in the hands of the unit-holders.
- Dividends received from Indian companies are tax-free in the hands of the shareholder.
- Short-term capital gains on transfer of shares of a company or units of an equity-oriented fund would be taxable at 15% if they have been subjected to STT.
- There is no threshold for payment to non-resident companies up to which no tax is required to be withheld.
- If the PAN of the deductee is not quoted, the rate of WHT will be the rate specified in relevant provisions of the Act, the rates in force, or the rate of 20%, whichever is higher. The government has notified rules that do not mandate quoting of PAN, subject to certain conditions.
- The payer is obligated to report specific information in the prescribed form (whether or not such payment is chargeable to tax).

Equalisation levy

Action Plan 1 (Digital Economy) of the OECD's BEPS project discussed several options to tackle direct tax challenges in the digital environment. Taking cues from this, an equalisation levy is available, the summary of which is as follows:

- Rate of levy: 6% of the amount of consideration for specified service.
- Meaning of 'specified service': Online advertisement, any provision for digital advertising space, or any other facility or service for the purpose of online advertisement, which includes any other service as may be notified by the Central Government in this regard.
- On whom: Non-resident receiving consideration for specified services from:
  - a person resident in India and carrying on business or profession, or
  - a non-resident having a PE in India.
- Exemption from income tax: The income arising to the non-resident from the specified service and chargeable to an equalisation levy will be exempt from income tax.
- Due date for deposit: 7th day of the following month.
- Non-applicability in specified cases: Equalisation levy will not be charged in the following cases:
  - the non-resident providing specified service has a PE in India and the specified service is effectively connected with the PE
  - the aggregate consideration received or receivable in the previous year by the non-resident does not exceed INR 100,000, or
  - the payment for the specified service by the Indian resident or PE is not for conducting business or a profession in India.

Treaty rates

Some tax treaties provide for lower WHT rates from certain types of income, as follows:

	WHT (%)			
Recipient	**Dividend (1)**	**Interest**	**Royalty (12)**	**Fee for technical services (12)**
Non-treaty	10	20	10	10
Treaty: (8)				
Albania	10	10	10	10
Armenia	10	10	10	10
Australia	15	15	10 (2)/15	10 (2)/15
Austria	10	10	10	10
Bangladesh	10 (3)/15	10	10	N/A (5)
Belarus	10 (9)/15	10	15	15
Belgium	15	10 (11)/15	10	10
Bhutan	10	10	10	10

	WHT (%)			
Recipient	Dividend (1)	Interest	Royalty (12)	Fee for technical services (12)
Botswana	7.5 (9)/10	10	10	10
Brazil	15	15	25 (15)/15	15
Bulgaria	15	15	15 (7)/20	20
Canada	15 (3)/25	15	10 (2)/15	10 (2)/15
China (People's Republic of China)	10	10	10	10
Chinese Taipei (Taiwan)	12.5	10	10	10
Colombia	5	10	10	10
Croatia	5 (17)/15	10	10	10
Cyprus	10	10	10	10
Czech Republic	10	10	10	10
Denmark	15 (9)/25	10 (11)/15	20	20
Egypt	N/A (5)	N/A (5)	N/A (5)	N/A (5)
Estonia	10	10	10	10
Ethiopia	7.5	10	10	10
Fiji	5	10	10	10
Finland	10	10	10	10
France	15 (6)	0/10/15 (6)	20 (6)	10 (6)
Georgia	10	10	10	10
Germany	10	10	10	10
Greece	N/A (14)	N/A (14)	N/A (14)	N/A (5)
Hong Kong (not yet notified by government of India)	5	10	10	10
Hungary	10 (6)	10 (6)	10 (6)	10 (6)
Iceland	10	10	10	10
Indonesia	10 (9)	10	10	N/A (5)
Ireland	10	10	10	10
Israel	10	10	10	10
Italy	15 (3)/25	15	20	20
Japan	10	10	10	10
Jordan	10	10	20	20
Kazakhstan	10	10	10	10
Kenya	10	10	10	10
Korea, Republic of	15 (4)	10 (13)	10	15
Kuwait	10	10	10	10
Kyrgyz Republic	10	10	15	15
Latvia	10	10	10	10
Libya	N/A (14)	N/A (14)	N/A (14)	N/A (5)
Lithuania	5 (3)/15	10	10	10
Luxembourg	10	10	10	10
Macedonia	10	10	10	10
Malaysia	5	10	10	10
Malta	10	10	10	10
Mauritius	5 (3)/15	7.5 (14)	15	N/A (5)
Mexico	10	10	10	10
Mongolia	15	15	15	15
Montenegro	5 (9)/15	10	10	10
Morocco	10	10	10	10

	WHT (%)			
Recipient	Dividend (1)	Interest	Royalty (12)	Fee for technical services (12)
Mozambique	7.5	10	10	N/A (5)
Myanmar	5	10	10	N/A (5)
Namibia	10	10	10	10
Nepal	5 (3)/10	10	15	N/A (5)
Netherlands	15 (6)	10 (6)/15	20	10 (6)
New Zealand	15	10	10	10
Norway	10	10	10	10
Oman	10 (3)/12.5	10	15	15
Philippines	15 (3)/20	10 (13)/15	15	N/A (5)
Poland	10	10	15	15
Portugal	10 (9)/15	10	10	10
Qatar	5 (3)/10	10	10	10
Romania	10	10	10	10
Russian Federation	10	10	10	10
Saudi Arabia	5	10	10	N/A (5)
Serbia	5 (9)/15	10	10	10
Singapore	10 (9)/15	10 (11)/15	10	10
Slovenia	5 (3)/15	10	10	10
South Africa	10	10	10	10
Spain	15	15	10 (6)/20	20 (6)
Sri Lanka	7.5	10	10	10 (6)
Sudan	10	10	10	10
Sweden	10 (6)	10 (6)	10 (6)	10 (6)
Switzerland	10	10	10	10
Syria	5 (3)/10	10	10	N/A (5)
Tajikistan	5 (3)/10	10	10	N/A (5)
Tanzania	5 (3)/10	10	10	N/A (16)
Thailand	10	10	10	N/A (5)
Trinidad & Tobago	10	10	10	10
Turkey	15	10 (11)/15	15	15
Turkmenistan	10	10	10	10
Uganda	10	10	10	10
Ukraine	10 (9)/15	10	10	10
United Arab Emirates	10	5 (11)/12.5	10	N/A (5)
United Kingdom	10 (18)/15	0/10 (13)/15	10 (2)/15	10 (2)/15
United States	15 (3)/25	10 (19)/15	10 (20)/15	10 (20)/15
Uruguay	5	10	10	10
Uzbekistan	10	10	10	10
Vietnam	10	10	10	10
Zambia	5 (10)/15	10	10	10

Notes

1. The treaty tax rates on dividends are not relevant since, under the current Indian tax legislation, most dividend income from Indian companies that is subject to DDT is exempt from income tax in the hands of the recipient.
2. 10% for the use or right to use any industrial, commercial, or scientific equipment; 15% in other cases.
3. If at least 10% of capital is owned by the beneficial owner (company) of the company paying the dividend or interest.

4. If at least 20% of capital is owned by the beneficial owner (company) of the company paying dividend or interest.
5. In absence of specific provision, it may be treated as business profits or independent personal services under respective treaties, whichever is applicable.
6. The 'most favoured nation' clause is applicable. The protocol to the treaty limits the scope and rate of taxation to that specified in similar articles in treaties signed by India with an OECD-member country or another country.
7. If royalty relates to copyrights of literary, artistic, or scientific work.
8. India has signed a comprehensive tax treaty with Hong Kong Special Administrative Region (HKSAR) of China but the same is yet to be notified.
9. If at least 25% of capital is owned by the beneficial owner (company) of the company paying the dividend.
10. If at least 25% of capital is owned by the company during at least six months before date of payment.
11. If paid on a loan granted by a bank/financial institution.
12. The tax rate for royalties and fees for technical services, under the domestic tax laws, is 10%. This rate is to be increased by a surcharge at 2.5% on the income tax and education cess at 2% and secondary and higher secondary education cess at 1% on the income tax including surcharge. As a consequence, the effective tax rate is 10.558%. This rate applies for payments made under an agreement entered into on or after 1 June 2005. Accordingly, a tax resident can either use the treaty rate or domestic tax rate, whichever is more beneficial.
13. If interest is received by a financial institution.
14. Taxable in the country of source as per domestic tax rates.
15. If royalty payments arise from the use or right to use trademarks.
16. Tax treaties of certain countries do not have a separate clause specifying the WHT rate for fees for technical services and fees for included services.
17. 5% if the beneficial owner is a company holding at least 10% of share capital; 15% in other cases.
18. 15% of gross amount of dividend in case such dividend is paid out of income derived from immovable property and such income is exempt from tax; 10% in all other cases.
19. 10% if such interest is paid on a loan granted by a bank carrying on a bona fide banking business or by a similar financial institution (including an insurance company).
20. 10% if payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial, or scientific equipment and fee for included services that are ancillary and subsidiary to the enjoyment of the property for which payment is received.

List of limited agreements between India and other countries

A list of the countries with which India has entered into limited agreements for double taxation relief with respect to income of airlines/merchant shipping, is given here.

- Afghanistan
- Ethiopia
- Iran
- Lebanon
- Maldives
- Pakistan
- People's Democratic Republic of Yemen
- Yemen Arab Republic

Tax information exchange agreements (TIEAs) between India and other countries

A list of the countries with which India has entered into TIEAs for effective exchange of information relating to tax matters is given below. In addition, several of the comprehensive treaties signed by India have an information exchange clause that has the same effect as signing of a TIEA. These are not listed here.

- Argentina
- Bahamas
- Bahrain
- Belize
- Bermuda
- British Virgin Islands
- Cayman Islands
- Gibraltar
- Guernsey
- Isle of Man
- Jersey
- Principality of Liechtenstein
- Principality of Monaco
- Liberia
- Macau, China
- Maldives
- Saint Kitts and Nevis
- San Marino
- Seychelles

Tax administration

Taxable period

In India, the tax year begins on 1 April and ends on 31 March.

Tax returns

Accounts for tax purposes must be made up to 31 March. For persons having business/ professional income, the income tax return is required to be filed electronically on or before 30 September of the succeeding tax year. In case the transfer pricing provisions are applicable, the due date for filing of the tax return is on or before 30 November.

In case a taxpayer desires to revise its filed return of income, it would be eligible to do so only up to 31 March of the year following the tax year or before the completion of assessment, whichever is earlier.

Further, in order to claim the tax incentives/deductions, the taxpayers have to furnish their tax returns on or before the due date specified for filing the tax returns.

Quarterly WHT returns

Quarterly statements of taxes withheld are required to be filed electronically with the tax authorities on or before 31 July, 31 October, and 31 January for the first three quarters of the tax year and on or before 31 May following the last quarter of the tax year.

Obligation to submit tax return for assets located outside India

A resident taxpayer having any asset (including financial interest in any entity) located outside India or signing authority in any account located outside India is mandatorily required to furnish a tax return.

In cases where taxpayers have assets outside India, the extant time limits of four and six years for reopening tax assessments (where income has escaped assessment) has been increased to 16 years. In cases where a person is treated as an agent of a non-resident, the time limit for issuing reassessment notice has been extended from two years to six years.

Payment of tax

Tax is payable in advance (if tax payable for the year exceeds INR 10,000) in specified instalments for every quarter on or before 15 June, 15 September, and 15 December for the first three quarters of the tax year and on or before 15 March for the last quarter of the tax year. Any balance of tax due on the basis of the return must be paid on a self-assessment basis before the return is filed. A tax return will be treated as defective if the tax liability along with interest is not paid on or before the date of submission of the tax return. Interest levied for default in payment of advance tax is computed beginning from the first day of the year following the tax year to the date of the assessment order.

Tax audit process

Audit for income tax purposes

Persons carrying on business are required to get their books of account audited for income tax purposes if the business turnover exceeds INR 10 million. For individuals opting for the presumptive taxation scheme, one shall not be required to get one's accounts audited if the total turnover or gross receipts of the relevant previous year does not exceed INR 20 million. This will be effective from tax year 2017/18 onwards. For persons carrying on a profession, crossing the turnover threshold of INR 5 million would attract the requirement to have its books of accounts audited from 1 April 2017. The penalty for non-compliance with this audit requirement is INR 0.15 million, subject to 1% of total turnover/gross receipts.

Special audit

Tax authorities, at any stage of proceedings, having regard to nature, complexity, and volume of accounts or doubts on correctness of accounts or other reasons, may, after taking necessary approval of the Chief Commissioner, direct a taxpayer to get its accounts audited and to furnish the report.

Statute of limitations

The statute of limitations under the Act in the case of submission of returns is one year from the end of the relevant tax year, and for assessment of returns filed is 33 months (45 months in case transfer pricing provisions are applicable) from the end of the relevant tax year for which the return is filed. The statute of limitations for reassessment ranges from five years to 17 years from the end of the relevant tax year.

E-assessment

With a view to roll out e-assessment across the country so as to impart greater transparency and accountability, the Central Government has been empowered to notify a new scheme for scrutiny assessments to achieve the desired purpose. This would enable the assessment to be carried out without any personal interface between the taxpayer and the revenue authorities.

General Anti Avoidance Rule (GAAR)

GAAR provisions have been introduced in the Finance Act, 2017 and are applicable from 1 April 2017. These provisions empower the tax department to declare an 'arrangement', or any part or step thereof, entered into by a taxpayer with the main purpose of obtaining tax benefit to be an 'Impermissible Avoidance Agreement' (IAA), the consequence of which would be denial of tax benefit under the Act or under the applicable tax treaty.

For GAAR provisions, an IAA means the main purpose of which is to obtain a tax benefit, and it:

- creates rights and obligations not at arm's length
- results in abuse/misuse of provisions of this Act (directly/indirectly)
- lacks/is deemed to lack commercial substance, or
- is carried out in a manner that is not ordinarily employed for *bona fide* purposes.

The following are consequences if an arrangement is regarded as an IAA:

- Disregard/re-characterise the arrangement.
- Disregard corporate structure.
- Deny treaty benefit.
- Reassign place of residence/situs of assets or transactions.
- Reallocate income, expenses, relief etc.
- Re-characterise equity-debt, income-expense, relief, etc.

Other issues

Mergers and acquisitions

The expression 'merger' has not been defined in the Income Tax Act but has been covered as part of the definition of the term 'amalgamation'. Amalgamation is defined as a merger of one or more companies with another, or the merger of two or more companies to form a new company, in such a way that all the assets and liabilities of the amalgamating company or companies become the assets and liabilities of the amalgamated company, are held by the amalgamated company for a minimum period of five years, and shareholders holding not less than 75% in value of the shares in the amalgamating company or companies become shareholders of the amalgamated company. In case of demerger, the cost of acquisition and period of holding of the assets related to the demerged company shall be available to the resulting company.

Capital gains

No capital gains tax is levied on the transfer of capital assets by an amalgamating company to the amalgamated company, provided the amalgamated company is an Indian company. Similar is the position in case of a demerger by a demerged company to a resulting company.

In cases where shares of an Indian company are transferred by a foreign company or a demerged foreign company to another foreign company or resulting foreign company, there is no tax payable, provided it satisfies certain specified conditions. Furthermore, the shareholder of the amalgamating company or demerged company is not liable to pay capital gains tax on the exchange of shares with that of the amalgamating company or the resulting company under the scheme of amalgamation.

Conversion of a bond or debenture of a company into equity shares is specifically exempt from capital gains tax. Furthermore, conversion of preference shares to equity shares will now be exempt from capital gains tax. The cost of acquisition and period of holding of the preference shares will be considered while determining the cost of acquisition and period of holding of equity shares acquired on such conversion. This is effective from tax year 2018/19 onwards.

Carryforward of accumulated losses of amalgamating company

The losses and unabsorbed deprecation of the amalgamating company are deemed to be those of the amalgamated company in the year in which the amalgamation takes place, provided it satisfies certain specified conditions.

In the case of amalgamation of a company owning an industrial undertaking, the amalgamated company shall achieve the level of production of at least 50% of the installed capacity of the undertaking before the end of four years from the date of amalgamation and continue to maintain the minimum level of production till the end of five years from the date of amalgamation. If these conditions are violated, the benefit claimed will be taxed in the hands of the amalgamated company in the year of default.

In case of demerger of a company, the accumulated losses or unabsorbed depreciation of the demerged company directly relatable to the undertaking or the division transferred is allowed to be carried forward and offset in the hands of the resulting company.

Amalgamations and demergers normally attract stamp duty at varying rates. Such rates are derived from the laws of the state involved. High court(s), stock exchange, and other regulatory clearances are required for amalgamations or demergers.

Inter-governmental agreements (IGAs)

The Indian government has signed an IGA with the United States (US) to implement the Foreign Account Tax Compliance Act (FATCA) in India. According to the IGA, foreign financial institutions (FFIs) in India are required to report tax information about US account holders to the Indian government, which will, in turn, relay the information about Indian account holders to the US Internal Revenue Service (IRS). Furthermore, the US IRS will provide similar information about Indian citizens having any accounts or assets in the United States. This automatic exchange of information began from 30 September 2015. Subsequent to the signing of the IGA, the Indian government enacted rules relating to FATCA reporting in India.

Indonesia

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Significant developments

Indonesia has legalised Law No.9 Year 2017 to allow financial information access by the Director General of Tax (DGT) from financial institutions for tax purposes. This also marks Indonesia's readiness to implement Automatic Exchange of Financial Account Information (AEoI) in September 2018.

In keeping with Indonesia's commitment to implement Base Erosion and Profit Shifting (BEPS) Action 13, Indonesian parent entities or Indonesian subsidiaries of multinational enterprises that meets certain conditions are required to prepare and file Country-by-Country (CbC) Report to the DGT starting with the 2016 tax year.

In addition, the Parliament and government are currently organising an overall tax reform, including the revision of General Tax Provisions and Procedures (*Ketentuan Umum dan Tata Cara Perpajakan* or KUP) Law. To date, the draft bill of KUP Law has entered into the Parliament, and preliminary discussions have already begun.

Separately, the government also has a vision to establish Indonesia as a country with proven digital capacity in Southeast Asia's largest economy by 2020. Therefore, the government has highlighted the need for a road map for the development of national e-commerce and regulations related to e-commerce, including tax incentives to support the development of digital small, micro, and medium enterprises.

Noting the increase of large-scale projects in Indonesia, the government has updated tax holiday incentives to be more simple and attractive for investors. The government also plans to provide tax incentives for companies conducting research and development (R&D), as well as vocational training, activities.

Taxes on corporate income

Resident corporations are taxed based on worldwide income. A foreign company carrying out business activities through a permanent establishment (PE) in Indonesia will generally be required to assume the same tax obligations as a resident taxpayer.

Taxable business profits are calculated on the basis of normal accounting principles as modified by certain tax adjustments. Generally, a deduction is allowed for all expenditures incurred to obtain, collect, and maintain taxable business profits. A timing difference may arise if an expenditure recorded as an expense for accounting cannot be immediately claimed as a deduction for tax (*see the Deductions section*).

Resident taxpayers and Indonesian PEs of foreign companies have to settle their tax liabilities either by direct payments, third party withholdings, or a combination of both.

Foreign companies without a PE in Indonesia have to settle their tax liabilities for their Indonesian-sourced income through withholding of the tax by the Indonesian party paying the income.

Corporate income tax (CIT) rates

A flat CIT rate of 25% applies to net taxable income.

Public company discount

Public companies that satisfy a minimum listing requirement of 40% and certain other conditions are entitled to a tax discount of 5% off the standard rate, providing an effective tax rate of 20%.

Small company discount

Small enterprises (i.e. corporate taxpayers with an annual turnover of not more than 50 billion rupiah [IDR]) are entitled to a 50% tax discount of the standard rate, which is imposed proportionally on taxable income on the part of gross turnover up to IDR 4.8 billion. Certain enterprises with gross turnover of not more than IDR 4.8 billion are subject to final income tax at 1% of turnover.

Final income tax

Certain types of income are subject to a final income tax at a specified percentage of the gross amount of income, without regard to any attributable expenses.

Income	Tax rate (%)
Rental of land and/or building	10
Proceeds from transfers of land and building rights	2.5 (1)
Fees for construction work performance	2/3/4
Fees for construction work planning	4/6
Fees for construction work supervision	4/6
Interest on time or saving deposits and on Bank of Indonesia Certificates (SBIs), other than that payable to banks operating in Indonesia and to government-approved pension funds	20 (2)
Interest on bonds, other than that payable to banks operating in Indonesia and government-approved pension funds	15 (3)
Proceeds from sale of shares on Indonesian stock exchanges. To use this rate, founder shareholders must pay tax at 0.5% of the market price of their shares upon listing; otherwise, gains on subsequent sales are taxed under normal rules	0.1
Income from lottery prizes	25
Certain income received by individuals and corporates (except PEs) with gross turnover of not more than IDR 4.8 billion in one fiscal year	1 (4)

Notes

1. Proceeds from the transfer of real estate assets to a Real Estate Investment Fund (*Kontrak Investasi Kolektif - Dana Investasi Real Estate* or KIK-DIRE) is subject to a 0.5% tax rate.
2. Different rates apply on interest received from time deposits sourced from export proceeds *(Devisa Hasil Ekspor*).
3. If the recipient is a mutual fund registered with the Financial Services Authority (*Otoritas Jasa Keuangan* or OJK), the tax rate is 5% until 2020 and 10% thereafter. If the recipient is a non-resident taxpayer, the tax rate is 20% or a lower rate in accordance with the relevant tax treaty.
4. Taxpayers must calculate, pay, and report the tax due to the Indonesian Tax Office (ITO) by themselves.

Resident companies, PEs, representatives of foreign companies, organisations, and appointed individuals are required to withhold the above final tax from the gross payments to resident taxpayers and PEs.

Special industries and activities

Companies engaged in upstream oil and gas and geothermal industries typically have to calculate CIT in accordance with their production sharing contracts (PSCs). Certain companies engaged in metal, mineral, and coal mining are governed by a contract of work (CoW) for the income tax calculation. Different provisions may apply to them, pertaining to CIT rates, deductible expenses, and how to calculate taxable income.

Note that such contractual-based concessions are no longer available to new mining projects since the enactment of the Mining Law in 2009. The Mining Law stipulates that general prevailing tax laws/regulations apply to mining projects; consequently, any tax facilities should be provided accordingly, except as otherwise stated in a particular mining licence.

Local income taxes

There are no provincial or local taxes on income in Indonesia. *For a list of other local taxes, see Regional taxes in the Other taxes section*.

Corporate residence

A company is treated as a resident of Indonesia for tax purposes by virtue of having its establishment or its place of management in Indonesia.

Permanent establishment (PE)

Under the Income Tax Law, a non-resident company may be treated as having a taxable presence if it runs a business or conducts activities in Indonesia, which can be in the form of:

- a place of management
- a branch of the company
- a representative office
- an office building
- a factory
- a workshop
- a warehouse
- a room for promotion and selling
- a mining and extraction of natural resources
- a mining working area for oil and natural gas
- a fishery, animal husbandry, agriculture, plantation, or forestry location
- a project of construction, installation, or assembly
- the furnishing of services in whatever form by employees or other person, insofar conducted not more than 60 days within a 12-month period
- a person or corporation acting as a dependent agent
- an agent or employee of an insurance company that is not established and domiciled in Indonesia that receives insurance premiums or insures risk in Indonesia, and
- the computers, electronic agent, or automated equipment owned, leased, or used by an electronic transactions provider to conduct business via the internet.

Where the non-resident company is resident in a country that has a tax treaty with Indonesia, the rules on a PE creation may be changed; usually there is a longer ‘time test’ for certain activities performed in Indonesia.

Other taxes

Value-added tax (VAT)

With a few exceptions, VAT is applicable on deliveries (sales) of goods and services within Indonesia at a rate of 10%. VAT on export of goods is zero-rated, while the import of goods is subject to VAT at a rate of 10%. Zero-rated VAT is also applicable on exported services, but subject to a Ministry of Finance (MoF) limitation. Currently, only certain exported services, including toll manufacturing services, are subject to the 0% VAT rate. Services performed within the Customs Area for customers outside of the Customs Area are considered as locally delivered and are therefore subject to the regular VAT rate of 10%. Inbound use or consumption of foreign services or intangible goods, with a few exceptions, is also subject to a self-assessed VAT at a rate of 10%.

The VAT law allows the government to change the VAT rate within the range of 5% to 15%. However, since the enactment of the VAT law in 1984, the government has never changed the VAT rate.

In general, VAT collection is based on the accrual principle, whereby VAT must be collected at the time of delivery of taxable goods or services. The term delivery, in this case, is defined as the time when risk and ownership of goods have been transferred or when income from a service delivery can be reliably estimated or measured. In the accrual system, income or receivables are acknowledged when a transaction takes place, regardless of whether the transaction has been paid for or not. The recognition of revenue or receivables is indicated by the issue of a commercial invoice, which is a source document for this recognition and a basis for recording it.

VAT filing is done on a monthly basis, with payment and filing being due no later than the last day of the month following the taxable delivery.

Luxury-goods sales tax (LST)

In addition to VAT, some goods (e.g. certain household appliances, sport equipment, motor vehicles, luxury residences) are subject to LST upon import or delivery by the manufacturer to another party at rates currently ranging from 10% to 125%.

Import duty

Import duty is payable at rates from 0% to 150% on the customs value of imported goods. Customs value is calculated on the cost, insurance, and freight (CIF) level.

Group	Good	Rate (%)
Automobiles	Passenger and commercial	5 to 50
Automobile components	Incompletely knocked down	0 to 7.5
	Part by part	0 to 10
Vessels	Ships, boats, and floating structures	0 to 5
Aircraft	Balloons, helicopters, aeroplanes, parachutes, and aircraft launching gear	0
Electronic goods	Camera, refrigerator, cellular phone, and others	0 to 15
Textile, textile products, and accessories	Bags, footwear, harnesses, apparels, clothing accessories, etc.	5 to 35
Beverages, ethyl alcohol, and alcoholic drinks	Ethyl alcohol, juice, beer, wine, spirits, and other beverages	5 to 150, or IDR 14,000/litre
Essential oils and resinoids	Odoriferous substances	5 to 150
Agricultural products	Animal and vegetable products	0 to 30

Group	Good	Rate (%)
Furniture	Bedding, mattresses, lamp and lighting fittings, and others	5 to 20
Toys	Toys, games and sport requisites, parts and accessories thereof	5 to 20
Plastic	Plastics and articles thereof	0 to 25
Rubber	Rubber and articles thereof	0 to 15
Wood	Wood and articles thereof	0 to 25
Steel	Steel and articles thereof	0 to 20
Others	Chemicals, pharmaceutical products, works of art, arms and ammunition, musical instruments, and others	0 to 40

As a commitment to liberalising trade, the Indonesian government is progressively lowering import duty rates on most products. Higher duty rates remain to protect certain industries and goods regarded as sensitive for security or social and cultural reasons.

Duty relief/exemption/deferral

The Indonesian government offers duty relief, duty exemption, and duty deferral concessions to foreign and domestic investors in order to promote the development of local and export industries. These concessions usually combine with other tax facilities, such as VAT and income tax. Such concessions include the *Badan Koordinasi Penanaman Modal* (BKPM) Masterlist, Bonded Zone, Bonded Warehouse, import duty exemption and drawback for exports, Free Trade Zone (FTZ), Association of Southeast Asian Nations (ASEAN) duty rates, Free Trade Area (FTA) agreement duty rates with several countries, Indonesia-Japan Economic Partnership Agreement (IJEPA), MITA (main partners) lanes, and Authorised Economic Operator.

Land and buildings tax

Land and buildings tax (*Pajak Bumi dan Bangunan* or PBB) is a part of regional taxes, which are governed under Regional Taxes and Retribution (*Pajak Daerah dan Retribusi Daerah* or PDRD) Law in which each regional government has to issue a regulation (*Peraturan Daerah* or PERDA) to regulate PBB in its territory.

The scope of PBB under PDRD Law covers all land and buildings except for the following industries, which are governed by separate regulations:

- Forestry.
- Plantation.
- Mineral and coal mining.
- Oil, gas, and geothermal mining.
- Other industries located in national waters outside the territory of the regional area.

Under PDRD Law, the PBB rate is maximum 0.3% and the tax due is calculated by applying the tax rate on the sale value of the tax object (*Nilai Jual Objek Pajak* or NJOP) deducted by non-taxable NJOP. The non-taxable NJOP is set at a minimum of IDR 10 million. Any changes are to be made by issuing a PERDA.

Tax on land and buildings transfer

A transfer of land and buildings will cause income tax on the deemed gain on the transfer/sale to be charged to the transferor/seller. The tax is set at 2.5% of the gross transfer value or the government-determined value, whichever is greater (*see Final income tax in the Taxes on corporate income section*).

Duty on the acquisition of land and building rights

In a land and building transfer, the acquirer is liable for duty on the acquisition of land and building rights (*Bea Pengalihan Hak atas Tanah dan Bangunan* or BPHTB) at a maximum of 5% of the greater of the transaction value or the government-determined value. Similar to PBB, BPHTB has been made a part of regional taxes.

Stamp duty

Stamp duty is nominal and payable as a fixed amount of either IDR 6,000 or IDR 3,000 on certain documents.

Payroll taxes

There are no additional payroll taxes applicable other than those for social security contributions (*see below*) and employee income tax withheld by employer on the salary payment.

Social security contributions

Employers are responsible for ascertaining that their employees are covered by the workers social security program managed by *Badan Penyelenggara Jaminan Sosial* (BPJS), which provides working accidents protection, death insurance, old age savings, health care, and pension. The program calls for premium contributions from both the employers and the employees. Employees' contributions are collected through payroll deductions. The premium contributions borne by employers are calculated as a percentage of regular salaries/wages, ranging from 0.24% to 4%.

The scheme applies to all employees, including expatriates who have been working in Indonesia for more than six months.

Regional taxes

A corporate taxpayer may be liable for a number of regional taxes and retributions. The rates range from 1.5% to 35% of a wide number of reference values determined by the relevant regional governments. The following are regional taxes, other than PBB and BPHTB, that may apply:

- Motor vehicle tax.
- Motor vehicle ownership transfer fee.
- Motor vehicle fuel tax.
- Surface water tax.
- Cigarette tax.
- Hotel tax.
- Restaurant tax.
- Entertainment tax.
- Advertisement tax.
- Road illumination tax.
- Non-metal and rock minerals tax.
- Parking tax.
- Ground water tax.
- Swallow-nest tax.

Branch income

Branch profits are subject to the ordinary CIT rate of 25%. The after-tax profits are subject to a withholding tax (WHT) (i.e. branch profits tax or BPT) at 20%, regardless of whether the profits are remitted to the home country. However, a concessional WHT rate may be applicable where a tax treaty is in force (*see the Withholding taxes section for more information*). The BPT may be exempt if the profits are entirely reinvested in Indonesia (*see the Tax credits and incentives section for more information*).

Income determination

Inventory valuation

Inventories must be measured at cost by using either the average or first in first out (FIFO) method. Once a costing method is adopted, it must be applied consistently.

Capital gains

Capital gains are generally assessable together with ordinary income and subject to tax at the standard CIT rate. However, gains from the transfer of land and buildings are not subject to regular CIT, but rather are subject to final income tax at a rate of 2.5% of the transaction value or the government-determined value, whichever is higher.

The proceeds from sales of shares listed on the Indonesian stock exchange are not subject to normal CIT. Instead, the proceeds are subject only to a final WHT of 0.1% of the gross sales consideration. An additional tax of 0.5% applies to the share value of founder shares at the time an initial public offering takes place, irrespective of whether the shares are held or sold. Shareholders may elect not to pay this tax, in which case the actual gain will be subject to normal tax at the time the shares are sold.

Dividend income

In principle, dividend income received by a resident taxpayer from a limited liability company (generally referred to as a *Perseroan Terbatas* or PT) is taxable as ordinary income for the taxpayer receiving the dividend. However, if the dividend recipient is a PT with a minimum shareholding of 25% in the company paying the dividend and the dividend is paid out of retained earnings, it is exempt from CIT.

Where the recipient is not resident in Indonesia, a WHT rate of 20% applies, subject to variation by tax treaties (*see the Withholding taxes section for more information*).

The same rules apply to stock dividends (bonus shares), including dividends paid out of share premium (*agio*).

Interest income

Interest income on time or saving deposits and on Bank of Indonesia Certificates (SBIs) received by a resident company or a PE is taxed at a final tax rate of 20%.

Royalty income

Income from royalty is subject to tax and will be taxed by a WHT mechanism. The WHT rate on royalty is 15% of the gross amount for resident taxpayers and 20% of the gross amount for non-resident taxpayers or the reduced rate set out in a tax treaty. The domestic WHT on this royalty can be used as a tax credit against the normal income tax of 25% for corporate taxpayers and/or 30% (max) for individual taxpayers.

Exchange gains and losses

Gains and losses arising from currency fluctuations are generally recognised on an accrual basis in accordance with the prevailing Indonesian Accounting Standards, which resemble International Accounting Standards in most respects.

Foreign income

Foreign branch income of an Indonesian company must be accounted for as Indonesian taxable income under the controlled foreign companies (CFCs) regulation. Profits of a CFCs are subject to deemed dividend rules in Indonesia. A CFC is a foreign entity that is at least 50% owned by an Indonesian taxpayer or at least 50% collectively owned by Indonesian taxpayers. The scope of CFC income also covers income from indirectly owned CFCs with a minimum of 50% ownership by another CFC, collective ownership by an Indonesian taxpayer's CFC, or collective ownership by a number of CFCs (including under the same or different Indonesian taxpayers).

The ownership threshold that is used to determine the CFC status is the ownership percentage at the end of the Indonesian taxpayer's fiscal year, which is based on either the percentage of paid-up capital or the percentage of paid-up capital with voting rights. The only situation in which the rules do not apply is when the CFC's shares are listed on a recognised stock exchange.

Deductions

In general, expenses incurred in the ordinary course of business (to obtain, collect, and maintain taxable income) are deductible, subject to the requirements for documentary support.

Note that expenses relating to gross income subject to final income tax are not deductible for CIT purposes.

Depreciation, amortisation, and depletion

Depreciable/amortisable assets include both tangible and intangible property or costs, including the cost of extending building use rights, rights for business use, rights for use, and goodwill, with a useful life of more than one year, except land that is owned and used in business. Depreciation and amortisation may be calculated under the straight-line method or the declining-balance method on an individual asset basis. Once a method is chosen, it should be applied consistently. In calculating depreciation, depreciable assets are divided into the following classes:

	Depreciation/amortisation rate (%)	
Class	**Straight-line method**	**Declining-balance method**
Property:		
Useful life of 4 years	25	50
Useful life of 8 years	12.5	25
Useful life of 16 years	6.25	12.5
Useful life of 20 years	5	10
Buildings:		
Permanent	5	-
Non-permanent	10	-

Special rules apply for assets used in certain business fields and/or certain areas. Tax depreciation need not conform to book depreciation.

The costs incurred for acquiring rights, with a beneficial life of more than one year, for mining, oil, and natural gas concessions; forest concessions; and other rights to exploit natural resources should be amortised by the production-unit method. Except for the right to acquire oil and natural gas concessions, the depletion rate used should not exceed 20% *per annum*.

Organisational and start-up expenses

The costs of incorporation and expansion of the capital of an enterprise are claimed in full in the year in which the expenditure is incurred or are amortised using either the declining-balance or straight-line method at the above rates.

Costs incurred before the commencement of commercial operations with a useful life of longer than one year are capitalised and amortised according to the above rates.

Interest expense

Interest incurred in the ordinary course of business is deductible as long as the related loan is used for business purposes.

Interest on loans relating to time deposits (which income is subject to a final tax) is not deductible.

Interest on loans used to buy shares where dividends to be received are not subject to income tax is also not deductible.

A debt-to-equity ratio of 4:1 is generally applicable, which means that the amount of debt allowable in order to obtain full deductibility of the financing cost is limited to four times the equity amount. Exemption applies to certain taxpayers.

Bad debts

Uncollectible debts are deductible for tax purposes, with the following conditions:

- The creditor has recognised the amount of uncollectible receivables as expenses in the commercial income statement.
- The taxpayer must submit a list of uncollectible account receivables to the Directorate General of Tax.
- A legal case to enforce collection has been brought to a District Court or government agency that handles state receivables, there is a written agreement on cancellation of receivables/debt release and discharge between the concerned creditor and debtor, it has been publicised in a general or a special publication, or the debtor has otherwise acknowledged that one's debts have been cancelled.

Charitable contributions

Donations for national disasters, education facilities, sport development, and social infrastructures, with certain conditions, may be deductible in the fiscal year when the donations are provided.

Benefits in kind

Most benefits received in kind by employees, such as free housing, are not tax-deductible to the entity providing the benefit. Free motor vehicle and telephone expenses, including depreciation, are tax-deductible but only for 50% of the total expenses incurred. Expenses for meals and transportation made available to all staff are tax-deductible. Apart from these, certain benefits in kind (e.g. housing provided in remote areas as designated by the MoF, Integrated Economic Development Zones as designated by Presidential Decree) can also be claimed as tax-deductible expenses.

Fines and penalties

Fines, penalties, and interest on underpayment of taxes are not deductible.

Taxes

Land and buildings tax and regional taxes may be deducted from taxable income. With several exceptions, input VAT is also deductible against taxable income as long as it is not claimed as a credit against output VAT.

Net operating losses

Losses may be carried forward for a maximum period of five years. Carrying back of losses is not permitted. Offsetting losses within a corporate group is not permitted.

Payments to foreign affiliates

WHT is applied as a final tax on the recipient for payments of royalties, interest, and service fees to foreign non-resident companies. Excessive and non-arm's-length payments to related parties are disallowed as deductions. The tax law denies deductions for all payments from a branch to its head office for royalties, interest, and services provided by the head office (exceptions apply for loans between bank branches and their head offices).

Group taxation

Consolidated returns are not allowed in Indonesia.

Transfer pricing

Transactions between related parties must be consistent with the arm's-length principle. If the arm's-length principle is not followed, the DGT is authorised to recalculate the taxable income or deductible costs arising from such transactions applying the arm's-length principle.

Under the General Tax Provisions and Procedures (*Ketentuan Umum dan Tata Cara Perpajakan* or KUP) Law, the government requires specific transfer pricing documentation to prove the arm's-length nature of related-party transactions.

The MoF issued a regulation, dated 30 December 2016, regarding transfer pricing documentation, which requires taxpayers under certain criteria to prepare transfer pricing documentation, namely the Master File, Local File, and Country-by-Country (CbC) Report.

Detailed transfer pricing disclosures are required in the CIT return, which include the following:

- The nature and value of transactions with related parties.
- The transfer pricing methods applied to those transactions and the rationale for selecting the methods.

- Whether the company has prepared transfer pricing documentation.

Transfer pricing disputes may be resolved through the domestic objection and appeal process, or, where the dispute involves a transaction with a related party in a country that is one of Indonesia's tax treaty partners, the parties may request double tax relief under the Mutual Agreement Procedures (MAP) article of the relevant tax treaty. There is a restriction that an MAP application cannot be lodged when the Tax Court has declared an end to the court hearing process, and an existing MAP will cease when the Tax Court announces its decision. If a party is not satisfied with the Tax Court decision, a judicial review by the Supreme Court is allowed.

The tax law authorises the DGT to enter into Advance Pricing Agreements (APAs) with taxpayers and/or another tax country's tax authority only on the future application of the arm's-length principle to transactions between related parties; consequently, taxpayers should not expect an APA to be 'rolled-back' to address any transfer pricing matters in open years in relation to the same/similar transactions. Once agreed, an APA will typically be valid for a maximum of three tax years after the tax year in which the APA is agreed or four years if the process involves cooperation with foreign tax authorities that escalate an APA application to be an MAP in order to settle any ongoing double taxation in accordance with a relevant tax treaty.

Increase in transfer pricing focused investigations

The number of tax audits with transfer pricing as the key focus area has continued to increase following the issuance of regulations relating to transfer pricing. The DGT has issued detailed guidelines that, broadly stated, typically follow Organisation for Economic Co-operation and Development (OECD) principles. Transactions under particularly close scrutiny include payments of royalties and technical or management services fees, inter-company services, royalty and financing transactions, and exports to related parties.

Where a taxpayer has no documentation available to substantiate these transactions, there is a high risk that deductions for the payments will be denied in full. In this regard, the 30-day time limit within which a taxpayer must produce any documentation requested by the ITO during an audit is being strictly enforced. Any documentation provided after the 30-day time limit is being disregarded by the ITO in its decision making process.

Transfer pricing specific audits are regularly conducted by the ITO, with the high priority targets generally identified based on:

- profit performance of the company (companies that have incurred consistent losses will be the highest priority, but there is also a risk of being selected for companies with profits below industry norms) and
- materiality of the company's related-party transactions.

The ITO has issued questionnaires to several taxpayers who are not under an audit that focus primarily on transfer pricing issues. It is possible that the information gathered by the ITO from these questionnaires will lead to follow-up investigations or audits in some cases.

The DGT has also reinforced tax audit procedures for taxpayers with related-party transactions. This regulation provides more clarity and is more relevant with the current transfer pricing issues in practice (e.g. the use of the median point as the basis of correction, mandatory use of the comparable uncontrolled price [CUP] method for interest, the use of multiple year data for comparables). Comprehensive forms required to be completed by the taxpayers during a tax audit are also provided in the regulation.

Thin capitalisation

The MoF is authorised to make a determination on an appropriate ratio of debt to equity. The general ratio of 4:1 is applicable for group companies, except for exempted taxpayers.

Controlled foreign companies (CFCs)

See Foreign income in the Income determination section for a description of the CFC regime.

Tax credits and incentives

Foreign tax credit

Tax paid or payable in foreign countries upon income from abroad received or obtained by a resident taxpayer may be credited against tax payable in Indonesia in the same fiscal year.

The amount of tax credit is the same amount as income tax paid or payable abroad, but shall not exceed tax payable calculated according to the Indonesian tax law.

Revaluation of fixed assets

Certain taxpayers may apply for fixed asset revaluation for tax purposes with approval from the DGT. 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%.

Income tax concessions

Tax holiday

The MoF may provide a tax holiday of 100% of the CIT due for 5 to 20 years from the start of commercial production, depending on the investment amount. After the end of the tax holiday, the companies will receive a 50% CIT reduction for two years.

This facility is provided to new investments in pioneer industries that have a wide range of connections, provide additional value and high externalities, introduce new technologies, and have strategic value for the national economy. Currently, this facility is available for the following business sectors:

- Integrated upstream basic metal.
- Integrated oil and gas refinery.
- Integrated petrochemicals from oil, gas, or coal.
- Integrated inorganic basic chemicals.
- Integrated organic basic chemicals from agriculture, plantation, or forestry products.
- Integrated pharmaceutical raw materials.
- Semi-conductor and other main components of computers that are integrated with computer manufacturing.
- Main components of communication equipment that are integrated with smartphone manufacturing.

- Main components of health equipment that are integrated with irradiation, electro medical, or electrotherapy manufacturing.
- Main components of industrial machinery that are integrated with machinery manufacturing.
- Main components of machinery that are integrated with motor vehicles manufacturing.
- Robotics components that are integrated with the manufacturing industry.
- Main components of vessels that are integrated with vessel manufacturing.
- Main components of aircraft that are integrated with aircraft manufacturing.
- Main components of trains that are integrated with train manufacturing.
- Power plant machinery.
- Economic infrastructure.

An application must be submitted to the Investment Coordinating Board (*Badan Koordinasi Penanaman Modal* or BKPM) Chairman prior to the start of commercial production. A proposal for the MoF's approval will be made by the BKPM Chairman after carrying out review on the applicant. Under the latest regulation, the proposal can be submitted to the MoF until 3 April 2023.

Inbound investment incentives

The MoF may provide the following tax concessions to PT companies following their investment in certain designated business areas or in certain designated regions:

- A reduction in net income of up to 30% of the amount invested, prorated at 5% for six years of the commercial production, provided that the assets invested are not transferred out within six years.
- Accelerated depreciation and/or amortisation deductions.
- Extension of tax losses carryforward for up to ten years.
- A reduction of the WHT rate on dividends paid to non-residents to 10% (or lower if treaty relief is available).

The applicant must meet one of the following high-level criteria to be eligible for the above tax facilities:

- High investment value or for export purposes.
- High absorption of manpower.
- High local content.

Recommendation from the BKPM Chairman must first be obtained, together with the application for investment approval, before MoF approval for the tax facilities can be sought.

Special Economic Zones (Kawasan Ekonomi Khusus or KEKs)

Taxpayers conducting business in KEKs may enjoy tax facilities. The business should cover the main activities determined for each KEK. The designation of an area as a KEK is set out in a specific government regulation.

CIT reduction facility may be granted for new taxpayers with new capital invested in the production chain of main activities in a KEK, as described below:

Investment plan (IDR, in billions)	Reduction period (in years)	CIT reduction
Less than 500	5 to 15	MoF discretion

Investment plan (IDR, in billions)	Reduction period (in years)	CIT reduction
500 up to 1,000	5 to 15	20% to 100%
More than 1,000	10 to 25	20% to 100%

Taxpayers being rejected for the CIT reduction facility and taxpayers carrying out other activities in a KEK may apply for similar inbound investment incentives under the income tax concessions.

On top of the above income tax facilities, taxpayers in a KEK are also entitled to the following tax facilities:

- Non-collection of VAT and LST on importation of certain goods.
- Non-collection of Article 22 Income Tax on importation of certain goods.
- Postponement of import duty on capital goods and equipment, and goods and materials for processing.
- Exemption of excise on importation of goods to be used to produce non-excisable goods.
- Non-collection of VAT and LST on the domestic purchases of certain goods.

Integrated Economic Development Zones (Kawasan Pengembangan Ekonomi Terpadu or KAPETs)

Companies conducting business in KAPET may enjoy tax facilities. The designation of an area as a KAPET is set out in a specific Presidential Decree.

An Entrepreneur in Bonded Zone (*Pengusaha di Kawasan Berikat* or PDKB) in a KAPET may be granted tax facilities in the form of:

- Income tax facilities similar to inbound investment incentives under the income tax concessions.
- Non-collection of VAT and LST on importation of certain goods.
- Exemption of Article 22 Income Tax on importation of certain goods.
- Postponement of import duty on capital goods and equipment, and goods and materials for processing.
- Non-collection of VAT and LST on the domestic purchases of certain goods.

Bonded Stockpiling Area

Bonded Stockpiling Area (*Tempat Penimbunan Berikat*) currently consists of:

- Bonded Zones.
- Bonded Warehouse.
- Bonded Exhibition Place.
- Duty Free Shop.
- Bonded Auction Place.
- Bonded Recycled Area.
- Bonded Logistic Centre.

We will only highlight three prominent areas in the below sections.

The tax facilities in these areas are as follows:

- Non-collection of VAT and LST on importation of certain goods.
- Non-collection of Article 22 Income Tax on importation of certain goods.

- Postponement of import duty on certain goods.
- Exemption of excise on importation of certain goods.
- Non-collection of VAT and LST on the domestic purchases of certain goods.

Bonded Zones

The Bonded Zones (*Kawasan Berikat*) facility is provided to companies producing finished goods that are mainly for export, with the domestic sales quota of 50% of the previous year export realisation value and/or sales value to other Bonded Zones/FTZs/KEKs. The import duty, VAT, LST, and Article 22 Income Tax are also exempted for importation of machinery.

Bonded Warehouse

The Bonded Warehouse (*Gudang Berikat*) facility is intended to store imported goods that can be processed with one or more activities within one year.

Bonded Logistic Centre

The Bonded Logistic Centre (*Pusat Logistik Berikat*) facility is similar to the Bonded Warehouse facility; however, it is intended to store both imported goods from outside the Customs Area and/or goods from other places within the Indonesia Customs Area that can be processed with one or more simple activities within three years.

Free Trade Zones (FTZs)

Goods entered into and goods delivered amongst companies inside an FTZ (*Kawasan Perdagangan Bebas*) may enjoy tax facility.

Taxpayers in FTZs are entitled to the following tax facilities:

- Exemption of VAT and LST on importation of certain goods.
- Non-collection of Article 22 Income Tax on importation of certain goods.
- Exemption of import duty on certain goods.
- Exemption of excise on importation of certain goods.
- Non-collection of VAT and LST on the domestic purchases of certain goods.
- Transactions of intangible goods and taxable services are exempted from VAT, except for those delivered to other Indonesia Customs Area and Bonded Stockpiling Area or Special Economic Zones companies.

Industrial Zones (Kawasan Industri or KIs)

The determination and licensing of a KI is as granted by the government. The applicable tax facilities depend on the classification of the Industrial Development Area (IDA) (*Wilayah Pengembangan Industri* or WPI) of the KI, namely:

- Advance IDA (WPI *Maju* or WPIM).
- Developing IDA (WPI *Berkembang* or WPIB).
- Potential I IDA (WPI *Potensial I* or WPIP I).
- Potential II IDA (WPI *Potensial II* or WPIP II).

Below are the available tax facilities for each type of WPI:

Tax and customs facility	WPIM*	WPIB	WPIP I	WPIP II
CIT reduction of 10% to 100% of the CIT due for 5 to 15 years from the start of commercial production	Yes	–	–	Yes

Tax and customs facility	WPIM*	WPIB	WPIP I	WPIP II
Income tax facilities similar to inbound investment incentives under the income tax concessions	Yes	Yes	Yes	–
VAT exemption on the imports/purchase of machines and equipment (excluding spare parts) that are directly used to produce VATable goods	Yes	Yes	Yes	Yes
Import duty exemption on the imports of machines or materials that are used to produce goods/services**	Yes	Yes	Yes	Yes

Notes

* WPIM may choose to apply income tax facility in the form of CIT reduction or inbound investment incentives.

** The applicable period of import duty exemption varies depending on the KI classification and the business cycle of the respective taxpayer (e.g. construction or developing stage).

Reinvestment of branch profits

PEs that reinvest their after-tax profits in Indonesia within the same year or no later than the following year are exempt from BPT on these profits. The reinvestment should be one of the following forms:

- As a founder or a participant founder in a newly established Indonesian company through capital participation.
- As a shareholder of an established Indonesian company through capital participation.
- Acquisition of a fixed asset used by the PE to conduct its business or activities in Indonesia.
- Investment in the form of an intangible asset used by the PE to conduct its business or activities in Indonesia.

Shares in a newly established company shall not be transferred until, at a minimum, two years from the date that the company commences commercial production. With regard to the investment in an established Indonesian company, acquisition of a fixed asset, or investment of an intangible asset, the investment shall not be transferred until, at a minimum, three years after the investment.

Other incentives

Income earned by venture capital companies in the form of profit sharing from their investments in Indonesia is exempt from tax, provided that the following conditions are met:

- Entities are small or medium-scale businesses in one of the sectors designated by the Indonesian government.
- Investments are not listed on the Indonesian stock exchange.

Withholding taxes

Indonesian income tax is collected mainly through a system of WHTs. Where a particular income item is subject to WHT, the payer is generally held responsible for withholding or collecting the tax. These WHTs are commonly referred to using the relevant article of the Income Tax (*Pajak Penghasilan* or PPh) Law, as follows.

Article 23/26 Income Tax (PPh 23/26)

PPh 23/26 is levied on a variety of payments to corporations and individuals, resident and non-resident, at the following rates:

	WHT (%)				
	Dividends				
Recipient	Portfolio	Substantial holdings	Interest	Royalties	Branch profits (8)
Resident corporations	15	0	15	15	N/A
Resident individuals	10	10	15	15	N/A
Non-resident corporations and individuals					
Non-treaty	20	20	20	20	0/20
Treaty:					
Algeria	15	15	0/15 (6a)	15	10
Armenia	15	10	0/10 (6a)	10	10
Australia	15	15	0/10 (6a)	10/15 (7b, 7c)	15
Austria	15	10	0/10 (6a)	10	12
Bangladesh	15	10	0/10 (6a)	10	10
Belgium	15	10	0/10 (6a)	10	10
Brunei	15	15	0/15 (6a)	15	10
Bulgaria	15	15	0/10 (6a)	10	15
Canada	15	10	0/10 (6a, 6b)	10	15
China (2)	10	10	0/10 (6a)	10	10
Croatia	10	10	0/10 (6a)	10	10
Czech Republic	15	10	0/12.5 (6a)	12.5	12.5
Denmark	20	10	0/10 (6a)	15	15
Egypt	15	15	0/15 (6a)	15	15
Finland	15	10	0/10 (6a)	10/15 (7d)	15
France	15	10	0/10/15 (6a, 6b)	10	10
Germany (1)	15	10	0/10 (6a)	10/15 (7b, 7c)	10
Hong Kong	10	5	0/10 (6a)	5	5
Hungary (3)	15	15	0/15 (6a)	15	20
India (1)	10	10	0/10 (6a)	10	15
Iran	7	7	0/10 (6a)	12	7
Italy	15	10	0/10 (6a, 6b)	10/15 (7b, 7c)	12
Japan	15	10	0/10 (6a)	10	10
Jordan (3)	10	10	0/10 (6a)	10	20
Korea (North)	10	10	0/10 (6a)	10	10
Korea (South) (2)	15	10	0/10 (6a)	15	10
Kuwait	10	10	0/5 (6a)	20	0/10
Laos	15	10	0/10 (6a)	10	10
Luxembourg (1)	15	10	0/10 (6a)	12.5	10
Malaysia (4)	10	10	0/10 (6a, 6b)	10	12.5
Mexico	10	10	0/10 (6a, 6b)	10	10
Mongolia	10	10	0/10 (6a)	10	10
Morocco	10	10	0/10 (6a)	10	10

Indonesia

	WHT (%)				
	Dividends				
Recipient	Portfolio	Substantial holdings	Interest	Royalties	Branch profits (8)
Netherlands	10/15	5	0/5/10 (6a, 6b)	10	10
New Zealand (3)	15	15	0/10 (6a)	15	20
Norway	15	15	0/10 (6a, 6b)	10/15 (7a, 7b, 7c)	15
Pakistan (1)	15	10	0/15 (6a)	15	10
Papua New Guinea (1)	15	15	0/10 (6a)	10	15
Philippines	20	15	0/10/15 (6a, 6b)	15	20
Poland	15	10	0/10 (6a)	15	10
Portugal	10	10	0/10 (6a)	10	10
Qatar	10	10	0/10 (6a)	5	10
Romania	15	12.5	0/12.5 (6a, 6b)	12.5/15 (7a, 7b, 7c, 7d)	12.5
Russia	15	15	0/15 (6a)	15	12.5
Seychelles (3)	10	10	0/10 (6a)	10	20
Singapore	15	10	0/10 (6a)	15	15
Slovakia	10	10	0/10 (6a)	10/15 (7d)	10
South Africa (3)	15	10	0/10 (6a)	10	20
Spain	15	10	0/10 (6a)	10	10
Sri Lanka	15	15	0/15 (6a)	15	20
Sudan	10	10	0/15 (6a)	10	10
Suriname	15	15	0/15 (6a)	15	15
Sweden	15	10	0/10 (6a)	10/15 (7b, 7c)	15
Switzerland (1)	15	10	0/10 (6a)	10	10
Syria	10	10	0/10 (6a)	15/20 (7d)	10
Taiwan	10	10	0/10 (6a)	10	5
Thailand	20	15	0/15 (6a)	15	20
Tunisia	12	12	0/12 (6a)	15	12
Turkey	15	10	0/10 (6a)	10	10
Ukraine	15	10	0/10 (6a, 6b)	10	10
United Arab Emirates	10	10	0/5 (6a, 6b)	5	5
United Kingdom	15	10	0/10 (6a, 6b)	10/15 (7b)	10
United States of America	15	10	0/10 (6a)	10	10
Uzbekistan	10	10	0/10 (6a)	10	10
Venezuela (1)	15	10	0/10 (6a, 6b)	20	10
Vietnam	15	15	0/15 (6a)	15	10
Zimbabwe (1, 5)	20	10	0/10 (6a)	15	10

Domestic Article 23 WHT is also payable at the rate of 2% for most types of services where the recipient of the payment is an Indonesian resident.

Notes

1. Service fees, including for technical, management, and consulting services, rendered in Indonesia are subject to WHT at rates of 5% for Switzerland; 7.5% for Germany; 10% for India, Luxembourg, Papua New Guinea, Venezuela, and Zimbabwe; and 15% for Pakistan.
2. VAT is reciprocally exempted from the income earned on the operation of ships or aircraft in international lanes.

3. The treaty is silent concerning BPT rate. The ITO interprets this to mean that the tax rate under Indonesian Tax Law (20%) should apply.
4. Labuan offshore companies (under the Labuan Offshore Business Activity Tax Act 1990) are not entitled to the tax treaty benefits.
5. A protocol amending the tax treaty has been signed, pending the ratification of the protocol and the exchange of ratification documents.
6. Interest:
   a. Exempt if paid to the government.
   b. Exempt if paid to a bank but linked to a government loan agreement or paid to specific financial institutions/banks.
7. Royalties:
   a. The use of, or the right to use, any copyright, patent, design or model, plan, secret formula or process, trademark, or other like property or right.
   b. The use of, or the right to use, any industrial, commercial, or scientific equipment.
   c. The supply of scientific, technical, industrial, or commercial knowledge or information.
   d. The use of, or the right to use, any copyright of literary, artistic, or scientific work, including cinematography films and films or tapes for television or radio broadcasting.
8. PEs that reinvest their after-tax profits in Indonesia within the same year or no later than the following year are exempt from BPT on these profits (*see the Tax credits and incentives section*).

The issue of beneficial ownership has come under tax office scrutiny. For treaty WHT rates to apply to passive income such as interests, dividends, and royalties, the recipient of such income must be the beneficial owner. The recipient must also provide a Certificate of Domicile (CoD) in the form required by the ITO and certified by their home country tax authority that the recipient is a tax resident of that country. The CoD in the form prepared by the other country's tax authority may only be used in limited circumstances. Further, the CoD form also requires a number of declarations to be made by the recipient that acknowledges that the use of the treaty jurisdiction was not merely for obtaining the benefit of the treaty. These declarations place onerous obligations on both the Indonesian payer and the recipient entity. Without a certified CoD, a WHT at a rate of 20% will apply. These aspects need to be considered when paying income of this nature.

Article 22 Income Tax (PPh 22)

PPh 22 is typically applicable to the following:

Event		Tax rate (%)	Tax base
1	The import of:		Import value (i.e. CIF value plus duties payable)
	a. Certain end customer goods	10	
	b. End customer goods other than (a)	7.5	
	c. Goods other than (a) and (b) using an Importer Identification Number (*Angka Pengenal Impor* or API):		
	i. Soybeans, wheat, and flour wheat	0.5	
	ii. Other than (i)	2.5	
	d. Goods other than (a) and (b) without an API	7.5	
2	The auctioned imported goods	7.5	Auction prices
3	The sale of goods to the government requiring payment from the State Treasury and Proxy of Budget User (*Kuasa Pengguna Anggaran* or KPA) (1)	1.5	Selling prices
4	The sale of goods to State-Owned Enterprises (*Badan Usaha Milik Negara* or BUMN) and some of their subsidiaries (1, 3)	1.5	Selling prices
5	The purchase of oil fuel by gas stations from Pertamina and its subsidiaries (2)	0.25	Selling prices
6	The purchase of oil fuel by gas stations from parties other than Pertamina and its subsidiaries (2)	0.3	Selling prices
7	The purchase of oil fuel by parties other than gas stations (2)	0.3	Selling prices
8	The purchase of gas fuel (2)	0.3	Selling prices

Event		Tax rate (%)	Tax base
9	The purchase of lubricants	0.3	Selling prices
10	The purchase of cement by local distributors	0.25	Selling prices
11	The purchase of paper products by local distributors	0.1	Selling prices
12	The purchase of steel products by local distributors	0.3	Selling prices
13	The purchase of automotive products by local distributors	0.45	Selling prices
14	The purchase of pharmaceutical products by local distributors	0.3	Selling prices
15	The purchase of motor vehicles from Sole Agents (*Agen Tunggal Pemegang Merek* or ATPM), Agents (*Agen Pemegang Merek* or APM), and general importers (4)	0.45	Selling prices
16	The sale of forestry, plantation, agriculture, cattle breeding, and fishery products to manufacturers or exporters (1)	0.25	Selling prices
17	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
18	The sale of coal, metal, and non-metal minerals by companies or individuals holding a mining license (*Izin Usaha Pertambangan* or IUP) (1)	1.5	Selling prices
19	The purchase of gold bars (5)	0.45	Selling prices
20	The purchase of very luxurious goods	5	Selling prices

Notes

1. In events (3), (4), (16), and (18), the PPh 22 collectors must withhold PPh 22 from the amount payable to a particular vendor, except payments for the purchase/use of:
   - oil fuel, gas fuel, lubricants, postal products
   - water and electricity
   - oil or gas (including upstream by products) from a contractor of a PSC, the contractor's head office, or the contractor's trading arms, and
   - geothermal or electricity from a contractor of a Joint Operation Contract.

   There is also an exemption for the purchase of goods with a value of up to IDR 2 million, IDR 10 million, and IDR 20 million for events (3), (4), and (16) respectively. In the other events, the importer or the buyer of the designated goods must pay PPh 22 in addition to the amounts payable for the goods imported or purchased.

2. The withheld PPh 22 constitutes a pre-payment of corporate/individual income tax liabilities, except for the purchase of oil and gas fuel by distributors/agents, which is categorised as final tax.
3. Exception applies on the sale of forestry, plantation, agriculture, cattle breeding, and fishery products since it is already subject to PPh 22 in event (16).
4. Exception applies on the purchase of very luxurious motor vehicles since it is already subject to PPh 22 in event (20).
5. Exemption applies on the sale to Bank Indonesia.

The tax does not apply, either automatically or with an Exemption Certificate issued by the DGT, on the following types of events:

- Import/purchase of goods not subject to income tax.
- Import of goods exempted from import duties and/or VAT, subject to 0% import duty, or where VAT is not collected.
- Goods that have been temporarily imported (i.e. goods for re-export).
- Goods for re-importing (i.e. exported and re-imported in the same quality or to be repaired/tested).
- Import of gold bars for the production of jewellery for re-export.
- Purchase of goods related to the use of government school operations subsidy (*Bantuan Operasional Sekolah* or BOS) fund.

- The purchase of grain or rice by the State Treasury, KPA, and the Bureau of Logistics (*Badan Urusan Logistik or* BULOG).
- The purchase of necessary food products by BULOG or appointed BUMN.

Taxpayers without a Tax Identification Number will be subject to a surcharge of 100% in addition to the standard tax rate.

Tax administration

Payments of tax and tax returns filing

Tax liabilities for a particular period or year must typically be paid to the State Treasury through a designated tax-payment bank (*bank persepsi*) and then accounted for at the DGT office through the filing of the relevant tax returns. The tax payments and tax return filing for a particular tax must be undertaken monthly or annually, depending upon the tax obligation in question. These payments and filing obligations can also be conducted electronically. Tax payments should generally be conducted electronically.

Corporate tax liabilities may be settled either by direct payments, third party withholdings, or a combination of both. Monthly tax instalments constitute the first part of tax payments to be made by taxpayers as a prepayment of their current year CIT liability. A monthly tax instalment is generally calculated using the most recent CIT return. The tax withheld by third parties on certain income or tax to be paid in advance on certain transactions (i.e. imports) also constitute prepayments for the current year corporate tax liability of the income recipient or the party conducting the import. If the total amounts of tax paid in advance through the year are less than the total CIT due, the company concerned has to settle the shortfall before filing its CIT return. Returns for transaction taxes, such as WHT, must be filed on a monthly basis.

A summary of these tax obligations is as follows:

Monthly tax obligations

Type of tax	Tax payment deadline	Tax return filing deadline
Article 21/26 (Payroll) WHT	The 10th day of the following month	The 20th day of the following month
Article 23/26 Income Tax	The 10th day of the following month	The 20th day of the following month
Article 25 Income Tax Instalment	The 15th day of the following month	The 20th day of the following month
Article 22 Income Tax on imports/payments to Tax Collectors	The 10th day of the following month	The 20th day of the following month
Article 4(2) Final Income Tax	The 10th day of the following month	The 20th day of the following month
VAT and LST	Prior to the tax return filing deadline	The end of the following month

Annual tax obligations

Type of tax	Tax payment deadline	Tax return filing deadline
CIT	The end of the fourth month after the book year-end before filing the tax return	The end of the fourth month after the book year-end
PBB	Six months after the receipt of a Tax Due Notification Letter from the ITO	N/A

Penalties

Late payments of the above taxes incur interest penalties at 2% per month, with a maximum of 48%. Part of a month, for example a single day, is considered a full month.

Late filing of a tax return or failure to file a tax return incurs an administrative penalty at the following amounts:

Type of tax return	IDR
VAT return	500,000
Other monthly tax returns	100,000
CIT return	1,000,000

Tax assessments

Indonesia uses a self-assessment system under which taxpayers are trusted to calculate, pay, and report their own taxes in accordance with prevailing tax laws and regulations. However, the DGT may issue tax assessment letters to a particular taxpayer if it finds that, based on a tax audit or on other information, the taxpayer has not fully paid all tax liabilities. A tax assessment letter may also be issued by the DGT to a taxpayer who ignores a warning letter to file a tax return within a specified period. Failure to maintain books in accordance with the prescribed standards is another condition that may lead the DGT to issue an official tax assessment.

Tax audit process

The tax audit of a company may cover only a particular tax or all taxes for a particular tax period (a tax month) or tax year. It may be conducted at the company's premises, at the DGT offices, or at both.

Conditions triggering a tax audit

A tax refund request will always trigger a tax audit. Due to the requirement for the DGT to decide on a refund request within 12 months, a tax audit will typically begin from a few weeks to several months from the refund request date. A corporate tax refund request will normally trigger a complete tax audit covering all taxes. A refund request of any other tax will normally trigger a tax audit covering only one particular tax. The DGT will likely broaden the tax audit scope to include other taxes.

Other events that may trigger a tax audit include the following:

- A tax return in an overpayment position (not necessarily accompanied by a refund request).
- An annual income tax return presenting/claiming a tax loss.
- The taxpayer has changed its fiscal year or bookkeeping method or performed fixed assets revaluation.
- A tax return not filed within the prescribed time or filed after the deadline stated in a warning letter, which has been selected to be audited based on a risk analysis.
- A tax return meeting certain (undisclosed) DGT criteria.

Statute of limitations

The DGT can issue an underpaid tax assessment letter within five years after the incurrence of a tax liability, the end of a tax period (month), or the end of (part of) a tax year.

Topics of focus for tax authorities

Indonesia is largely a self-assessment tax environment, and enforcement remains a priority of the tax authorities. The DGT continues its efforts in improving compliance by targeting tax audits on transfer pricing and certain industries (particularly those in the oil and gas and coal mining industry).

On the other hand, the DGT has also made some efforts to collect more information from various sources and is issuing several incentives to increase tax compliance as well as boosting national tax revenue (i.e. incentives for the payment of tax in arrears and the sunset policy that eliminates or reduces administrative sanctions in certain cases).

Other issues

Business combinations and splits

Transfers of assets in business mergers, consolidations, or business splits must generally be dealt with at market value. Gains resulting from this kind of restructuring are assessable, while losses are generally claimable as a deduction from income. However, a tax-neutral merger or consolidation, under which assets are transferred at book value, can be conducted but is subject to the approval of the DGT. To obtain this approval, the merger or consolidation plan in question must pass a business-purpose test. Tax-driven arrangements are prohibited, and tax losses from the combining companies may not be passed to the surviving company.

Subject to a similar, specific DGT approval, the same concession is also available for business splits that constitute part of an initial public offering (IPO) plan. In this case, within one year of the DGT's approval being given, the company concerned must have made an effective declaration regarding registration for an IPO with the OJK. In the event of complications beyond the company's control, the period may be extended by the DGT for up to four years.

Tax information exchange agreements (TIEAs)

Indonesia has TIEAs with the following jurisdictions:

- Bahamas (2)
- Bermuda (1)
- Guernsey
- Isle of Man
- Jersey
- San Marino (1)

Notes

1. Ratified but not yet effective, pending the exchange of ratification documents.
2. The TIEA has been signed, pending the ratification of the TIEA and the exchange of ratification documents.

Mutual Administrative Assistance in Tax Matters

Indonesia signed the Convention on Mutual Administrative Assistance in Tax Matters on 3 November 2011 and ratified it on 17 October 2014. Indonesia also signed a Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information on 4 June 2015 and is committed to apply this using the Common Reporting Standard (CRS) issued by the OECD.

Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS)

Indonesia signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS) on 7 June 2017, and it provided a list of reservations and notifications on the same date, which are still subject to ratification. In this provisional provision, Indonesia has put 33 tax treaties to be covered by the Convention.

US Foreign Account Tax Compliance Act (FATCA)

Indonesia has principally agreed to sign the InterGovernmental Agreement (IGA) 1 for FATCA compliance purposes.

Japan

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Significant developments

2018 Tax Reform

On 28 March 2018, the 2018 Tax Reform Act was approved by the Diet, and, on 31 March 2018, the 2018 Tax Reform Act, the Enforcement Orders, and Regulations were promulgated, which are effective for corporate tax years ending on or after 1 April 2018, in principle. The 2018 Tax Reform Act provides for tax measures to help improve corporate productivity by 'Internet of Things' (IoT) investment and increase salary income to revitalise the economy.

Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS) (MLI)

On 18 May 2018, the MLI was approved by the Diet. Although Japan has not yet deposited the ratification instruments to the Organisation for Economic Co-operation and Development (OECD), it is expected that Japan will deposit them by the end of September 2018 to enable the MLI (for Japan) to enter into force on 1 January 2018.

Consumption tax

Due to a tax amendment, the consumption tax increase that was originally scheduled to rise to 10% on 1 April 2017 was delayed to 1 October 2019; however, concessions have been introduced with lower rates for selected goods to lessen the burden for the lower income tax brackets. To cope with the multiple consumption tax rates, an invoicing method will be introduced, although not until 1 April 2023, with transitional measures in place for the three-year and six months interim.

Taxes on corporate income

A domestic corporation in Japan is taxed on its worldwide income, including foreign branch income, while 95% of dividends received by a company from a foreign company in which it has held at least 25% (or could be lower under relevant tax treaties) of the outstanding shares for a continuous period of six months or more can be excluded from the company's taxable income. *See the description of Dividend income in the Income determination section for more information*.

A foreign corporation is taxed only on its Japan-source income.

Corporation tax

The corporation tax rates are provided in the table below (effective from fiscal years beginning on or after 1 April 2016 and 1 April 2018).

	Corporation tax rate (%)	
Company size and income	**1 April 2016**	**1 April 2018**
Paid-in capital of over 100 million Japanese yen (JPY)	23.4	23.2
Paid-in capital of JPY 100 million or less, except for a company wholly owned by a company that has paid-in capital of JPY 500 million or more:		
First JPY 8 million *per annum*	15.0	15.0
Over JPY 8 million *per annum*	23.4	23.2

National local corporate tax

As of 1 April 2018, corporate taxpayers are obligated to file and pay the national local corporate tax at a fixed rate of 10.3% of their corporate tax liabilities. Previously, the national local corporate tax rate was 4.4%.

Standard enterprise tax (and local corporate special tax)

Enterprise tax is imposed on a corporation's income allocated to each prefecture. This allocation is generally made on the basis of the number of employees and number of offices in each location. The local corporate special tax, which is a rate multiplied by the income portion of enterprise tax, will be abolished from tax years beginning on or after 1 October 2019 and replaced by enterprise tax (including a size-based tax regime).

The standard rates of enterprise tax, including local corporate special tax, are shown below.

Taxable base	Enterprise tax (%)	Local corporate special tax
First JPY 4 million *per annum*	3.4	
Next JPY 4 million *per annum*	5.1	43.2% of the current enterprise tax
Over JPY 8 million *per annum*	6.7	

If the paid-in capital of a corporation is JPY 10 million or more and the corporation has places of business in more than two prefectures, the graduated rates above are not applicable.

For utilities and insurance companies, the standard tax rate is shown as follows:

Taxable base	Enterprise tax (%)	Local corporate special tax
Net revenue (net utility charges or net insurance premiums)	0.9	43.2% of the current enterprise tax

Size-based enterprise tax (and local corporate special tax)

Instead of the above general enterprise tax, a 'size-based' enterprise tax (*Gaikei Hyojun Kazei*) is applied to a company whose paid-in capital is more than JPY 100 million as of the year-end.

Factors such as the size of a corporation's personnel costs and its capital (the amount of paid-in capital) will determine the additional amount of tax payable. The existing profit-based enterprise tax will also continue to apply at the tax rates indicated below. Therefore, a loss company in Japan may be required to pay tax based on value-added activities and the corporation's paid-in capital.

The applicable standard rates are as follows:

	Size-based enterprise tax (%)	
Taxable base	**2015 Tax Reform**	**2016 Tax Reform and further amendments per the amendment bill**
Fiscal year beginning	1 April 2015	1 October 2019
Value added base	0.72	1.2
Capital base	0.3	0.5
Income base *		
First JPY 4 million	3.1 (1.6)	1.9 (0.3)
Next JPY 4 million	4.6 (2.3)	2.7 (0.5)
Over JPY 8 million	6.0 (3.1)	3.6 (0.7)
Local corporate special tax (the rate is multiplied by the income base of size-based enterprise tax), which is collected as national tax by filing corporate tax returns	93.5	414.2 **

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

** The local corporate special tax will be abolished from 1 October 2019 and replaced with an increase to the enterprise tax rate.

Inhabitant's tax

Inhabitant's tax is imposed on a corporation's income allocated to each prefecture and city (municipal borough). The allocation is generally made on the basis of the number of employees, in the same way as enterprise tax.

The standard tax rate is 3.2% as prefectural tax and 9.7% as municipal tax. However, the tax rate is increased to 4.2% for prefectural tax and 12.1% for municipal tax, depending upon the determination of each local government. From fiscal years beginning on or after 1 October 2019, the rate is increased as follows:

	Current		Expected from 1 October 2019	
Inhabitant's tax	**Standard rate (%)**	**Maximum rate (%)**	**Standard rate (%)**	**Maximum rate (%)**
Prefectural tax portion	3.2	4.2	1.0	2.0
Municipal tax rate	9.7	12.1	6.0	8.4
Local corporate tax rate	4.4		10.3	

In addition to the above, inhabitant's tax is imposed on a *per capita* basis, in the range from JPY 70,000 (in cases where the amount of paid-in capital is JPY 10 million or less and the number of employees in each prefecture and city is 50 or less) to JPY 3.8

million (in cases where the amount of paid-in capital is over JPY 5 billion and the number of employees in each prefecture and city is over 50). The inhabitant's tax amount is determined by the local government by the factors of paid-in capital and the number of employees.

Effective tax rate

The total corporate income tax burden (i.e. effective tax rate) varies depending upon the size of a company's paid-in capital. Since enterprise tax is deductible, the effective tax rate is less than the total of the statutory rates of corporation tax, inhabitant's tax, and enterprise tax.

The following is the summary of the effective applicable tax rates in the case of small and medium enterprises (SMEs) and large corporations operating in Tokyo (taking no thought of an additional-value-based tax and capital-based tax out of the enterprise tax above):

	Effective corporation tax rate (%)	
Tax year	**SMEs**	**Large corporations**
Beginning on or after 1 April 2016	34.81	30.86
Beginning on or after 1 April 2018	34.60	30.62

Corporate residence

Domestic and foreign corporation

A company that has its head office in Japan is a domestic corporation. The nationality of its shareholders or place of central management is not relevant.

A corporation other than a domestic corporation is regarded as a foreign corporation.

Permanent establishment (PE)

Under domestic tax law, the scope of Japan-source income in respect of which a foreign corporation is taxable depends upon the type of taxable presence that it has in Japan. Pursuant to the amendments of Article 5 of the OECD Model Tax Treaty (OECD MTC) in November 2017 and the signing of the MLI on 7 June 2017 by the Japanese government, articles related to the PE were revised by the 2018 Tax Reform. The articles of the Corporate Tax Law (CTL) and CTL Enforcement Ordinance (CTLEO) were revised to agree with the updated Article 5 of the OECD MTC. The revised definition of PE will apply to the tax years beginning on or after 1 January 2019. After the amendment, the types of taxable presence that a foreign corporation may have in Japan include the following:

- Branch, factory, other fixed places in which business is conducted in Japan, mine, quarry, building for rent, etc., but exclude a specified place used only for the purpose of storage, display, or delivery of goods or merchandise belonging to the enterprise and any other activity of a preparatory or auxiliary character (Direct PE).
- Construction, installation, assembly project, or supervisory services related thereto for a period of greater than one year, but exclude a specified place used only for the purpose of storage, display, or delivery of goods or merchandise belonging to the enterprise and any other activity of a preparatory or auxiliary character (Construction PE).

- A person other than an agent of an independent status (i.e. Agent PE) acting in a contracting state on behalf of an enterprise and has, and habitually exercises, in a contracting state, an authority to conclude contracts, in doing so, habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, and these contracts are:
  - in the name of the enterprise
  - for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use, or
  - for the provision of services by that enterprise.

  In the above case, the enterprise shall be deemed to have a PE in that state in respect of any activities that person undertakes for the enterprise, unless the activities of such person are limited to preparatory or auxiliary character.

  If a person acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, that person shall not be considered to be an independent agent.

As a matter of law, the articles of Japan's tax treaties have precedence over domestic tax law. By the amendments of the definition of PE under the domestic law, there may be some difference in the scope of PE from that of the existing tax treaties. Under the circumstances, the articles of the relevant tax treaties will override the above articles. Once a PE has been established for a foreign corporation under domestic law, all Japan-source income is taxable to the PE to the extent it is 'attributable to' the PE.

Other taxes

Consumption tax

Consumption tax (value-added tax or VAT) is levied when a business enterprise transfers goods, provides services, or imports goods into Japan. The applicable rate is 8%. As of 1 October 2019, the rate will increase to 10%. Exports and certain services to non-residents are taxed at a zero rate. Specified transactions, such as sales or lease of land, sales of securities, and provision of public services, are not subject to taxation.

Consumption tax paid by the business enterprise attributable to taxable revenue shall be creditable/refundable by filing the consumption tax return to the extent that such transaction is recorded in the accounting book and relevant invoices are kept.

In response to the increase in consumption tax rate to 10% from 1 October 2019, lower consumption tax rates on certain goods will be introduced. Also, in response to the multiple tax rates, an invoice system will be introduced from 1 April 2023. In the three-year and six months transitional period to the introduction of an invoice system, several measures will be implemented.

The lower consumption tax rate of 8% will still apply to food (excluding when purchased in restaurants) along with newspaper subscriptions where there is at least an issue twice per week. Until the invoice system is introduced, the credit for consumption taxes paid will follow the current method for tracking, where the lower tax rate on applicable items should be indicated in the invoice. With the increased administration cost of tracking the different rates, the simplified method of determining consumption taxes paid will be allowed.

After the new invoice system is introduced, qualified invoices issued by the registered businesses should be maintained for claiming credits of consumption taxes paid. Businesses (other than exempt entities) will need to file an application with their tax office to become qualified for issuing qualified invoices indicating details such as the business registration number, the applicable tax rate, etc.

Note that consumption tax is also imposed on the cross-border provision of digital services (e.g. e-books, music, and advertising) by foreign service providers. In this respect, a reverse-charge mechanism is applicable for business-to-business (B2B) transactions, and foreign service providers may need to register for consumption tax purposes with regard to business-to-consumer (B2C) transactions.

Also, Japanese sponsors are subject to a reverse-change system for sports or music/art attractions in Japan provided by foreign entertainment providers.

Customs duty

A customs duty is levied on imported goods based on the custom tariff table.

Excise taxes

Excise taxes were abolished by introduction of consumption tax.

Fixed assets tax

The annual fixed assets tax is levied by the local tax authorities on real property and depreciable fixed assets used for business purposes. Real property is taxed at 1.7% (standard rate including city planning tax) of the value appraised by the local tax authorities. The depreciable fixed assets tax is assessed at 1.4% of cost after statutory depreciation.

Stamp duty

A stamp duty is levied on certain documents prepared in Japan. The tax amount is generally determined based on the amount stated in the document.

Registration and licence tax

Registration and licence tax is levied where certain property is registered, at a rate from 0.1% to 2% of the taxable basis or at a fixed amount. The taxable basis depends upon the property being registered (e.g. the amount of paid-in capital registered by a company or the value of real estate as assessed by local tax authorities).

Payroll taxes

In general, the employer has an obligation to withhold payroll taxes monthly, and for annual year-end adjustment.

Labour and social insurance paid by employer

There are four types of insurance systems in Japan that enterprises employing workers that meet certain conditions must enrol in. Workers' accident compensation insurance is borne entirely by the employer. Employment insurance, health insurance/nursing care insurance, and employees' pension insurance is born by both the employer and employee.

The employer is generally liable to pay a share of the following contributions on salary or bonus, including fringe benefits, to be paid in Japan. The employer's share consists of the following contributions:

Contribution	Standard premiums on monthly salary	Standard premiums on bonus
Health insurance for the Metropolis of Tokyo (each prefecture has its own health insurance rate, and rates are slightly higher for individuals between the ages of 40 and 65)	5.735% (on a maximum of JPY 1,390,000 of wages per month)	5.735% (on an annual cap of JPY 5.73 million of irregular annual total payments)
Welfare pension, plus child allowance (1)	9.15% (on a maximum of JPY 620,000 of wages per month)	9.15% (on a maximum of JPY 1.5 million of irregular payments per month)
Employment insurance	0.90%	0.90%
Total (2)	14.921%	14.921%

Notes

1. The rate of 9.15% for welfare pension will be applied from September 2017. Premiums on child allowance will be imposed separately at 0.29%.
2. In addition, workers' accident compensation insurance will be imposed. The rate varies depending on the type of business.

Family corporation tax

If an individual shareholder together with family members own, either directly or indirectly, more than 50% of the total issued shares or voting rights of a Japanese corporation, the corporation is treated as a family corporation (with the exception of corporations with paid-in capital of JPY 100 million or less) and is subject to the family corporation tax in addition to corporation tax.

A family corporation is liable for an additional tax at the rates shown below on its undistributed current earnings in excess of specified limits.

Taxable undistributed current earnings	Family corporation tax rate (%)
First JPY 30 million *per annum*	10
Next JPY 70 million *per annum*	15
Over JPY 100 million *per annum*	20

Business premises tax

Business premises tax is levied and designated by each city in Japan, such as Tokyo, Osaka, Nagoya, Fukuoka, and other cities with a population of more than 300,000. A company that uses business premises in excess of 1,000 square metres and/or has more than 100 employees in a designated city is responsible to pay this tax based on the usage of the business (JPY 600 per square metre) and gross payroll (0.25% of gross payroll).

Branch income

Branch profits are taxed in the same manner as corporate profits. However, the family corporation tax does not apply to a branch of a foreign corporation. In addition, no withholding tax (WHT) is imposed on the repatriation of branch profits to the home office.

Income determination

The taxable income of a corporation is the aggregate income from all sources. There is no specific requirement to differentiate between the types of income. In principle, accounting for tax purposes follows Generally Accepted Accounting Principles (GAAP) in Japan, and income of a corporation is determined on an accrual basis.

Inventory valuation

Inventory cost should be determined by applying one of the following methods accepted for corporate tax purposes: actual individual cost, first in first out (FIFO), weighted average, moving average, most recent retail, selling price reduction, and lower of cost or market.

Capital gains

Capital gains and losses are classified as ordinary income and losses, respectively.

Under certain circumstances (e.g. qualified reinvestment, exchange property), taxes generally levied on capital gains may be deferred (i.e. provided rollover relief) as long as certain requirements are met. A special relief is available in the case of expropriation of real property by either the national or local government.

The recognition of capital gains or losses from the transfer of certain assets between group companies are to be deferred until the asset is transferred to another group company or a non-group company.

Dividend income

The threshold ownership percentage for corporate dividend exclusion is illustrated in the following table.

The holding period of six months or more until the fiscal year-end for which the dividend will be paid is required to apply the dividend income exclusion for the ownership of more than 1/3 to 100%. The dividend income exclusion for an ‘other domestic corporation‘ and ‘portfolio investment’ is allowed by reference to the ownership percentage as of the fiscal year-end for which the dividend will be paid.

Type of investment	Ownership %	Exclusion %
Wholly owned domestic subsidiary	100%	100%
Affiliated domestic corporation	More than 1/3	100% less allocable interest (1)
Other domestic corporation	More than 5% but less than 1/3	50%
Portfolio investment	Less than 5%	20% (2)
Exchange trust fund (ETF)		20% (treated as a portfolio investment)
Other investment trusts		0%

Notes

1. Under certain simplified calculations to determine allocable interest, the ‘base period’ is the fiscal years beginning between 1 April 2015 and 31 March 2017.
2. For dividends from portfolio investments received by insurance companies, the exclusion percentage will be 40%.

95% of dividends received by a company from a foreign company in which it has held at least 25% of the outstanding shares for a continuous period of six months or more, ending on the date on which the dividend is declared, can be excluded from the company's taxable income.

If the foreign company is resident in a country with which Japan has concluded a tax treaty for the avoidance of double taxation, and such treaty provides for the allowance of an indirect foreign tax credit for taxes paid by the foreign company on the profits out of which the dividend is paid where the company holds a certain percentage of the foreign company's outstanding shares (e.g. 10% based on the tax treaty between the United States [US] and Japan), that percentage will apply for the purpose of determining the availability of the above exemption to the extent that it is lower than 25%.

The BEPS Action Plan 2 proposed that measures be taken to neutralise the tax effects of so-called 'hybrid mismatch' arrangements where, because of differences in the treatment of certain payments between jurisdictions, an item of income is not taxed in either the payer or the payee country because the payment is deductible in the payer country but not taxable in the recipient country. Thus, the recommendation in the BEPS Action Plan is to modify local tax law in order for the recipient country to tax the receipt.

Before the 2015 amendment, any dividends received by a Japanese corporation from a foreign affiliate was 95% exempt from taxation in Japan regardless of the tax treatment in the payer country. This position was clarified in question and answer (Q&A) guidance issued by the National Tax Agency. Based upon the recommendation of the BEPS Action Plan 2, the 2015 Tax Reform Act excludes such types of dividends from the dividend exclusion regime. As a result, any dividends paid to Japanese corporate taxpayers under so-called 'mandatorily redeemable preferred shares' (MRPS) issued by Australian affiliates or by Brazilian affiliates where the dividends are paid in a manner similar to interest and deductible for Brazilian tax purposes will no longer be excluded from taxation in Japan.

To the extent any portion of the dividend is deductible for foreign tax purposes, the general principle is that all of the dividend should be taxable in Japan. However, if a portion of the dividend is not tax deductible in the foreign jurisdiction, dividend exclusion will be allowed only if the taxpayer discloses all of the appropriate information regarding the portion of the dividend that is not deductible in the foreign jurisdiction and backup details for the calculation in a timely filed tax return and maintains the relevant documents for inspection by the tax authorities.

Any foreign tax imposed on the taxable dividend in Japan will be eligible for foreign tax credit relief.

The new rules apply for any dividends received by a Japanese corporate taxpayer whose fiscal year began on or after 1 April 2016. However, if the Japanese corporate taxpayer owned the stock of the foreign affiliate as of 1 April 2016, dividends received for years beginning between 1 April 2016 and 31 March 2018 are subject to the old rules (i.e. still eligible for exclusion).

The WHT for dividends is applicable at a rate of 15% national tax and 5% local tax or 20% (national tax) depending on the type of stock from which the dividends were received, and a tax credit may also be available for such WHT. The WHT (national tax) is subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.

Interest income

Interest received is included in taxable income. If interest is subject to the foreign WHT, a foreign tax credit may be available for such WHT. The WHT for interest is applicable at a rate of 15% national tax and 5% local tax for interest paid to a non-resident. As with dividend income, the WHT (national tax) is subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037. Note that under the 2013 Tax Reform, only national tax will be withheld at source for interest income received on or after 1 January 2016 by a corporate recipient.

Royalty income

Royalty received is included in taxable income. If royalty is subject to the foreign WHT, a foreign tax credit may be available for such WHT. The WHT is applicable at a rate of 20% national tax for royalty paid to a non-resident.

Foreign income

A Japanese corporation is subject to Japanese corporate income taxes on its worldwide income. However, to avoid double taxation of foreign-source income, Japanese corporations are allowed to claim a tax credit against corporation and inhabitant's taxes for foreign income taxes paid directly. *See Foreign tax credit in the Tax credits and incentives section for more information*.

Undistributed profits of a foreign subsidiary (i.e. controlled foreign company [CFC]) to which an applicable tax rate is 30% (in case of a shell company) or 20% are included in the Japanese parent company's taxable income under certain conditions. *See Anti-tax haven (CFC) rules in the Group taxation section for more information*.

Deductions

Depreciation and amortisation

Depreciation is deductible in the calculation of taxable income for corporation tax purposes. Depreciable assets include tangible property (e.g. buildings, attachments to buildings, structures, machinery and equipment). Certain intangible assets are also eligible for amortisation (e.g. goodwill, patents, trademarks).

With regard to depreciation methods, a taxpayer may adopt one of the allowable methods for each of the type of depreciable property, except for buildings and structures and attachments to buildings. For selected structural improvements acquired on or after 1 April 2016, only the straight-line method will be permitted (i.e. the declining-balance accelerated depreciation method will no longer be allowed). Tangible property is generally depreciated using either the straight-line method or the declining-balance method. Intangible property is generally amortised under the straight-line method.

Useful lives for assets are set forth on the table in detail. For reference, the following is the brief table of useful lives for typical assets.

Types of assets	Useful lives (years)
Concrete buildings	21 to 50 (depending on uses)
Metal building	12 to 38 (depending on uses)
Electrical facilities and lighting	15
Heating and air conditioning	15
Motor vehicles	3 to 6 (depending on uses)
Personal computers	4
Digital telephone equipment	6
Machinery and equipment	3 to 22 (depending on uses)
Patents	8
Software	3 or 5 (depending on uses)

Start-up expenses

Start-up expenses, such as corporation organisation costs and opening costs (i.e. costs to begin business after the corporation is established), are treated as deferred assets and allowed to be amortised on a voluntary basis.

Interest expenses

Interest expenses on borrowing are deductible in the calculation of taxable income in principle. However, the interest payment to related parties in the corporate group may be disallowed to be deducted to some extent in certain cases. *See 'Thin capitalisation' and 'Interest expense deduction limitation' in the Group taxation section*.

Reserves

Reserves recorded in the books of accounts, except for reserves for doubtful receivables and return of goods not sold, are not deductible for corporate tax purposes.

Reserve for doubtful receivables

A reserve for doubtful receivables is available to SMEs, banks, insurance companies, and other similar financial corporations.

The deductibility of a reserve for doubtful receivables is limited by the following two components: (i) an estimate of irrecoverable amounts from a debtor and (ii) a calculation of the limit in the aggregate based on either the actual historical bad debt percentage or statutory percentage (reduced for large corporations), excluding the irrecoverable amount of receivable in (i) above.

Reserve for return of goods not sold

A deductible reserve for return of goods not sold is available to corporations such as publishers, wholesalers of books, and others, provided that the corporation sells the merchandise under an unconditional repurchase agreement.

Charitable contributions

Except for certain designated donations, the tax deduction for charitable contributions is limited to certain amounts, as follows:

Donation	Deduction limit
General donation	((0.25% of capital plus capital surplus) + (2.5% of income)) x 1/4

Donation	Deduction limit
Donation made to designated public purpose companies	((0.375% of capital plus capital surplus) + (6.25% of income)) x 1/2

Donations subject to this limitation include economic benefits considered to be given as a subsidy. Donations to foreign affiliates are not fully deductible.

In cases where a donation occurs between group companies (as defined), there will be no tax implications for either the donor or donee (i.e. no deduction for the donor and no taxation for the donee).

Directors' remuneration

The remuneration paid to directors is deductible only in the following four cases:

- Fixed monthly payments.
- Fixed payments (either cash amount or the number of shares or stock options) in accordance with an advance notice to the tax office.
- Performance bonuses, either in the form of cash, stocks, or stock options, paid in proportion to the company's earnings to directors who engage in the operation of the company's business, to the extent that certain requirements are met.
- Retirement compensation (where the amount is calculated by the service period but not on a performance basis).

If the amount of remuneration is deemed unreasonable by the tax authority, only the reasonable amount is deductible for tax purposes.

Entertainment expenses

In principle, entertainment expenses are not deductible for tax purposes. However, an SME, defined as a company with paid-in capital of JPY 100 million or less (except for a company wholly owned by a company that has paid-in capital of JPY 500 million or more after the group taxation regime is effective) may take a tax deduction up to the smaller of the actual disbursement for the entertainment expense or JPY 8 million. With regard to expenses for eating and drinking, a company may deduct such expenses as far as the expense does not exceed JPY 5,000 per person (excluding expenditures for internal purposes) for tax purposes.

Corporations are able to deduct 50% of the entertainment expenses for food and drink (excluding entertainment for internal purposes).

The above treatment is applicable to the fiscal years beginning before 31 March 2018.

Fines and penalties

Fines and penalties are not deductible.

Taxes

Enterprise tax and business premises tax are deductible in the calculation of the taxable income for corporation tax purposes on a cash basis. However, corporation tax and inhabitant's tax are not deductible. Fixed assets tax and other taxes are deductible, when assessed. Foreign income taxes also may be deductible if the Japanese corporation does not elect to claim a foreign tax credit.

Net operating losses

For corporation tax and enterprise tax purposes (indirectly for inhabitant's tax purposes), a tax loss can be carried forward to offset future income in the case that a taxpayer files a 'blue form' tax return (*see Tax returns in the Tax administration section*) or if the tax loss is incurred as a result of certain disaster events.

Based on the 2016 Tax Reform Act, changes in the limitation for the net operating loss deduction will be implemented over three years. Thereafter, the limitation will be reduced to 50%, although the limitation carryover period will be extended from the current nine years to ten years for losses incurred on or after years beginning on or after 1 April 2018. SMEs are not subject to the loss deduction limitation.

	Fiscal year 2015 (1)	Fiscal year 2016	Fiscal year 2017	Fiscal year 2018
Limitation ratio for large corporations	65%	60%	55%	50% (2)
Carryover period for loss utilisation as well as assessment by tax authorities and request for downward adjustment by taxpayer (assuming loss period financial documentation is maintained)	9 years	9 years	9 years	10 years (2)

Notes

1. For fiscal years beginning on or after 1 April 2015 and before 1 April 2016 in which the taxpayer claims a net operating loss deduction.
2. Applicable to tax losses incurred in fiscal years beginning on or after 1 April 2018.

Certain newly established corporations and companies coming out of a rehabilitation process will not be subject to the loss limitation rules for a certain period.

Type of corporation applicable	Years in which full deduction is allowable	Years where regular limitation applies even if full deduction otherwise allowable
Newly established corporations (1) and corporations coming out of the rehabilitation process (2)	Seven years from establishment of the corporation or seven years from the decision of the court to exit the rehabilitation process.	For years ending on or after (i) a company is listed on a stock exchange, or (ii) the company is deemed to be rehabilitated.

Notes

1. SMEs, 100% subsidiary of larger corporations, or 100% parent corporation after share transfer are excluded.
2. SMEs are excluded.

Where there is a change in ownership of a corporation followed by certain events, such as the cessation of business or a significant change in its business within a five-year period following a business acquisition, the utilisation of its tax loss is restricted.

Carryback of tax losses is generally available for one year for national corporation tax purposes. This carryback rule was suspended until the fiscal year ending 31 March 2018 (except in specified circumstances, e.g. year of liquidation).

No carryback of losses is allowed for enterprise tax and inhabitant's tax.

Payments to foreign affiliates

In order to support a deduction in Japan for expenses incurred by a foreign affiliate and charged to a Japanese corporation, in general, it should be demonstrated that the service arrangement between the foreign affiliate and the Japanese corporation satisfies arm's-length criteria for purposes of Japan's transfer pricing laws and regulations.

Generally, fees that are paid by a Japanese subsidiary to a foreign affiliate should be deductible for Japanese tax purposes if the following conditions are met:

- The services should have the same character as services that take place between non-related companies or such services are essential to Japan's activities.
- There is a written service agreement.
- The services were requested by the Japanese corporation.
- The rendering of services is documented with evidence (e.g. requests for services from the Japanese subsidiary, regular invoices sent by the foreign affiliate).
- The service charges are reasonable.

Group taxation

Consolidated tax regime

Under the consolidated tax regime, a consolidated group can report and pay national corporate income tax on a consolidated basis. A consolidated group may be formed by a Japanese parent company and its 100% owned (directly or indirectly) Japanese subsidiaries. The taxpayer may file an application to elect a consolidated group filing for tax purposes, but the election must include all of the parent's eligible subsidiaries. Once the election is made, the consolidated filing, in principle, cannot be revoked unless there is a specific event, such as an ownership change, that causes the qualifying conditions of a consolidated filing to fail or an application to discontinue the consolidated group has been approved by the Commissioner of the National Tax Agency (NTA).

The taxable income of the consolidated group is computed on a consolidated basis by aggregating the taxable income or losses of each member of the consolidated group followed by the consolidation adjustments. Profits from intra-group transactions, except for transfer of certain assets as defined, should be included in the aggregate taxable income. Gains or losses from the intra-group transfer of certain assets are deferred.

Pre-consolidation tax losses of a subsidiary can be carried forward into a consolidated tax group if certain conditions are met, but may only be offset against taxable income of the subsidiary for the calculation of consolidation income.

The consolidated national corporate income tax liability is determined by applying the corporate income tax rate to the consolidated taxable income and adjusted for consolidated tax credits. The total tax liabilities are allocated back to each member company. The parent company files the consolidated return and pays the national corporate income tax for the group; however, each member company remains jointly and severally liable for the consolidated group's total national corporate income tax liability.

Local corporate income taxes levied on member companies are paid on a separate company basis, but the amount of local tax payable may be affected because of the consolidated filing.

Group taxation regime

A group taxation regime is applicable to domestic companies that are wholly owned by a domestic company, foreign company, or individual ('group companies'). Unlike the consolidated tax regime, the group taxation regime automatically applies to group companies.

The key points of this regime are summarised as follows:

- The recognition of capital gains or losses from the transfer of certain assets (including the transfer of assets as a result of a non-qualified or taxable merger) between group companies is deferred until the asset is transferred to another group company or a non-group company. The scope of assets is the same as that under the tax consolidation system (i.e. fixed assets, land, securities, monetary receivables, and deferred expenses [excluding securities for trading purposes and assets with a book value of less than JPY 10 million]).
- Where a donation occurs between group companies, there are no tax implications for either the donor or donee (i.e. no deduction for the donor and no taxation for the donee). Note that this treatment is not applied to a group company owned by an individual. This is consistent with the treatment of a donation between members of a consolidated tax group.
- A dividend received from a group company can be fully excluded from taxable income without any reduction for allocable interest expense. This is consistent with the treatment of dividends between members of a consolidated tax group.

A group company that would otherwise qualify as an SME on a stand-alone basis is not eligible for SME benefits (e.g. reduced corporate tax rate, preferable allowable ratios for deductible portion of bad debt provisions, partial deductibility of entertainment expenses, carryback of tax losses) if the SME is owned by a parent company or two or more parent companies of the group that has paid-in capital of JPY 500 million or more.

Where a corporation that is a member of a 100% group is in the process of liquidation and is expected to be dissolved, any loss from the impairment or devaluation of the shares of the liquidating corporation cannot be recognised by the parent company as a tax deductible expense.

Transfer pricing

If a corporation that is subject to corporation tax sells property to or buys property from a foreign-related person, or provides services or conducts other transactions with a foreign-related person, and consideration is received or paid by the corporation, the transaction is required to be carried out at an arm's-length price for corporation tax purposes.

A foreign-related person is a foreign corporation that maintains certain special relationships with the subject corporation, such as parent-subsidiary, brother-sister, or substantial control relationship.

The arm's-length price for the sale or purchase of inventory may be determined using one of the following methods:

- Comparable uncontrolled price method.
- Resale price method.
- Cost plus method.
- Berry Ratio method.
- Other method (i.e. profit split method and transactional net margin method [TNMM]).

The 'most appropriate method' should be applied in order to calculate the arm's-length price.

An advanced pricing agreement (APA) system is available to confirm the arm's-length pricing system proposed by a taxpayer. In general, corporations entering into an APA are advised to file a request for mutual agreement procedures (MAP) in order to obtain the agreement of the competent authorities of each country.

In October 2015, the OECD released the final BEPS reporting package with Action 13 relating to transfer pricing and related documentation. Taking into consideration the compliance costs for taxpayers along with increased transparency, the 2016 Japan Tax Reform Act 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 (CbC) Report</td><td>Country revenue, pre-tax income, taxes payable, etc.</td><td rowspan="2">Must be e-filed within one year of the last fiscal day of the ultimate parent</td><td rowspan="2">Applicable for 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</td><td>By due date of tax return, to retain for seven years</td><td>Applicable for corporate tax in fiscal years beginning on or after 1 April 2017</td></tr>
</table>

Thin capitalisation

Interest paid on debt to controlling foreign shareholders is disallowed to the extent the average balance of debt on which that interest is paid is more than three times the equity of controlling foreign shareholders.

Interest expense deduction limitation

The deductible portion of a corporation's net interest expense to a related party is restricted to 50% of the adjusted income. The net interest is calculated as interest expense to related parties less corresponding interest income. The adjusted income is defined as taxable income, adding back interest expense, depreciation expense, and exempted dividend income but excluding extraordinary income or loss.

Anti-tax haven (controlled foreign company or CFC) rules

Undistributed profits of a foreign subsidiary (i.e. CFC, which is defined as a foreign related corporation by [i] equity ownership test [owned more than 50% by Japanese corporations or residents] or [ii] de facto control test) to which an applicable tax rate is 30% (in case of a shell company) or 20% are included in the Japanese parent company's taxable income under certain conditions.

In the 2017 Tax Reform, major changes were made considering the BEPS recommendations to shift to a more of an income-based approach (although elements of the entity approach remain). After the amendments, income earned by a CFC is 'aggregated' (i.e. included within Japanese taxable income) in three different ways:

- Entity-based aggregation where all of the income of a CFC is taxable to a Japanese shareholder if (i) the main business of the foreign-controlled subsidiary is not 'active' (as defined) and (ii) the foreign tax rate is lower than a 20% 'trigger' rate.
- Entity-based aggregation where all of the income of a CFC is taxable to a Japanese shareholder if (i) the CFC fails certain 'substance' and 'administration and control' tests and is thereby treated as a 'paper company' or 'cash box company', and (ii) the foreign tax rate is lower than a 30% 'trigger' rate.
- Income-based aggregation where, even if the above entity-based aggregation rules do not create income inclusion on an entity basis, the relevant income of a CFC is taxable to a Japanese shareholder if (i) income of the CFC includes certain 'passive' categories of income and (ii) the foreign tax rate is lower than a 20% 'trigger' rate.

A Japanese corporation owning a 10% or more direct or indirect interest in a CFC is required to include its pro-rata share of the taxable retained earnings of the CFC in its gross income under certain circumstances.

A dividend paid by a CFC is not deductible when calculating its undistributed income.

The new rules apply for fiscal years of foreign subsidiaries starting on or after 1 April 2018.

Tax credits and incentives

Foreign tax credit

A Japanese corporation is subject to Japanese corporate income taxes on its worldwide income. However, to avoid double taxation of foreign-source income, Japanese corporations are allowed to claim a tax credit against corporation and inhabitant's taxes for foreign income taxes paid directly.

Creditable foreign taxes are defined as taxes that (i) are incurred directly by the taxpayer; (ii) are levied by foreign governments and local authorities in accordance with local tax laws; (iii) are levied on corporate income; and (iv) have the same characteristics as Japanese income tax, corporation tax, and local income-based taxes. A tax for which a refund can be claimed optionally by the taxpayer after the tax payment, or a tax whose payment grace period can be decided by the taxpayer, is not regarded as a foreign tax.

In order to prevent the credit from reducing corporation tax on Japan-source income, certain limitations are set on the amount of foreign taxes that can actually be credited. The ceiling is currently 35% for the foreign taxes paid.

A foreign tax credit is not applicable for enterprise tax purposes, although foreign branch income attributable to a business executed outside Japan is exempt from enterprise tax.

Generally speaking, the foreign tax credit system does not apply to the extent the dividend income from the foreign subsidiary is subject to the dividend exemption system.

Foreign corporations with a PE in Japan should note that when a foreign corporation's PE in Japan is subject to taxation in Japan as well as in jurisdictions other than its country of residence, double taxation may arise. To alleviate an unfair tax burden, a foreign tax credit regime is also applicable to PEs in Japan similar to that which applies to Japanese corporations. However, foreign tax (including WHT) paid in the enterprise's country of residency would not, in principle, be creditable under consequential changes to the foreign tax credit regime.

Tax credit for research and development (R&D) cost

Pursuant to the 2015 Tax Reform, the R&D tax credit system was amended whereby the credit limit was increased and the 'Open Innovation' type R&D credit was expanded. The 2017 Tax Reform was built on these changes as follows:

- The credit rates will increase in line with an increase of R&D expenditures.
- R&D expenditures to develop certain kinds of new service-type businesses will be brought within the scope of the R&D tax credit in order to support the development of new business opportunities from the 'Internet of Things' (IoT), 'Big Data', artificial intelligence (AI), etc.
- Conditions for claiming the 'Open Innovation' type of R&D credit will be relaxed.

The amendments apply for tax years beginning on or after 1 April 2017.

Salary increase tax credits

Under the 2018 Tax Act, the salary increase tax credits are amended for large corporations so that only those corporations increasing domestic investment would be eligible for the credits. The salary increase tax credits will be available for corporations filing 'blue form' tax returns that meet the conditions described below. The revised salary increase tax credit rules will be applicable for fiscal years beginning on or after 1 April 2018 until 31 March 2021.

		Before the amendments	**After the amendments**
Conditions	1	(Increased salary payment / Salary payment to employees in base year) ≥ 5%	Abolished
	2	Salary payment in the current fiscal year ≥ Salary payment in the preceding fiscal year	Salary payment in the current fiscal year ≥ Salary payment in the preceding fiscal year
	3	(Average salary payment in the current fiscal year – Average salary payment in the preceding fiscal year) / Average salary payment in the preceding fiscal year ≥ 2%	(Average salary payment in the current fiscal year – Average salary payment in the preceding fiscal year) / Average salary payment in the preceding fiscal year ≥ 3%
	4	N/A	Domestic capital expenditure ≥ 90% x Total depreciation
Tax credit		10% of the increased salary payment + 2% of the salary payment made in the preceding year	15% of increased salary payment (20% if training costs have increased by 20% or more)
Limitation on tax credit		Up to 10% of the corporate tax liability	Up to 20% of the corporate tax liability

Internet of Things (IoT) investment tax incentive

A tax incentive (either accelerated depreciation or tax credit) for costs related to the development of certain data gathering and analytic information systems under the Special Measures Act for the Improvement of Productivity (Productivity Act) is available to companies that file blue form tax returns and have obtained approval of an 'innovative data utilization plan'. Companies will be eligible for either accelerated depreciation (30%) or tax credit (3% or 5%) if they have acquired software as well as machinery or equipment worth JPY 50 million or more pursuant to the approved plan. The IoT investment tax incentive will be applicable from the effective date of the Productivity Act (6 June 2018) until 31 March 2021.

The amount of tax credit available will be higher for companies that satisfy a 'salary increase condition' (i.e. the average salary for employees of the company is increased for the year by more than 3%).

Special tax treatment for investment in certain equipment

SMEs filing 'blue form' tax returns may elect, under certain conditions, to claim accelerated depreciation of 100% of the base acquisition cost or a special tax credit equivalent to 10% of the base acquisition cost on designated equipment to the extent that it is acquired between 1 April 2014 and 31 March 2019. The maximum tax credit is limited to 20% of the taxpayers' corporate tax liability.

The 'Incentive for New Investment into Production Facilities' is applicable to any industry that invests in new production facilities (30% special depreciation or 3% tax credit on acquisition cost, up to 20% of corporate tax liability, etc., and subject to certain conditions). In addition, an investment incentive applies to SMEs that invest in equipment and furnishings pursuant to certain facility remodelling (30% special depreciation or 7% tax credit on acquisition cost, up to 20% of corporate tax liability [one-year carryforward of any excess], and subject to certain conditions). The SME tax incentive is granted to an SME engaged in the distribution, retailing, service, and/or agriculture business. This incentive is effective for tax years beginning on or after 1 April 2013 through 31 March 2019.

Incentive for venture capital investment

To assist venture capital investment, certain procedures to accredit venture capital partnerships were legislated in the Industrial Competitiveness Enhancement Law. Investment tax incentives were also introduced to allow corporate investors the ability to take a loss from a venture capital investment on an accelerated basis compared to current rules. A qualified investor is allowed to deduct a tax reserve for the investment loss at up to 50% of the book value of the investment. This incentive is effective for investors into a qualified partnership designated on or before 31 March 2019.

Incentives for the revitalisation of local 'hubs'

A taxpayer is eligible for certain tax incentives if it relates to or expands certain kinds of operations in local areas (generally other than Tokyo, Osaka, or Nagoya). Details as to the kinds of operations eligible will be included in a future Revised Regional Revitalization Law.

Any qualifying investments have the following depreciation incentives with respect to investments in buildings:

Depreciation incentives	Investment pursuant to an approved relocation plan	Investment pursuant to expanding an existing operation
Type of depreciation (if plan is approved prior to 31 March 2020 and asset is acquired within two years of approval).	Additional first year depreciation of 25% of the acquisition cost (depreciation is accelerated).	Additional first year depreciation of 15% of the acquisition cost (depreciation is accelerated).

Alternatively, a taxpayer may choose to take a tax credit rather than accelerated depreciation, as follows:

Tax credits	Investment pursuant to an approved relocation plan	Investment pursuant to expanding an existing operation
Tax credits (if plan is approved prior to 31 March 2020 and asset is acquired within two years of approval)	Acquisition costs x 7%	Acquisition costs x 4%

Minimum investment is JPY 20 million for large corporations and JPY 10 million for SMEs.

Alternate to the investment incentive above, an employment-related tax credit is allowed for increased employment in a local hub if hired within two years of the plan approval. The credit shall be JPY 500,000 times the number of increased employees at a maximum (if certain conditions are not met, the credit becomes JPY 200,000 per employee).

In either tax incentive, the amount of the above tax credits can only offset up to 20% of a corporation's tax liability.

Local government contributions

As part of the Regional Revitalization Act, 'blue form' corporate tax filers who make donations to approved regional donation plans up until 31 March 2020 will be able to claim a tax credit against corporate, enterprise, and inhabitant's taxes in addition to taking a deduction from the corporate tax. This is known as the corporate hometown tax, or *furusato nozei* system.

National strategic zones

For a 'blue form' filing corporation with an approved plan for qualified investment in a National Strategic Special Area up until 31 March 2020, a deduction of 20% of income is available for five years from the date of establishment.

Withholding taxes

Tax treaty network

As of 1 June 2018, Japan has entered into 70 tax treaties with 123 countries and/or regions. Companies making certain payments are required to withhold income taxes using the following rates.

	WHT (%)			
	Dividends			
Recipient	Portfolio (3)	Substantial holdings (1)	Interest	Royalties (2)
Japanese corporations	20	20	0/20 (4)	0
Resident individuals	20	20	0/20 (4)	0
Foreign corporations, non-resident individuals:				
Non-treaty (5)	15/20 (3)	20 (3)	0/15/20 (4)	20
Treaty (6):				
Australia	10	0/5	10	5
Austria	20	10	10	10
Bahamas (7)	-	-	-	-
Bangladesh	15	10	10	10
Belgium (25)	15	10	10	10
	10	0	0/10 (27)	0
Bermuda (7)	-	-	-	-
Brazil	12.5	12.5	12.5	12.5/15/25 (8)
British Virgin Islands (7)	-	-	-	-
Brunei	10	5	10	10
Bulgaria	15	10	10	10
Canada	15	5	10	10
Cayman Islands (7)	-	-	-	-
China, People's Republic of	10	10	10	10
Czechoslovakia (former) (9)	15	10	10	0/10 (9)
Denmark (25)	15	10	10	10
	5/15 (28)	0	0	0
Egypt	15	15	15/20 (10)	15/20 (10)
Estonia (25)	10	0	0/10 (29)	0
Finland	15	10	10	10
France	10	0/5 (30)	10	0
Germany	5/15 (31)	0 (31)	0	0
Guernsey (7)	-	-	-	-
Hong Kong	10	5	10	5
Hungary	10	10	10	0/10 (11)
Iceland (25)	5/15 (32)	0 (32)	0	0
India	10	10	10	10 (12)
Indonesia	15	10	10	10
Ireland, Republic of	15	10	10	10
Israel	15	5	10	10
Italy	15	10	10	10
Jersey (7)	-	-	-	-
Kazakhstan	15	5	10	5 (13)
Korea, Republic of	15	5	10	10
Kuwait	10	5	10	10
Latvia (26)	0	0	0	0
Liechtenstein (7)	-	-	-	-
Lithuania (25)	0	0	0	0
Luxembourg	15	5	10	10
Macao (7)	-	-	-	-
Malaysia	15	5	10	10

Recipient	WHT (%) Dividends Portfolio (3)	Dividends Substantial holdings (1)	Interest	Royalties (2)
Man, Isle of (7)	-	-	-	-
Mexico	15	0/5 (14)	10/15 (14)	10
Netherlands	10	0/5 (15)	0/10 (15)	0
New Zealand	15	0	10	5
Norway	15	5	10	10
Oman	10	5	0/10 (33)	10
Pakistan	10	5/7.5 (16)	10	10
Panama (7)	-	-	-	-
Philippines	15	10	10	10/15 (17)
Poland	10	10	10	0/10 (11)
Portuguese Republic	10	5	0/5/10 (34)	5
Qatar	10	5	0/10 (35)	5
Romania	10	10	10	10/15 (18)
Samoa (7)	-	-	-	-
Saudi Arabia	10	5	0/10 (36)	5/10 (19)
Singapore	15	5	0/10 (36)	10
Slovenia (26)	5	5	0/5 (37)	5
South Africa	15	5	10	10
Spain	15	10	10	10
Sri Lanka	20	20	0/15/20 (20)	0/10 (20)
Sweden	10	0 (21)	0	0
Switzerland	10	0/5	0/10 (35)	0
Taiwan	10	10	0/10 (38)	10
Thailand	15 (3)	15/20 (22)	10/25 (22)	15
Turkey	15	10	10/15 (23)	10
USSR (former) (24, 25)	15	15	10	0/10 (24)
	10/15 (39)	5 (39)	0	0
United Arab Emirates	10	5	10	10
United Kingdom	10	0	0	0
United States	10 (40)	0/5 (40)	0/10 (41)	0
Vietnam	10	10	10	10
Zambia	0	0	10	10

Notes

1. The tax treaty rates apply only to corporate shareholders. The applicable treaty should be checked for conditions required to claim the reduced rate. Note that WHT may be subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.
2. The applicable treaty should be reviewed because certain tax treaties exclude film royalties and/or gain from copyright transfer from taxable income. Note that WHT may be subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.
3. 15% for publicly traded shares (for non-resident individual, only applicable to minority interest [less than 3% ownership]) and investment trusts. Note that WHT may be subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.
4. Interest on bank deposits and/or certain designated financial instruments is subject to a 15% national WHT and 5% local inhabitants WHT (20% combined). Taxation of such interest is fully realised by tax withholding, so resident individuals are not required to aggregate such interest income with other income. Interest on loans made by resident individuals is not subject to WHT; instead, it is taxed in the

aggregate with other income. Such WHT is subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.

5. Dividends, interest, and royalties earned by non-resident individuals and/or foreign corporations are subject to a 20% national WHT under Japanese domestic tax laws in principle. An exceptional rate of 15% is applied to interest on bank deposits and certain designated financial instruments. Interest on loans, however, is taxed at a 20% rate. A special exemption from WHT applies to certain long-term corporate bonds issued to non-residents in foreign countries. Note that WHT may be subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.
6. Tax treaties with many countries provide reduced tax rates, as indicated. Some treaties, however, provide higher tax rates (e.g. Brazil, Thailand) or do not provide rates (e.g. Egypt, New Zealand). In these instances, rates specified under Japanese domestic tax laws apply. Each treaty should be consulted to see if a reduced rate for dividends (in the case of substantial holdings) is applicable.
7. The tax treaty was concluded mainly for the purpose of information exchange.
8. The tax treaty with Brazil provides a 25% tax rate for certain royalties (trademark). However, the WHT rate cannot exceed 20.42% (including the income surtax of 2.1%) on any royalties to be received by a non-resident taxpayer of Japan under Japanese income tax law. Film royalties are taxed at 15%. Any other royalties are taxed at 12.5%.
9. The treaty with the former Czechoslovakia is applied to the Czech Republic and the Slovak Republic. It stipulates that cultural royalties are tax exempt.
10. In the tax treaty, no rate on interest is specified, therefore Japanese domestic rate is applied. Film royalties are taxed at 20%, and other royalties are taxed at 15%.
11. Cultural royalties are tax exempt.
12. The rate of 10% for royalties includes consideration for technical services.
13. The rate for royalties is reduced from 10% to 5% by Protocol.
14. Dividends received from subsidiaries, by parent companies that have met certain conditions, are exempt from WHT. Interest received by government and other specific entities is exempt. Interest received by banks, financial institutions, or paid as a consequence of sale on credit of any equipment is subject to 10% WHT. Any other interest is taxed at 15%.
15. Dividends received from subsidiaries for which the parent company has 50% or more shareholding are tax exempt. Interest received by government and other specific entities, or paid as a consequence of sale on credit of any equipment, merchandise, or service, is tax exempt.
16. A 5% rate is applied to a company that has 50% or more shares with direct voting rights, and a rate of 7.5% is applied to a company that has 25% or more shares with direct voting rights.
17. Film royalties are taxed at 15%. Any other royalties are taxed at 10%.
18. Cultural royalties are taxed at 10%.
19. Royalties paid for the use of certain equipment are taxed at 5%.
20. Interest paid to financial institutions is tax exempt, as well as film and copyright royalties. Patent royalties are subject to a 10% rate.
21. If certain conditions for beneficial owners are met, dividends are taxable only in the contracting state of which the beneficial owner is a resident.
22. Dividends paid by a corporation that is engaged in industrial undertakings are taxed at 15%. Interest paid to financial institutions is taxed at 10%.
23. Interest paid to financial institutions is taxed at 10%.
24. The treaty with the former USSR is applied to Armenia, Azerbaijan, Belarus, Georgia, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan. It stipulates that cultural royalties are tax exempt.
25. The new treaty was signed but has not yet become effective.
26. The treaty will apply with respect to taxes levied on the basis of a taxable year for taxes for any taxable years beginning on or after 1 January 2018 and with respect to taxes not levied on the basis of a taxable year for taxes levied on or after 1 January 2018.
27. Exempted when paid and beneficially owned by enterprises, etc; 10% for others.
28. Exempted when paid by a company of Japan, holding at least 10% of voting power for six months, or beneficially owned by pension funds; 15% for others.
29. Exempted when received by governments, etc.; 10% for others.
30. Exempted when paid by a company of Japan, holding at least 15% (direct or indirect) or 25% (direct) shares for six months; 5% for holding at least 10% (direct or indirect) shares for six months.
31. Exempted when holding at least 25% for 18 months; 5% when holding at least 10% for six months; 15% for others.
32. Exempted when holding at least 25% of voting shares for six months or beneficially owned by pension funds; 5% when holding at least 10% of voting shares for six months; 15% for others.
33. Exempted when received by governments, etc.; 10% for others.
34. Exempted when received by governments, etc.; 5% when received by banks; 10% for others.
35. Exempted when received by governments, financial institutions, etc.; 10% for others.
36. Exempted when received by governments or central bank, 10% for others.
37. Exempted when received by governments, etc.; 5% for others.
38. Exempted when received by governments, etc., 10% for others.
39. Exempted when received by beneficially owned by pension funds; 5% when holding at least 15% of voting power for 365 days; 15% when shares deriving at least 50% of their value from immovable property; 10% for others.
40. Exempted when holding more than 50% of voting shares for 12 months or beneficially owned by pension funds; 5% when holding at least 10% of voting shares; 10% for others.

41. Exempted when received by governments or financial institutions; 10% for others.

Tax administration

Taxable period

The tax year is the corporation's annual accounting period specified in its articles of incorporation. A Japan branch of a foreign corporation must use the same accounting period that is adopted by the corporation in its home country.

Tax returns

Corporate income tax returns (i.e. the national corporation tax return, enterprise tax return, and local inhabitants' tax return) are self-assessment tax returns.

If a corporation meets certain conditions, such as keeping certain accounting books, and makes an application for it in advance, it is allowed to file a 'blue form' tax return. A 'blue form' filing corporation may benefit from loss carryforward and other benefits.

A corporation (including a branch) is required to file the final tax return within two months after the end of its annual accounting period. If a corporation cannot file the final return because of specific reasons, the due date of the final return may be extended by up to four months (a corporation should be a company subject to the statutory financial audit as required in the corporate law) with the tax authority's approval.

Payment of tax

Income taxes payable on the final corporate income tax return should be paid on or before the filing due date of the final tax returns (usually two months after the end of the corporation's accounting period). If an extension of time for filing is granted, the taxes may be paid on or before the extended due date with interest accrued at a rate of 1.8% (for the year 2018) *per annum* for the period from the day following the original due date (i.e. two months after the end of an accounting period) to the date of the actual payment.

Provisional tax payments are required for a corporation that has a fiscal period longer than six months. Provisional taxes generally are computed as one-half of the tax liabilities for the previous year, but they may be reduced by the filing of interim tax returns that reflect semi-annual results of the operations. The provisional tax payment is required to be made within two months after the end of the sixth month of the corporation's accounting period.

Penalties

If the tax return is filed late, a late filing penalty is imposed at 15% to 20% of the tax balance due. In the case that a corporation voluntarily files the tax return after the due date, this penalty may be reduced to 5%. The rate is increased to 15% (for non-filing) and 10% (for amendment filing) once the tax audit notice is received.

An under-payment penalty is imposed at 10% to 15% of additional tax due. In the case that a corporation amends a tax return and tax liabilities voluntarily after the due date, this penalty may not be levied.

In addition, interest for the late payment of tax is levied at 2.6% *per annum* for the first two months and increases to 8.9% *per annum* thereafter (for the year 2018).

Consolidated taxation

The parent company will file the consolidated tax return and pay national corporate income tax for the group. The consolidated tax return and payment due dates are the same as previously discussed; however, the due date of the final return may be extended for two months.

For local corporate income taxes, each member of the consolidated group must separately file the returns and pay the taxes.

Tax audit process

Generally speaking, corporate tax audit is performed in cycles of three to five years' duration. However, this period may be shortened in the case that some significant tax matters were pointed out in the prior audit and so on. If taxpayers request a downward correction, a tax audit will be performed to make sure of it.

With regard to tax audit procedures, tax laws have not clarified them thus far. Prior to conducting a tax audit, in principle, tax agents are required to notify taxpayers, and, upon completion of tax audits, tax agents are required to provide to taxpayers a brief written summary of their findings, etc.

Once an audit is complete, the basic principle is that a second audit is not allowed. However, if newly acquired information is obtained by the tax authorities that lead them to conclude that the reported taxable income should have been different, then the tax authorities can conduct another audit of the taxpayer. This limitation on the ability of the tax authorities to conduct a second audit only applies if the first audit was conducted on-site. If a 'desk audit' is only conducted, where the tax authorities do not conduct the audit on-site, no limitation applies.

Statute of limitations

The statute of limitations to request a downward correction of prior year tax liabilities is five years (six years for transfer pricing) from when the original tax return was filed.

The statute of limitations with regard to upward corrections by the tax authorities is also five years (six years for transfer pricing).

Topics of focus for tax authorities

Tax authorities are often focusing on cross-border, inter-company transactions (i.e. transfer pricing or donation issues), PE, and significant group restructuring, among other issues. Any developments in discussion on the G20/OECD BEPS project will also be of great interest for Japanese authorities.

Other issues

Requirement for banks to collect and remit information regarding bank accounts owned by non-residents

A tax reporting system is applicable under which individuals are required to report information to the relevant branch of the financial institution, which will, in turn, submit such information to the tax authorities in Japan.

The person who contracts with the financial institution for a deposit to a bank account in Japan on or after 1 January 2017 is required to report the relevant information to the bank, including (i) name, (ii) address, (iii) date of birth, and (iv) resident country. If the resident country is outside Japan, the individual is required to report the taxpayer identification number in the taxpayer's resident country. The financial institution is required to report the individual information collected as well as details regarding the account (balances, transactions, etc.) as of 31 December by the following 30 April.

Corporate tax measures for reorganisations

Corporate spin-offs

Corporate demerger

Before the 2017 Tax Reform, a corporate demerger by a corporation with many shareholders where the shares in the new company are given to the shareholders does not qualify as a tax qualified demerger. These rules are relaxed under the 2017 Tax Reform Act whereby a spin-off of a specific business by a corporation without a controlling shareholder becomes tax qualified under certain conditions.

Distribution in kind

Before the 2017 Tax Reform, a distribution in kind by a corporation with many shareholders is not tax qualified. Under the 2017 Tax Reform Act, a spin-off conducted as a distribution in kind of shares in a 100% subsidiary becomes tax qualified under certain conditions.

Minority shareholder squeeze-outs

Under the 2017 Tax Reform Act, creating a 100% subsidiary through a squeeze out process using shares with compulsory acquisition rights, share consolidation, and a request to sell back shares, is considered a type of corporate reorganisation. As part of bringing such squeeze outs within the corporate reorganisation framework, special measures will be introduced, including mark-to-market rules and the special rules on consolidated taxation.

In a merger or share-for-share transfer, if the merging corporation or the 100% parent corporation owns 2/3 or more of the merged corporation or the 100% subsidiary, consideration other than shares can be provided to minority shareholders without disqualifying the corporate reorganisation.

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Significant developments

The main focus of the 2018 Corporate Income Tax Law (CITL) reform is to encourage job creation by reforming the existing tax credits for corporate investment to create jobs and additional incentives to stimulate youth employment. Another focus is placed on strengthening the collection of income tax on high-income earners by expanding tax revenue sources through raising the CIT rate for taxable income over 300 billion Korean won (KRW). In addition, the reform proposals include significant changes that would affect cross-border transactions of multinational companies. In the government's commitment to implement the Organisation for Economic Co-operation and Development's (OECD's) recommendations under the base erosion and profit shifting (BEPS) project, the proposals contain new rules to restrict the deduction for hybrid financial instruments and interest expense deductions.

Taxes on corporate income

Resident corporations are taxed on their worldwide income, whereas non-resident corporations with a permanent establishment (PE) in Korea are taxed only to the extent of their Korean-source income. Non-resident corporations without a PE in Korea are generally taxed through a withholding tax (WHT) on each separate item of Korean-source income (*see the Withholding taxes section*).

The following tax table summarises the CIT rates applicable for the fiscal year starting on or after 1 January 2018:

Tax base (KRW million)		Tax rate *	
Over (column 1)	**Less than**	**Tax on column 1 (KRW) ***	**Marginal tax rate (%)**
0	200	0	10
200	20,000	20	20
20,000	300,000	3,980	22
300,000		65,580	25

* Before applying the local income tax.

Additional tax on corporate income

The tax reform has provided that the 10% additional tax provision introduced in 2015 to facilitate the use of corporate retained earnings to fund facility investment, payroll increase, and dividend payment, which was supposed to be terminated by the end of December 2017, has been extended for three additional years until the end of December 2020 and raised tax rates to 20%. The additional tax shall apply to companies whose net assets exceed KRW 50 billion (excluding small and medium-sized enterprises [SMEs]) and companies belonging to business groups subject to restrictions on cross-shareholdings under the Act on Monopoly Regulation and Fair Trade.

Companies should elect one of the following methods in computing the additional tax:

- ([adjusted taxable income for the year x 65%] - the total amount of facility investment, wage increases, and mutual cooperation payments) x 20%, or
- ([adjusted taxable income for the year x 15%] - the total amount of wage increases and mutual cooperation payments) x 20%.

Agriculture and fishery surtax

When a corporate taxpayer claims certain tax credits or exemptions under the Special Tax Treatment Control Law (STTCL), a 20% agriculture and fishery surtax is levied on the reduced CIT liability.

Minimum tax

Corporate taxpayers are liable for the minimum tax, which is defined as the greater of 10% (if the tax base is KRW 10 billion or less, 12% on the tax base exceeding KRW 10 billion but not more than KRW 100 billion, 17% on the tax base exceeding KRW 100 billion) of the taxable income before certain tax deductions and credits pursuant to the STTCL or the actual CIT liability after various deductions and credits.

For SMEs, the minimum tax is the greater of 7% of taxable income before certain tax deductions and credits or actual CIT liability after the deductions and credits. For middle market companies that exceed the size of SMEs (so-called 'medium-scale companies'), an 8% minimum tax rate is applicable for the first three years, starting from the year when the size exceeds an SME for the first time, and a 9% rate is applicable for the next two years.

Local income tax

The local income tax is a separate income tax that has its own tax base, tax exemption and credits, and tax rates. The local income tax rates for corporations are 1% on the first KRW 200 million, 2% for the tax base between KRW 200 million and KRW 20 billion, 2.2% for the tax base between KRW 20 billion and KRW 300 billion, and 2.5% for the excess.

Corporate residence

A corporation having its head office or principal office in Korea is a resident corporation. A corporation with a place of effective management in Korea is also treated as a resident corporation.

Permanent establishment (PE)

A non-resident corporation is generally deemed to have a tax presence (i.e. PE) in Korea in the following cases, among others:

- It has any fixed place of business in Korea, where the business of the entity is wholly or partly carried on.
- It is represented by a dependent agent in Korea, who has the authority to conclude contracts on its behalf and who has repeatedly exercised that authority.

- Its employee(s) provides services in Korea for more than six months within 12 consecutive months.
- Its employee(s) continuously or repeatedly renders similar services in Korea for two or more years, even if each service visit is for less than six months within 12 consecutive months.

Exceptions to a PE in Korea for a non-resident corporation include fixed places of business used only for purchasing or storage of goods, advertising, publicity, collecting or furnishing of information, or other activities that are preparatory or auxiliary in nature.

Other taxes

Value-added tax (VAT)

VAT is levied at a rate of 10% on the supply of goods and services, except zero-rated VAT on certain supply of goods and services (e.g. goods for exportation, certain eligible services rendered to non-residents earning foreign currency, international transportation service by ships and aircraft) and exemption on certain goods and services (e.g. basic life necessities and services, such as unprocessed foodstuffs and agricultural products; medical and health services; finance and insurance services; duty-exempt goods).

Electronic VAT invoicing is a compulsory requirement. If a taxpayer fails to issue the electronic VAT invoice or report electronically to tax authorities, the relevant penalties shall be imposed.

Customs duties

Customs duties are generally assessed on imported goods. 'Importation' refers to the delivery of goods into Korea (in case of goods passing through a bonded area, delivery of such goods into Korea from such a bonded area) to be consumed or to be used in Korea.

Property tax

An annual property tax ranging from 0.07% to 5% is charged on the statutory value of land, buildings, houses, vessels, and aircraft. Five times the property tax rate is applied to factories that are newly constructed or expanded in a designated metropolitan area for the first five years.

Securities transaction tax

Securities transaction tax (at the rate of 0.5% for unlisted shares or interest) is imposed on the transfer of shares or interest, but the government is authorised to adjust the tax rate in certain circumstances. The flexible tax rate prescribed by the Presidential Decree is 0.3% (including 0.15% of agriculture and fishery surtax) for shares traded on the Korea Stock Exchange and 0.3% for shares traded on the Korean Securities Dealers Automated Quotations (KOSDAQ) or the Korea New Exchange (KONEX).

Acquisition tax

Acquisition tax is charged on the price of real estate, motor vehicles, construction equipment, golf membership, boats, etc. The acquisition tax rate varies depending on the type of assets subject to the tax, ranging from 2% to 7%. A weighted rate is charged on acquisitions in a designated metropolitan area or on acquisition of luxury items, such as villas, golf courses, and yachts.

Stamp tax

Stamp tax is levied on a person who prepares a document certifying establishment, transfer, or change of rights to property in Korea. The stamp tax ranges from KRW 50 to KRW 350,000, depending on the type of taxable document. The electronic stamp system has been implemented to make it mandatory to use stamps bought online rather than paper stamps bought in banks or post offices.

Registration tax

Registration tax ranging from 0.02% to 5% is charged upon the act of registering the creation, alteration, or lapse of property rights or other titles and incorporation with the concerned authorities. Registration tax upon the registration of title or right and incorporation for corporations located in a designated metropolitan area may be subject to three times the normal rate of 0.4%.

Gift tax

Gift tax is imposed on a person who acquires any property or value increase by gift. If CIT or individual income tax is imposed on the gifted property, however, the gift tax shall not be imposed. Gift tax ranges from 10% on not more than KRW 100 million in tax base to the top marginal tax rate of 50%.

Inheritance tax

Inheritance tax is imposed upon a person or a company that acquires property through inheritance or bequest. However, an inheritor that is a for-profit company shall be exempt from the inheritance tax. Inheritance tax rates are the same as those for gift tax.

Payroll taxes

Employers are required to withhold income taxes at source on a monthly basis, finalise their employees’ tax liability, and file the final tax settlement receipt with the tax authorities no later than the tenth day of March of the following year.

Social security contributions

There are four types of social security contributions in Korea, namely national pension, national health insurance, employment insurance, and worker’s accident compensation insurance. Employers and employees are almost equally required to bear a total amount of 8.5% of salaries for the first three types of social security taxes (i.e. national pension, national health insurance, and employment insurance), while the worker’s accident compensation insurance is borne by employers only, which varies by industry, ranging from 0.85% (banking, insurance) to 28.25% (coal mining) of salaries.

Branch income

In general, a branch office of a foreign corporation is taxed in the same manner as resident companies.

Remittance of retained earnings from a Korean branch to its head office is subject to reporting to a designated foreign exchange bank in Korea under the Foreign Exchange Transaction Act.

If the tax treaty between Korea and the country in which a foreign corporation is residing allows the imposition of a branch profits tax, the tax is imposed on the adjusted taxable income of the Korean branch.

Where applicable, the branch profits tax is levied in addition to the regular CIT, which is imposed at the rate of 20% (or at a reduced rate as provided in a treaty) of the adjusted taxable income of the Korean branch.

Income determination

Gross income consists of gains, profits, income from trade and commerce, dealings in property, rents, royalties, and income derived from any transactions carried on for gain or profit.

Inventory valuation

Inventories generally are stated at either the lower of cost or market (LCM) or cost method. Any one of LCM and six cost methods, including specific identification, first in first out (FIFO), last in first out (LIFO), weighted-average, moving-average, and retail method, can be elected for tax purposes. The method elected should be applied consistently each year unless an application for change has been submitted before three months from the year-end. Different valuation methods may be used for different categories (i.e. manufactured goods and merchandised goods, semi-finished goods and goods in process, raw materials, supplies in stock) and different business places.

For inventory costing under Korean International Financial Reporting Standards (K-IFRS), LIFO is not an acceptable accounting method. Consequently, in a year when a taxpayer first adopts K-IFRS and duly reports the change of inventory valuation method from LIFO to one of the other costing methods (e.g. FIFO, weighted average), the taxpayer is allowed to exclude the inventory valuation gain arising from the change and include it in its taxable income over the next five-year period using a straight-line method.

Stock valuation

The valuation of securities or bonds shall be made using the cost method. For the cost method, the weighted-average cost method or moving-average cost method shall be applied for the purpose of valuation of securities, and the specific-identification method may be used for valuation of bonds.

Capital gains

Generally, capital gains are taxed at the same CIT rate as ordinary taxable income. For the purposes of taxation, gross income does not include income derived from gains from capital transactions, such as capital surplus, gains on reduction of paid-in capital, etc. However, gains from treasury stock transactions are taxed, and losses are deductible from taxable income.

Note that capital gains from the disposal of non-business purpose land or houses may be subject to additional capital gains tax at the rate of 10% (40% in the case of non-registered land or houses) in addition to the normal CIT.

Dividend income

All distributions to shareholders are taxed as dividend income, whether paid in cash or in stock.

However, a qualified domestic holding company that owns more than 80% (40% in case of listed subsidiary) share ownership in its domestic subsidiary will receive a 100% deduction for dividends, while an 80% deduction is allowed for share ownership of 80% (40% in case of listed subsidiary) or less. A domestic corporation other than a qualified holding company will also receive a 100% deduction for share ownership of 100%, 50% for more than 50% (30% in case of listed subsidiary) share ownership, and 30% for share ownership of 50% (30% in case of listed subsidiary) or less.

Interest income

Except for certain cases, all interest income must be included in taxable income. Generally, interest income is included in taxable income as it is received.

Rental income

Income from the leasing of property shall be included in taxable income. In cases where a company is subject to an estimated tax by the tax authority due to the absence of books of accounts, the deemed rental income as calculated at a term deposit interest rate on the lease deposit received by the company will be included in taxable income.

Royalty income

Royalties are considered to be taxable income when earned.

Gains and losses on foreign currency translation

Companies are allowed to recognise unrealised gains and losses on foreign currency translation of their monetary assets and liabilities in a foreign currency. This recognition is also allowed with respect to currency forward transactions and swaps to hedge foreign exchange risks of such assets and liabilities. In this regard, a taxpayer can choose whether to recognise unrealised gains and losses or not for tax purposes. Once elected, the same method must be consistently used.

Foreign income

Resident corporations are taxed on their worldwide income. A Korean company is taxed on its foreign-source income as earned at normal CIT rates. To avoid double taxation, taxes imposed by foreign governments on the foreign-source income recognised by a resident company are allowed as a credit against CIT or as deductible expenses in computing the taxable income.

Generally, income of foreign subsidiaries incorporated outside Korea is not included in the taxable income of a resident company until the declaration of dividends from the foreign subsidiaries. Therefore, the Korean tax impact may be delayed through deferring the declaration of dividends unless the controlled foreign corporate (CFC) rule under the Law for Coordination of International Tax Affairs (LCITA) is applied.

The CFC rule provides that the undistributed earnings of a resident company's foreign subsidiary located in a low-tax jurisdiction (where the effective tax rate on the income before tax for the past three years averages 15% or less) are taxed as deemed dividends to the resident company that has direct and indirect interest of 10% or more in such subsidiary. The CFC rule does not apply in cases where a foreign subsidiary has fixed facilities (e.g. office, factory) in a low-tax jurisdiction for the conduct of business, it manages or controls the business by itself, and the business is mainly performed in the jurisdiction. Even in this case, however, where passive income (e.g. income from investment in securities or lending loans) is more than 50% of gross income, the CFC rule shall be applicable. Furthermore, in cases where the passive income is between 50% and 5% of the foreign subsidiary's gross income, the CFC rule will apply in a limited manner (i.e. a CFC's undistributed earnings will be included in taxable income of the CFC's domestic related parties in proportion of such passive income to its gross income). However, dividends will be excluded in calculating the amount of passive income if they are derived from shares issued by the company that is 10% or more owned by a CFC.

If dividends from a qualifying subsidiary are included in taxable income of a resident company, the foreign tax paid by a qualifying subsidiary on the subsidiary's taxable income is eligible for a foreign tax credit in the hands of the resident company regardless of whether there are tax treaties with the relevant foreign countries. For this purpose, a qualifying subsidiary refers to the company in which a resident corporation owns 25% or more of its shares for the period of six consecutive months or more prior to the date of dividend declaration. Unused foreign tax credits can be carried forward for five years.

Deductions

In general, expenses incurred in the ordinary course of business are deductible, subject to the requirements for documentary support.

A corporation's disbursements of more than KRW 30,000 for goods or services provided are required to be supported by qualifying evidences, such as credit card sales vouchers, cash receipts, tax invoices, and those vouchers and invoices stored in the company's enterprise resource planning (ERP) system. The corporation is required to maintain these documents for five years. If the corporation fails to maintain proper evidences, a 2% penalty shall be levied on the amount of disbursement.

Accrued expenses are not deductible until the expenses are fixed or determined.

Depreciation and amortisation

Depreciation of all property, plant, and equipment (PP&E), which includes buildings, machinery, and vehicles, used to generate income is allowed as a deduction for CIT. Generally, interest on debt acquired to purchase, manufacture, or construct PP&E must be capitalised until the PP&E is operational. This does not apply to the interest associated with the expansion or improvement of existing PP&E. A detailed list of fixed assets, gross values (including capitalised interest), the useful lives of the assets, and the current year's depreciation charge must be submitted to the tax authorities when filing the annual CIT return.

The tax law allows the following methods for calculating depreciation:

- Straight-line or declining-balance method for tangible fixed assets, other than plant and buildings.
- Straight-line method for plant, buildings, and intangible assets.
- Service-output or straight-line method for mining rights.

- Service-output, declining-balance, or straight-line method for tangible fixed assets used in mining.

In determining depreciation using a straight-line method, salvage value of the assets is regarded as zero. However, where the declining-balance method is used, 5% salvage value is required. Changes in the depreciation method must be approved by the tax authorities in advance, and such approval may only be obtained in exceptional cases (i.e. merger between two corporations having different depreciation methods). Although the tax law specifies the standard useful lives for each type of assets, the useful life of a fixed asset can be increased or decreased by 25% of the standard useful life at the taxpayer's election. The elected depreciation method and useful life should be consistently applied. Also, a taxpayer can apply for a change to the useful life within 50% of the standard useful life, which requires an approval from tax authorities.

The standard useful life and the scope of elective useful life for assets are provided in the following tables:

Tangible fixed assets	Standard useful life (years)	Scope of elective useful life (years)
Vehicles (excluding those used for transportation businesses and leasing service of machinery, equipment, and consumer goods), tools, equipment, and fixtures	5	4 to 6
Ships and aircraft (excluding those used for fishery, transportation, and leasing service of machinery, equipment, and consumer goods)	12	9 to 15
All buildings and constructions of brick structure, block structure, concrete structure, mud structure, mud wall structure, wooden structure, wooden frame mortar structure, and other structures	20	15 to 25
All the buildings and constructions of steel-frame/iron bar concrete structures, stone structures, brick/stone structures, steel-frame structures	40	30 to 50

Note that machinery and equipment used for specific industries shall be subject to different useful lives from four years (e.g. bag manufacturing) to 20 years (e.g. water supply service).

Intangible fixed assets	Useful life (years)
Goodwill, design rights, utility model rights, trademarks	5
Patents	7
Fishery rights, extraction rights under the law of development of mineral resources at the sea bottom (may elect activity method), right of management for toll roads, water rights, right of use for electricity and gas service facilities, right of use for tap water facilities for industrial use, right of use for general tap water facilities, right of use for heating facilities	10
Mining rights (may elect activity method), right of use for exclusive telegraph and telephone facilities, right of use for exclusive sidetracks, right of management for sewage disposal, right of management for tap water facilities	20
Right of use for dams	50

Note that for used fixed assets (including assets acquired through mergers or spin-offs) that have been used for more than half of their standard useful lives, a new useful life may be filed with the tax authorities of between 50% of the standard useful life and the standard useful life.

According to the CITL, depreciation is allowed for tax deduction only when expensed for book purposes. However, in order to alleviate any dramatic increase in tax burden due to decreased depreciation expenses through the adoption of K-IFRS, additional expense deduction may be allowed through tax adjustment. For tax purposes, depreciable assets acquired on or before 2013 may be depreciated at the rate equivalent to the average of three years before the adoption of K-IFRS. Depreciable assets acquired after 2014 may be depreciated using the tax useful lives only if they are the same type of existing assets used for the same business line and the calculation method of deduction is regulated.

Deduction of company car expenses

For company cars provided to officers or employees (whether owned or leased), the amended CITL includes requirements for a company to have appropriate operation records or sufficient evidence to claim the deduction. The depreciation of a company car is limited to KRW 8 million annually for CIT purpose. In addition, the deduction of company car expenses, including depreciation, shall be disallowed for the portion of private use.

Goodwill

Amortisable goodwill for tax purposes is defined as 'value transferred with consideration, apart from transferred assets included in business transfer, valuated by taking into account business premium factors of the transferor such as permission/licence, legal privileges, geographical advantages, business secrets, credit, reputation, transaction partners, etc.'. Goodwill shall be amortised over five years using the straight-line method for tax purposes.

Start-up expenses

Start-up expenses, such as incorporation expenses, founders' salary, and registration fees and taxes, are deductible if the expenses are recorded per the articles of incorporation and are actually paid.

Interest expenses

Interest incurred in the ordinary course of business is deductible as long as the related loan is used for business purposes. There are, however, a number of exceptions to the general rule, as follows:

- If borrowings from a foreign shareholder, or from a third party under a payment guarantee by the foreign shareholder, exceed two times the equity of the relevant foreign shareholder, the paid interest and discount fee as to the relevant excessive portion will be disallowed and further treated as a dividend payment.
- Debenture for which the creditor is unknown.
- Bonds and securities on which recipient of interest is unknown.
- Construction loans and loans for the purchase of land and fixed assets up to the date on which the assets are acquired or completed must be capitalised as a part of the cost of the asset and depreciated over the life of the asset. Interest after the date of completion or acquisition is deductible as incurred.
- Interest on loans related to non-business purpose assets or funds loaned to related parties.
- Interest expense paid to an overseas related company that exceeds 30% of taxable income before depreciation and interest of the domestic company.

Contingent liabilities

In general, contingent liabilities are not deductible, except for reserves under the following items, which are counted as losses within the tax limit:

- Reserves for bad debts.
- Liability reserves and emergency reserves prescribed in the Insurance Business Law.
- Reserves for non-profit organisations.
- Reserves for the write-off of a compensation claim set aside by trust guarantee funds in each business year.

The amounts enumerated below are also counted as losses in calculating income for the business year:

- The amount of gains from insurance claims used to acquire the same kinds of fixed assets as the lost fixed assets, or to improve the damaged fixed assets within two years after the first day of the business year following the business year in which the gains fall.
- The amount of a beneficiary's share of construction costs received by a domestic corporation engaged in the electricity or gas business, etc. used for the acquisition of fixed assets.
- The amount of the national treasury subsidies actually used for acquisition or improvement of fixed assets for business.

Bad debt

For companies that are not financial institutions, a doubtful accounts reserve is allowed as a deduction for tax purposes at the greater of 1% on the tax book value of the receivables at a year-end or actual bad debt ratio (deductible bad debts in a current year divided by the preceding year's tax book value of receivables). Bad debts are allowed as a deduction when certain legal proceedings are satisfied or the statute of limitations has lapsed.

Charitable contributions

Donations to public interest entities, such as government authorities and social welfare organisations, as well as donations for academic research, technical development, etc., are classified as *Bub-jung* donations. *Bub-jung* donations are tax-deductible at up to 50% of the total taxable income for the concerned fiscal year after deduction of net operating loss (NOL). *Ji-jung* donations to public entities prescribed by the CITL are also tax-deductible at up to 10% of the total taxable income for the fiscal year after the deduction of deductible *Bub-jung* donations and NOL.

The amount in excess of such limit may be carried over for five years. Donations other than the statutory donations above will not be deductible for tax purposes.

Employee remuneration

There is no statutory limit for employee remuneration as long as it is reasonable, which includes salaries, wages, stipends, bonuses, retirement payments, pensions, and meal and housing allowances, as well as all other kinds of subsidies, payments, and compensation. Remuneration of foreign employees is determined according to their engagement contracts.

Pension expense

Employers hiring one or more employees are required to set aside severance pay or retirement pensions for their employees. Defined contribution (DC) and defined benefits (DB) are the two available schemes for the retirement pension system. Under the DC scheme, the premiums paid by the employer are deductible upon payment, while deductions for the reserve under the DB scheme are subject to a limit.

Payment for directors

Bonuses paid to directors in excess of the amount determined in the articles of incorporation or at a shareholders' meeting, etc. are not deductible. Also, severance benefits paid to directors in excess of the amount prescribed in the tax law are not deductible.

Entertainment expenses

Entertainment expenses of more than KRW 10,000 on an event basis must be supported by corporate credit card vouchers, cash receipts, or tax invoices in order to be deductible. In addition, the entertainment expenses in excess of the tax limit are not deductible.

The deductible limit for entertainment expenses in a business year is computed as:

- an amount calculated by multiplying KRW 12 million (KRW 18 million [temporarily increased to KRW 24 million for the tax years beginning on or after 1 January 2015 and ending on 31 December 2018] for an SME) by the number of months in the respective business year divided by 12, plus
- an amount calculated by multiplying the amount of gross receipts for a business year by the rates listed in the following table (in the case of receipts from transactions between related parties, 10% of the amount calculated by multiplying the receipts by the following rates shall be applied).

Amount of gross receipts (KRW)	Rate
10 billion or less	0.2%
Over 10 billion up to 50 billion	KRW 20 million + 0.1% of the excess over KRW 10 billion
Greater than 50 billion	KRW 60 million + 0.03% of the excess over KRW 50 billion

Insurance premiums

Insurance premiums paid to an insurance company are deductible if the business enterprise is the listed beneficiary. Insurance premiums for which the beneficiary is the employee are also deductible; however, they are treated as salaries for the employees and are subject to WHT on earned income (this excludes the severance insurance premium or social security taxes that are borne by employers).

Fines and penalties

Fines, penalties, and interest on underpayment of taxes are not deductible.

Taxes

Income taxes are generally not deductible in determining income subject to CIT.

Net operating losses (NOLs)

In general, an NOL carryover is allowed for ten years. The amended CITL restricts a company from deducting the NOL in excess of 70% (60% for the fiscal year beginning 1 January 2019 and thereafter) of the taxable income of fiscal year starting 1 January 2018 and ending 31 December 2018. The CITL maintains the current restriction on a foreign corporation from deducting the NOL in excess of 80% of the taxable income. However, SMEs and certain qualifying companies under recovery process, etc., which will be exempt from this rule, are allowed to deduct the NOL without limitation.

Generally, loss carrybacks are not allowed. However, SMEs can carry back an NOL for one year.

Payments to foreign affiliates

With sufficient supporting documentation and under the arm's-length principle, interest, royalty, and management service fees paid to foreign affiliates are deductible for CIT purposes.

Under the LCITA, the following conditions must be met in order for a management service fee charged by a foreign related party to a domestic company to be deductible:

- The services must be provided based on an agreement entered into by the service provider prior to the service transaction.
- The provision of the service can be verified by a schedule of services, description of services, description of the company providing services and its employees, detailed explanation of expenses incurred, and other supporting documentation.
- A company must be able to anticipate the company's additional profit or reduced expense through the services provided by a foreign affiliate.
- Payment for the provided services should be consistent with arm's-length standards.

Group taxation

The consolidated corporate tax filing system can be adopted for a domestic corporation in cases where two or more wholly-owned subsidiaries exist. A taxpayer may elect the consolidated filing scheme upon approval from the tax authorities, but it cannot be revoked for at least five years after the election of the consolidated tax filing.

Transfer pricing

The LCITA authorises the tax authorities to adjust the transfer price based on an arm's-length price and to determine or recalculate the taxable income of a domestic company (including PE of a foreign company) when the transfer price for the transaction between the domestic company and its foreign related party is either below or above an arm's-length price.

The LCITA lists the following methods for determining an arm's-length price: the comparable uncontrolled price (CUP) method, the resale price method, the cost-plus method, the profit-split method, the transactional net margin method, and other reasonable methods. Other reasonable methods can be used only if it is unfeasible to apply one of the aforementioned methods.

The method used and the reason for adopting that particular one for an arm's-length price determination must be disclosed to the tax authorities by a taxpayer in a report submitted along with the taxpayer's annual tax return.

Transfer pricing documentation requirement

In line with the OECD BEPS Action 13, the LCITA includes a reporting requirement for multinational companies in Korea to submit a consolidated report (including local file and master file) on their cross-border, related-party transactions, affecting not only Korean corporations but also foreign corporations having a PE in Korea that meet all of the following conditions: (i) annual gross sales of an individual entity exceeding KRW 100 billion and (ii) international related-party transactions exceeding KRW 50 billion per year. Required information to be submitted for reporting includes organisation, business, intangible assets, related-party transactions, etc. relating to the group and the local entity. Failure to comply with the reporting requirement will result in a penalty.

The amended Law for the LCITA introduces the requirement to submit country-by-country (CbC) reporting following the implementation of the new transfer pricing rules requiring multinationals in Korea to submit local files and master files on their cross-border transactions. The CbC report must be filed within 12 months after the end of the ultimate parents' income tax year. This rule is applicable to the required information for fiscal years starting on or after 1 January 2017.

Thin capitalisation

In cases where a Korean company borrows from its foreign-controlling shareholder and the debt-to-equity ratio exceeds 2:1, a portion of interest payable on the excess borrowing is characterised as dividends subject to Korean WHT (reduced rate if a tax treaty applies) while being treated as non-deductible in computing taxable income.

In line with the OECD's recommendation on the limitation of interest expense deductions (BEPS Action 4), the new rule shall restrict interest deduction on top of the existing thin capitalisation rule. Deduction of net interest (i.e. the amount of interest expense paid to overseas related parties minus the interest income received from overseas related parties) claimed by a domestic company for international transactions will be limited to 30% of the adjusted taxable income (i.e. taxable income before depreciation and net interest expenses) of the domestic company. This will be implemented from the fiscal year beginning on or after 1 January 2019.

Controlled foreign corporations (CFCs)

Under the Korean CFC rule, when a Korean national directly or indirectly owns at least 10% in a foreign corporation and the foreign company's average effective income tax rate for the three most recent consecutive years is 15% or less, the undistributed earnings of the CFC shall be deemed to be paid as a dividend to the Korean national and subject to tax in Korea.

For more information on the CFC rule, see Foreign income in the Income determination section.

Deduction limit on hybrid financial instruments

In a commitment to implement the hybrid mismatch rules recommended by the OECD (BEPS Action 2), a new rule shall limit expense deductions for hybrid mismatch arrangements. Hybrid financial instruments include financial instruments that have debt or equity positions at the same time but are treated as a debt in one country but treated as an equity in the other country (e.g. participating bonds). In principle, expense deduction will be denied for the amount of payment that is not taxed in a counterpart jurisdiction. This rule will apply for the fiscal year beginning on or after 1 January 2018.

Related-party transactions

Under the provision of the CITL, the tax authorities may recalculate the corporation's taxable income when CIT is unreasonably reduced due to transactions with related parties. Generally, if the discrepancy between the transaction price and fair market value exceeds 5% of the fair market value or KRW 300 million, the transaction will be subject to this provision.

Tax credits and incentives

Foreign tax credit

Taxes imposed by foreign governments on income recognised by a resident taxpayer are allowed as a credit within the limit against the income taxes to be paid in Korea, or as deductible expenses in computing the taxable income. The excess foreign tax credit can be carried forward five years.

Indirect foreign tax credit is also available for a Korean parent company in cases where the dividends from a foreign subsidiary are included in the taxable income of the Korean parent company. The conditions on indirect tax credit exclude the overseas grandson subsidiary and raise the shareholding ratio from 10% or more to 25% or more.

Special tax deductions for SMEs

A special deduction on corporate taxes is available for SMEs when they are engaged in a qualified business. The tax deduction ratio ranges from 5% to 30%, depending on corporate location, size, business types, etc., with a cap of KRW 100 million. This incentive is applied to taxable income arising in the tax years that end before 31 December 2020.

Investment incentives

Tax credits are generally available for qualified investment in facilities for productivity enhancement, safety, job-creating investments, etc.

Tax credit for investment in facilities for productivity enhancement

If a resident makes an investment in facilities or equipment to increase productivity by no later than the end of December 2019, then 1% (3% for medium-scale companies and 7% for SMEs) of such investment amount shall be deducted from CIT. The unused tax credit can be carried forward to the next five years.

Tax credit for investment in facilities for safety

If a resident or a domestic corporation makes an investment in a facility (excluding any investment in used assets) for safety that is considered necessary for industrial purposes no later than the end of December 2019, then an amount of 1% (3% for medium-scale companies and 7% for SMEs) of such investment shall be deducted from CIT. The unused tax credit can be carried forward to the next five years.

Tax credit for investment for commercialisation of new growth-engine and core technologies

The amended tax law has introduced a new tax credit in respect of investment in facilities designed to promote the commercialisation of new growth-engine or core technology (e.g. facilities for the manufacturing of new drugs for which patents are obtained by a company based on clinical trials). The tax credit rate is 10% of the amount of investment for SMEs, while the rates are adjusted to 7% for medium-scale companies and 5% for large corporations. This tax credit is applied to investment made until the end of December 2018.

Tax credit for job creation

The STTCL has introduced an employment-promoting tax incentive in respect of new employment depending on the number of increased employees, with certain limits if a company is engaged in businesses except for those that fall under the category of consumption-oriented services (e.g. entertainment and beverage service). This incentive is based on the scheme of having redesigned those tax credits for job-creating investment and to support youth job creation. The amount of tax credit varies: up to KRW 11 million per new employee for SMEs, up to KRW 7 million for medium-scale companies, and up to KRW 3 million for large companies. The proposed change will be temporarily available for two years (one year for large companies) from the year beginning on or after 1 January 2018. The unused tax credit can be carried forward to the next five years.

Tax credit for increase in corporate payroll

The tax law applies tax credits (5% for large companies, 10% for medium-scale companies, and 20% for SMEs) on the incremental amount in average corporate payroll over a certain base level calculated in a prescribed manner by taking into account either the average corporate payroll over the previous three years or the average payroll increase among the SMEs in Korea. This is conditional on there being no decline in the number of full-time employees from the previous year. The tax credit, which was supposed to terminate by the end of December 2017, has been extended three additional years until the end of December 2020. The unused tax credit can be carried forward to the next five years.

Tax credit for re-hiring retired female employees of SMEs

The tax law allows a tax credit to promote the re-employment of female employees of SMEs who retired for pregnancy, childbirth, or care and other personal reasons as prescribed in the Presidential Decree. The tax credit is designed to allow SMEs to subtract the amount, as much as 30% of labour costs of SMEs (15% for a medium-scale companies) paid per re-hired female employee, from their corporation tax payable for the period of two years following the month of re-employment if prescribed conditions are met. The tax credit, which was supposed to terminate by the end of December 2017, has been extended to apply if a company executes an employment contract until the end of December 2020. The unused credit can be carried forward to the next five years.

Research and development (R&D) tax incentives

The STTCL provides various tax incentives to stimulate R&D activities. These include a tax credit for research and manpower development expenses, a tax credit for technology transfer, and tax credits for merger or acquisition of a technology innovative SME.

Tax credit for development of research and manpower

Companies presently claim a tax credit in relation to qualifying R&D expenditure to the extent of either (i) 0% to 2% (8% for medium-scale companies, 25% for SMEs) of the current R&D expenses or (ii) 25% (40% for medium-scale companies, 50% for SMEs) of the incremental portion of the current R&D expenses over the previous year. The incremental method can be applied only when the R&D expenses for the prior year exceed the average R&D expenses for the previous four years. However, for the R&D expenditures in qualified new growth engine and core technology areas designated in the presidential decree, the preferred credit rates are applied 20% to 40%, depending on the type of company. The unused credit can be carried forward to the next five years.

Tax credit for technology transfer among SMEs (Korean patent box regime)

Tax credit and reductions have been introduced to facilitate the transfer of technology between companies so as to enhance technical competencies and the recovery of funds invested in technology more efficiently. CIT on income derived by SMEs and specified medium-scale companies from the transfer of patents, etc. to a Korean national is reduced by 50%. The tax law grants a 25% tax credit for income derived by SMEs and medium-scale companies from the leasing of patents or utility model rights where the company has first filed a registration of such rights. The tax credit is 5% (10% for SMEs) of the amount paid to acquire patents, etc. (ceiling at 10% of CIT). This temporary credit is applicable to transfers, purchases, or leases taking place until the end of December 2018. The unused credit can be carried forward to the next five years.

Tax credit for merger or acquisition of a technology innovative SME

In cases where a domestic company merges with a technology innovative SME in a qualified manner, the merger company shall be permitted to take a 10% tax credit with respect to the payment made in such a merger, up to the value of the acquired technology. This 10% tax credit will also be available for a company that acquires shares in a technology innovative SME in a qualified manner no later than the end of December 2018. In this case, if any of requirements for a qualified manner fails to be met, the amount of tax credited will be collected. The unused credit can be carried forward to the next five years.

Tax credit for investment in facilities for technology and human resources development

A corporation purchasing facilities no later than 31 December 2018 prescribed in the Presidential Decree with the purpose of R&D and job training is eligible for a tax credit of up to 1% (3% for medium-scale companies, 6% for SMEs) of such investment. The unused tax credit can be carried forward five years.

Energy/environmental incentives

Tax credit for investment in energy-saving facilities

If a resident makes an investment (excluding any investment in used goods) no later than 31 December 2018 in energy-saving facilities, 1% (3% for medium-scale companies, 6% for SMEs) of such investment shall be deducted from CIT. The unused tax credit can be carried forward five years.

Tax credit for investment in facilities for environmental protection

If a resident makes an investment (excluding any investment in used goods) in any facility for the purpose of environmental conservation no later than 31 December 2018, then 3% (5% for medium-scale companies, 10% for SMEs) of the investment amount shall be deducted from CIT. The unused tax credit can be carried forward five years.

Inbound investment incentives

The Korean government provides various incentives and benefits for inducing foreign investment under the Foreign Investment Promotion Law.

Among others, foreign-invested companies that engage in certain qualified high-technology businesses can apply for 100% exemption from CIT for five years, beginning from the first year of profitable operations (from the fifth year, if not profitable until then) and a 50% reduction for the following two years in proportion to the foreign shareholding ratio. An exemption from WHT on dividends, which was available for foreign investors in the same manner as above during the same grace period, is no longer granted for tax exemption applications filed on or after 1 January 2014. However, the WHT exemption on dividends already approved will not be affected by the tax law change. In addition, the taxpayer can apply for 100% exemption from acquisition tax and property tax on assets acquired for their exempt business for five years after the business commencement date and 50% reduction for the following two years. For local tax exemption, some local governments grant longer exemption periods (up to 15 years) and higher exemption ratios in accordance with their local ordinances. Qualified foreign investment also can be eligible for exemption from customs duties, VAT, and individual consumption tax on imported capital goods.

In addition, foreign investors satisfying specified criteria are provided with tax incentives and other benefits for investment in specially designated areas, including foreign investment zones (FIZs), free economic zones (FEZs), free trade zones (FTZs), and strategic industrial complexes exclusively developed for foreign invested companies. The tax incentives for qualifying foreign investors in individual type FIZs and FEZs and certain strategic industrial complexes that are approved by the related committee under laws governing the operation of the zones are similar to those of the above foreign invested high-tech companies. Qualifying investors in complex type FIZs, FEZs, FTZs, and strategic industrial complexes may receive the 100% exemption from corporate or individual income tax as well as local taxes for the first three years and 50% reduction for the next two years. They also receive exemption from customs duties on imported goods.

The amended tax law has reformed the scope of businesses eligible for foreign investment tax incentives to be aligned with those that qualify for the foregoing R&D tax credit. This change is applied to foreign investment for which tax incentive is applied on or after 7 February 2017.

To receive tax incentives for inbound investment, an application for tax incentives, together with supporting documents, should be filed with the tax authorities by the end of the fiscal year that the business commencement date belongs to. In addition, foreign investment made via specific countries is excluded from the exemption from corporate or individual income tax and local taxes for inbound investment. They include those countries with which Korea has not entered into income tax treaties (including tax information exchange agreements [TIEAs] and investment promotion and protection agreements), such as Botswana, Republic of Cyprus, Dominican Republic, Guatemala, Lebanon, Nauru, Niue, Seychelles, and Trinidad and Tobago.

Foreign direct investment (FDI) incentive limitations

The FDI credit limits incentives granted to qualified FDIs. The ceiling has been set to encompass both investment amount and job-creation. In terms of investment amount, the level of incentives for FDI is allowed up to 50% of the aggregated FDI amount for companies benefiting from a seven-year incentive period (40% ceiling for companies enjoying a five-year incentive period). In terms of job-creation, the level of incentives for FDI is allowed up to 50% of the aggregated FDI amount for companies benefiting from a seven-year incentive period (40% for companies enjoying a five-year incentive period) based on the number of employees.

Companies that have enjoyed tax benefits based on job-creation will be subject to tax assessment in cases where there is a net decrease in employment within the subsequent two years in comparison to the year that the relevant tax credit was obtained.

Withholding taxes

Foreign corporations with income derived from sources in Korea are subject to CIT on such income. If the foreign corporation has no 'domestic place of business' in Korea, it will be subject to tax on its Korean-source income on a withholding basis in accordance with the tax laws and the relevant tax treaty, if applicable. Any Korean-source income attributable to a domestic fixed place of business of a foreign corporation will be subject to Korean CIT.

For residents of countries having a tax treaty with Korea, reduced WHT rates may apply. An application form must be submitted to the withholding agents in order to apply the treaty rate. If a beneficiary cannot be identified in the application form, the withholding agents should withhold the tax at the non-treaty rate.

For dividends, interest, and royalties, the WHT rates are limited as follows:

	WHT (%)		
Recipient	**Dividends**	**Interest**	**Royalties**
Resident corporations (1)	0	14/25	0
Resident individuals (1)	14	14/25/30	0
Non-resident corporations and individuals:			
Non-treaty (2)	20	14/20 (35)	20 (38)
Treaty:			
Albania	5/10 (8)	10	10
Algeria	5/15 (8)	10	2/10 (14)
Australia	15	15	15
Austria	5/15 (8)	10	2/10 (14)
Azerbaijan	7	10 (36)	5/10 (21)
Bahrain	5/10 (8)	5	10
Bangladesh	10/15 (3)	10	10
Belarus	5/15 (8)	10	5
Belgium	15	10	10
Brazil	10	10/15 (5)	10/25 (6)

	WHT (%)		
Recipient	**Dividends**	**Interest**	**Royalties**
Brunei	5/10 (8)	10	10
Bulgaria	5/10 (7)	10	5
Canada	5/15 (8)	10	10
Chile	5/10 (8)	10/15 (30)	5/15 (32)
China, People's Republic of	5/10 (8)	10	10
Colombia, Republic of	5/10 (11)	10	10
Croatia	5/15 (8)	5	0
Czech Republic	5/10 (8)	10	10
Denmark	15	15	10/15 (4)
Ecuador	5/10 (3)	12	5/12 (21)
Egypt	10/15 (8)	10/15 (9)	15
Estonia	5/10 (8)	10	5/10 (32)
Ethiopia	5/8 (8)	7.5 (36)	5
Fiji	10/15 (8)	10	10
Finland	10/15 (8)	10	10
France	10/15 (3)	10	10
Gabon	5/15 (8)	10	10
Georgia	5/10 (3)	10	10
Germany	5/15 (8)	10	2/10 (14)
Greece	5/15 (8)	8	10
Hong Kong	10/15 (8)	10	10
Hungary	5/10 (8)	0	0
Iceland, Republic of	5/15 (8)	10	10
India	15	10	10
Indonesia	10/15 (8)	10	15
Iran	10	10	10
Ireland, Republic of	10/15 (3)	0	0
Israel	5/10/15 (12)	7.5/10 (13)	2/5 (14)
Italy	10/15 (8)	10	10
Japan	5/15 (8)	10	10
Jordan	10	10	10
Kazakhstan	5/15 (3)	10	2/10 (14)
Kenya	8/10 (8)	12	10
Kuwait	5	5	15
Kyrgyzstan	5/10 (8)	10	5/10 (32)
Laos	5/10 (3)	10	5
Latvia	5/10 (8)	10	5/10 (32)
Lithuania	5/10 (8)	10	5/10 (37)
Luxembourg	10/15 (8)	10	10/15 (15)
Malaysia	10/15 (8)	15	10/15 (16)
Malta	5/15 (8)	10	0
Mexico	0/15 (17)	5/15 (18)	10
Mongolia	5	5	10
Morocco	5/10 (8)	10	5/10 (19)
Myanmar	10	10	10/15 (4)
Nepal	5/10/15 (31)	10	15
Netherlands	10/15 (8)	10/15 (20)	10/15 (21)
New Zealand	15	10	10
Norway	15	15	10/15 (21)

Korea, Republic of

Recipient	WHT (%) Dividends	Interest	Royalties
Oman	5/10 (3)	5	8
Pakistan	10/12.5 (11)	12.5	10
Panama	5/15 (8)	5	3/10 (32)
Papua New Guinea	15	10	10
Peru	10	15	10/15 (39)
Philippines (2)	10/25 (22)	10/15 (23)	10/15 (24)
Poland	5/10 (3)	10	5
Portugal	10/15 (8)	15	10
Qatar	10	10	5
Romania	7/10 (8)	10	7/10 (21)
Russia	5/10 (25)	0	5
Saudi Arabia, Kingdom of	5/10 (8)	5	5/10 (32)
Serbia	5/10 (8)	10	5/10 (19)
Singapore	10/15 (8)	10	15
Slovak Republic	5/10 (8)	10	0/10 (33)
Slovenia	5/15 (8)	5	5
South Africa (2)	5/15 (8)	10	10
Spain	10/15 (8)	10	10
Sri Lanka	10/15 (8)	10	10
Sweden	10/15 (8)	10/15 (10)	10/15 (21)
Switzerland	5/15 (3)	5/10 (18)	5
Tajikistan	5/10 (8)	8	10
Thailand (2)	10	10/15 (26)	5/10/15 (34)
Tunisia	15	12	15
Turkey	15/20 (8)	10/15 (27)	10
Turkmenistan	10	10	10
Ukraine	5/15 (11)	5	5
United Arab Emirates	5/10 (3)	10	0
United Kingdom	5/15 (8)	10	2/10 (14)
United States (2)	10/15 (29)	12	10/15 (28)
Uruguay	5/15 (11)	10	10
Uzbekistan	5/15 (8)	5	2/15 (14)
Venezuela	5/10 (3)	5/10 (18)	5/10 (32)
Vietnam	10	10	5/15 (21)

Notes

1. Dividends and interest paid to resident individuals by corporations generally are subject to a 14% WHT rate. In addition to this, there is a resident surtax of 10% on the CIT liability.
2. In addition to the indicated tax rate, a resident surtax is charged at a rate of 10% of the respective tax rate.
3. Lower rate applies in case of equity ownership of 10% or more.
4. 10% rate applies to royalties paid for the use of or the right associated with industrial activities.
5. 10% rate applies if the loan period extends to seven years or more, the recipient is a financial institution, and the loan is used for certain designated purposes.
6. 25% rate applies to royalties associated with the use of trademarks or trademark rights.
7. 5% rate applies in case of equity ownership of 15% or more.
8. Lower rate applies in case of equity ownership of 25% or more.
9. 10% rate applies if the term of loans exceeds three years.
10. 10% rate applies when a recipient of interest income is a bank and income is connected with a loan with a term in excess of seven years.
11. Lower rate applies in case of equity ownership of 20% or more.
12. 5% rate applies if a recipient holds 10% or more ownership in a paying corporation but, even in case of 10% or more ownership, 10% rate applies if the dividends are paid out of profits subject to tax at a

lower rate than the normal corporate tax rate of a country where a payer resides. In other cases, 15% rate applies.
13. 7.5% rate applies when a recipient of interest income is a bank or a financial institution.
14. 2% rate applies to royalties paid for use of or the right to use industrial, commercial, or scientific equipment.
15. 10% rate applies if it is for the use of or the right to use industrial, commercial, and scientific equipment or information.
16. 15% rate applies if royalties are for use of or the right to use cinematography films or tapes for radio or television broadcasting or any copyright of literary or artistic work.
17. 0% rate applies in case of equity ownership of 10% or more.
18. 5% rate applies if a recipient is a bank.
19. 5% rate applies to royalties for use of copyrighted literature and music.
20. 10% rate applies if the term of the loans exceeds seven years.
21. Lower rate applies if it is for the use of or the right to use a patent, trademark, design, or secret formula, or industrial, commercial, and scientific equipment or information.
22. 10% rate applies in cases of equity ownership of 25% or more, or dividend paid by a resident company engaged in a preferred pioneer area and registered with the Board of Investment.
23. 10% rate applies in cases where the interest is paid in respect of public offering of bonds, debentures, or similar obligations or interest paid by a company that is a resident of the Philippines, registered with the Board of Investment, and engaged in preferred pioneer areas of investment under the investment incentive laws.
24. 10% rate applies in case of royalties paid by a company that is a resident of the Philippines, registered with the Board of Investment, and engaged in preferred pioneer areas of investment under the investment incentives laws.
25. 5% rate applies if a recipient holds 30% or more of equity interest in the amount of at least 100,000 United States dollars (USD).
26. 10% rate applies if a beneficial owner of the income is a financial institution (including insurance company) or resident of Thailand who is paid with respect to indebtedness arising as a consequence of a sale on credit by a resident of Thailand of any equipment, merchandise, or services, except where the sale was between persons not dealing with each other at arm's length.
27. 10% rate applies if the term of the loan exceeds two years.
28. 10% rate applies to royalties for use of copyrighted literature, music, films, and television or radio broadcasts. Otherwise, 15% rate applies.
29. 10% rate applies if equity ownership is 10% or more and not more than 25% of the gross income of a paying corporation for a preceding tax year consists of interest or dividends.
30. 10% rate applies when a recipient of interest income is a bank or an insurance company.
31. 5% rate applies when a recipient holds 25% or more of equity interest, and 10%, when a recipient holds 10% or more of equity interest. In other cases, 15% rate applies.
32. 5% rate applies to royalties paid for the use of or the right associated with industrial, commercial, or scientific equipment.
33. 0% rate applies to royalties paid for the use of academic rights.
34. 5% rate applies to royalties paid for the use of or the right associated with any copyright of literary, artistic, or scientific work, including software, and motion pictures and works on film, tape, or other means of reproduction for use in connection with radio or television broadcasting. 10% rate applies to royalties paid for the use of or the right to use a patent, trademark, design or model, plan, secret formula, or process. 15% rate applies to royalties paid for the use of or the right to use industrial, commercial, or scientific equipment, or for information concerning industrial, commercial, or scientific experience.
35. 14% rate applies if interest arises from bonds issued by a Korean company or government bodies.
36. 0% rate applies if a recipient of interest income is government, central bank, etc.
37. 5% rate applies to royalties paid for the use of industrial, commercial, or scientific equipment.
38. Fees arising from rental of industrial, commercial, scientific equipment, etc. are classified as rental income subject to 2% WHT.
39. 10% rate applies to royalties paid for technical support.

If a foreign company is located in a foreign jurisdiction designated as a tax haven by the Minister of Strategy & Finance, any Korean-source income of such foreign company will be subject to the domestic withholding rate of 20% regardless of whether or not the foreign company is resident of a treaty country. Currently, only Labuan is designated as such a jurisdiction. The foreign company may claim a refund of any excess WHT paid within three years if it proves to the Korean Tax Office that it is entitled to the reduced treaty rates as the substantive and beneficial owner of the income. Alternatively, a foreign company may attempt to seek a pre-approval in order to have the treaty benefits apply upfront by making an application to the Commissioner of Taxation.

Tax administration

Taxable period

In Korea, the taxable year is on a fiscal-year basis as elected by the taxpayer. However, it cannot exceed 12 months.

Tax returns

A corporation must file an interim tax return with due payment for the first six months of the fiscal year, and the filing/payment must be made within two months after the end of the interim six-month period.

A corporation must file an annual tax return with due payment for the fiscal year, and the filing/payment must be made within three months (four months for the consolidated tax return) from the end of the fiscal year. In case the external audit is not completed and the financial statements are not fixed, a corporation can request for extension of tax filing by one month with delinquent interest of 1.8% *per annum*.

Payment of tax

Where the tax amount to be paid by a resident corporation is in excess of KRW 10 million, part of the tax amount to be paid may be paid in instalments within one month of the date of the expiration of the payment period (two months for SMEs).

Where the tax amount to be paid is KRW 20 million or less, the excess of KRW 10 million may be paid in instalments; and where the tax amount to be paid exceeds KRW 20 million, 50% or less of the tax amount may be paid in instalments.

Functional currency

In instances where the taxpayer adopts to use a foreign currency as its functional currency, there are three ways to calculate the CIT base: (i) calculate the tax base using the financial statements in functional currency and translate it into Korean won; (ii) prepare the financial statements in Korean won and calculate the tax base; or (iii) translate the financial statements into Korean won and calculate the tax base. Once elected, the same method must be consistently used.

Tax audit process

For large companies whose sales revenue exceeds KRW 300 billion, a tax audit will be conducted every five years. Other companies are selected by certain standards, which were announced by the National Tax Service (NTS). An official notification of an intended tax audit must be made 15 days prior to the audit.

Statute of limitations

The statute of limitations is generally five years from the statutory filing due date of the annual CIT return. However, the statute of limitations is extended further in the following cases:

- Seven years if a taxpayer does not file its tax base by the statutory due date.
- Ten years if a taxpayer evades taxes by fraud or unjustifiable means.
- 15 years for fraud or unjustifiable means involving cross-border transactions. For this purpose, a 'cross-border' transaction means when a party or parties to the transaction include(s) non-resident(s) or foreign corporation(s) (excluding domestic business places of non-resident(s) or foreign corporation(s)).

Period of extinctive prescription for collection of national taxes

The period of extinctive prescription for collection of national taxes is five years (ten years for national tax payable worth KRW 500 million or more) from the date on which the government's right to collect a national tax becomes exercisable. Along with the five-year extinction prescription period of national tax collection, the extinction prescription period of tax refund request of taxpayers is extended to five years, which was previously three years from the tax return filing due date, effective for tax refund requests made on or after 1 January 2015.

Topics of focus for tax authorities

The recent topics of focus for tax authorities are as follows:

- Implementation of new tax information reporting systems as planned in the BEPS project.
- Increased tax audit on tax avoidance through internal transactions or gifts among group companies and major shareholders.
- Increased scrutiny over the prevention of offshore tax evasion through a cross-border tax information exchange program.
- Selection of tax audit targets through a sophisticated analysing and verification system and expansion of the number of corporate taxpayers subject to the regular five-year period audit cycle.
- New provision in the National Tax Basic Law to add accounting credibility to the existing tax audit selection criteria. Accounting credibility includes auditor's opinion, hours spent for external audit, etc.
- Increased application of forensic and electronic audit schemes and use of big data analysis to examine potential tax avoidance.

Additionally, the tax policy that the newly elected president has pledged during his campaign should be noted. To finance spending on expanded social welfare investment, the taxation systems on corporate taxpayers and high income earners are expected to be reinforced.

Other issues

Exchange controls

Most transactions involving foreign exchange generally do not require approval or reporting under the Foreign Exchange Transaction Act (FETA), with a few exceptions as prescribed by the FETA. Receipt of foreign exchange from outside Korea is freely permitted, and payments to foreign companies are not regulated. Most restrictions on Korean companies' foreign currency transactions with foreigners have been removed. However, the government continues to monitor certain flows of foreign currency in an attempt to minimise incoming speculative currency and outgoing capital flight.

Advance reporting is required for most capital transactions. For example, foreign currency loans obtained by a Korean resident or loans provided by a Korean resident to an overseas resident should be reported in advance. Foreign currency deposits should also be reported in advance. The agency to which the reporting should be made again differs based on materiality of the transaction amount or transaction type.

In addition, reporting in advance to the appropriate agency is required for the netting of receivables and payables with a foreign resident, third party payments where a payment is made to a foreign resident other than the transaction counterpart, and cross calculation, which is similar to netting, but the concerned company opens a bank account in which the offsetting takes place for future receivables and payables.

Ever since Korea's currency crisis, most restrictions on short-term as well as mid and long-term borrowings from overseas by corporations have been removed. Most foreign currency loans are allowed and are subject to reporting to a foreign exchange bank. There are no specific regulations, except the reporting requirements, on borrowings from overseas by foreign investment companies in Korea.

Automatic exchange of tax information

The Korea-United States (US) agreement on Automatic Exchange of Tax Information was ratified by the National Assembly on 7 September 2016. Based on the agreement, the tax authorities of both countries collect financial information on financial accounts held by individuals and entities and exchange this information. Korea-based financial institutions conduct their Foreign Account Tax Compliance Act (FATCA) due diligence procedures and report information on certain financial accounts held by US individuals and entities to the NTS, and then, the NTS will report this information to the US Internal Revenue Service (IRS). The type of information generally includes the name, address, tax identification number, account number, account balance as of the end of a relevant reporting period, and gross amount of income (such as interest and dividends).

Starting from 2017, Korea has exchanged with 53 countries, including the United Kingdom, Cayman Islands, British Virgin Islands, etc., certain information on financial accounts and income according to the Multilateral Competent Authority Agreements (MCAA). From 2018, Korea has exchanged such information with more countries because additional countries, including Switzerland, Singapore, etc., signed the MCAA. The NTS should be motivated to actively mobilise its infrastructure to exchange offshore financial and non-financial tax information for the purpose of pursuing taxpayers suspected of being engaged in offshore tax avoidance and conducting tax audits of such tax avoidance.

Choice of business entity

The following types of commercial entities are permitted in Korea:

- Corporation (*Hoesa*): There are five classes of corporation, outlined as follows:
  - Limited corporation:
    - *Jusik Hoesa* (JH): A corporation incorporated by one or more promoters, with each shareholder's liability limited to the amount of contributed capital. This type of entity is the most commonly used in Korea.
    - *Yuhan Hoesa* (YH): A corporation incorporated by one or more members, with each member's liability limited to the amount of that member's contribution to the corporation.
    - *Yuhan Chegim Hoesa*: A corporation incorporated by one or more members, with each member's liability limited to the amount of that member's capital contribution. With significantly fewer restrictions for establishment and operation, *Yuhan Chegim Hoesa* provides more flexibility and self-control than YH.
  - Unlimited corporation:

    - *Hapmyong Hoesa*: A corporation incorporated jointly by more than two members who are responsible for corporate obligations if the assets of the corporation are insufficient to fully satisfy those obligations.
    - *Hapja Hoesa*: A corporation composed of one or more partners who have unlimited liability and one or more partners with limited liability.
- Partnership: *Hapja Johap* is a legal form of partnership allowed under the Commercial Code.
- Joint venture: A joint venture is generally established as a domestically incorporated corporation whose shareholders have limited liability regarding the obligations of the corporation under the Commercial Code.
- Branch: A foreign corporation can perform its business operation in Korea by setting up a taxable presence in the form of a branch office. The branch office can be classified as a corporation and be taxable under the CITL if one of the following conditions is met; otherwise, the foreign entity shall be classified as an individual and be subject to the Individual Income Tax Law:
    - The foreign entity is a corporation under the laws of one's home country.
    - The foreign entity is composed of only limited liability members.
    - The foreign entity has an independent ownership of assets or separate right of lawsuit from its members.
    - An entity similar to the foreign entity is classified as a corporation under Korean law.
- Liaison office: A foreign corporation can establish a liaison office, which is not allowed to execute income-generating business activities in Korea.
- Sole proprietorship: Sole proprietorships are not a legal form of entity in Korea.

Guidance on taxation of an off-shore partnership

Under the CITL, a foreign corporation is defined as a corporation that has a head office or principal office in a foreign country (only if the foreign corporation shall not have the place of effective management in Korea).

Based on the nature of business, an off-shore partnership would be categorised as a foreign corporation if one of the following conditions is met:

- Has a legal personality.
- Only comprised of partners with limited liability.
- Has the legal rights and liabilities that are distinct from its members, including taking possession of assets or having the legal capacity to be a party against a law suit.
- The same or the most similar kind of domestic business entity constitutes a corporation under Korean laws.

Off-shore partnerships with a legal personality like corporate entities prescribed in the Korean Commercial Act, such as stock corporations (*Chusik Hoesa*), limited corporations (*Yuhan Hoesa, Yuhan Chegim Hoesa*), and unlimited corporations (*Hapmyong Hoesa, Hapja Hoesa*), are treated as foreign corporations for Korean CIT purposes. Also, off-shore partnerships having the nature of limited corporations prescribed in the Korean Commercial Act, such as stock corporations (*Chusik Hoesa*) and limited corporations (*Yuhan Hoesa, Yuhan Chegim Hoesa*), are treated as foreign corporations.

Lao People's Democratic Republic

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Significant developments

There have been no significant corporate tax developments in Lao People's Democratic Republic (PDR) during the past year.

Taxes on corporate income

Profits tax (PT)

All companies (including all forms of legal entities) that are registered under Lao PDR law are subject to PT on their worldwide income. Companies formed under foreign law, operating a business in Lao PDR, and conducting business in Lao PDR are subject to tax on their income derived in Lao PDR.

The standard rate of PT for companies in Lao PDR is 24% of net profit after adjustments for non-deductible expenses and others according to Lao Tax Law No. 70/NA, dated 15 December 2015. The 24% rate applies to both domestic and foreign investors.

Tax holidays and reduced PT rates are applicable to companies whose investment activities qualify as promoted investment activities (*see the Tax credits and incentives section for more information*) or large investments in mining and hydro power project (tax incentive is dependent on negotiation).

Lump-sum tax

The lump-sum tax is imposed on small and medium business operators that are not registered in the value-added tax (VAT) system and companies that did not prepare Lao accounting books. The lump-sum tax is paid in lieu of the PT, based on an agreement with the tax office; consequently, the lump-sum tax is regarded as a tax within the PT category.

Local income taxes

There are no provincial or local income taxes in Lao PDR.

Corporate residence

There is no definition of residence or permanent establishment (PE) provided in the amended Lao Tax Law No. 70/NA, dated 15 December 2015 (effective 24 May 2016), as well as the latest VAT Law, dated 23 July 2014 (effective 3 July 2015).

According to the double tax treaties (DTTs) of Lao PDR, 'permanent establishment' means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

It is understood that the reason for having no PE definition in the law is because there is foreign withholding tax (FWHT) levied on foreign entities conducting their business activities in Lao PDR. *For more information about the FWHT, please see the Withholding taxes section*.

Currently, the government is reassessing tax privileges and DTTs that they have offered to some businesses/signed with some countries in the past, and they have planned to cancel some; however, this is not yet final.

Other taxes

Value-added tax (VAT)

The standard VAT rate is 10%.

VAT is imposed on the final consumer of goods and services. Domestic goods and services used for production, trading, and consumption in Lao PDR, goods imported into Lao PDR, and services rendered by foreigners to Lao PDR customers are subject to VAT.

Certain goods and services are exempt from VAT. Exempted items include unprocessed agricultural products, seeds, fertilisers, textbooks, education services, medical services, certain bank services, and financial institution services.

Exported goods are zero-rated, except export of natural resources that aren't finished goods, which are subject to 10% VAT. The conventional credit method is used to calculate the VAT payable (i.e. output VAT less input VAT). Excess input VAT can be carried forward for six months (extendable) relating to goods and services. Excess input VAT arising from the capital expenditures that are regarded as fixed assets can be claimed until it is fully utilised. Input VAT for exports is refundable.

There is no concept of export services in the VAT Law. It appears that all services from all sources are subject to VAT.

Business operators engaged in production or trading of taxable goods and services must register in the VAT system if their annual revenue is 400 million Lao kip (LAK) or more. Companies below this threshold may voluntarily register. Only registered VAT payers may claim VAT refunds.

One unique feature of Lao PDR VAT is that VAT is imposed on the services rendered by overseas service providers to domestic service users (withholding VAT). Domestic service users have an obligation to withhold VAT on top of the service fees paid to overseas service providers. The rate of withholding VAT is 10%.

Import duties

All goods imported into Lao PDR are subject to import duty. Exemptions are available to enterprises operating promoted investment activities (*see the Tax credits and incentives section for more information*).

Lao PDR has adopted the General Agreement on Tariffs and Trade (GATT) valuation principles.

Duty rates are based on the Association of Southeast Asian Nations (ASEAN) harmonised tariff nomenclature for imports from ASEAN member countries (ASEAN Trade in Goods Agreement [ATIGA]).

Lao PDR has also signed free trade agreements (FTAs) with ASEAN dialogue countries: Australia and New Zealand (under their Closer Economic Relations FTA), China, India, Japan, and Korea; otherwise, normal rates are applied. Duty rates range between 0% and 40%, depending on whether the goods are ASEAN or other source.

Excise taxes

Excise tax is levied on consumers of certain imported goods, domestic produced goods, and services within the territory of Lao PDR. The rates range from 5% to 90%. Importers file and pay excise tax at the time of filing at the customs declarations at the customs checkpoints. Domestic producers and service suppliers shall file their monthly excise tax returns no later than the 15th day of the following month.

Property taxes

The land tax is based on both the location and the size of the land and is levied at annual rates per square metre. Land tax is payable in the first quarter of the relevant calendar year.

Transfer taxes

There are no transfer taxes in Lao PDR.

Stamp taxes

The stamp taxes in Lao PDR range from LAK 2,000 to LAK 20,000, depending on the types of documents.

Payroll taxes

Income from salaries and wages, including extra allowances, over-time work, position allowances, career allowances, annual bonuses, meeting allowances for members of the executive board of the companies, and other benefits received in cash and in kind, is subject to income tax withholding by employers at the progressive rates ranging from 0% to 24%. Personal income tax (PIT) is calculated based on gross revenue, as mentioned above, on a monthly basis, and is not recalculated again on an annual basis.

Social Security Scheme contributions

An enterprise with ten or more employees must register itself and its employees in the Social Security Scheme and make contribution to the scheme. Both the enterprise and its employees are obligated to contribute to the Social Security Scheme a combined 11.5% of the employees' basic salaries or wages. The enterprise contributes 6%, and each employee contributes 5.5%.

According to Notification No. 0824/NSSFO of Ministry of Labour and Social Welfare, the basic amount for Social Security Scheme calculation is LAK 4.5 million.

The Social Security Scheme contribution shall be paid by 15th day of the following month.

Administrative fees

Under the Tax Law, government sectors can collect fees for issuing fiscal licences, business licences, permits, visas, advertisement boards, broadcasting rights, and other services. The charges and service fees are set periodically by Presidential Decree.

Branch income

Branches of foreign companies are taxable on their income from carrying on business in Lao PDR. However, not all foreign companies can establish a branch in Lao PDR. Branches are applicable only to industries such as banking, financial institutions, aviation, and consulting.

Income determination

The PT calculation is based on an entity's actual accounting profits, prepared in accordance with the Lao Accounting Manual, as adjusted for tax purposes. The Lao PDR tax regulations are silent on the treatment of a large number of items. Generally, in such cases, the tax treatment will follow the accounting treatment. Some of the more common differences are depreciation, entertainment expenses, and the non-deductibility of reserves and provisions (until actually paid). In addition, there is a limitation on some expenses, such as travel expenses and charitable contributions.

Inventory valuation

Inventory valuation for tax purposes follows the method used for accounting purposes in Lao PDR. All allowances are non-deductible expenses.

Capital gains

There is no separate tax on capital gains in Lao PDR. However, profits from the sale of shares are subject to tax at the following rates based on the Law on Tax No. 70/NA, dated 15 December 2015:

- In case there is evidence of a cost certificate: 10% of the gain.
- In case there is no evidence of a cost certificate: 2% of the value of the selling price.

There is no tax for the gain on sale of investments in listed companies in Lao PDR.

The buyer of shares, except for purchase/sale of shares of a company listed in the stock market, is required to withhold and remit the tax.

The rate of income tax on sales or transfers of real property are as follows based on Law on Tax No. 70/NA, dated 15 December 2015:

- In case there is evidence of the cost of trading or transfer certificate: 5% of the gain.
- In case there is no evidence of the cost of trading or transfer certificate: 2% of the selling price.

Dividend income

Dividends received from another Lao PDR company or a foreign company are taxed at a flat rate of 10%, except for dividend income of listed companies in Lao PDR.

Interest income

Interest income is taxable in Lao PDR, except for interest income derived from loans lent by commercial banks and interest income derived from money deposited with commercial banks. The rate of income tax on interest income is 10%.

Rental/royalties income

Rental income and royalties income are taxable in Lao PDR. The rate of income tax on rental income is 10%, and the rate of income tax on royalties income is 5%.

Unrealised exchange gains/losses

Unrealised exchange gains are not taxable and losses are not deductible in Lao PDR.

Foreign income

There is no controlled foreign company (CFC) or similar regime in Lao PDR. Profits of a foreign subsidiary are taxable when remitted as dividends.

Deductions

Accrued expenses are deductible in Lao PDR. Reserves and provisions are not deductible until actually settled.

Depreciation

Depreciation rates prescribed under the Lao Tax Law No. 70/NA, dated 15 December 2015, may differ from financial accounting. Depreciation is on a straight-line basis over prescribed useful lives, as follows:

Assets	Years
Buildings used for industrial purposes:	
With useful life of 20 years or less	20
With useful life over 20 years	50
Buildings used for commercial and residential purposes:	
Permanent structures	20
Semi-permanent structures	10
Machinery, equipment, vehicles	5
Software	2
Land and water transport vehicles	5
Ships, cruises, ferries, and other similar boats	10
Office equipment	5
Passenger aeroplane and cargo	Depending on flight hour

Goodwill

There is no specific guidance on the deductibility of goodwill or amortisation in Lao PDR.

Start-up expenses

Start-up expenses are amortisable over two years in Lao PDR.

Interest expenses

Interest is deductible on an accrual basis following the accounting treatment. All interest payments must be supported by documents showing that the payments are commercially reasonable. Interest paid to a shareholder is not deductible.

Bad debt

Bad debt reserves are not deductible in Lao PDR. However, a deduction is allowed if a certain procedure has been followed, one still cannot recover the debt, and the debt is ultimately written off.

Charitable contributions

Charitable contributions in Lao PDR are limited to 0.30% of total annual business turnover.

Travel expenses

Travel expenses for administrative activities are limited to 0.60% of total annual business turnover.

Reception and telephone expense

Reception and telephone costs are each limited to 0.40% of total annual business turnover.

Entertainment expenses

Entertainment expenses are non-deductible in Lao PDR.

Advertisements

Advertisement costs are limited to 0.50% of total annual business turnover.

Pension expenses

Pension expenses are deductible when paid in Lao PDR.

Bribes, kickbacks, and illegal payments

Bribes, kickbacks, and illegal payments are not deductible in Lao PDR.

Fines and penalties

Fines and penalties are not deductible in Lao PDR.

Taxes

PT and input VAT paid when purchasing fixed assets are not deductible for PT calculation purposes.

Net operating and capital losses

Tax losses can be carried forward for three years, but no carryback is allowed. A change in control will not impact a company's loss carryforward. Capital losses are treated as ordinary losses.

Payments to foreign affiliates

Payments to foreign affiliates are deductible if in the ordinary course of business.

Group taxation

Consolidation or grouping is not permitted, and each entity must file on a separate basis in Lao PDR.

Transfer pricing

There are no specific transfer pricing rules in Lao PDR. However, inter-company transactions should be at arm's length.

Thin capitalisation

The ratio of debt to capital must not exceed 70% of the total capital for concession investment activities. There are no thin capitalisation rules for general investment activities in Lao PDR.

Controlled foreign companies (CFCs)

There is no CFC or similar regime in Lao PDR.

Tax credits and incentives

Foreign tax credit

There is no foreign tax credit regime in the Law on Tax. However, certain tax treaties entered into by Lao PDR do have provisions for either deductibility of foreign tax or a credit.

PT incentives

PT incentives are provided under the Law on Investment Promotion 2016. This law divides investment areas into three zones, namely Zone 1, Zone 2, and Zone 3. The PT exemptions are as follows:

Zone	Areas	PT exempted (years)	Additional PT exempted (years)
1	Poor zone, remote zone with socio-economic infrastructure unfavourable to investment.	10	5*
2	Zone with socio-economic infrastructure favourable to investment.	4	3*
3	Special economic zone.	Shall comply with the specific regulation.	

* Note: If invest in the activities set out in item 2, 3, 5, and 6 of Article 9 of the Law on Investment Promotion, as follows:

- Item 2: Clean, toxic-free agriculture, planting seed production, animal breeding, industrial plantation, forestry development, protection of environment and bio diversity, activities promoting rural development and poverty reduction.
- Item 3: Environmental friendly agricultural processing industry, national traditional and unique handicraft processing industry.
- Item 5: Educations, sports, human resources development and labour skill development, vocational training institutions or centres, production of educational and sports equipment.
- Item 6: Construction of modern hospitals, pharmaceutical and medical equipment factory, production and treatment by traditional medicine.

PT exemption starts from the date of the investing enterprise generating business revenues. After finishing the period of PT exemption as mentioned above, the enterprise shall pay PT in accordance to the Law on Tax.

Concession business shall comply with relevant laws or according to the concession agreement.

Incentives related to customs duty and other taxes

In addition to the incentives related to PT, investors shall also be entitled to the following customs duty and other tax incentives:

- Exemption from PT in the accounting year after the incentives for PT exemption for a business that spends its net profit to expand its business.
- Import of materials, equipment, which may not be supplied or produced in Lao PDR, to form the fixed assets, and machinery and vehicles directly used for production will receive customs duty exemption and pay VAT at the rate of 0%. Importation of all types of fuel, gas, lubricant, administrative vehicles, and other materials shall comply with the relevant laws and regulations.
- Import of raw materials, equipment, and spare parts to be used in the production for export shall be exempted from customs duty at the time of import and granted the custom duty exemption at the time of export and pay VAT at the rate of 0%. Use of domestic raw materials that are not natural resources for producing finished and semi-finished products at the time of export shall pay VAT at the rate of 0%.
- Investors can transfer the annual losses to the next following year to be deducted from profit within the period of three years; however, the losses shall be audited and certified by the tax officer. After this period, the remaining loss is not allowed to be deducted from profit anymore.
- In the case of the Special and Specific Economic Zones, the incentives related to customs duties and other taxes shall comply with the Decrees on the establishment and management of each zone.

Specific promotion incentives

Investment in hospitals, kindergartens, academic schools, vocational schools, colleges, universities, research centres, and some activities related to public utilities shall obtain an exemption of rental or land concession as follows:

- Zone 1: Exemption of rental or land concession for a maximum of 15 years.
- Zone 2: Exemption of rental or land concession for a maximum of 8 years.
- Zone 3: Shall comply with the specific regulation.

Withholding taxes

WHT is applied to various types of payments made to domestic and foreign recipients.

Payment	WHT rate (%)
Dividend	10
Interest from lending activities (non-bank), commission, and guarantee fees	10
Profit from sale of shares	2 to 10
Income from business activities of the State Organizations, Lao Front for National Construction, Mass Organization, and Civil Society	10
Prizes and lottery prizes with the value of LAK 5 million and above	10
Intellectual property (IP) royalty	5
Sale or transfer of real property	2 to 5

Lao PDR has DTTs with the following countries, and WHT rates under the treaties are as follows:

	WHT (%)		
Recipient	**Dividends**	**Interest**	**Royalties**
Belarus (not in force) (1)	5/10 (2)	8	5
Brunei	-	-	-
China	5	5	5
Kuwait (not in force)	-	-	-
Luxembourg	5/15 (3)	10	5
Malaysia	5	10	10
Myanmar	-	-	-
North Korea	5	10	5
Russia	10	10	0
Singapore	5/8 (4)	5	5
South Korea	-	-	-
Thailand	10	10	5
Vietnam	10	10	5

Notes

1. Not effective. Requested for ratification.
2. 5% of the gross amount of the dividends if the beneficial owner is a company (other than a partnership) that directly holds at least 10% of the capital of the company paying the dividend; 10% of the gross amount of the dividends in all other cases.
3. 5% of the gross amount of the dividends if the beneficial owner is a company (other than a partnership) that directly holds at least 10% of the capital of the company paying the dividend; 15% of the gross amount of the dividends in all other cases.
4. 5% of the gross amount of the dividends if the beneficial owner is a company (other than a partnership) that directly holds at least 10% of the capital of the company paying the dividend; 8% of the gross amount of the dividends in all other cases.

Foreign withholding tax (FWHT)

An FWHT applies where a registered entity in Lao PDR contracts with a foreign supplier of goods and services (i.e. regardless of whether the services are provided in Lao PDR or outside Lao PDR) not registered in Lao PDR. The FWHT comprises both a PT and VAT (i.e. service only) element and is the final tax on the foreign supplier. The FWHT withholding and filing obligation rests with the Lao PDR customer, and it is applied before payment to the foreign supplier.

For foreign suppliers, PT must be withheld at a deemed percentage of taxable turnover. The deemed rates are determined according to the nature of the contract or activity.

Activity	**Deemed profit margin (% of business revenue)**	**Deemed PT rate (%)**
Commerce	5	1.2
Production	3	0.72
Services:		
Transportation goods and services	5	1.2
Building service - repair	10	2.4
Exploration - mineral	20	4.8
Excavation - trees	5	1.2
Exploration - embankments	15	3.6

Activity	Deemed profit margin (% of business revenue)	Deemed PT rate (%)
Entertainment services	25	6.0
Consulting services	10	2.4
Broker and developer	20	4.8
Other services	10	2.4

The above rates are under Article 33 of the Law on Tax No. 70/NA, dated 15 December 2015.

These PT rates are then added to the VAT at 10% to determine the total FWHT. For example, a foreign service charge of LAK 1,000 would result in LAK 48 of withholding PT and add on of LAK 100 of VAT for a total FWHT of LAK 148. Payments to foreign suppliers for services rendered are subject to both PT WHT and VAT WHT, while payments for foreign suppliers of goods are only subject to PT WHT since VAT is paid before the goods enter Lao PDR.

Tax administration

Taxable period

PT is determined on a calendar-year basis.

Tax returns

According to the Lao Tax Law No. 70/NA, dated 15 December 2015, the annual tax return is due by 10 January of the subsequent year. Submission of the final tax return will be followed by an audit by the Tax Department.

Payment of tax

PT is payable quarterly in advance, with a final payment after year-end. The first three payments must be paid by 10 April, 10 July, and 10 October of the current tax year. The final payment is due with the submission of the final tax return by 10 January of the subsequent year. The quarterly payments are either based on the actual or prior year's PT (or expected tax for the current year). Any excess PT payment can be carried forward to the subsequent year.

Tax audit process

According to the Enterprise Law 2013, the audit of a large company, who has assets of more than LAK 50 billion, is mentioned. However, in practice, the tax authorities will access the company after the annual tax filing and issue a certificate to the company after they complete their audit process. Most large companies are audited annually in Lao PDR.

Statute of limitations

The statute of limitations is generally three years in Lao PDR.

Topics of focus for tax authorities

There are no areas of special focus in tax examinations in Lao PDR.

Macau

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Significant developments

Tax incentives for the tax year 2018

On 13 December 2017, the Legislative Assembly approved certain tax incentives proposed by the Chief Executive of Macau in the Budget for the financial year 2018. The key tax incentives include the following:

- The tax-free income threshold for complementary (corporate) tax has been increased from 32,000 Macanese patacas (MOP) to MOP 600,000 for income derived in the tax year 2017. Taxable income over MOP 600,000 is taxed at 12%.
- The standard MOP 3,500 reduction in property tax liabilities will continue to be available in the tax year 2018 for both self-use and rental properties. This incentive does not apply to corporate and Macau non-residents.
- Restaurants will continue to be exempt from tourism tax in the tax year 2018.
- Insurance policies written or renewed in the tax year 2018 and banking transactions in the tax year 2018 will continue to be exempt from stamp duty.
- Admission tickets for performances, exhibitions, and entertainment programs will continue to be exempt from stamp duty in the tax year 2018.
- Commercial and industrial operations will continue to be exempt from the annual industrial tax in the tax year 2018.

Taxes on corporate income

Complementary tax is imposed on the worldwide income earned by Macau-registered entities, irrespective of where their residence or headquarters are situated and irrespective of the nature of the income. The exception to the foregoing is rental income from leasing of immovable properties located in Macau, which is taxed separately under the property tax regime.

Generally, if a foreign entity is engaged in commercial/industrial activities and/or rendering services in Macau, the resultant gain from such commercial/industrial activities and/or services rendered will be subject to complementary tax.

According to the Macau Complementary Tax Law, complementary tax is imposed on a progressive rate scale ranging from 3% to 9% for taxable profits below or equal to MOP 300,000 and 12% for taxable profits over MOP 300,000. Taxable profits below MOP 32,000 are exempt from tax.

According to the Budget for the financial year 2018 approved by the Legislative Assembly (2018 Budget), the tax-free income threshold for complementary tax has been increased from MOP 32,000 to MOP 600,000 for income derived in the tax year 2017 (taxable income in excess of MOP 600,000 is taxed at 12%). The changes in the tax-free income threshold and the tax brackets are subject to approval by the Legislative Assembly on an annual basis unless such amendments are written into the relevant tax laws.

Types of taxpayers and associated tax bases

Group A taxpayers

Taxpayer entities whose registered capital reached MOP 1 million, or whose average taxable profits reached MOP 500,000 per year in three consecutive years, will automatically become Group A taxpayers in the tax year following the year in which the relevant notification is issued by the Macau Finance Bureau (MFB). A taxpayer entity can also elect to become a Group A taxpayer by filing a Group A declaration form. Profits of Group A taxpayers are assessed based on the actual accounting income after making necessary tax adjustments.

Group B taxpayers

Group B taxpayers refer to any individual or any other form of companies not mentioned above and those taxpayers that do not keep detailed accounting records. Profits of Group B taxpayers are assessed on a deemed basis if the reported income is below the internal parameters set by the MFB for taxpayers in similar industries.

Corporate residence

Corporate residence is generally determined by reference to the place of establishment.

Permanent establishment (PE)

There is no specific definition of PE in the Macau Complementary Tax Law. Technically speaking, there are two major criteria for determining whether a foreign entity should be subject to complementary tax, and the key phrases are ‘engaging in commercial/industrial activities’ and/or ‘rendering services in Macau’. These phrases are also not defined. Generally, if a foreign entity is engaged in commercial/industrial activities and/or rendering services in Macau, the resultant gain from such commercial/industrial activities and/or services rendered will be subject to complementary tax.

Other taxes

Value-added tax (VAT)

There is no VAT regime in Macau.

Customs duties/import tariffs

Apart from consumption tax imposed on tobacco and spirits entering into Macau, there are no customs duties/import tariffs in Macau.

Consumption tax (excise duty)

Consumption tax is imposed only on tobacco and spirits entering into Macau.

There are two methods for determining the amount of consumption tax payable, by quantity or by value. The former method of assessment is based on the weight or volume of goods and the latter is based on the price of the goods imported into Macau.

The rate of consumption tax varies depending on the classification of the imported goods.

Property tax

Property tax is imposed annually on the owner of buildings situated in Macau. This is first payable after acquiring a property or upon the expiry of the property tax exemption period, if applicable. Different exemption periods are granted, depending on the location of the property. Additional exemption periods may apply in special cases.

For leased properties, property tax is charged at 10% on the actual rental income, and, by application, a maximum deduction based on 10% of the rental income derived to cover repair and maintenance expenses incurred will be granted if approved by the MFB.

For self-use properties, property tax is charged at 6% on the official ratable value as established by the appointed committee of the MFB. A deduction of 10% of the official ratable value to cover repair and maintenance expenses will be automatically granted for self-use property. If the property is not occupied, the owner can apply for an exemption from property tax, the approval of which is entirely at the discretion of the MFB.

According to the 2018 Budget, there is a standard MOP 3,500 reduction in the property tax liabilities assessed in the tax year 2018 for both self-used and rental properties. This incentive does not apply to corporate and Macau non-residents.

Stamp duty

Stamp duty is payable on certain types of documents and stampable transactions at a small fixed amount or at rates ranging from 0.1% to 10% on the value represented by the documents and transactions.

The charge to stamp duty has been extended to property transfers and the irrevocable transfer of certain assets. Stamp duty at progressive rates ranging from 1% to 3% is payable on transfer of immovable property with a surcharge of 5% on the duty payable, resulting in effective stamp duty rates of 1.05% to 3.15%. The irrevocable transfer of certain assets without consideration is subject to a 5% stamp duty.

Insurance policies, written or renewed, and banking transactions have been exempt from stamp duty since 2005. This exemption has been approved by the Legislative Assembly and will continue to be available in the tax year 2018.

Admission tickets for performances, exhibitions, and any kind of entertainment programmes are exempt from stamp tax for the tax year 2018, as approved by the Legislative Assembly. This exemption, if extended, will be published by the Macau government on an annual basis.

Additional stamp duty for acquisition of second residential property and beyond

A transferee acquiring residential property will be subject to additional stamp duty if the transferee owns other residential property at the time of acquisition. Such additional stamp duty is applicable to individual, corporate, as well as a transferee acquiring more than 80% of a company that owns Macau residential property. The applicable rate is 5% on the transfer consideration for acquisition of the second residential property and 10% on the transfer consideration for acquisition of the third residential property and onward. A transferee holding only one residential property but wishing to dispose it and acquire another residential property as replacement can apply for refund of the additional stamp duty paid if the disposal takes place within one year from the date of acquisition.

Special Stamp Duty (SSD)

The transferor of a residential property, commercial property, office, car-parking space, or property under construction is subject to SSD at 20% on the value of the property if the property is resold within a year of its purchase. The SSD rate is reduced to 10% if the resale takes place between one and two years after the purchase. The SSD is also applicable to transfers of an 80% or more shareholding interest in a Macau company that has properties.

Buyer Stamp Duty (BSD)

A company, an entrepreneur, or a non-Macau resident acquiring a residential property in Macau is subject to BSD at a flat rate of 10%, on top of the existing Stamp Duty and SSD, if applicable.

Professional (Salaries) Tax

Professional Tax is payable by anyone receiving income from employment services performed in Macau or from a Macau employment. In Macau, the Professional Tax reporting, withholding, and remittance obligations rest with the employer.

Payroll taxes

There is a pay-as-you-earn (PAYE) system, similar to those used in other countries, which is applicable to salaried individuals only. The employing entity is obligated to report and collect the amount of professional tax payable from its employees each month and remit such payments to the MFB before the 15th day of the month following the quarter-end for local resident employees and foreign employees with valid work visas.

Social security fund contribution

Social security fund contribution in the total amount of MOP 90 per month is payable for resident employees. The employer contributes two-thirds of the amount (i.e. MOP 60) and the employee contributes one-third of the amount (i.e. MOP 30).

Annual industrial tax

The annual industrial tax has been exempted for the tax year 2018 and has been exempted on an annual basis by the Macau government since 2002.

Under the Industrial Tax Code, all commercial or industrial operations carried out in Macau are subject to industrial tax at the beginning of each year. The amount of the tax is dependent upon the nature of the business. The table below is an illustration of the tax amounts applicable to certain types of businesses in Macau.

Type of business	Tax (MOP)
Commercial banks	80,000
Construction companies	500
Hotels	500

Type of business	Tax (MOP)
Insurance companies	500
Textile companies	500

Special gaming tax

Special gaming tax is levied at 35% on the gross gaming revenue derived by gaming concessionaires authorised to carry on the operation of games of chance in Macau under Law 16/2001.

Tourism tax

Tourism tax is imposed at the rate of 5% on bills of services, excluding telecommunication and laundry services, and service charges of up to 10% rendered in Macau by establishments such as hotels, guest houses, dancing halls, night clubs, massage/sauna parlours, gymnasiums, karaoke, and the like. Such tax is generally borne by consumers.

Restaurants are exempt from tourism tax in the tax year 2018 and have been exempt, via an exemption published on an annual basis by the Macau government, since 2002.

Motor vehicle tax

Motor vehicle tax is imposed on the sale of new motor vehicles to consumers and the importation of new motor vehicles for self-use. Exemptions are available to certain persons and organisations and for certain specific usages. Generally, motor vehicle tax is levied based on the listed selling prices as registered with the MFB. The rate of motor vehicle tax varies depending on the type of motor vehicle and its value.

Land rent

Land rent is payable by lessees of leasehold land in Macau on an annual basis according to the amount specified in the relevant lease contract.

According to the 2018 Budget, land rent below MOP 100 shall not be collected by the MFB in the tax year 2018. However, any such amount already collected shall not be refunded.

Branch income

Branch income is subject to tax at the same rate as that for corporations. The taxable income is ascertained based on branch accounts.

Income determination

The paragraphs below describe the tax acceptable treatments under the prevailing Complementary Tax Law and are for reference only.

Inventory valuation

Inventory should be stated at actual cost, and conformity between book and tax reporting is required. Market selling price or replacement cost is allowed only in special circumstances, and prior approval of the Director of the MFB is required for adoption of such inventory valuation methods. The write-down of inventory values is not permitted.

Capital gains

Gains or losses from the realisation of capital assets of a corporate taxpayer are treated as current revenue or expense items for complementary tax purposes.

Dividend income

Dividends from all sources are subject to complementary tax in the hands of a recipient incorporated in Macau unless the dividends were paid out of profits that have been taxed at the corporate level in Macau. Where dividends to shareholders are paid out of profits of a Macau entity that have not been taxed in Macau, complementary tax will technically be charged on the dividend distribution to the shareholders.

Interest income

Interest income received by or accrued to a corporate taxpayer in Macau is subject to complementary tax.

Royalty income

Royalty income received by or accrued to a corporate taxpayer in Macau is subject to complementary tax. There is currently no withholding tax (WHT) imposed on royalties paid or accrued to a non-resident provided that such non-resident has not carried on commercial/industrial activities in Macau.

Foreign income

Companies incorporated in Macau are subject to complementary tax on worldwide income, wherever received or credited. There are no provisions in the Macau Complementary Tax Law that allow foreign income to be deferred for tax purposes. Currently, double taxation relief is available under the respective double taxation agreements (DTAs) that Macau has with Cabo Verde, the People's Republic of China, Mozambique, and Portugal.

Deductions

Please note that the assessor is empowered to disallow any business expenses (e.g. entertainment, travelling) where the amount incurred is considered to be excessive.

Depreciation

An initial allowance of 20% is granted on buildings. The rates of tax depreciation are detailed in Decree-Law No.4/90/M, dated 5 March 1990. The Decree-Law prescribes the maximum annual tax depreciation rates and the number of years of asset life for different asset classes under the straight-line method. For illustration, the maximum depreciation rates and the maximum useful life currently applicable to the general types of assets are set out below:

Assets	Maximum annual percentage rate (%)	Maximum number of years
Industrial buildings	4	50
Office and residential buildings	2	100

Assets	Maximum annual percentage rate (%)	Maximum number of years
Machinery and installations, air conditioning, elevators, equipment	10 to 20	20 to 10
Tools	20 to 33.3	10 to 6
Laboratory, telex and interior telephone equipment, furniture, filing systems, typewriters, and accounting machines	16.66 to 25	12 to 8
Computer hardware	25	8
Office installations	14.29	14
Trucks	14.29	14
Automobiles	20	10
Intangible assets, pre-operating expenses incurred prior to commencement of business	33.33	6
Deferred expenses arising in connection with increases in share capital, changes in form of business enterprises, issuance of debentures, marketing and other studies, and financial expenses incurred for the acquisition or own production of fixed assets prior to completion	33.33	6
Patents	10	20
Manufacturing licences, concessionary agreements, and similar rights	*	*
Trademark	*	*

** At the discretion of the authorities.*

In the case of commercial and industrial buildings, depreciation is not allowed for the value attributable to the cost of the freehold land. Where the value of the freehold land cannot be determined from the total cost of land and buildings, a portion equal to 20% is deemed to be attributable to the land value for the purpose of determining the value of buildings to be depreciated.

Depreciation can be claimed either on a prorated basis in accordance with the prescribed annual rates for assets that are not acquired at the beginning of the financial year or on an annual basis.

The cost of repairs and maintenance exceeding 10% of the acquisition cost of the asset in a given year is deemed to be an expense of a capital nature and should be capitalised and depreciated over the remaining life of the asset.

Goodwill

Cost of acquisition of goodwill/amortisation of goodwill is generally deductible to the extent it is incurred in the generation of assessable profits.

Interest expenses

There is no thin capitalisation rule in Macau. However, the MFB may assess the reasonableness of the interest rate charged for interest expense paid to related parties.

Bad debts

The amount provided against doubtful trade receivables is an allowable tax deduction, but the provision cannot exceed 2% of the total receivables, except in the case of banks, where the minimum provisions required under the local banking regulations are fully tax-deductible.

Debts considered uncollectible may be written off only when adequate proof can be shown, usually by way of bankruptcy court proceedings.

Charitable contributions

A deduction of up to 0.2% of the company's turnover is allowable for donations to charitable organisations recognised by the tax authority.

Pension expenses

The employer's contribution to the staff provident fund legally registered in Macau is fully tax-deductible, up to 15% of the employees' basic salary.

Fine and penalties

Tax fines are not deductible.

Taxes

Taxes, except for complementary tax and taxes paid on corporate profits, are generally deductible to the extent they are incurred in the generation of assessable profits.

Other significant items

- An amount provided against stock obsolescence of up to 3% of the total stock value at year-end is allowed as a tax deduction.
- Losses arising from insurable risks are not allowable as a tax deduction.
- Staff social welfare expenses paid for the benefit of employees (e.g. canteens, libraries) are fully tax-deductible.

Net operating losses

Agreed tax losses can be carried forward for three consecutive years for Group A taxpayers. Group B taxpayers are not allowed to carry their tax losses forward to future years. Tax losses cannot be carried back in Macau.

Payments to foreign affiliates

The regulations make no specific mention of royalties and service fees paid to foreign affiliates. The MFB generally monitors the deductibility of such payments. Payments to foreign service providers for consulting services or construction-related services are not deductible if such consulting contracts are not properly registered in Macau.

Group taxation

There is no provision for group taxation in Macau.

Transfer pricing

There is no transfer pricing provision in the Macau tax regime.

Thin capitalisation

There is no thin capitalisation provision in the Macau tax regime.

Controlled foreign companies (CFCs)

There are no CFC rules in the Macau tax regime.

Tax credits and incentives

Foreign tax credit

There is no foreign tax credit provision in the Macau Complementary Tax Law. Foreign tax credit is only available under the relevant provisions of the comprehensive tax arrangements/agreements that Macau has entered into with the People's Republic of China, Portugal, Mozambique, and Cabo Verde, respectively.

Capital investment incentives

A 50% reduction in complementary tax and stamp duty on certain transactions, as well as exemptions from annual industrial tax (currently exempt for all taxpayers) and property tax (up to periods prescribed by the MFB), are allowable for taxpayers in the manufacturing industry (as defined in the Decree-Law) whose capital investment is aimed at the introduction of new products or high technology, improvement of productivity, and increase in exports of goods to new markets.

Where profits are retained in reserves and reinvested in installation of new equipment within the following three financial years, the reinvested reserves can be deducted from taxable profits, provided that the reinvested reserves are attributable to profits earned from normal business operations and the investment is considered to be beneficial for the economic development of Macau.

Offshore services business incentives

Profits derived by approved offshore institutions from prescribed offshore service-related activities are exempt from all forms of taxes, such as complementary tax, annual industrial tax (currently exempt for all taxpayers), and stamp duties.

Incentives for owners of touristic facilities

Additional incentives, such as an extended property tax exemption period, exemption from annual industrial tax (currently exempt for all taxpayers), reduction in stamp duty, as well as acceleration of depreciation for complementary tax purposes, are available to owners of facilities that qualify as touristic facilities.

Withholding taxes

Currently, there is no provision in the Macau Complementary Tax Law for the withholding of taxes from payments made by domestic corporations to overseas companies.

Tax administration

Taxable period

The Macau tax year is on a calendar-year basis.

Tax returns

Assessments are made by the MFB upon review of the tax returns, which must be lodged before 31 March or 30 June of each year for Group B or Group A taxpayers, respectively.

Payment of tax

A provisional tax payment calculated based on the declared taxable profit for a Group A taxpayer or final assessed profit for a Group B taxpayer is payable in two equal instalments, in September and November. However, if the amount is not greater than MOP 3,000, payment will be requested in one lump sum amount in September. For Group A taxpayers, a final tax assessment will be issued upon completion of the tax assessment by the MFB and additional tax payment, if any, will be due around a month's time after issuance.

Tax audit process

There is no specific tax audit cycle in Macau. The MFB is empowered by the Macau Complementary Tax Law to carry out a tax audit whenever the information provided by a taxpayer in its tax return is considered unclear or insufficient, and subsequent replies to the MFB's queries, if any, are considered inadequate.

Statute of limitations

The statute of limitations period is five assessment years from the relevant year of assessment for both Group A and Group B taxpayers.

Topics of focus for tax authorities

The MFB generally focuses on the deductibility of expenses (e.g. staff costs, provisions, depreciation, management fees, payments made to overseas service providers, bad debts, donations).

Other issues

Choice of business entity

A foreign company conducting business (except for short-term projects) in Macau is obligated to set up a legal establishment, which can be in the form of a company or a branch.

There are two types of Macau companies: companies limited by shares and companies limited by quotas. The capital and corporate governance requirements for a company limited by shares are higher than a company limited by quotas, and, in general, a company limited by quotas is used by investors that are not in regulated industries.

Exchange of information

Law 20/2009 is the legislation that governs the exchange of information by Macau with other tax jurisdictions within the scope of bilateral tax treaties or arrangements. Its objective is to promote the transparency of the Macau tax administration and to demonstrate Macau's willingness to cooperate with treaty partners in combating tax avoidance or tax evasion activities.

The information to be exchanged under Law 20/2009 is strictly confined to information collected for tax purposes only, and includes the following:

- Information collected within the jurisdiction of the MFB.
- Information collected by the MFB from financial institutions that are governed by the Macau Financial System Act and offshore institutions that are governed by the Macau Offshore Law (the Institutions).

So far, Macau has concluded tax information exchange agreements (TIEAs) or DTAs that comply with the latest internationally agreed standards with 22 different tax jurisdictions. The following tables summarise the TIEAs and DTAs that Macau has signed, and the TIEAs and DTAs that are in negotiation:

TIEAs have been signed by Macau with the following countries:

- Argentina
- Australia
- Denmark
- Faroe Islands
- Finland
- Greenland
- Guernsey
- Iceland
- India
- Ireland
- Jamaica
- Japan
- Malta
- Norway
- Sweden
- United Kingdom of Great Britain and Northern Ireland

TIEAs are in negotiation with the following countries:

- Germany
- New Zealand

DTAs have been signed by Macau with the following countries:

Treaty partners	Effective date
Belgium	Not yet effective
Cabo Verde	11 January 2011
The Mainland of China	1 January 2004 (Note that the first protocol and the second protocol became effective on 15 September 2010 and 8 October 2011, respectively)
Mozambique	11 January 2011
Portugal	1 January 1999
Vietnam	Not yet effective

A DTA with Hong Kong is in negotiation.

It is believed that more comprehensive DTAs or TIEAs will be signed between Macau and other tax jurisdictions in the near future to demonstrate Macau's willingness to continue to cooperate with the Organisation for Economic Co-operation and Development (OECD) countries in combating tax avoidance or evasion activities.

As the information of a Macau taxpayer is becoming more transparent under comprehensive DTAs or TIEAs, it is important for Macau companies with cross-border transactions to perform periodic tax health checks to ensure that tax planning arrangements, if any, that have been put in place in the past, remain technically defensible. As Macau offshore companies continue to be a 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.

Foreign Account Tax Compliance Act (FATCA)

On 14 December 2016, Macau and the United States (US) signed an inter-governmental agreement (IGA) that will facilitate compliance with the US FATCA by financial institutions in Macau. FATCA is an anti-tax evasion regime enacted by the United States to detect US taxpayers who use accounts with non-US financial institutions to conceal income and assets from the US Internal Revenue Service (IRS). The IGA signed between Macau and the United States is Model 2, which requires financial institutions in Macau to report the relevant account information of US taxpayers to the US IRS directly, supplemented by group requests made by the US IRS, on a need basis, for exchange of information on relevant US taxpayers at a government level. Under the IGA, financial institutions in Macau need to register and conclude separate individual agreements with the US IRS. Under the agreements, these institutions shall seek the consent of their account holders who are US taxpayers for reporting their account information to the US IRS annually. The IGA covers exemptions for financial institutions or products that present low risks for tax evasion by US taxpayers.

Malaysia

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Significant developments

Goods and services tax (GST)

The new government has reduced the GST standard tax rate of 6% to 0%, effective from 1 June 2018. The new government has also announced that the sales and services tax will be reintroduced in place of GST, which is to be abolished. These changes are expected to take place in September 2018.

Digital advertising

The Malaysian tax authorities recently issued a practice note to state their position that payments for use of applications (Apps) to create advertising campaigns constitute royalty under the domestic law.

Taxes on corporate income

For both resident and non-resident companies, corporate income tax (CIT) is imposed on income accruing in or derived from Malaysia. The current CIT rates are provided in the following table:

Type of company	Chargeable income (MYR)	CIT rate for year of assessment 2018 (%)
Resident company (other than company described below)		24*
Resident company: • with paid-up capital of 2.5 million Malaysian ringgit (MYR) or less • that does not control, directly or indirectly, another company that has paid-up capital of more than MYR 2.5 million, and • is not controlled, directly or indirectly, by another company that has paid-up capital of more than MYR 2.5 million.	On the first 500,000	18
	In excess of 500,000	24*
Non-resident company		24

* For years of assessment 2017 and 2018, CIT is reduced based on the incremental chargeable income for companies, limited liability partnerships, trust bodies, executor of estate of an individual domiciled outside Malaysia at the time of death, and receiver appointed by the court. The rates as follows are applicable:

% of increase in chargeable income compared to immediate preceding year of assessment	% point reduction	Income tax rate applicable for incremental portion of chargeable income (%)
Less than 5.00	Nil	24

% of increase in chargeable income compared to immediate preceding year of assessment	% point reduction	Income tax rate applicable for incremental portion of chargeable income (%)
5.00 to 9.99	1	23
10.00 to 14.99	2	22
15.00 to 19.99	3	21
20.00 and above	4	20

Petroleum income tax

Petroleum income tax is imposed at the rate of 38% on income from petroleum operations in Malaysia. An effective petroleum income tax rate of 25% applies on income from petroleum operations in marginal fields. No other taxes are imposed on income from petroleum operations.

Local income taxes

There are no other local, state, or provincial government taxes on income in Malaysia.

Corporate residence

A company is tax resident in Malaysia in a basis year (normally the financial year) if, at any time during the basis year, the management and control of its affairs are exercised in Malaysia. Generally, a company is regarded as resident in Malaysia if, at any time during the basis period for a year of assessment, at least one meeting of the Board of Directors is held in Malaysia concerning the management and control of the company.

Permanent establishment (PE)

Generally, a non-resident entity is regarded as having a PE in Malaysia if it has a fixed place of business in Malaysia, where the business of the entity is wholly or partly carried on. A non-resident company may also be deemed to have a PE in Malaysia under certain circumstances, such as the following:

- It is represented by a dependent agent in Malaysia who has the authority to conclude contracts on its behalf and who has repeatedly exercised that authority.
- It carries on supervisory activities in Malaysia for six/nine months in connection with a construction, installation, or assembly project.

Other taxes

Goods and services tax (GST)

GST was introduced on 1 April 2015 at the standard rate of 6%. Businesses making taxable supplies where the annual sales turnover exceeds MYR 500,000 must register for GST, which is administered by the Royal Malaysian Customs Department. Effective from 1 June 2018, the GST rate has been reduced to 0%. The GST will be replaced by the sales and services tax in September 2018.

Import duties

Import duties are levied on goods that are subject to import duties and imported into the country. Import duties are generally levied on an *ad valorem* basis but may also be imposed on a specific basis. The *ad valorem* rates of import duties range from 2% to

60%. Raw materials, machinery, essential foodstuffs, and pharmaceutical products are generally non-dutiable or subject to duties at lower rates.

Excise duties

Excise duties are imposed on a selected range of goods manufactured and imported into Malaysia. Goods that are subject to excise duty include beer/stout, cider and perry, rice wine, mead, un-denatured ethyl alcohol, brandy, whisky, rum and tafia, gin, cigarettes containing tobacco, motor vehicles, motorcycles, playing cards, and mahjong tiles.

The rate of excise duties vary from a composite rate of MYR 0.1 per litre and 15% of the value for certain types of spirituous beverages, to as much as 105% of the value of motorcars (depending on engine capacity).

Property tax

Property tax is levied on the gross annual value of property as determined by the local state authorities.

Real property gains tax (RPGT)

RPGT is charged upon gains from disposals of real property, which is defined as:

- any land situated in Malaysia, as well as any interest, option, or other right in or over such land, or
- shares in a real property company (RPC), which is a controlled company holding real property or shares in another RPC or a combination of both, where the total defined value is not less than 75% of its total tangible assets.

RPGT is imposed on companies as follows:

Holding period from date of acquisition	RPGT rate (%)
Up to three years	30
In the fourth year	20
In the fifth year	15
Exceeding five years	5

Stamp duty

Malaysia imposes stamp duty, which is payable by the buyer/transferee, on chargeable instruments. Some examples are provided as follows:

Transaction type	Value chargeable	Stamp duty rate (%)
Sale/transfer of properties (excluding stock, shares, or marketable securities)	Market value	1 to 3
Sale/transfer of stock, shares, or marketable securities	Consideration paid or market value, whichever is higher	0.3
Service/loan agreements	Value of services/loans	0.5

Payroll taxes

Under the Monthly Tax Deduction scheme, employers are required to deduct the prescribed amount of tax from employees' salaries each month, to be remitted to the tax authorities not later than the 15th day of each calendar month.

Social security contributions

Employees' Provident Fund (EPF)

The Malaysian EPF is a compulsory pension scheme for all Malaysians. The EPF provides for compulsory retirement savings and contributions for all Malaysian citizens and Malaysian permanent residents who are working in Malaysia. It is not compulsory for non-Malaysian citizens and non-Malaysian permanent residents to contribute to the EPF, but they may elect to do so.

	Malaysian citizens and permanent residents (mandatory)		Expatriates and foreign workers (voluntary)	
	% of contribution of employee's wages (minimum)			
Contribution by	**Employer**	**Employee**	**Employer**	**Employee**
Up to age 60:				
Income > MYR 5,000	12.0%	11.0%	MYR 5 per person	11.0%
Income ≤ MYR 5,000	13.0%			
Age 60 and above, up to 75:				
Income > MYR 5,000	6.0%	5.5%	MYR 5 per person	5.5%
Income ≤ MYR 5,000	6.5%			

Social Security Organisation

Malaysia also has a Social Security Organisation (SOCSO) who administers the Employment Injury Insurance Scheme (EIIS) and the Invalidity Pension Scheme (IPS). All employees with monthly wages below MYR 4,000 are covered by the schemes, and employees who qualify for the schemes will continue to remain within the schemes notwithstanding that their monthly wages may subsequently exceed MYR 4,000. A monthly contribution must be made and may fall under one of two categories:

- Both the employer and employee make monthly contributions to EIIS and IPS. The sum is based on the employee's monthly wages and is restricted to a maximum of MYR 69.05 for the employer and MYR 19.75 for the employee.
- The employer makes a contribution to EIIS only for employees who are not eligible to be covered under the IPS, with the amount restricted to a monthly maximum of MYR 49.90.

Human resource development levy

Employers engaged in the manufacturing and services sectors that employ more than a specified number of employees must contribute to the Human Resource Development Fund (HRDF). The levy required to be paid is at the rate of 1% of the employees' monthly wages on a monthly basis.

Windfall profit levy

A levy is imposed on crude palm oil and crude palm kernel oil where the price exceeds MYR 2,500 per ton in Peninsula Malaysia, and MYR 3,000 per ton in the states of Sabah and Sarawak.

Contract levy

A levy of 0.125% on contract works having a contract sum above MYR 500,000 is imposed on every registered contractor by the Construction Industry Development Board.

Branch income

Tax rates on branch profits of a company are the same as CIT rates. No tax is withheld on transfer of profits to a foreign head office.

Income determination

Inventory valuation

Inventories are generally stated at lower of cost or net realisable value. Cost may be determined using one of several methods (e.g. unit cost, average cost, or first in first out [FIFO]), as long as the basis used is consistent for each year.

Capital gains

Generally, gains on capital assets are not subject to tax, except for gains arising from the disposal of real property situated in Malaysia, which is subject to RPGT (*see the Other taxes section for more information*).

Dividend income

Malaysia is under the single-tier tax system. Dividends are exempt in the hands of shareholders. Companies are not required to deduct tax from dividends paid to shareholders, and no tax credits will be available for offset against the recipient's tax liability. Corporate shareholders receiving exempt single-tier dividends can, in turn, distribute such dividends to their own shareholders, who are also exempt on such receipts.

Stock dividends

A Malaysian corporation may distribute bonus shares tax-free to shareholders.

Interest income

Interest income accruing in or derived from Malaysia or received in Malaysia from outside Malaysia is subject to CIT. However, exemption is provided on interest income received in Malaysia from outside Malaysia. Other exemptions granted include interest income earned by a non-resident person from deposits placed in designated financial institutions in Malaysia.

Royalty income

Royalty income accruing in or derived from Malaysia or received in Malaysia from outside Malaysia is subject to CIT. Malaysia has a wide definition of royalty that also includes software, visual images or sounds transmitted via satellite, cable, or fibre optic, and radio frequency spectrum. Payments to non-residents falling within the definition of royalty will be subject to withholding tax (WHT) requirements. However, certain royalty income earned by a non-resident person may be exempted from tax.

Foreign income

Under the Income Tax Act 1967, a Malaysian tax-resident company and a unit trust are not taxed on their foreign-sourced income, regardless of whether such income is received in Malaysia. However, income of a resident company from the business of air/sea transport, banking, or insurance is assessable on a worldwide basis.

Taxation on a worldwide basis does not apply when income attributable to a Labuan business activity of a Labuan branch or subsidiary of a Malaysian bank is subject to tax under the Labuan Business Activity Tax Act 1990. This exception will not apply if the Labuan entity has made an irrevocable election to be taxed under the Income Tax Act 1967 in respect of its Labuan business activity.

Relief from double taxation is available by means of a bilateral credit if there is a governing tax treaty or unilateral relief where there is no treaty. The relief is restricted to the lower of Malaysian tax payable or foreign tax paid if there is a treaty, or one-half of the foreign tax paid if there is no treaty.

Undistributed income of foreign subsidiaries is not taxable.

Deductions

Capital allowance

Capital allowance (tax depreciation) on industrial buildings, plant, and machinery is available at prescribed rates for all types of businesses. Initial allowance is granted in the year the expenditure is incurred and the asset is in use for the purpose of the business. Annual allowance at the prescribed rates calculated on cost is given for every year during which the asset is in use at the end of the basis year for the purposes of the business. The following are examples of capital allowance rates currently available:

Qualifying asset	Initial allowance (%)	Annual allowance (%)
Industrial building, whether constructed or purchased	10	3
Heavy machinery	20	20
General plant and machinery	20	14
Furniture and fixtures	20	10
Office equipment	20	10
Motor vehicles*	20	20*
Small value assets of less than MYR 1,300 (subject to a maximum total cost of MYR 13,000)	-	100

* Restrictions apply on maximum qualifying capital expenditure.

Accelerated capital allowance is available for certain types of industrial building, plant, and machinery, some of which includes buildings used as a warehouse, buildings used as a school or an educational institution, computers, information technology equipment, environmental protection equipment, waste recycling equipment, and plant and machinery used in specific industries.

Goodwill

Cost of acquisition of goodwill/amortisation of goodwill is not deductible, as these expenses are capital in nature.

Start-up expenses

In general, start-up expenses incurred before the commencement of a trade, profession, or business are capital in nature, as they were expended to put the person in a position to earn income. However, there are specific deductions allowed, such as incorporation expenses and recruitment expenses (conditions apply).

Interest expenses

Interest expense is allowed as a deduction if the expense was incurred on any money borrowed and employed in the production of gross income or laid out on assets used or held for the production of gross income. Where a borrowing is partly used to finance non-business operations, the proportion of interest expense will be allowed against the non-business income.

Bad debt

Debts must be specifically identified and reasonably estimated to be irrecoverable to qualify for a tax deduction.

Donations to charitable institutions

A deduction is allowed for cash donations to approved institutions (defined) made in the basis period for a year of assessment. The deduction is limited to 10% of the aggregate income of that company for a year of assessment.

Fines and penalties

Fines and penalties are generally not deductible.

Taxes

Taxes on income are generally not deductible, whereas indirect taxes are deductible.

Net operating losses

The carryforward of business losses and capital allowances is not available for deduction in subsequent years of assessment if the company does not meet the conditions of a shareholders' continuity test. However, per policy issued by the Ministry of Finance, these conditions currently apply only to dormant companies. Carryforward of business losses and capital allowances is unlimited in time for non-dormant companies.

Current-year business losses may be utilised against all sources of income. Utilisation of carried-forward losses is restricted to income from business sources only. Utilisation of capital allowance is also restricted to income from the same underlying business source.

Currently, there are no provisions to carry back losses to prior years of assessment.

Payments to foreign affiliates

A Malaysian company can claim a deduction for royalties, management service fees, and interest charges paid to foreign affiliates, provided that these are made at arm's length and the relevant WHTs, where applicable, have been paid.

Group taxation

A company that qualifies for group relief may surrender a maximum of 70% of its adjusted loss for a year of assessment to one or more related companies if the following conditions are met by both the claimant and surrendering companies:

- Both must be resident and incorporated in Malaysia.

- Each has paid-up capital of ordinary shares exceeding MYR 2.5 million at the beginning of the basis period.
- Both have the same (12-month) accounting period.
- They are 'related' throughout the basis period for a particular year of assessment as well as the 12 months preceding that basis period.
- Both are not currently enjoying specific stipulated incentives, such as pioneer status, investment tax allowance, reinvestment allowance, etc.

'Related company' is defined by the Income Tax Act 1967 and involves the application of a two-tier test. The companies are regarded as 'related' if:

- either company owns at least 70% of the ordinary share capital of the other company or a third company owns at least 70% of each of the companies, and
- the holders of ordinary shares are entitled to at least 70% of the distributable profits and assets of the company on winding up.

Companies that wish to avail themselves of group relief must make an irrevocable election to surrender or claim the tax loss in the return to be filed with the Inland Revenue Board for that year of assessment.

Transfer pricing

The Director General of Inland Revenue (DGIR) is empowered to make adjustments on transactions of goods and services if the DGIR is of the opinion that the transactions were not entered into on an arm's-length basis.

The transfer pricing rules that apply to controlled transactions (defined, including financial assistance) specify the methods to determine the arm's-length price and the circumstances under which the DGIR may re-characterise transactions. The advance pricing arrangement (APA) rules that apply only to cross-border transactions outline the application procedures for unilateral, bilateral, or multilateral APAs.

Country-by-country (CbC) reporting

The CbC Rules require that Malaysian multinational corporation (MNC) groups with total consolidated group revenues of MYR 3 billion to prepare and submit CbC reports to the tax authorities no later than 12 months after the close of each financial year. Malaysian entities of foreign MNC groups will generally not be required to prepare and file CbC reports as the obligation to file will be with the ultimate holding company in the jurisdiction it is tax resident in. However, the Malaysian entities of the foreign MNC group will have an obligation to inform/notify the tax authorities, by the end of its financial year, if it is the holding company or has been appointed as the surrogate holding company. If it is neither the holding company nor surrogate holding company, the Malaysian entities must notify the tax authorities of the identity and tax residence of the entity responsible for preparing the CbC report.

Earning stripping rules

The thin capitalisation provision is to be replaced with the implementation of the earning stripping rules with effect from 1 January 2019. Under the rules, interest deductions will be limited to a fixed percentage (within the range of 10% to 30%) of profit, measured using earnings before interest, taxes, depreciation, and amortisation (EBITDA). The rules have yet to be issued or gazetted.

Controlled foreign companies (CFCs)

There are no CFC rules in Malaysia.

Tax credits and incentives

Malaysia has a wide variety of incentives covering the major industry sectors. Tax incentives can be granted through income exemption or by way of allowances. Generally, when income is exempted, any dividends paid out of such exempt income are not taxable in the hands of the shareholders. Where incentives are given by way of allowances, any unutilised allowances generally may be carried forward indefinitely to be utilised against future statutory income. The following are the major types of incentives available in Malaysia.

Pioneer status (PS) and investment tax allowance (ITA)

Companies in the manufacturing, agricultural, hotel, and tourism sectors, or any other industrial or commercial sector, that participate in a promoted activity or produce a promoted product may be eligible for either PS or an ITA.

PS is given by way of exemption from CIT on 70% of the statutory income for five years and the remaining 30% is taxed at the prevailing CIT rate. An ITA is granted on 60% qualifying capital expenditure incurred for a period of five years to be utilised against 70% of the statutory income, while the 30% balance is taxed at the prevailing CIT rate.

A company that intends to undertake reinvestment before expiration of its PS or ITA status may opt for reinvestment allowance, provided it surrenders its PS or ITA status.

The PS and ITA incentives are enhanced for the following types of projects:

	Pioneer status		Investment tax allowance	
Qualifying industry	**Incentive**	**TRP (1)**	**Incentive**	**TRP (1)**
Projects of national and strategic importance involving heavy capital investment and high technology.	100% of SI (2)	5 + 5	100% QCE (3) against 100% SI	5
High-technology companies engaged in areas of new and emerging technologies.	100% of SI	5	60% QCE against 100% SI	5
Companies manufacturing specialised machinery and equipment.	100% of SI	10	100% QCE against 100% SI	5
Existing locally owned companies reinvesting in production of heavy machinery, specialised machinery, and equipment.	70% of increased SI	5	60% new QCE against 70% SI	5
Companies providing technical and vocational training, and private higher education institution providing qualifying science courses.	-	-	100% QCE against 70% SI	10
New companies investing and existing companies reinvesting in utilising oil palm biomass to produce value-added products.	100% of SI	10	100% QCE against 100% SI	5
Small scale companies (defined) that meet with specified conditions.	100% of SI	5	60% QCE against 100% SI	5

Qualifying industry	Pioneer status Incentive	Pioneer status TRP (1)	Investment tax allowance Incentive	Investment tax allowance TRP (1)
Hotel operators undertaking new investments in 4 and 5 star hotels in Sabah/Sarawak (for applications until 31 December 2020).	100% of SI	5	100% QCE against 100% SI	5
Hotel operators undertaking new investments in 4 and 5 star hotels in Peninsular Malaysia (for applications until 31 December 2020).	70% of SI	5	60% QCE against 70% SI	5

Notes

1. Tax relief period (in terms of years).
2. Statutory income.
3. Qualifying capital expenditure.

Special incentive schemes

Reinvestment allowance

A resident company in operation for not less than 36 months that incurs capital expenditure to expand, modernise, automate, or diversify its existing manufacturing business or approved agricultural project is entitled to reinvestment allowance as follows:

- The allowance is given for 15 years from the first year of claim.
- An allowance of 60% of QCE incurred to be utilised against 70% of statutory income. The remaining 30% is taxed as the prevailing CIT rate.
- The 70% restriction does not apply to projects that achieved the level of productivity as prescribed by the Minister of Finance.
- The allowance will be withdrawn if the asset for which the allowance is granted is disposed of within five years.

A special reinvestment allowance is provided by extending the existing incentive period for up to three years, from year of assessment 2016 to 2018.

Approved service projects

A resident company undertaking a project approved by the Minister of Finance in the transportation, communications, utilities, and services subsectors may enjoy the following incentives:

- Investment allowance of 60% of QCE incurred within five years to be utilised against 70% statutory income.
- Alternatively, income tax exemption of 70% of statutory income for a period of five years.
- Buildings used solely for the purposes of such projects qualify for an industrial building allowance.

Export incentives

A resident company engaged in manufacturing or agriculture that exports manufactured products, agricultural produce, or services is entitled to allowances between 10% and 100% of increased exports (subject to satisfying prescribed conditions), which is deductible at up to 70% of statutory income.

Regional operations

Principal hub

A principal hub is a locally incorporated company that uses Malaysia as a base for conducting its regional and global businesses and operations through management, control, and support of key functions, such as management of risk, strategic decisions, finance, and human resources. CIT at tiered rates (0%, 5%, or 10%) is given for a period of up to ten years, subject to conditions being met (for applications from 1 May 2015 to 31 December 2020).

Other available non-fiscal incentives available include:

- No equity/ownership conditions.
- Foreign exchange administration flexibilities and expatriate positions.
- Customs duty exemption for raw materials, components, or finished products brought into free zones, licensed and bonded warehouses for production or repackaging, cargo consolidation, and integration before distribution to its final customers for goods-based companies.

International trading company

International trading companies are exempt for five years on income equivalent to 20% of increased export value, up to a maximum of 70% of statutory income. To qualify for the incentive, the company must meet the following three conditions:

- Be incorporated in Malaysia, with 60% Malaysian ownership.
- Achieve minimum annual sales of MYR 10 million, not more than 20% of which may be derived from the trading of commodities.
- Use local services (banking, finance, and insurance) and infrastructure (local ports and airports) in its operations.

Financial services sector

Islamic banking and takaful business

Effective from year of assessment 2007 until year of assessment 2016, full income tax exemption for ten years is granted to:

- Islamic banks licensed under the Islamic Financial Services Act 2013, on income from Islamic banking business conducted in international currencies.
- *Takaful* (Islamic insurance) companies licensed under the Islamic Financial Services Act 2013, on income from *takaful* business conducted in international currencies.

The above incentive will be extended until year of assessment 2020 when the gazette order is issued.

Stamp duty exemption is also provided on instruments executed (from 1 January 2017 to 31 December 2020) pertaining to Islamic banking and *takaful* business transacted in international currencies.

Islamic fund management

Full income tax exemption is available on statutory income on management fees received by resident fund management companies for managing funds of foreign and local investors established under Syariah principles (until year of assessment 2020). Such funds must be approved by the Securities Commission.

Special purpose vehicle (SPV) for Islamic financing

An SPV established solely for the purpose of issuance of Islamic securities under the Syariah principles (approved by the Securities Commission or established under the Labuan Companies Act 1990) is not subject to income tax and is not required to comply with administrative procedures under the income tax law. The company that establishes the approved SPV is deemed to be the recipient of the SPV's income and will be taxed accordingly, but that company will be allowed a deduction for the cost of issuance of Islamic securities.

Tun Razak Exchange (TRX) (formerly known as Kuala Lumpur International Financial District)

The TRX is a joint property development comprising office towers for finance and banking, residences, and retail spaces in Kuala Lumpur. To accelerate the development of the TRX, the following incentives have been given:

- Stamp duty exemption on loan and service agreements for TRX Marquee status companies.
- Industrial building allowance and accelerated capital allowance for TRX Marquee status companies.
- Income tax exemption of 70% of statutory income for five years for property developers in TRX.
- Additional 50% tax deduction of rental payment incurred by TRX Marquee status companies for buildings used for business in TRX.
- Deduction of relocation cost incurred by TRX Marquee status companies to relocate to TRX.

Real estate investment trusts (REIT)/Property trust fund (PTF)

REIT/PTFs are vehicles that mobilise funds from unit holders comprising individuals and companies for investments in the property sector and related assets. REIT/PTFs are exempted from tax on all income, provided that at least 90% of their total income is distributed to unit holders. With effect from year of assessment 2017, this exemption only applies to REIT/PTFs that are listed on the Bursa Malaysia. If the 90% distribution condition is not complied with, all income will be taxed at the prevailing income tax rate at the REIT/PTF level and tax credit will be claimed by the unit holders on distributions received from the REIT/PTF.

Unit holders are taxed as follows:

Unit holders	WHT rate
Individuals (whether resident or non-resident), body of persons, or other unincorporated persons	10% (until 31 December 2019)
Non-resident company	24%
Resident company	None (income to be included in annual tax return)
Institutional investor (pension fund, collective investment scheme, or other person approved by the Minister of Finance)	10% (until 31 December 2019)

Other incentives available are:

- RPGT and stamp duty exemptions on disposal/transfer of real property to an REIT/PTF.

- Tax deduction given for consultancy, legal, and valuation service fees incurred on the establishment of an REIT.

Foreign fund management company

A foreign fund management company providing fund management services to foreign clients is taxed at a concessionary rate of 10% in respect of income derived from the management of foreign funds, while income arising from services rendered to clients in Malaysia is taxed at the prevailing CIT rate.

A foreign fund management company is a Malaysian incorporated company licensed under the Capital Markets and Services Act 2007. Its activities are regulated by the Securities Commission.

Venture capital company (VCC)

A VCC investing in a venture company (VC), which is not the VCC's related company at the point of first investment, will be given a deduction on the value of investment made in a VC. Where the deduction is not claimed, the VCC is eligible for the following income tax exemption on income from all sources, other than interest income from savings or fixed deposits, and profits from Syariah-based deposits:

Conditions	Exemption period
• At least 70% of invested funds is invested in VC, or • At least 50% of invested funds is invested in VC in the form of seed capital.	10 years

Budget 2018 proposes to reduce the investment limit in a VC at the seed, start-up capital, or early stage financing to 50%, allow the balance of 50% for other investments, and make the exemption period for five years from year of assessment 2018 to 2022, when gazetted.

Petroleum sector

The following incentives are provided for petroleum operations:

- Accelerated capital allowance on qualifying capital expenditure incurred from year of assessment 2010 to 2024 for petroleum operations in marginal fields.
- Investment allowance of 60% of qualifying capital expenditure to be utilised against 70% statutory income for a period of ten years.
- Exemption for a portion of chargeable income from marginal fields resulting in a reduction of the effective tax rate from 38% to 25% for petroleum operations in marginal fields.

Special economic regions

The following special economic regions were launched as part of the Malaysian government's plan for regional growth and development:

Economic region	Location
Iskandar Malaysia (formerly known as Iskandar Development Region [IDR]): *www.iskandarmalaysia.com.my*	Southern Johor
Northern Corridor Economic Region: *www.koridorutara.com.my*	States of Perlis, Kedah, Penang, and northern Perak
East Coast Economic Region: *www.ecerdc.com.my*	States of Kelantan, Terengganu, Pahang, and district of Mersing in Johor

Malaysia

Economic region	Location
Sabah Development Corridor: *www.sedia.com.my*	Western, central, and eastern regions of Sabah
Sarawak Corridor of Renewable Energy: *www.sarawakscore.com.my*	Central Sarawak

Special incentives, on top of the existing incentives given by the Malaysian government, will be customised for the purpose of each economic region. At present, special legislation has been enacted only in respect of Iskandar Malaysia (IM) and East Coast Economic Region (ECER).

Iskandar Malaysia

Entity	Incentive
IDR-status company	10 years income tax exemption on statutory income from the provision of qualifying services to a person situated within designated nodes in the IDR or outside Malaysia. Operations commenced before 31 December 2015.
Developer	Income tax exemption on rental or disposal of buildings in designated nodes (until year of assessment 2020).
Development manager	Income tax exemption on statutory income from the provision of management, supervisory, and marketing services to an approved developer (until year of assessment 2020).
Non-resident service provider	Income tax and WHT exemptions on income from technical fees or royalties received from IDR-status companies.
Individuals working in IDR	A qualified knowledge worker is taxed at the rate of 15% on chargeable income from employment with a designated company engaged in a qualified activity (e.g. green technology, educational services, healthcare services, creative industries, financial advisory and consulting services, logistics services, tourism) in that specified region. Employment must have commenced between 24 October 2009 and 31 December 2015.

East Coast Economic Region

Entity	Incentive
Qualifying person undertaking qualifying activity	Income tax exemption on SI for 10 years or income tax exemption equivalent to 100% of QCE incurred for 5 years (applications received from 13 June 2008 to 31 December 2020). WHT exemption on fees for technical advice, assistance, or services, or royalty paid to non-residents (until 31 December 2020). Stamp duty exemption on instruments of transfer of real property, or lease of land, or building used for the purpose of carrying on a qualifying activity (executed on or after 13 June 2008 but not later than 31 December 2020).
Qualifying person undertaking special qualifying activity	Income tax exemption at a rate of 70% to 100%, for a period as determined by the Minister (applications received from 13 June 2008 to 31 December 2020). Income tax exemption equivalent to a rate of 60% to 100% of QCE incurred and within a period as determined by the Minister (applications received from 13 June 2008 to 31 December 2020). WHT exemption on fees for technical advice, assistance, or services, or royalty paid to non-residents (until 31 December 2020).

Entity	Incentive
Approved developer undertaking development in industrial park or free zone	Income tax exemption for 10 years in respect of income derived from: • disposal of any right over any land, or disposal of a building, or rights over building, or part of building, or • rental of building or part of building. Applications received from 13 June 2008 to 31 December 2020.
Approved park managers	Income tax exemption, for 10 years, of SI derived from the provision of park management services in the industrial park or free zones (applications received from 13 June 2008 to 31 December 2020).
Approved development manager	Income tax exemption, for 10 years, of SI derived from the provision of management, supervisory, or marketing services relating to the development of an industrial park or free zone (applications received from 13 June 2008 to 31 December 2020).
Investor investing in related company	A deduction equivalent to the value of investment made into a related company carrying out qualifying activity or special qualifying activity (applications received from 13 June 2008 to 31 December 2020).
Qualifying person who sponsors a hallmark event	A deduction for an amount not exceeding MYR 1 million per year of assessment in respect of cash contribution or contribution in kind for a hallmark event carried on in ECER from 13 June 2008 to 31 December 2020 (applications received from 13 June 2008 to 31 December 2020).

Incentive for less-developed areas

To enhance the special incentive package available in the economic corridors to include more less-developed areas, the following incentives are given to existing companies expanding to less-developed areas or newly established companies (for applications from 1 January 2015 to 31 December 2020):

- 100% income tax exemption for up to 15 years of assessment (5+5+5) commencing from the first year of assessment statutory income is derived, or
- income tax exemption of 100% of qualifying capital expenditure (ITA) that can be offset against 100% statutory income for ten years.

The company must undertake manufacturing or services activities in less-developed areas that create employment and rural development.

The other incentives available for less-developed areas are:

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

Information and communication technology (ICT)

MSC Malaysia

MSC Malaysia is Malaysia's initiative for the global information technology (IT) industry and is designed to be the research and development (R&D) centre for industries based on IT. It is an ICT hub equipped with high-capacity global telecommunications and logistics networks. MSC Malaysia is also supported by secure cyber laws, strategic policies, and a range of financial and non-financial incentives for investors. It is managed by the Multimedia Development Corporation (MDeC), a 'one-stop shop' that acts as the approving authority for companies applying for MSC Malaysia status.

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. MSC Malaysia companies are eligible for incentives, which include the following:

- PS (five + extendable by five years) of 100% on statutory income or ITA of 100% for five years for a new company or existing company on its additional income.
- Eligibility for R&D grants (for majority Malaysian-owned MSC Malaysia company).
- Exemption from indirect taxes on multimedia equipment.
- Unrestricted employment of local and foreign knowledge workers.
- Freedom to source funds globally for investments.
- Protection of intellectual property and cyber laws.
- No censorship of the Internet.
- Globally competitive telecommunication tariffs and services guarantees, world-class physical and IT infrastructure, and excellent R&D facilities.

Green incentives

Green technology projects

Companies that undertake any of the following green technology projects will be eligible for an ITA of 100% of QCE against 70% statutory income for QCE incurred from 25 October 2013 to year of assessment 2020 (applications to be received by 31 December 2020):

- Renewable energy.
- Energy efficiency.
- Green building.
- Green data centre.
- Waste management.

Green technology services

Companies that provides services, such as advisory, design, feasibility study, testing, and commission, in the following areas will be eligible for income tax exemption of 100% of statutory income from year of assessment 2013 to 2020 (applications to be received by 31 December 2020):

- Renewable energy.
- Energy efficiency.
- Electric vehicle.
- Green building.
- Green data centre.
- Green certification and verification.
- Green township.

Green technology assets

Companies that purchase green technology assets listed on the MyHijau directory will be eligible for an ITA of 100% of QCE incurred from 25 October 2013 to year of assessment 2020 (applications to be received by 31 December 2020).

Waste eco parks (WEPs)

The following industry players in WEPs will be eligible for incentives for applications received from 1 January 2016 until 31 December 2020. The WEP incentive is to promote waste management in an integrated manner.

Entity	Incentive	Incentive period
Developer	70% income tax exemption of statutory income derived from rentals of buildings, fees from usage of waste collection and separation facilities, and fees from waste water treatment facilities located in the WEP.	Year of assessment 2016 to 2025
Manager	70% income tax exemption of statutory income derived from services related to management, maintenance, supervision, and marketing of the WEP.	Year of assessment 2016 to 2025
Operator	• 100% income tax exemption for five years on statutory income derived from qualifying activities undertaken in the WEP, or • ITA of 100% of QCE incurred within five years, against 70% of statutory income.	Five years

Biotechnology industry

Companies undertaking biotechnology activity with approved bionexus status from Malaysian Biotechnology Corporation Sdn Bhd will be eligible for the following incentives:

- Full income tax exemption on statutory income for ten years from the first year in which the company derives statutory income or ITA of 100% on QCE incurred for a period of five years.
- Concessionary tax rate of 20% on statutory income from qualifying activities for ten years upon expiry of the tax exempt period.
- Accelerated industrial building allowance (over ten years) for buildings used solely for the purpose of its new business or expansion project.
- Exemption of import duty and sales tax on import of raw materials and machinery.

Research and development (R&D)

Contract R&D company

Companies that provide R&D services to third parties are eligible for:

- full exemption of their statutory income for a period of five years (extendable by five years), or
- ITA of 100% of QCE incurred within a period of ten (extendable by ten years) to be utilised against 70% of statutory income.

R&D company

The ITA incentive is also available to companies undertaking R&D services for their group and third parties.

In-house R&D

Companies undertaking in-house R&D projects are eligible for ITA at the rate of 50% of QCE incurred within a period of ten years (extendable by ten years) to be utilised against 70% of statutory income.

Commercialisation of resource-based R&D findings

A company that invests for the sole purpose of financing a project on commercialisation of resource-based R&D findings (which is wholly owned by a public research institute or public institute of higher learning in Malaysia) is given a deduction equivalent to the value of that investment.

The subsidiary undertaking the commercialisation of R&D findings is granted 100% tax exemption on statutory income for ten years.

Other incentives

Shipping

A tax-resident person (including a partnership) carrying on shipping business using Malaysian ships is given income tax exemption of 70% of statutory income, determined on a per ship basis. The balance of 30% of statutory income is deemed to be total income chargeable to tax.

Incentives for Mines Wellness City (MWC)

The Malaysian Investment Development Authority has issued guidelines on incentives for MWC:

	Incentive	Application period
Operator	• PS of 70% of statutory income for five years for income from qualifying activities in MWC. • ITA of 60% on QCE incurred within five years, against 70% of statutory income.	Applications received on or after 1 January 2013 to 31 December 2026.
Development manager	PS of 100% exemption on statutory income from management, consultancy, supervisory, or marketing services to MWC developer in MWC from the first year of assessment statutory income is derived until year of assessment 2023.	Applications received on or after 1 January 2013.
Developer	1. 100% exemption on statutory income from disposal of rights over land/building from the first year of assessment statutory income is derived until year of assessment 2023, or 2. Income tax exemption on rental income from the first year of assessment statutory income is derived until year of assessment 2026, and 3. Stamp duty exemption of 50% on instrument of transfer/lease of land/building.	1 and 2: Applications received on or after 1 January 2013. 3: Instruments executed from 1 January 2013 to 31 December 2023.

Capital allowance for increased automation

Manufacturing companies that have been in operation for at least 36 months are eligible for the following incentives, where they have incurred expenditure in automation equipment used directly in the manufacturing activities and resulting in reduced man hours and increased productivity:

- For high labour intensive industries (rubber products, plastics, wood, furniture, and textiles industries): 200% automation capital allowance on first MYR 4 million QCE (years of assessment 2015 to 2017, proposed extension to 31 December 2020).
- Other industries: 200% automation capital allowance on first MYR 2 million QCE (years of assessment 2015 to 2020).

Foreign tax credit

See Foreign income in the Income determination section for a discussion of the foreign tax credit regime.

Withholding taxes

Corporations making payments of the following types of income are required to withhold tax at the rates shown in the table below. *See Note 5 for other sources of income subject to WHT.*

	WHT (%)			
Recipient	**Dividends (1)**	**Interest (2)**	**Royalties (3a, 3b)**	**Special classes of income/ Rentals (4, 5)**
Resident corporations	0	0	0	
Resident individuals	0	0/5	0	
Non-resident corporations and individuals:				
Non-treaty	0	0/15	10	10
Treaty:				
Albania	0	0/10	10	10
Australia	0	0/15	0/10	0
Austria	0	0/15	10	10
Bahrain	0	0/5	8 (3c)	10
Bangladesh	0	0/15	0/10	10
Belgium	0	0/10/15	10	10
Bosnia and Herzegovina *	0	0/10	8	10
Brunei	0	0/10	10	10
Canada	0	0/15	0/10 (3d)	10
Chile	0	15	10	5
China, People's Republic of	0	0/10	10	10
Croatia	0	0/10	10	10
Czech Republic	0	0/12	10	10
Denmark	0	0/15	0/10	10
Egypt	0	0/15	10	10
Fiji	0	0/15	10	10
Finland	0	0/15	0/10	10
France	0	0/15	0/10	10
Germany	0	0/10	7	7
Hong Kong	0	0/10	8	5
Hungary	0	0/15	10	10
India	0	0/10	10	10
Indonesia	0	0/10	10	10
Iran	0	0/15	10	10
Ireland, Republic of	0	0/10	8	10
Italy	0	0/15	0/10 (3d)	10
Japan	0	0/10	10	10
Jordan	0	0/15	10	10
Kazakhstan	0	0/10	10	10
Korea, Republic of	0	0/15	0/10	10

Malaysia

	WHT (%)			
Recipient	Dividends (1)	Interest (2)	Royalties (3a, 3b)	Special classes of income/ Rentals (4, 5)
Kuwait	0	0/10	10	10
Kyrgyzstan	0	0/10	10	10
Laos	0	0/10	10	10
Lebanese Republic	0	0/10	8	10
Luxembourg	0	0/10	8	8
Malta	0	0/15	10	10
Mauritius	0	0/15	10	10
Mongolia	0	0/10	10	10
Morocco	0	0/10	10	10
Myanmar	0	0/10	10	10
Namibia	0	0/10	5	5
Netherlands	0	0/10	0/8	8
New Zealand	0	0/15	0/10 (3e)	10
Norway	0	0/15	0/10 (3f)	10
Pakistan	0	0/15	0/10	10
Papua New Guinea	0	0/15	10	10
Philippines	0	0/15	0/10	10
Poland	0	0/15	0/10	10
Poland (new) *	0	0/10	8	8
Qatar	0	0/5	8	8
Romania	0	0/15	0/10	10
Russian Federation	0	0/15	10	10
San Marino	0	0/10	10	10
Saudi Arabia	0	0/5	8	8
Senegal *	0	0/10	10	10
Seychelles Republic	0	0/10	10	10
Singapore	0	0/10	8	5
Slovakia	0	0/10	10	5
South Africa	0	0/10	5	5
Spain	0	0/10	7	5
Sri Lanka	0	0/10	10	10
Sudan	0	0/10	10	10
Sweden	0	0/10	8	8
Switzerland	0	0/10	0/10	10
Syria	0	0/10	10	10
Thailand	0	0/15	0/10 (3f)	10
Turkey	0	0/15	10	10
Turkmenistan	0	0/10	10	0
United Arab Emirates	0	0/5	10	10
United Kingdom	0	0/10	8	8
Uzbekistan	0	0/10	10	10
Venezuela	0	0/15	10	10
Vietnam	0	0/10	10	10
Zimbabwe	0	0/10	10	10

Notes

* Treaties pending ratification

Restricted tax treaties dealing with taxation of specific transport operations in international traffic have also been signed with Argentina and the United States (US).

1. Dividends:
   - Malaysia has no WHT on dividends in addition to tax on the profits out of which the dividends are declared. Some treaties provide for a maximum WHT on dividends should Malaysia impose such a WHT in the future.
2. Interest:
   - Interest on loans given to or guaranteed by the Malaysian government is exempt from tax.
   - Interest paid to a non-resident by a commercial or merchant bank operating in Malaysia is also exempt from tax.
3. Royalty:
   a. Approved royalty payments under certain treaty provisions are exempt from WHT.
   b. Royalty income received by non-resident franchisors under franchised education scheme programmes by the Ministry of Education is exempted from tax.
   c. Royalty does not include payments in respect of the operation of oil or gas wells, or the extraction of mineral deposits or other natural resources.
   d. Royalty does not include amount paid in respect of motion picture films or of tapes for radio or television broadcasting.
   e. Royalty does not include natural resource royalties.
   f. Royalty does not include royalty paid in respect of (literary or artistic copyrights - Norway only) or of motion picture films or of tapes for television (or radio - Thailand only) broadcasting, or of the operation of a mine, oil well, quarry, or any other place of extraction of natural resources or of timber or other forest produce.
4. Special classes of income:
   - Contract payments to non-resident contractors in respect of services under a contract project are subject to a 13% deduction of tax (10% on account of the contractors' tax liability and 3% on account of their employees' tax liability). This deduction of tax at source does not represent a final tax, which is determined upon the filing of the tax return.
   - Payments made to non-residents in respect of the provision of technical services performed in Malaysia and rental of movable properties are subject to a 10% WHT (unless exempted under statutory provisions for purpose of granting incentives).
5. Other income:
   - WHT is also applied in respect of income of a non-resident from sources other than the following:
     - Sources shown in the preceding table.
     - A business source.
     - An employment source.
   - The rate of WHT on such income is 10%. This is applicable on payments made to residents of all the treaty partners listed, except for certain countries (including Germany, Turkmenistan, Bosnia and Herzegovina, Senegal, and Jordan) where the respective tax treaties have provided for such type of income to be taxed only in the contracting state in which the recipient is resident.

Tax administration

Taxable period

Assessment of income is on a current-year basis. A company is taxed on income from all sources (whether business or non-business) arising in its financial year ending in the calendar year that coincides with that particular year of assessment. For example, a company that closes its accounts on 30 June of each year is taxed on income earned during the financial year ending on 30 June 2018 for year of assessment 2018.

Tax returns

Under the self-assessment system, companies are required to submit a return of income within seven months from the date of closing of accounts. Particulars required to be specified in the return include the amount of chargeable income and tax payable by the company. The tax return is deemed to be a notice of assessment and is deemed served on the company upon the date the tax return is submitted.

'E-filing' or online filing of tax returns via the Internet is available. E-filing is encouraged by the Inland Revenue Board.

Payment of tax

Tax payable under an assessment upon submission of a tax return is due and payable by the last day of the seventh month from the date of closing of accounts.

Companies are required to furnish estimates of their tax payable for a year of assessment no later than 30 days before the beginning of the basis period (normally the financial year). However, a newly established company with paid-up capital of MYR 2.5 million or less that meets with certain specified conditions is exempted from this requirement for two years, beginning from the year of assessment in which the company commences operation. A revised estimate can be submitted in the sixth and ninth months of the basis period for a year of assessment.

Companies are then required to pay tax by monthly instalments (based on the estimates submitted) commencing from the second month of the company's basis period.

A company commencing operations in a year of assessment is not required to furnish estimates of tax payable or to make instalment payments if the basis period for the year of assessment in which the company commences operations is less than six months.

Tax audit process

Following the issuance of the general tax audit framework, tax audit frameworks for the financial and insurance industry and for WHTs were issued. These tax audit frameworks outline the rights and responsibilities of audit officers, taxpayers, and tax agents in respect of a tax audit. A tax audit may cover a period of one to three years of assessment determined in accordance with the audit focus. The years of assessment to be covered in a tax audit may, however, be extended depending on the issues identified during an audit.

Statute of limitations

Additional assessments can be made within five years after the expiration of the relevant year of assessment. This time limit is not applicable where fraud, wilful default, or negligence has been committed.

Topics of focus for tax authorities

Some issues that the tax authorities have focused on recently include:

- Deductibility of certain expenses (e.g. entertainment, provisions, management service fees, allocated expenses from foreign related counterparts).
- The correctness of tax incentive claims.

Other issues

Intergovernmental agreements (IGAs)

Malaysia and the United States had, on 30 June 2014, reached an agreement in substance on a Model 1 IGA to implement the Foreign Account Tax Compliance Act (FATCA). Although not signed, Malaysia has, however, been included in the US Treasury's list of jurisdictions that are treated as having an IGA in effect with the United States.

Under the IGA, reporting Malaysia-based financial institutions will provide the Malaysian Inland Revenue Board with the required information of accounts of US persons. The information of which will then be exchanged between the Malaysian and US tax authorities. The IGA is currently being finalised and will be signed on a date to be announced.

Common Reporting Standard (CRS)

Malaysia is committed to exchanging CRS information from 2018. Under the CRS, Malaysian financial institutions (MYFIs) are required to collect and report financial account information on non-residents.

The reporting financial Institution is defined to mean any financial institution (FI):

- that is resident in Malaysia (excluding branches located outside Malaysia), and
- any branch of an FI that is not resident in Malaysia if it is located in Malaysia.

Once an MYFI has applied the due diligence procedures in respect of the accounts it holds and has identified reportable accounts, it must report certain information regarding those accounts to the tax authorities. A reporting MYFI with no reportable accounts is required to make a nil return annually to the Malaysian Inland Revenue Board.

Mongolia

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Significant developments

Currently, the Mongolian government is in the process of introducing new tax legislations, which are in public discussion. These laws are expected to be implemented in 2019. Specific changes and updates will be provided when more information is available.

Introduction of 'ultimate holder' concept for tax purposes

The Parliament of Mongolia amended the General Taxation Law of Mongolia and other several laws on 9 December 2017. Under these amendments, a concept of an 'ultimate holder' of a legal entity is newly introduced for tax purposes. Any change of ultimate holders of a legal entity that maintains a mining licence or land-use (or possess) right is deemed as a sale of its mining licence or land-use right and subject to a 30% corporate income tax (CIT).

Taxes on corporate income

Mongolian resident economic entities are taxable on aggregate annual income earned worldwide. Non-resident economic entities carrying out business activities in Mongolia are taxable on the income earned in the territory of Mongolia and from Mongolian sources.

Mongolian CIT is levied at the following rates, using a progressive-rate scale that ranges from 10% to 25%, as follows:

- 10% applies to the first 3 billion Mongolian tugrik (MNT) of annual taxable income.
- 25% applies to any excess of MNT 3 billion of annual taxable income.

However, the income described in the chart below is excluded when determining the annual taxable income and is taxed at different tax rates on a gross basis:

Source of income	Applicable tax rate (%)
Dividends	10
Royalties	10
Interest	10
Gambling, betting games, and lotteries (net)	40
Sale of immovable property	2
Sale of rights (e.g. mining licences, special activity licences, and other rights granted by the authorised organisations for conducting specific activities)	30

'Ultimate holder'

With the introduction of the amendment to the General Taxation Law of Mongolia, a concept of an 'ultimate holder' of a legal entity is newly introduced for tax purposes.

Any change of ultimate holders of a legal entity that maintains a mining licence or land-use (or possess) right is deemed as a sale of its mining licence or land-use right and subject to a 30% CIT. Importantly, a tax obligation is imposed on the legal entity holding such rights, but not the person who earns the income from the transaction.

'Ultimate holder' refers to the following types of persons who exercise control over management and assets of a legal entity, directly or indirectly, with a chain of ownership at one or more levels of legal entities through a number of shares, percentage of participation, or a number of voting rights:

- Holders of a majority of voting rights of a legal entity.
- Holders of a majority number of shares or shares with the highest market value of a legal entity.
- Similar others.

Assessing taxable income

In general, taxable income shall be assessed based on the value of rights pro-rated to the number of shares or percentage of participation that are transferred from a right-holding entity or its ultimate holders. For the purpose of certainty, the Ministry of Finance passed the Decrees No. 379 and 380, dated 25 December 2017, which set the following methodologies to assess taxable income:

- Methodology to assess and impose taxes on income from sales of the right to use or possess land (Decree No. 379).
- Methodology to determine the value of mining licences and assess taxes on income from transfer of mining licences (Decree No. 380).

Penalties

Breach of the above-mentioned legislative requirements (including failure to comply with requirements for assessing taxes, reporting and/or concealing relevant documents and information, and providing false documentation for tax purposes) shall be subject to cancellation of the respective rights (a mining licence and/or the respective right to use or possess land).

Local income taxes

CIT is levied at the state level in Mongolia. There are no provincial or local corporate income taxes.

Corporate residence

A resident legal entity is an economic entity formed under the laws of Mongolia or a foreign economic entity that has its place of management in Mongolia. There has not been further development of this concept, so it cannot be assumed that the standard place of effective management or control test will apply.

A non-resident company is a foreign economic entity that conducts its business in Mongolia and earns income from Mongolian sources.

Permanent establishment (PE)

Although there is a theoretical possibility to establish a branch of a foreign entity in Mongolia, it is currently not practically possible due to uncertainties in the law related to the legal status of such entity, filing procedures, etc.

It is also possible to register a non-resident PE in Mongolia with the tax authorities, but practically, only for foreign entities from countries that Mongolia has double tax treaties (DTTs) with. However, neither the legal status nor respective taxation rules are clear. According to the draft law on CIT, which is under public discussion at the moment, the time threshold for PE creation can be three months.

Other taxes

Value-added tax (VAT)

According to the VAT Law, a person (covering legal entities, individuals, and PEs) whose sales income has reached MNT 50 million or more has to be registered as a VAT withholder. The threshold for voluntary registration is MNT 10 million of sales income. A sale of fixed assets is not considered for the VAT registration thresholds.

VAT at the rate of 10% is imposed on the supply of goods, services, and works imported, exported, and sold in Mongolia.

One of specific features of the Mongolian VAT legislation is that works and services received from a non-resident (irrespective of whether they are supplied in Mongolia or not) are subject to VAT under the reverse-charge procedure (the RC VAT).

Customs duty

A customs tariff varies between 5% and 40% depending on the type of goods imported into Mongolia, except for gas condense, petroleum oils, crude, oils obtained from bituminous minerals, automatic data processing machines, electrical machinery, equipment and parts, medical equipment, and pure-bred livestock, which are zero-rated.

Export duties apply to certain exported goods, such as unprocessed camel wool, wood, and wooden materials.

Excise tax

Excise tax is levied on goods manufactured in or imported into Mongolia, such as tobacco, alcohol, gasoline and diesel fuel, and passenger vehicles. Excise tax is also levied on the physical units of special-purpose technical devices and equipment used for betting games and gambling and on the activities of individuals and legal entities that conduct such activities. Currently, the excise tax rate on the goods such as alcohol and tobacco varies between MNT 320 and MNT 19,140 per 1 litre of alcohol and 100 cigarettes of tobacco, and it will be increased by 5% in 2019 and 4% in 2020 and later years. For special-purpose technical devices and equipment, it varies between MNT 4.35 million and MNT 116 million per unit according to the origin and type.

The excise tax rates for gasoline and diesel that are produced in Mongolia are as follows:

- Gasoline:
  - MNT 0 to MNT 15,950 per tonne (up to 90 octane).
  - MNT 0 to MNT 17,400 per tonne (above 90 octane).
- Diesel: MNT 0 to MNT 21,750 per tonne.

For imported gasoline and diesel, the excise tax rates vary between MNT 0 and MNT 850,000, depending on the port of import.

Excise tax for imported automobiles varies between MNT 375,000 and MNT 65,975,000, depending on the year of production, type of automobile, and engine capacity.

Immovable property tax

Immovable property tax is an annual tax that varies between 0.6% and 1%, depending on the decisions made by the local representatives' committee, on the value of the immovable property that is owned. For tax purposes, the value used is the value registered with the government registration authority. If the property is unregistered, the insured value is used. In the absence of either a registered or insured value, the accounting value is used.

This tax does not apply to property of legal entities that are financed through the state budget, to any dwelling houses, or to any public nature buildings and construction.

Transfer taxes

Mongolia does not have a separate transfer tax. Transfer of certain rights (like land possession or usage rights and mining licences) is treated as sale of right and taxed at 30% under CIT law (*for more details, please refer to the Taxes on corporate income section*). For individuals, transfer of a land right is subject to 10% under personal income tax (PIT) law.

In the case of transfer of property, stamp duty will be applied.

Stamp duty

Under the Law of Mongolia on State Stamp Duties, there are 45 types of activities subject to stamp duties, including the following:

- Settlement of a legal dispute by a court.
- Court involvement in arbitration.
- Notary services.
- Consulate services.
- State registration services for legal entities.
- Registration services for foreign invested economic entities and representative offices of foreign organisations.
- Other specific activities that need permissions and rights from the state authorities.

The amount of duty varies depending on the types of services or activities involved.

Payroll taxes

There are no payroll taxes applicable for the employer other than social insurance contribution by employer (*see below*). The employer should withhold PIT at 10% or 20% from employees' employment income (10% rate is applied for Mongolian tax residents, whereas 20% rate is applied for tax non-residents) and submit PIT returns electronically on a quarterly basis.

Social insurance contribution by employer

Employers' social insurance contribution depends on the industry type and is subject to rates between 12% and 14%, which is comprised of 8% for pension, 1% for benefits, 2% for health, 0.2% for unemployment, and 0.8% to 2.8% for industrial accident and occupational disease insurance. Employer charges are not capped. Social insurance taxes paid by employers are deductible in determining taxable income.

The employer should also withhold social insurance taxes (10%) from employees and submit returns electronically and by paper before the 5th day of the following month on a monthly basis. Payments should be made before the end of the month to the social insurance fund account.

Fees and taxes applicable to the extractive industry

A range of fees and other taxes are payable for activities in the extractive industry. The primary ones include the following:

- Mining License Fee that is agreed to up front and stated in the mining licence.
- Mining Royalty Tax.
- Water Pollution Fee.
- Air Pollution Fee.
- Land Use Fee.
- Natural Resources Usage Fee.

Branch income

The repatriation of profits from branches of foreign legal entities is subject to branch profits tax at a rate of 20%.

Please note that it appears it is no longer possible for foreign legal entities to establish a branch in Mongolia. However, the above provision remains in place for branches that were previously established in Mongolia.

Income determination

Inventory valuation

There is no specific provision in the tax law for inventory valuation.

Capital gains

Capital and ordinary transactions are treated in the same way for tax purposes (i.e. included in annual taxable income). An exception is provided for income from sales of immovable property, which is subject to tax of 2% on gross sales proceeds.

In terms of tax base, taxation rules of capital gains of non-residents is not clear. The CIT Law could be interpreted in a way that the net gain from disposal of shares in a Mongolian company should be subject to CIT. However, since there was no mechanism in practice for non-resident companies to declare income in Mongolia and show the basis for the taxable gain, only withholding tax (WHT) (20% on the gross payment) charged at source of payment is available. With the introduction of an 'ultimate holder' concept, applicable from 1 January 2018, under the general rule, the Mongolian entities whose shares are traded will act as withholding agents to report and withhold the taxes of non-resident income from sale of its shares when there is a mining licence or a land right attached to the shares. Except for cases with mining licences and land rights, no mechanism for taxation of capital gains currently exists if the transaction takes place between two non-residents that have no taxable presence in Mongolia.

Dividend income

Dividend income earned by a Mongolian resident entity is subject to WHT of 10%. Dividend income to be remitted out of the country to a foreign tax resident is subject to WHT at 20% but may be reduced by an applicable DTT.

Interest income

Interest income is subject to a special income tax of 10%. Interest income to be remitted out of the country to a foreign tax resident is subject to WHT at 20% but may be reduced by an applicable DTT.

Rental income

Rental income is included in taxable income for tax determination.

Royalty income

Royalty income is taxed at a special rate of 10%. Royalty income to be remitted out of the country to a foreign tax resident is subject to WHT at 20% but may be reduced by an applicable DTT.

Partnership income

There is no transparent partnership concept in Mongolia. Partnership income is treated as income of a legal entity and is subject to CIT.

Unrealised currency exchange gains/losses

Unrealised currency exchange gains are not considered as taxable income, and, at the same time, unrealised losses are not deductible from taxable income.

Foreign income

Mongolian legal entities pay tax on their worldwide income. Unremitted earnings are taxed the same as ordinary earnings.

Credit relief is available with respect to foreign tax on income arising from countries that have DTTs with Mongolia, capped at the level of Mongolian tax that would have been due on the same income in Mongolia.

Deductions

Expenses mostly associated with generating aggregate annual income are deductible for CIT purposes (provided proper documentation is in place), and a list of these expenses is provided in the legislation. Expenses not on this list are not deductible.

Accrued expenses

Accrued expenses are deductible only if they are supported by valid documentation.

Contingent liabilities

Contingent liabilities are not deductible.

Depreciation and amortisation

Depreciation of fixed assets and amortisation of intangibles are deductible within the limits provided in tax legislation. A straight-line method is used and the years of usage are determined for tax purposes.

Non-current asset class		Useful life (in years)
1	Building and construction	40
2	Machinery and equipment	10
3	Computer, computer parts, and software	3
4	Intangible asset with undefined useful life	10
5	Intangible asset with defined useful life (includes licence for mineral exploration and extraction)	Period in force
6	Other non-current asset	10
7	Building and facilities of manufacture, management of technology park, unit production, and buildings within technology park	20
8	Machineries, mechanism, equipment, technical parts of manufacturing within the management technology park, unit production, and technology park	3

Goodwill

There is no specific provision in the tax law regarding the deductibility of goodwill.

Organisational and start-up expenses

Organisational and start-up expenses are not deductible.

Interest expenses

Interest expenses are deductible. However, there are limits with respect to the deductibility of interest expense. *See Thin capitalisation in the Group taxation section for more information*.

Bad debt

Bad debt provisions are not deductible. There is no clear guidance in the tax legislation as to whether bad debt is deductible or not; however, in practice, the tax authorities disallow deductibility of bad debt.

Charitable contributions

Charitable contributions are not deductible, except for donations to the fund of vocational training.

Pension expenses

Compulsory pension insurance premiums paid to the Social Security Authority of Mongolia are deductible. Additional voluntary insurance premiums are deductible but shall not exceed 15% of taxable income. Pension provisions or internal pension fund expenses are not deductible.

Payment for directors

If a payment for directors is a salary payment on which social insurance and PIT is levied, it is considered as deductible.

Bribes, kickbacks, and illegal payments

Bribes, kickbacks, and illegal payments are not in the list of permitted deductions. Per anti-corruption law, monetary amounts involved with respect to such payments will be confiscated and criminal proceedings will be instituted.

Fines and penalties

Fines and penalties are not deductible for tax purposes.

Taxes

Certain taxes paid by a taxpayer, as well as social contributions of employers, are generally deductible for tax purposes.

Tax losses

Tax losses generally may be carried forward for up to two years. However, the annual amount of carried forward losses deductible from taxable income may not exceed 50% of the taxable income in the tax year.

Legal entities involved in the infrastructure and mining industries may carry forward 100% of their losses for up to four to eight years, depending on their investment period and based on government regulations.

There is no provision for the carryback of losses.

Payments to foreign affiliates

As a general rule, deductible expenses shall be supported by proper documentation. Deductibility of payments to foreign affiliates depends on the nature of the payment, as follows:

- Interest payments are deductible but with restrictions (i.e. thin capitalisation rule may apply, interest paid on loans for construction of buildings and installation of equipment needs to be capitalised during that period).
- Dividend payments are not deductible.
- Technical assistance service payments are deductible if applicable taxes were levied.
- Payments for other services are deductible if applicable taxes were levied.

Group taxation

There are no rules permitting grouping for tax purposes in Mongolia.

Transfer pricing

Transfer pricing provisions are addressed in the CIT Law and the General Tax Law of Mongolia.

Per the CIT Law of Mongolia, if the following relation is present with a taxpayer, then it is considered as 'a related party':

- Holds 20% or more of the common stock.
- Has the right to receive 20% or more of the dividends or distributions.
- Has the right to appoint 20% or more of the management of the economic entity or is otherwise able to determine its policies.

If related parties have sold or transferred goods, performed work, or rendered services among themselves below or above fair market value, the tax authority shall determine gross taxable income of such goods, work, and services based on value involving transactions of similar goods, work, and services among non-related parties.

The General Tax Law provides for a broader definition of related entities for transfer pricing purposes, which is "entities authorised to directly and indirectly participate in management, control, and property rights of any foreign and Mongolian legal entities". Per Article 48.3 of the General Tax Law, "if prices, payments, and fees (hereinafter the 'price') used in cooperative production, in the provision of technical services, in sending human resources, in purchase and sales transactions between related entities abroad and Mongolia are higher or lower than fair market value, then the fair market value method shall be used in order to determine taxable income".

Beginning from 2017, the Mongolian tax authorities introduced the rules strengthening the reporting requirements for transactions between related parties (transfer pricing rules). Under these reporting requirements, in particular, the affected Mongolian entities will need to disclose the very specific information, including the amount of income (profit) and/or expenses related to the covered related-party transactions, their profitability, transfer pricing methods applied, list of comparable entities used for a benchmarking study, etc. In case of non-submission/delay of submission of the transfer pricing report, there is an administration penalty (MNT 1.5 million).

Thin capitalisation

A thin capitalisation rule applies to direct shareholders, and interest paid in excess of the 3:1 debt-to-equity ratio is not deductible and is treated as a dividend. This is applied on an investor-by-investor basis as opposed to the company as a whole; no restriction applies to interest that is not paid to an investor.

Controlled foreign companies (CFCs)

There are no special CFC rules in Mongolia.

Tax credits and incentives

At present, the following types of incentives exist in Mongolia:

- Until 1 January 2021, a tax credit of 90% is available to a taxpayer conducting business activities in the following industries, provided annual/assessable income of a taxpayer does not exceed MNT 1.5 billion:
  - Agriculture, livestock industry, farming industry, and other auxiliary activities.
  - Food industry.
  - Fabric and clothing industry.
  - Construction materials industry.
- Tax stabilisation of certain taxes per investment made (*see below*).
- Interest on government notes payable (bonds) is exempt from CIT.

- Income earned from the production and/or sale of produced equipment and spare parts intended for the activities of small or medium-sized production businesses in the territory of Mongolia is exempt from CIT.
- Income earned from the sale of a technique or equipment that economises natural resources, reduces environmental contamination, and is nature-oriented is exempt from CIT.
- Tax losses incurred by a business entity involved in the infrastructure and mining sector in a given tax year shall be deducted from taxable income for four to eight consecutive years after such tax year. The period will depend on the size of the investment, as defined from time to time by the responsible government agency.
- In the event that a business entity or a citizen has been found to have made a donation of up to MNT 1 million to support non-governmental organisations founded by citizens having developmental disabilities, such amount shall be deducted from taxable income of such business entity or citizen for the given tax year.
- A 50% tax reduction is available from CIT for an economic entity that produces or grows the following products:
  - Cereal, potatoes, and vegetables.
  - Milk.
  - Fruits and berries.
  - Fodder plants.
- Free Trade Zones (FTZs) have a special regime in terms of tax and customs (*see below*).

Foreign investment incentives

The Law on Investment provides tax incentives, including exemptions from tax, tax credits, possibility to use accelerated depreciation for tax purposes, tax loss carryforward, and deduction of employee training costs from taxable income.

Tax stabilisation

The Law on Investment also provides a ‘stabilisation certificate’ in order to create a more stable tax environment in Mongolia. By obtaining a stabilisation certificate, investors can stabilise applicable rates of the following taxes:

- CIT.
- Customs duties.
- VAT.
- Minerals royalties.

The holder of a stabilisation certificate can stabilise tax rates for a period from 5 to 18 years, depending on amount of investment, industry of investment, and geographic location of investment in Mongolia (*see Stabilisation certificate terms below*). Under the valid period of a stabilisation certificate, investors also have the right to apply effective tax rates provided in general legislation if such rates are more beneficial for investors.

The criteria of issuing a stabilisation certificate are:

- the total investment amount specified in the business plan and feasibility study reaches thresholds specified in the stabilisation certificate terms (*see below*)
- an environmental impact assessment should be carried out
- the investment should create new permanent jobs, and
- the investment should introduce innovative technology.

An investor who made an investment in tobacco and alcohol related activities cannot benefit from tax stabilisation.

If certain conditions are met, the stabilisation certificate period may be extended by 1.5 times for some projects.

The conditions are that the projects:

- produce products that substitute for imported products or export-oriented products that are important for the long-term social and economic development of Mongolia, that will require investment of more than MNT 500 billion, and have a development period of more than three years, or
- produce value-added, processed products for export.

In addition to above, the law provides for incentives with respect to customs duty (exemption) and VAT (zero-rate) on imported equipment and machinery during the construction period of specific projects, as below:

- Construction of a factory for processing construction materials, petroleum, agricultural products, and products intended for export.
- Nano, bio, and innovation technology plant construction.
- Construction of power plants and railroads.

Stabilisation certificate terms

For the mining, heavy industry, and infrastructure sectors, a stabilisation certificate is issued as follows:

	Stabilisation certificate terms (years)					
Investment amount (MNT in billions)	Ulaanbaatar Region	Central Region (Gobisumber, Dornogobi, Dundgobi, Darkhan-Uul, Umnugobi, Selenge, Tuw)	Khangai Region (Arkhangai, Bayankhongor, Bulgan, Orkhon, Uwurkhangai, Khuwsgul)	Eastern Region (Dornod, Sukhbaatar, Khentii)	Western Region (Bayan-Ulgii, Gobi-Altai, Zawkhan, Uws, Khowd)	Period within which investment must be made (years)
30 to 100	5	6	6	7	8	2
100 to 300	8	9	9	10	11	3
300 to 500	10	11	11	12	13	4
more than 500	15	16	16	17	18	5

For any other sector, a stabilisation certificate is issued as follows:

Investment amount (MNT in billions)						
Ulaanbaatar Region	Central Region (Gobisumber, Dornogobi, Dundgobi, Darkhan-Uul, Umnugobi, Selenge, Tuw)	Khangai Region (Arkhangai, Bayankhongor, Bulgan, Orkhon, Uwurkhangai, Khuwsgul)	Eastern Region (Dornod, Sukhbaatar, Khentii)	Western Region (Bayan-Ulgii, Gobi-Altai, Zawkhan, Uws, Khowd)	Stabilisation certificate terms (years)	Period within which investment must be made (years)
10 to 30	5 to 15	4 to 12	3 to 10	2 to 8	5	2
30 to 100	15 to 50	12 to 40	10 to 30	8 to 25	8	3
100 to 200	50 to 100	40 to 80	30 to 60	25 to 50	10	4
more than 200	more than 100	more than 80	more than 60	more than 50	15	5

Free Trade Zones (FTZs)

Establishing FTZs

According to the FTZ Law, FTZs can be established not only at the border ports but also in qualifying regions proposed by the government. The Parliament will decide the proposed plan.

FTZs are under state protection. A joint free border trade zone covering multiple countries' borders can be established and will be regulated through international agreements between the governments.

Tax and customs regime

CIT

Businesses that have invested 500,000 United States dollars (USD) or more in the FTZs operating to improve infrastructures, such as energy and heating sources, pipeline networks, clean water supplies, wastewater sewage, auto roads, railways, airports, and basic communication lines, shall receive a CIT discount equal to 50% of their invested capital in the FTZ.

For businesses with more than USD 300,000 invested in building warehouses, loading and unloading facilities, hotels, tourist camps, or manufacturers of export and import-substituted goods in the FTZ shall receive a CIT discount equal to 50% of their invested capital in the FTZ.

Loss-making entities in the FTZs can carry forward their losses reflected on their CIT return up to five years from the time of becoming fully operational to reduce their future tax payable.

Entities using innovated and enhanced technology in their businesses shall be fully exempted from CIT for the first five years from the time of starting operation in the FTZs.

VAT

Goods imported to the FTZs are not subject to VAT. If goods are to be transferred from the customs territory to the FTZs, there will also be no VAT on those goods, and any previously paid VAT will be reimbursed accordingly based on related documents.

There will be a 0% rate on VAT for domestic goods to be transferred from the customs territory to the FTZs.

In addition to purchases per Article 38.1.4 of the Law on Custom Tax and Tariff (which refer to goods for passengers' personal use), purchases in the FTZ of up to MNT 3 million made by passengers are exempt from VAT when entered into the customs territory.

There will be no VAT imposed on goods and services manufactured and sold by registered individuals and businesses in the FTZs.

Customs and excise taxes

Goods imported to the FTZs are not subject to customs and excise taxes. If goods are to be transferred from the customs territory to the FTZs, there will be no customs and excise taxes on those goods, and any of these taxes previously paid will be reimbursed accordingly based on related documents.

In addition to purchases per Article 38.1.4 of the Law on Custom Tax and Tariff (which refer to goods for passengers' personal use), purchases in the FTZ of up to MNT 3 million made by passengers are exempt from customs tax when entered into the customs territory.

Any goods, except purchases made by passengers as mentioned above, are subject to customs and related taxes as required in the regulation when transferred from the FTZs to the customs territory.

Goods exported from the FTZs are not subject to taxation.

Land payments and property taxes in the FTZ

Individuals and businesses may request a land possession and usage right in the FTZs through either project bid or auction.

Entities operating in trade, tourism, and hotel sectors in the FTZs are fully exempted from land possession and usage right payment for the first five years from commencement of operation. This payment is further reduced up to 50% for the following three years.

Businesses operating to improve infrastructures in the FTZs, such as energy and heating sources, pipeline networks, clean water supplies, wastewater sewage, auto roads, railways, airports, and basic communication lines, will be fully exempted from land payment for the first ten years from start of operation.

Buildings and facilities built and registered in the FTZs are fully exempted from the immovable property tax.

Foreign tax credit

A foreign tax credit is available for foreign taxes paid up to the amount of the Mongolian tax liability that would have been due on the same amount based on an applicable DTT.

Withholding taxes

Dividends, interest, and royalties paid, and payments made for goods sold and work/services provided (directly or electronically), to non-residents are subject to WHT at a 20% rate. Interest provided to non-residents on bonds issued by Mongolian commercial banks and listed on the domestic or foreign stock exchange are subject to WHT at 10%.

Dividends, interest, and royalties paid to resident companies and individuals are all subject to WHT at 10%.

Current DTTs

	Beneficial WHT rates (%)			
Recipient	**Dividends**	**Interest**	**Royalties**	**Technical fees**
Non-treaty	20	20	20	20
Treaty:				
Austria	5/10 (1)	10	5/10 (11)	N/A
Belarus, Republic of	10	10	10	N/A
Belgium	5/15 (2)	10	5	N/A
Bulgaria	10	10	10	N/A
Canada	5/15 (7)	10	5/10 (12)	5
China	5	10	10	N/A
Czech Republic	10	10	10	N/A
France	5/15 (7)	10	5	N/A
Germany	5/10 (1, 4)	10	10	N/A
Hungary	5/15 (9)	10	5	N/A
India	15	15	15	15
Indonesia	10	10	10	N/A
Kazakhstan	10	10	10	N/A
Korea, Democratic People's Republic of	5	5	10	N/A
Korea, Republic of	5	5	10	N/A
Kyrgyzstan	10	10	10	N/A
Malaysia	10	10	10	10
Poland	10	10	5	N/A
Russia	10	10	In accordance with domestic legislation	N/A
Singapore	0/5/10 (6, 9)	5/10 (10)	5	N/A
Switzerland	5/15 (5)	10	5	N/A
Turkey	10	10	10	N/A
Ukraine	10	10	10	N/A
United Kingdom	5/15 (3)	7/10 (8)	5	N/A
Vietnam	10	10	10	10

Notes

1. 5% if the recipient is a company (excluding partnerships) and directly owns at least 10% of the capital of the company paying dividends.
2. 5% if the beneficial owner is a company (excluding partnerships) and directly or indirectly holds at least 10% of the capital of the company paying dividends.
3. 5% if the beneficial owner is a company that directly or indirectly controls at least 10% of the voting power in the company paying dividends.
4. 5% if the beneficial owner is a company (excluding partnerships) and directly owns at least 10% of the company.
5. 5% if the beneficial owner is a company (excluding partnerships) and directly owns at least 25% of the capital of the company paying dividends.
6. No tax if dividends paid to the government/certain public bodies.
7. 5% if the beneficial owner is a company and directly or indirectly holds at least 10% of the capital of the company paying dividends.
8. 7% if interest is paid to a bank that is the beneficial owner of the interest and carrying on a *bona fide* banking business.
9. 5% if the beneficial owner is a company and directly owns at least 25% of the capital of the company paying dividends.
10. 5% if interest is received by a bank or a similar financial institution.
11. 5% if the beneficial owner of the royalties in the meaning of any patent, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial, or scientific experience; 10% in all other cases.
12. 5% if the beneficial owner of the royalties in the meaning of copyright royalties and other payments for production or reproduction of any literary, dramatic, and other work, royalties for the use of, or the right to use, computer software or any patent, or for information concerning industrial, commercial, or scientific experience; 10% in all other cases.

Tax administration

Taxable period

The tax year is the calendar year.

Tax returns

Companies must submit a quarterly return by the 20th day of the month following the end of each quarter and an annual return by 10 February after the end of the tax year.

A withholder must prepare and submit a quarterly return of the tax deducted by the 20th day of the first month of the following quarter and an annual return by 10 February after the end of the tax year.

Payment of tax

A taxpayer shall pay the taxes due in advance by the 25th day of each month in accordance with the payment schedule based on the previous year. Year-end settlement is made by 10 February of the following year (along with the annual tax statement).

In practice, the Mongolian tax authorities allow concessions as follows:

Where total tax paid exceeds the tax liability, the excess may be credited against other taxes due or credited against future tax payments. The overpayment also may, theoretically, be refunded; however, the practice of refunding in Mongolia is not clear or consistent.

An economic entity or organisation that has withheld tax from a payment of dividends, royalties, sale of rights, or a payment of income to a taxpayer should transfer the WHT to the tax authorities within seven working days. Tax withheld relating to the sale of immovable property should be transferred to the tax authorities within ten working days.

Tax audit process

The tax audit cycle is not clearly stated in the tax laws. However, the regular cycle in Mongolia is three to five years in practice, and it is very common if the company requests a refund from tax authorities or liquidates its company. Moreover, a tax audit can come anytime if the tax authorities suspect some risk or misuse of the legislation or receive information from a trustworthy source about tax evasion.

Statute of limitations

The statute of limitations in Mongolia is five years for tax arrears, fines, and penalties. However, the dispute settlement timeframe shall not pertain to payment of tax, fine, and penalty debts.

Topics of focus for tax authorities

The tax authorities normally focus their attention on issues like understatement of income, overstatement of expenses, and withholding obligations of taxpayers.

Another hot topic in Mongolia right now is transfer pricing. The transfer pricing concept is at an early stage of development. Nevertheless, the basic principle governing Mongolian transfer pricing rules is that transactions between related parties should be undertaken at fair market value.

The tax authorities introduced new transfer pricing regulation. This transfer pricing regulation applies to controlled transactions between related parties. The list of controlled transactions, transfer pricing methods to be applied, transfer pricing documentation requirements, and very concise comparability analysis items are based on the Organisation for Economic Co-operation and Development (OECD) Transfer Pricing Guidelines.

PE is also becoming one of the focus areas of the tax authorities. Although it is possible for PEs to be registered as taxpayers, determination of taxable income of PE is still in question.

Myanmar

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Significant developments

Union Taxation Law 2018 was enacted on 30 March 2018, and the provisions of the Law are effective from 1 April 2018. In particular, the Union Taxation Law 2018 has introduced changes to the fiscal year-end of taxpayers, commercial tax, and specific goods tax regime.

Taxes on corporate income

Foreign investors may register their companies under the Myanmar Companies Act (CA) or in conjunction with the Myanmar Investment Law (MIL) or Myanmar Special Economic Zone Law (Myanmar SEZ Law). The new MIL 2016 was enacted on 18 October 2016. The new MIL is a consolidation of the Myanmar Citizen Investment Law (2013) and the Myanmar Foreign Investment Law (MFIL) (2012). The Myanmar Citizen Investment Law and MFIL have been repealed with effect from 18 October 2016. New rules governing the implementation of the new MIL were enacted on 30 March 2017. Investment permits issued under the old investment laws continue to be valid.

The differences between companies registered under the CA and the Myanmar Investment Commission (MIC)/SEZ are in relation to their eligibility for tax incentives and longer land use terms, as well as minimum foreign share capital requirements.

Generally, resident companies are taxed on a worldwide basis, and, as such, income from sources outside Myanmar is taxable.

Non-resident companies are taxed only on income derived from sources within Myanmar. Income received from any capital assets within Myanmar and from any source of income within Myanmar is deemed to be income received within Myanmar. The income is generally subject to tax under the normal rules for residents.

A company registered under the MIC/SEZ is entitled to enjoy certain exemptions and relief from taxes (*see the Tax credits and incentives section for details*).

Type of taxpayer or income	Tax rate (%)
Companies incorporated in Myanmar under the Myanmar CA or Special Companies Act	25
Enterprises operating under the MIC or SEZ	25
Non-resident foreign organisations registered under the Myanmar CA or Special Companies Act, such as a branch of a foreign company	25

Local income taxes

There is no separate corporate income tax at the local level.

Corporate residence

A resident company is a company as defined and formed under the Myanmar CA or any other existing law of Myanmar.

A non-resident company is one that is not formed under the Myanmar CA or any other existing law of Myanmar. Generally, foreign branches registered in Myanmar are deemed to be non-resident companies.

Permanent establishment (PE)

Currently, there is no definition of a PE under the Myanmar Income Tax Act. Under the Myanmar Income Tax Act, the Myanmar tax authorities are empowered to collect income tax from a non-resident foreigner on its income sourced within Myanmar. In current practice, the Myanmar tax authorities seek to collect taxes from a non-resident foreigner on its income received from Myanmar by way of a withholding tax (WHT) mechanism, regardless of whether the foreigner has a PE or taxable presence in Myanmar or not. The term 'PE' may be defined in the tax treaties that Myanmar has with other countries. Subject to the relevant tax treaty, a foreigner who is tax resident of the treaty country may not be subject to Myanmar taxes if it does not have a PE in Myanmar.

Other taxes

Value-added tax (VAT)

There is no VAT in Myanmar.

Commercial tax

Commercial tax, at rates ranging from 0% to 8%, is levied as a turnover tax on goods and services. Generally, commercial tax is imposed at the rate of 5%. The commercial tax that a business charges and collects is known as output tax, which has to be paid to the Myanmar tax authorities. Commercial tax incurred on business purchases and expenses are known as input tax. Businesses that are registered for commercial tax can claim commercial input tax if certain conditions are satisfied.

Commercial tax is imposed on a wide range of specified goods and services traded, produced, or rendered within the country, based on the sales proceeds, and on imported goods (*see Customs duties below for details*). There are 86 goods exempted from commercial tax.

All services are subject to 5% commercial tax except for 30 types of services that are specifically exempt from commercial tax (e.g. life insurance, banking and financial services that are operated with the permission of the Central Bank of Myanmar, microfinance, public transportation, publishing services).

No commercial tax is imposed if the proceeds from production and sales of goods, receipts from services, or proceeds from trading for a financial year are not more than 50 million Myanmar kyats (MMK).

Commercial tax is zero-rated on all exports, except for electricity (8%) and crude oil (5%).

Companies registered under the MIC/SEZ may, at the discretion of the MIC/SEZ Committee, be granted exemption from commercial tax during certain stipulated periods (*see the Tax credits and incentives section for details*).

Specific goods tax

The Specific Goods Tax Law replaces commercial tax on a list of specific goods that are imported into Myanmar, manufactured in Myanmar, or exported to a foreign country. The list of specific goods include cigarettes, tobacco leaves, virginia leaves, cheroots, cigars, pipe tobaccos, and betel-chewing tobacco; beers, wine, and alcoholic beverages; wood logs and wood cuttings; raw jade, rubies, sapphires, emeralds, diamonds, and other precious gems; polished jade, rubies, sapphires, emeralds, diamonds, and other precious gems; jewellery studded with polished jade, rubies, sapphires, emeralds, diamonds, and other precious gems; vans, saloons, sedans and estate wagons, and coupe cars except double cab 4-door pickups from the range of 1501 cc to 4001 cc and above; and kerosene, petrol, diesel, and aviation jet fuel, as well as natural gas. The specific goods tax rates range from 5% to 80%.

Specific goods tax is zero-rated on all exports, except for natural gas, wood logs and wood cuttings, raw gemstones, and processed gemstones. The tax rates range from 5% to 15%.

Under the Specific Goods Tax Law, only a manufacturer of special goods can claim and offset the specific goods tax incurred on purchase of raw materials/semi-finished goods against the specific goods tax charged on sale of specific goods.

On top of special goods tax, commercial tax of 5% will also be imposed.

Companies registered under the MIC/SEZ may, at the discretion of the MIC/SEZ Committee, be granted exemption from internal taxes, which may cover specific goods tax, during certain stipulated periods (*see the Tax credits and incentives section for details*).

Customs duties

Customs duty is levied under the Customs Tariff of Myanmar (2017) at rates of up to 40%.

Companies registered under the MIC/SEZ may, at the discretion of the MIC/SEZ Committee, be granted exemption from customs duties during certain stipulated periods (*see the Tax credits and incentives section for details*).

Excise duties

Excise duty is levied on alcoholic drinks and is collected by the General Administration Department under the Ministry of Home Affairs.

Property taxes

Immovable property (land and buildings) in Myanmar is subject to property tax.

Stamp duties

Stamp duty is levied on various types of instruments, and some rates are given below:

- 2% of the amount or value of the consideration for conveyances of properties, for the sale or transfer of immovable property except those in the Nay Pyi Taw, plus an additional 2% for a consideration equal to the market value of the property. Conveyance of immovable properties located in Yangon is subject to an additional duty of 2% pursuant to Yangon Development Trust Act 1921. Conveyance of immovable properties located in Nay Pyi Taw is subject to an additional duty of 2% pursuant to Nay Pyi Taw Development Law 2009.
- 0.1% of share value for the transfer of shares.
- 0.5% of the amount or value secured for bonds.
- 0.5% of the annual value of rent for immovable properties lease agreements between one and three years, and 2% of the average annual value of rent where the term of the lease agreement is more than three years. 2% stamp duty will also be applicable on lease premium.

Capital gains taxes

Capital gains tax is levied on gains from the sale, exchange, or transfer of capital assets (i.e. any land, building, vehicle, and any capital assets of an enterprise, which include shares, bonds, and similar instruments).

Capital gains from the sale, exchange, or transfer of capital assets in the oil and gas sector are taxed at different rates from those in other sectors.

Type of taxpayer	Tax rate (%)
Resident companies	10
Non-resident companies	10
Transfer of shares in an oil and gas company or interest in production sharing contracts	40 to 50

Tax returns for capital gains must be filed within 30 days from the date of disposal of the capital assets. Capital gains tax payments are required to be made within 30 days from the date of disposal of the capital assets. The date of disposal refers to the date of execution of the deed of disposal or the date of delivery of the capital assets, whichever is earlier.

Registration taxes

There is a registration fee of MMK 250,000 payable to the Directorate of Investment and Company Administration for setting up a company or a branch in Myanmar. In addition to the registration fee, there may be other administrative expenses or stamp duty payable on the company's memorandum of agreement and memorandum of understanding.

Payroll taxes

An employer is responsible for deducting income tax due from salaries at the time of payment to employees and must pay the amount within seven days from the date of deduction. If the employer fails to deduct and pay the tax, the employer is deemed to be a defaulter and held responsible for such payment. In addition, the employer is also responsible for filing the statement of annual salary within three months after the end of the income year, and failure to file by the stipulated deadline (i.e. 30 June every year) may result in a penalty of 10% of the amount of tax to be deducted on annual salaries.

Social security contributions

An employer with five or more employees is required to provide Social Security Scheme benefits to those workers, such as health and social care insurance and insurance against employment-related injuries.

The rates of contribution by employees and employers are 2% and 3% of the total salaries and wages, respectively. The contribution must be made in Myanmar kyats for all currencies that the salaries are paid in within 15 days of the following month, using the exchange rate prescribed by the Myanmar Foreign Trade Bank (MFTB) on the first day of the relevant month.

The maximum contribution is limited to MMK 9,000 by the employer and MMK 6,000 by the employee.

Contributions made by the employees are deductible for tax purposes in the hands of the employees. The employer is obligated to withhold the employees' contributions from their salaries.

Branch income

Generally, foreign branches are deemed to be non-resident companies. Non-resident companies are taxed only on income derived from sources within Myanmar. Non-resident companies pay tax at the same rate as resident companies. This means a branch of a foreign company will pay tax at the 25% rate. The income is generally subject to tax under the normal rules for residents.

Income determination

Income is categorised as income from a profession, business, property, capital gains, other sources, and undisclosed sources, as well as income that has escaped tax assessment. Income from capital gains is assessed separately.

Tax is levied on total income, after the deduction of allowable expenditure and depreciation.

The Ministry of Planning and Finance, with the approval of the government, may, by notification, prescribe, amend, and add assessable income and rates of income tax.

Inventory valuation

There are no prescribed inventory valuation methods for tax purposes.

Capital gains

Income from capital gains is assessed separately. *See Capital gains tax in the Other taxes section for details*.

Dividend income

Myanmar has a one-tier corporate tax system, under which shares of profits received by a Myanmar taxpayer from an association of persons (i.e. partnerships, joint ventures, companies, etc.) are exempted from income tax.

Interest income

Interest income and income from movable property are treated as business income.

Royalty income

There is no specific provision under the current Myanmar Income Tax Law governing the taxability of royalty income. Royalty income is generally treated as business income.

Foreign income

Resident companies are taxed on a worldwide basis, and, as such, income from sources outside Myanmar is taxable in Myanmar.

Non-resident companies are not taxed on their foreign income.

There is no deferral regime available to foreign income in Myanmar.

Deductions

In respect of business income, deductions are allowed for expenditure incurred for the purpose of earning income.

Non-deductible items include capital expenditure, personal expenditure, expenditure that is not commensurate with the volume of business, irrelevant expenses and expenses incurred not for production of income, payments made to any member of an association of persons other than a company or a cooperative society, and inappropriate expenditure.

Depreciation and amortisation

Income from movable property is considered as business income, and depreciation allowance for the cost of such movable property can be deducted. Income from immovable property is generally computed in the same way as business income, except that no depreciation allowance can be deducted.

Technically, a taxpayer entity is required to claim tax depreciation on the qualifying assets used for its business purposes based on rates prescribed under the Myanmar Income Tax Law, using a prescribed tax depreciation claim form. A taxpayer is entitled to full-year tax depreciation in the year the asset is acquired. On the other hand, no tax depreciation is allowed in the year the asset is disposed of.

The tax depreciation rates of fixed assets, as prescribed under the Income Tax Regulations, are as follows:

- Buildings: 1.25% to 10%.
- Furniture and fittings installed in buildings: 5% to 10%.
- Machinery and plant: 2.5% to 20%.
- Various kinds of vehicles: 12.5% to 20%.
- Any fixed assets that are not prescribed: 5%.

Goodwill

There is no specific provision under the current Myanmar Income Tax Law governing the tax deductibility of goodwill.

Start-up expenses

There is no specific provision under the current Myanmar Income Tax Law governing the tax deductibility of start-up expenses. Generally, any operating expenses incurred before the commencement of business are not tax deductible. Myanmar tax authorities view pre-commencement expenses as capital in nature and not deductible for tax purposes. In current practice, capital expenditures incurred prior to the commencement of business should be allowed for tax depreciation where they relate to qualifying fixed assets.

Interest expenses

There is currently no specific provision in the Myanmar Income Tax Law indicating the tax treatment of interest expenses. In current practice, interest expenses and the related financing costs are likely deductible only in the year these expenses are incurred, provided that the interest expenses incurred are commensurate with the volume of business or benefits that the taxpayer received. Interest expenses incurred before the commencement of business generally are not tax deductible or tax depreciable.

Bad debt

There is no specific provision under the current Myanmar Income Tax Law governing the tax deductibility of bad debt.

Charitable contributions

Deductible charitable donations are limited to those made to the approved charitable organisations/activities and are subject to an overall limitation of 25% of total income.

Fines and penalties

Fines and penalties are generally not deductible as they are not incurred in the production of business income.

Taxes

There is no specific provision under the current Myanmar Income Tax Law governing the tax deductibility of taxes paid.

Net operating losses

Ordinary losses

Losses from any source may be set off against income accruing from any other sources in that year, except where the loss is from capital assets or a share of loss from an association of persons. Losses that are not fully deducted in a year can be carried forward and set off against profits in the next three consecutive years.

There is no provision for the carrying back of losses.

Capital losses

Capital losses and a share of loss from an association of persons cannot be set off against income from other sources or carried forward.

Payments to foreign affiliates

A Myanmar corporation can claim a deduction for royalties, management service fees, and interest charges paid to affiliates, provided that these payments are commensurate with the volume of business.

Group taxation

There is no group taxation regime in Myanmar.

Transfer pricing regime

There are currently no transfer pricing rules in Myanmar.

Thin capitalisation rules

Generally, there is currently no specific safe harbour with respect to a debt-to-equity ratio for Myanmar tax purposes. The Central Bank of Myanmar (CBM) has set a maximum debt-to-equity ratio of 3:1 or 4:1 (as part of the criteria for a Myanmar entity to obtain a foreign loan).

Controlled foreign company (CFC) regime

There are currently no CFC rules in Myanmar.

Tax credits and incentives

Myanmar Investment Law (MIL)

The new MIL 2016 was enacted on 18 October 2016. The new MIL is a consolidation of the Myanmar Citizen Investment Law (2013) and the MFIL (2012). The Myanmar Citizen Investment Law and MFIL have been repealed with effect from 18 October 2016.

The list of tax benefits under the new MIL are as follows:

1. For investments in sectors listed in a notification to be issued by the Commission in order to promote investment, exemption from corporate tax for seven, five, or three years, depending on whether the investment takes place in an underdeveloped, moderately developed, or adequately developed region or state. The designation of these zones are subject to change from time to time, depending on the development in the respective regions.
2. Income tax exemptions shall only be granted to sectors that the Commission has specified as sectors that are promoted for investments.
3. The Commission may allow more favourable exemptions and reliefs for locations where Myanmar citizen-owned businesses are operated. The government may also provide subsidies, funding, capacity building, and training to Myanmar citizen investors and citizen-owned small and medium-sized enterprises.
4. Exemption from customs duties or other internal taxes or both on machineries, equipment, instruments machinery components, spare parts, construction materials not available locally, and materials used in the business that are imported as they are actually required, during the construction period, or during the preparatory period of the investment business.

5. Exemption or relief from customs duties and/or other domestic taxes on raw materials and semi-finished goods that are imported for the production of export goods by wholly export investment businesses.
6. Right to obtain a refund, based on the amount of exported goods, of customs duties and/or other domestic taxes paid at the time of importation of raw materials and semi-finished goods that are used to manufacture the products in the country and re-export them.
7. If the volume of investment is increased and the original investment business is expanded during the period of investment, exemption or relief from customs duties or other internal taxes or both on machineries, equipment, instruments, machinery components, spare parts, materials used in the business, and construction materials not available locally, which are imported as they are actually required for use in the business that is being expanded.
8. Exemption or relief from income tax if the profits obtained from the investment business is reinvested in the same business or in a similar type of investment business within one year.
9. Right to deduct depreciation for the purpose of income tax assessment, after computing such depreciation from the year of commencement of commercial operation based on an accelerated depreciation rate (which is less than the stipulated lifetime of the asset).
10. Right to deduct expenses from assessable income incurred for research and development (R&D) related to the investment activities/business required for the development of the country and carried out in the country.
11. Foreign investors will pay income tax at the rates applicable to citizens residing within the country.

Union of Myanmar Foreign Investment Law (MFIL) incentives

Under the MFIL, companies registered under the MFIL that have obtained permits from the MIC were entitled to the following special benefits and tax incentives, which were granted at the MIC's discretion:

1. Exemption from income tax for up to five consecutive years for an enterprise. The exemption may be extended for a further reasonable period, depending on the success of the enterprise.
2. Exemption or relief from income tax on profits of a business that are maintained in a reserve fund and subsequently re-invested in Myanmar.
3. The right to deduct depreciation of machinery, equipment, building, or other capital assets used in the business at rates prescribed by the MIC.
4. Relief from income tax for up to 50% of the profits accrued from the export of manufactured goods.
5. The right to pay income tax on the income of foreigners at the rates applicable to citizens residing within the country.
6. The right to deduct from taxable income R&D costs that are necessary for the country.
7. The right to carry forward tax losses for up to three consecutive years, provided the losses are sustained within two years from the end of the tax exemption in (1) above.
8. Exemption or relief from customs duty and/or other internal taxes on imported machinery, equipment, instruments, machinery components, spare parts, and materials used in the business, which are required for use during the period of construction.

9. Exemption or relief from customs duty or other internal taxes on imported raw materials for the first three years of commercial production following the completion of construction.
10. If the investor increases the amount of investment and expands the business within the approved timeframe, it may enjoy exemption and/or relief from customs duty or other internal taxes on machinery, equipment, instruments, machinery components, spare parts, and materials that are imported for the expansion of business.
11. Exemption from commercial tax on goods that are manufactured for export.

Except for item (1) above, the other exemptions and reliefs are subject to discretion of the MIC.

Special economic zones (SEZs)

In addition to foreign investment under the MFIL, foreign investors may invest under the Myanmar Special Economic Zone Law of 2014 (Myanmar SEZ Law).

The Myanmar SEZ Law is a basic law for any SEZ within Myanmar. The main regulatory body handling foreign investment under the Myanmar SEZ Law is the Central Body for the Myanmar SEZ.

The Myanmar SEZ Law contains provisions relating to the exempted zone, business promoted zone, other zone, exempted zone business, other business, developers and investors, exemptions and reliefs, restrictions, duties of developers or investors, land use, banks and finance management and insurance business, management and inspection of commodities by the customs department, quarantine, labour and guarantee of non-nationalisation, dispute resolution, WHT, bank and financial management and insurance business, etc.

Incentives under the Myanmar SEZ Law include:

For investors:

- Income tax holidays for the first seven years starting from the date of commercial operation in respect of those investment businesses operated in an exempted zone or exempted zone businesses.
- Income tax holidays for the first five years starting from the date of commercial operation in respect of those investment businesses operated in a business promoted zone or other business in a promoted zone.
- 50% income tax relief for the investment businesses operated in an exempted zone and a business promoted zone for the second five-year period.
- For the third five-year period, 50% income tax relief on the profits of the business if they are maintained for re-investment in a reserve fund and re-invested therein within one year after the reserve is made.
- Exemption on customs duty and other taxes for raw materials, machinery and equipment, and certain types of goods imported for investors in exempted zones; whereas, for investors in prompted zones, exemption on customs duty and other taxes for the first five years in respect of machinery and equipment imported that are required for construction starting from the date of commercial operation, followed by 50% relief of customs duty and other taxes for a further five years.
- Carry forward of loss for five years from the year the loss is sustained.

For developers:

- Income tax holidays for the first eight years starting from the date of commercial operation.
- 50% income tax relief for the second five-year period.
- For the third five-year period, 50% income tax relief on the profits of the business if they are maintained for re-investment in a reserve fund and re-invested therein within one year after the reserve is made.
- Exemption on customs duty and other taxes for raw materials, machinery and equipment, and certain types of goods imported.
- Carry forward of loss for five years from the year the loss is sustained.

Land use may be granted under an initial lease of up to 50 years and renewable for a period of an additional 25 years. Developers/investors may rent, mortgage, or sell land and buildings to another person for investment purposes within the term granted with the approval of the management committee concerned.

Investors seeking to register an entity under the SEZ need to obtain an investment permit from the relevant SEZ Management Committee.

Foreign tax credit

There is no provision for unilateral relief. Relief may be available pursuant to a tax treaty, but the application of the tax treaties is at the sole discretion of the Ministry of Planning and Finance.

Withholding taxes

Any person making the following payments is required to withhold income tax at the time of payment at the rates listed below. The tax withheld must be paid to the Internal Revenue Department (IRD) within seven days from the date of withholding.

Tax withheld from payments to residents (and branches registered in Myanmar) will be set off against the tax due on their final assessments. Tax withheld from payments to non-resident companies (except the branches registered in Myanmar) is a final tax.

The application of the tax treaties is at the sole discretion of the Ministry of Planning and Finance.

For payments made by state organisations, state enterprises, development committees, co-operative societies, foreign companies, foreign enterprises and organisations, local companies, and under an existing law for purchase of goods, work performed, or supply of services and hiring within the country under a tender, contract, quotation, or other modes, the WHT rate is 2% if the payment is made to a resident and 2.5% if it is made to a non-resident.

	WHT (%)		
Recipient	**Dividends (1)**	**Interest**	**Royalties**
Resident national or resident foreigner	0	0	10
Non-resident corporations and individuals:			
Non-treaty	0	15	15
Treaty:			

	WHT (%)		
Recipient	**Dividends (1)**	**Interest**	**Royalties**
India	0	10 (2)	10
Korea, Republic of	0	10 (2)	10/15 (3)
Laos	0	10	10
Malaysia	0	10 (2)	10
Singapore	0	8/10 (2, 4)	10/15 (3)
Thailand	0	10 (2)	5/10/15 (5)
United Kingdom	0	Not covered	0 (6)
Vietnam	0	10 (2)	10

Notes

1. There is no WHT on dividends, branch profits, and share of profits of an association of persons that have been taxed.
2. Exempt if paid to the government.
3. Lower rate for payments in connection with patents, designs, secret formulas/processes, or industrial, commercial, or scientific equipment/experience.
4. Lower rate if received by a bank or a financial institution.
5. The 5% rate applies for payments in connection with copyrights of literary, artistic, or scientific work, and the 10% rate applies to payments for services of a managerial or consultancy nature, and for information concerning industrial, commercial, or scientific experience.
6. Exempt if the amount is fair and reasonable.

Tax administration

Taxable period

The taxable period of a company is the same as its financial year (income year), which is from 1 April to 31 March. Income earned during the financial year is assessed to tax in the assessment year, which is the year following the financial year. Under the Union Taxation Law 2018, it is stated that the tax fiscal year for 2018/19 will remain the same (i.e. 1 April to 31 March) for all taxpayers except state-owned enterprises, which are required to file tax returns based on the budget year ending 30 September starting 2018/19, from 1 October 2018.

It is also stated in the Union Taxation Law 2018 that the fiscal year for Specific Goods Tax Law, Commercial Tax Law, and Income Tax Law shall be the same for all taxpayers, including both private taxpayers and state-owned enterprises, starting from 1 October 2019. In other words, all taxpayers are required to follow the new financial period of 30 September year-end beginning 1 October 2019. At this juncture, there is no guideline issued by the IRD/Directorate of Investment and Company Administration (DICA) addressing transition issues regarding the change of financial year-end for 2019/20 for private taxpayers. A private taxpayer is likely to have a financial period from 1 April 2018 to 31 March 2019 followed by a financial period from 1 April 2019 to 30 September 2019.

Tax returns

In general, annual income tax returns must be filed within three months from the end of the financial year.

Tax returns for capital gains must be filed within 30 days from the date of disposal of the capital assets.

If a taxpayer discontinues one's business, returns must be filed within one month from the date of discontinuance of business.

The failure of a taxpayer to file income tax returns, knowing that assessable income has been obtained, is deemed to have 'fraudulent intention'.

Payment of tax

Advance corporate tax payments are made in quarterly instalments within ten days from the end of the relevant quarter throughout the income tax year based on the estimated total income for the year. The advance payments and any taxes withheld are creditable against the final tax liability. The date for settling the final tax liability is specified in the notice of demand issued by the IRD.

Capital gains tax needs to be paid within 30 days from the date of disposal of capital assets.

Tax audit process

Under the Myanmar Income Tax Law, if it is found that there is a fraudulent intention to evade tax, the assessment or reassessment of income tax can be made at any time on the income that has escaped assessment of tax.

Failure by a taxpayer to file a return of income knowing that assessable income has been obtained, failure to comply with the notice of the IRD to submit accounts and documents, including the tax return and profit and loss accounts within the time prescribed, or submitting forged instruments and other documents are included within the meaning of fraudulent intention. If the tax authority in the course of investigation finds that a taxpayer has concealed income or particulars relating to income, the taxpayer may be permitted to fully disclose the facts within the specified time. In addition, the taxpayer must pay a penalty equal to 100% of the tax increased on account of the concealment. If the taxpayer fails to disclose the particulars within the specified time or discloses less than the income concealed, the taxpayer will also be subject to prosecution, in addition to paying the tax and penalty. If the taxpayer is found guilty, the taxpayer may be punishable with imprisonment for between three to ten years.

Statute of limitations

The statute of limitation to raise an assessment is three years after the financial year-end. It does not apply in cases of fraudulent default. Mere filing of the income tax return and payment of advance tax in time does not constitute a final tax assessment.

Topics of focus for tax authorities

The following issues are currently being focused on by the tax authorities:

- Timely filing of tax returns and payment of taxes (i.e. corporate tax, commercial tax, employer tax, specific goods tax, etc.).
- Tax deductibility of donations for corporate tax purposes.
- WHT compliance on both domestic and cross-border transactions.
- Stamp duty compliance (i.e. the application of the duty rates and timeliness of payment).
- Related-party transactions (e.g. payment of management fee to head office, shareholder loans).

New Zealand

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Significant developments

Employee share schemes

In March 2018, the government enacted the Taxation (Annual Rates for 2017/18, Employment and Investment Income, and Remedial Matters) Act 2018. The Act introduces new rules for the taxation of employee share schemes and how to determine the amount and time of derivation of income and when expenditure is incurred under an employee share scheme. The purpose of the changes is to effect tax neutral treatment of employee share schemes relative to cash-based schemes. The rules also include a new definition of employee share scheme that means the rules apply to share benefits provided to employees (past, present, and future) and shareholder-employees. With some exceptions, the rules will come into effect from 29 September 2018, which is six months after legislative enactment.

Base erosion and profit shifting (BEPS) update

In May 2018, the Taxation (Neutralising Base Erosion and Profit Shifting) Bill, which was introduced into Parliament in December 2017, was reported back. The Bill represents the accumulation of extensive work conducted by Officials following the finalisation of the Organisation for Economic Co-operation and Development's (OECD's) BEPS framework in late 2015. Measures contained within the Bill seek to prevent multinationals from achieving tax advantages by using:

- artificially high interest rates on loans from related parties to extract profits out of New Zealand
- hybrid mismatching arrangements that exploit differences between countries' tax rules to achieve an advantageous tax position
- artificial arrangements to avoid having a permanent establishment (PE) for tax purposes in New Zealand, and
- related-party transactions to shift profits into offshore group members in a manner that does not reflect the actual economic activities undertaken in New Zealand and offshore.

The Bill is expected to be enacted by mid-2018.

Research and development (R&D) tax credit

The government released a Discussion Document for public consultation in May 2018, which proposes the introduction of a 12.5% R&D tax credit on eligible expenditure for businesses undertaking R&D in New Zealand. A maximum tax credit of 15 million New Zealand dollars (NZD) will be available each year.

It is expected that the tax credit will be enacted in early 2019 and be available for eligible expenditure incurred from 1 April 2019.

Goods and services tax (GST) on low-value imported goods

In May 2018, the government sought feedback on a proposal to introduce GST on the importation of low-value goods. The proposal would require offshore suppliers of goods supplied to New Zealand consumers to charge and remit GST on goods valued at less than NZD 400. Offshore suppliers supplying a total value of goods and services to New Zealand consumers above NZD 60,000 in a 12-month period would be required to register for GST purposes.

Consultation is currently underway, with the changes expected to be introduced to Parliament before the end of 2018 and effective from 1 October 2019.

Customs and excise duties

The Customs and Excise Act was enacted in March 2018 and represents a monumental step towards replacing and modernising the current customs legislation. Some of the key substantive changes affecting importers, exporters, and manufacturers include:

- moves to streamline the GST at the border for business importers
- a more flexible disputes regime
- ability to declare a provisional value for imported goods in specified cases
- ability to obtain rulings on more matters, including valuation, and
- more clarity on administrative penalties.

Double tax agreements (DTAs)

New Zealand is currently negotiating new and updating DTAs with a number of countries, including China, Luxembourg, and the United Kingdom.

The OECD's Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) was signed by New Zealand on 7 June 2017. The signing of the MLI will enable signatory countries to quickly update existing DTAs to include articles on PE avoidance, treaty abuse, dispute resolution, and hybrid mismatches.

An update to the existing DTA between New Zealand and Hong Kong was signed in June 2017. The new protocol allows automatic and spontaneous exchanges of tax information, with the first automatic exchange of information expected to occur before 30 September 2018.

Taxes on corporate income

New Zealand resident companies are taxed on their worldwide income, and non-resident companies (including branches) are taxed on New Zealand-sourced income.

The New Zealand corporate income tax (CIT) rate is 28%.

Local income taxes

There are no state or municipal income taxes in New Zealand.

Corporate residence

Residence is determined by place of incorporation, location of head office, centre of management, or by directors' exercising control of the company in New Zealand.

Permanent establishment (PE)

Generally, DTAs to which New Zealand is a party define a PE by reference to a fixed place of business through which the company's business is carried on. A PE can also exist without a fixed place of business if the employees of the overseas company habitually exercise an authority to conclude contracts in New Zealand or provide services in New Zealand for a period of time.

Other taxes

Goods and services tax (GST)

GST is a form of value-added tax (VAT) that applies to most supplies of goods and services, including services and intangibles supplied remotely by an offshore supplier to New Zealand resident consumers. The narrow category of exempt supplies includes financial services. The rate applied to taxable supplies is currently 15% or 0%.

The 0% rate applies to a few supplies only, including exports and financial services supplied to other registered businesses. The 0% rate also applies to the sale of land between two GST-registered parties if the purchaser acquires the land with the intention of using it to make taxable supplies and the land is not intended to be used as a principal place of residence for the purchaser or an associate.

There is also a 'reverse charge' mechanism that requires the self-assessment of GST on the value of certain services imported by GST-registered persons.

GST is also imposed on remote services provided by non-residents to New Zealand private consumers. The concept of 'remote services' is wide and includes streamed and downloaded digital products (e.g. music, movie, and game downloads, e-books, e-magazines) as well as remotely provided webinars, software, web design and publishing, insurance, gambling, consulting, IT, and professional services.

Non-residents who do not make taxable supplies in New Zealand can register for GST, provided they meet certain criteria, allowing them to claim a refund for their input GST costs.

Customs duties

Customs duty is levied on some imported goods at rates generally ranging from 1% to 10%.

Excise duty

Excise duty is levied, in addition to GST, on alcoholic beverages (e.g. wines, beers, spirits), tobacco products, and certain fuels (e.g. compressed natural gas, gasoline). The excise duties are levied item-by-item at rates that vary considerably.

Property taxes

Local authorities levy tax known as 'rates' on land within their territorial boundaries. Rates are levied on properties based on the properties' rateable value.

Residential land withholding tax (RLWT)

RLWT applies to the sale of residential land in New Zealand by an 'RLWT offshore person'. RLWT applies where the land was acquired on or after 1 October 2015 through 28 March 2018 and owned for less than two years before being sold, or where the land was acquired on or after 29 March 2018 and owned for less than five years before being sold.

An 'RLWT offshore person' includes all non-New Zealand citizens and non-permanent residents. It also includes a New Zealand citizen who is living overseas if they have been overseas for the last three years. A holder of a New Zealand residence class visa may be an offshore person if they are outside New Zealand and have not been in New Zealand within the last 12 months. New Zealand trusts and companies may also be 'offshore persons' if there are significant offshore interests in them.

The amount of RLWT to be deducted is the lessor of:

- 10% of the sale
- the gain on sale x the RLWT rate (28% for companies, incorporated clubs, and societies; 33% for individuals, all other non-individuals, and companies acting as trustees of a trust), or
- the sale price less outstanding local authority rates or less security discharged amount, depending on which party is withholding the tax.

Transfer taxes

There are no taxes on the transfer of property in New Zealand.

Stamp duty

Stamp duty has been abolished in respect of instruments executed after 20 May 1999.

Accident compensation levy

A statutory-based scheme of accident insurance is funded in part by premiums payable by employers and employees.

Premiums paid by employers (including the self-employed) fund insurance for work-related accidents. Employers are liable to pay a residual claims levy and an employer levy. The employer levy payable is determined according to the industry or risk classification of the employer and the level of earnings of employees.

Fringe benefit tax (FBT)

Employers are subject to a tax-deductible FBT on the value of non-cash fringe benefits provided to their employees. Employers can elect to pay FBT at flat rates (for the 2018/19 income year, 49.25% on attributed benefits and 42.86% on pool benefits, i.e. those benefits that cannot be attributed to a particular employee) applied against the value of the benefit or can attribute fringe benefits to individual employees and pay FBT based on each employee's marginal tax rate.

Under the attribution option, the applicable FBT rate depends on the net remuneration (including fringe benefits) paid to the employee. The attribution calculation treats the fringe benefit as if it was paid in cash and calculates FBT as the notional increase in income that otherwise would have arisen.

The current multi-rates are:

Net remuneration (NZD)	FBT rate (%)
12,530 or less	11.73
12,531 to 40,580	21.21
40,581 to 55,980	42.86
Greater than 55,980	49.25

Fringe benefits include motor vehicles available for private use, loans at below prescribed interest rates, contributions to medical insurance schemes, and non-monetary employer contributions to superannuation schemes.

In relation to motor vehicles, employers can value a vehicle on an annual basis either using 20% of the cost price or market value (GST inclusive) of the vehicle (depending on whether the vehicle is owned or leased by the employer) or 36% of the vehicle's tax written down value (GST inclusive). In each case, the FBT value must be reduced proportionately for whole days when the vehicle is not available for private use at any time.

FBT is also applicable to benefits received by an employee from a third party where there is an arrangement between the employer and the third party and where the benefit would be subject to FBT if it had been provided by the employer.

Employer superannuation contribution tax (ESCT)

Employers' contributions to an approved superannuation fund (excluding foreign schemes) are subject to ESCT. This includes employer contributions to KiwiSaver (or other qualifying registered superannuation schemes).

ESCT is generally deducted at the employee's relevant progressive rate based on the total salary or wages and employer superannuation cash contributions paid to the employee in the previous year.

Salary or wages plus superannuation contributions (NZD)	ESCT rate (%)
Up to 16,800	10.5
16,801 to 57,600	17.5
57,601 to 84,000	30.0
Over 84,000	33.0

Non-resident contractor's tax (NRCT)

New Zealand imposes an obligation to deduct NRCT on those making contract payments to non-residents in relation to certain contract activities undertaken in New Zealand. Contract activities generally relate to services but also include the granting of a right to use property in New Zealand. The NRCT rate is generally 15% (or 45% for individuals and 20% for companies if the relevant paperwork is not provided). Some contractors are eligible to apply for a certificate of exemption or a reduced rate certificate.

In additional to a certificate of exemption, no NRCT is required to be withheld if the non-resident has full relief from tax under a DTA and is present in New Zealand for no more than 92 days in a 12-month period.

Payments for contract work amounting to less than NZD 15,000 in a 12-month period are also exempt from NRCT. In such cases, contractors themselves are responsible for paying any New Zealand tax owed at the end of the year (provided there is no relief from tax under a DTA).

Branch income

A non-resident company is taxed on income generated by business wholly or partially carried on in New Zealand. Branch profits are subject to ordinary corporate rates of taxation, and there is no withholding tax (WHT) on repatriated profits.

Income determination

Inventory valuation

Inventory must be valued by a cost-valuation method or, where market-selling value is lower than cost, may be valued at market-selling value. If the inventory is shares, it must be valued at cost. Cost is determined under New Zealand Generally Accepted Accounting Practice (NZ GAAP). Acceptable cost flow methods are first in first out (FIFO) or weighted-average cost. Some valuation concessions are available to small taxpayers.

Capital gains

There is no separate capital gains tax. However, the income tax legislation specifically includes various forms of gain that would otherwise be considered a capital gain within the definition of 'income'. Taxable income includes gains on the sale of real estate in certain circumstances and on personal property where the taxpayer acquired the property for resale or deals in such property or where a profit-making purpose or scheme can be deemed or imputed.

Dividend income

Inter-corporate dividends paid between New Zealand resident companies are exempt where there is 100% common ownership.

Dividends from a foreign company

A dividend derived by a company resident in New Zealand from a foreign company is treated as exempt income unless it is:

- a dividend on a fixed rate share or a dividend for which the foreign company has received a tax deduction in its home jurisdiction, or
- a dividend from a portfolio foreign investment fund (FIF) (i.e. interests under 10%) that is exempt from FIF rules (e.g. an interest in an Australian listed company).

Dividends from foreign companies derived by taxpayers other than companies are taxable (generally with a credit for any foreign WHTs).

Supplementary dividend tax credit regime

Previously, the supplementary dividend tax credit regime (commonly referred to as FITC) ensured that foreign investors were not taxed at more than the New Zealand corporate tax rate by effectively rebating the New Zealand WHT to the extent that the dividend was fully imputed. As non-resident withholding tax (NRWT) rates have been reduced to nil on most fully imputed dividends, a supplementary dividend tax credit is generally no longer required.

The supplementary dividend tax credit regime applies only to fully imputed dividends paid to shareholders holding less than 10% of the shares in the company and NRWT rates of at least 15%.

Broadly therefore:

- only portfolio investors (i.e. those with less than 10% holdings) with NRWT rates of at least 15% will qualify for relief under the supplementary dividend rules, and
- a zero rate of NRWT applies to dividends paid to non-portfolio shareholders (i.e. shareholders with more than 10% holdings) and to any other dividends subject to lower tax rates, to the extent they are fully imputed.

Stock dividends

Bonus issues can be taxable or non-taxable. With a taxable bonus issue, the amount capitalised becomes available for tax-free distribution upon a subsequent share cancellation. With a non-taxable bonus issue, the amount capitalised is not available for tax-free distribution upon a subsequent share cancellation.

Shares issued under profit distribution plans (PDPs) are treated as taxable dividends.

Interest income

All interest derived by a company is income. The financial arrangement rules may require income for tax purposes to be recognised on an accrual basis. When this is not required (because the person is classified as a 'cash basis' person), interest income is recognised as and when it is received.

Royalty income

All royalty payments derived by a company is income. Royalty income includes payments for the supply of knowhow. It also includes a payment of any kind derived as consideration for a copyright, patent, plant variety right, trademark, design or model, plan, and secret formula.

Other significant items

The taxation of debt and debt instruments is governed by the financial arrangements rules, a specific set of timing rules. Income or expenditure (including foreign exchange gains and losses) from financial arrangements must be recognised on an accrual basis (generally, yield to maturity or other commercially acceptable method). These rules do not apply to the income or expenditure of a non-resident if the financial arrangement does not relate to a business carried on in New Zealand.

Foreign income

A New Zealand corporation is taxed on foreign passive income as earned. Double taxation with respect to all types of taxable income, including interest, rents, and royalties, is avoided by the recognition of foreign tax credits.

New Zealand does not offer specific tax deferral rules.

Deductions

Depreciation and depletion

For tax purposes, depreciation of property can be computed under the diminishing-value method, the straight-line method, or a pooling method. The rates of depreciation depend on the following factors:

- Type of asset.
- Whether the asset is acquired new or second-hand (i.e. used).

Taxpayers must use the economic depreciation rates prescribed by Inland Revenue. Fixed-life intangible property (including the right to use land and resource consents) is depreciable on a straight-line basis over its legal life. Any depreciation recovered on the sale of an asset (up to its original cost) is taxable in the year of sale.

The double-declining-balance (diminishing value) method applies to most plant and equipment. Under the double-declining-balance method, equipment with an estimated useful life of ten years results in diminishing value depreciation deductions of 20% *per annum* (i.e. double the straight-line rate of 10% over the equipment's ten-year life). Buildings, certain motor vehicles, high-residual-value property, fixed-life intangible property, and property acquired prior to the introduction of the new rules cannot be depreciated under the double-declining-balance method.

The depreciation rate for buildings with an estimated useful life of 50 years or more is 0% as of the 2011/12 income year.

Goodwill

Goodwill is generally regarded as a capital asset, thus any payment for goodwill is non-deductible. There is a limited exception for payments made to preserve goodwill.

Start-up expenses

Expenses incurred by a company before the commencement of the business are generally regarded as outgoings of a capital nature and are therefore not deductible. However, certain expenditure on scientific research may be deductible, provided that it is incurred for the purpose of the company deriving assessable income.

Research and development (R&D)

R&D costs are tax deductible. Expenses written off as immaterial and not tested against certain asset-recognition criteria are not automatically deductible for tax purposes.

Unsuccessful software development costs

Taxpayers are allowed an upfront deduction for expenditure incurred on unsuccessful software development projects in the year that the development is abandoned.

Interest expense

Generally, interest incurred by most companies is deductible, subject to thin capitalisation rules (*see the Group taxation section*).

Bad debt

A company is allowed a deduction for bad debt in the income year in which the debt is physically written off by the company.

Charitable contributions

A company is generally allowed a deduction for charitable contributions it makes to an approved Inland Revenue donee organisation or a charity that performs its activities in New Zealand. The list of approved donee organisations is available on Inland Revenue's website. The deduction available for charitable contributions is limited to the company's net income for that income year.

Entertainment expenditure

Entertainment expenditure is generally only 50% deductible. However, entertainment expenditure incurred overseas is 100% deductible.

Legal expenditure

Legal expenditure is deductible if the expenditure is:

- incurred in deriving assessable or excluded income or
- incurred in the course of carrying on a business for the purpose of deriving assessable or excluded income.

However, the expenditure is not deductible if it is of a capital, private, or domestic nature.

Taxpayers with business-related legal expenditure of NZD 10,000 or less are able to deduct the full amount of the expenditure in the year it is incurred, whether or not it is capital in nature.

Fines and penalties

Generally, no deduction is available where a company has incurred expenditure on fines or penalties paid in breach of statute or regulation. Expenditure on other fines and penalties requires further evaluation before its deductibility can be determined.

Taxes

FBT is deductible, as is GST payable on the value of a fringe benefit.

Net operating losses

Losses may be carried forward indefinitely for offset against future profits, subject to the company maintaining 49% continuity of ownership. There is no loss carryback. Losses of a subsidiary are preserved on a spinout (i.e. when shares in the subsidiary are transferred to shareholders of its parent company).

Payments to foreign affiliates

A New Zealand corporation can claim a deduction for royalties, management service fees, and interest charges paid to non-resident associates, provided the charges satisfy the 'arm's-length principle', which forms the basis of New Zealand's transfer pricing regime.

Group taxation

Groups of resident companies that have 100% common ownership may elect to be subject to the consolidated group regime. The group is effectively treated as a single company, and transfers of assets, dividends, interest, and management fees among members of the group are generally disregarded for tax purposes. The group files a single return and is issued a single assessment. Group members are jointly and severally liable for tax purposes, unless an election is made to limit the liability to one or more companies in the group.

Outside of the consolidated group regime, companies that are 66% or more commonly owned constitute a 'group'. Group companies are able to offset losses by election as well as by subvention payment. A subvention payment is a payment made by the profit company to the loss company and cannot exceed the amount of the loss company's loss. The payment is deductible to the profit company and assessable to the loss company.

Companies that are more than 66% commonly owned but not wholly owned may transfer imputation credits as part of loss grouping (i.e. loss offsets or subvention payments). This allows the company receiving the benefit of the loss grouping to pay a fully imputed dividend despite engaging in loss grouping and allows the company to retain the benefit of the loss transfer.

Certain companies subject to special bases of assessment (e.g. mining companies other than petroleum extraction companies) are excluded from the grouping provisions. Branches of non-resident companies may be included, provided they continue to carry on business in New Zealand through a fixed establishment.

Losses incurred by a dual-resident company are not available for offset by election or subvention payment.

Transfer pricing

The transfer pricing rules are based on OECD principles and require taxpayers to value all cross-border transactions with associates on an arm's-length basis.

The transfer pricing rules apply to arrangements for the acquisition or supply of goods, services, money, intangible property, and anything else (other than non-fixed rate shares) where the supplier and acquirer are associated persons. Similar rules apply to the apportionment of branch profits.

Various methods are available for determining the 'arm's-length consideration'. The taxpayer is required to use the method that produces the most reliable measure of the amount that independent parties would have paid or received in respect of the same or similar transactions. Inland Revenue has published guidelines that make it clear that documentation is required to support a taxpayer's transfer prices. However, currently there is no legal requirement to maintain transfer pricing documentation in New Zealand.

Significant changes are proposed to the transfer pricing rules as part of a series of BEPS-related proposals included in legislation before Parliament. The new concept of a 'control group' is being introduced, which is when members of a group are consolidated for accounting purposes. Those who meet the definition of a 'control group' will be subject to more restricted transfer pricing rules. These changes are expected to come into effect for income years beginning on or after 1 July 2018.

Country-by-country (CbC) reporting requirements

New CbC reporting requirements have been published by the OECD in order to address BEPS. In New Zealand, the first reporting of CbC data took place during the 2017 calendar year.

Each year, the New Zealand Inland Revenue will contact the New Zealand headquartered corporate groups required to file the CbC report and provide templates and guidance.

Thin capitalisation

'Inbound' thin capitalisation rules apply to New Zealand taxpayers controlled by non-residents, including branches of non-residents. The aim of the rules is to ensure that New Zealand entities or branches do not deduct a disproportionately high amount of the worldwide group's interest expense. This is achieved by deeming income in New Zealand when, and to the extent that, the New Zealand entities in the group are thinly capitalised (i.e. excessively debt funded).

The inbound rules include situations where non-residents are 'acting together' and include trusts where the majority of settlements have come from non-residents or from entities subject to the thin capitalisation rules.

The 'outbound' thin capitalisation rules are intended to operate as a base protection measure to prevent New Zealand residents with controlled foreign company (CFC) investments and certain FIF investments from allocating an excessive portion of their interest cost against the New Zealand tax base.

To reduce taxpayer compliance costs, the outbound thin capitalisation rules do not apply when the New Zealand taxpayer has 90% or more of their assets in New Zealand.

Further concessions are available under the 'outbound rules' to taxpayers who do not fall below this threshold. If the taxpayer's interest deduction and dividends paid for fixed rate shares (the finance cost) is below NZD 1 million, no apportionment of deductible interest is required. If the finance cost is above NZD 1 million, but below NZD 2 million, the interest apportionment may be reduced.

An apportionment of deductible interest is required under the thin capitalisation rules when the debt percentage (calculated as the total group interest bearing debt/total group assets of a New Zealand entity or group) exceeds both:

- 60% (for 'inbound' thin capitalisation) or 75% (for 'outbound' thin capitalisation) and
- 110% of the worldwide group's debt percentage.

The use of the debt-to-asset ratio differs from most thin capitalisation models that apply to an entity's debt-to-equity ratio. All interest (both related and unrelated party) is subject to apportionment.

Foreign-owned banks operating in New Zealand are subject to specific thin capitalisation rules that deem income if the bank does not hold a level of equity equivalent to 6% of their New Zealand banking risk-weighted assets. In addition, banks are required to have sufficient equity to equity fund offshore investments that do not give rise to New Zealand taxable income in full.

Significant changes are proposed to the thin capitalisation rules as part of a series of BEPS-related proposals currently before Parliament. These changes are expected to come into effect for income years beginning on or after 1 July 2018. The proposed changes include:

- A 'restricted transfer pricing rule' within the transfer pricing regime, which would require inbound related-party loans to be priced as plain vanilla senior debt with a rebuttable presumption of parental support, unless the foreign parent has substantial third-party debt that includes those terms.
- An administrative safe harbour in the form of an interest rate cap calculated with reference to the credit rating of the New Zealand borrower's ultimate parent company.
- An anti-avoidance rule to ensure that taxpayers do not repay loans just before year-end for thin capitalisation purposes.
- Measuring total assets net of non-debt liabilities, excluding any interest-free shareholders loans.

Controlled foreign companies (CFCs)

The CFC regime imposes New Zealand tax on the notional share of income attributable to residents (companies, trusts, and individuals) with interests in certain CFCs.

Central to the regime is the definition of a CFC. When five or fewer New Zealand residents directly or indirectly control more than 50% of a foreign company, or when a single New Zealand resident directly or indirectly controls 40% or more of a foreign company (unless a non-associated non-resident has equal or greater control), that company is a CFC. For interests that do not meet the definition of a CFC, the investment may be taxed under the FIF regime (*see below*).

Note that a person with an income interest in a CFC does not have attributed CFC income or losses if:

- the Australian exemption applies or
- the CFC passes an active business test.

If the exemptions do not apply, only the CFC's passive (attributable) income is subject to tax on attribution (on an accrual basis). However, no income attribution is required if a New Zealand resident has an income interest of less than 10% in the CFC.

Active business test

A CFC passes the active business test if it has passive (attributable) income that is less than 5% of its total income. For the purposes of the test, taxpayers measure passive and total income using either financial accounting (audited International Financial Reporting Standards [IFRS] or NZ GAAP accounts) or tax measures of income.

CFCs in the same country may be consolidated for calculating the 5% ratio, subject to certain conditions.

Australian exemption

A person with an interest in a CFC does not have attributed CFC income or a loss if the CFC is a resident in, and subject to income tax in, Australia and meets certain other criteria.

Passive (attributable) income

Attributable, or passive, income is income that is highly mobile and not location-specific (i.e. income where there is a risk that it could easily be shifted out of the New Zealand tax base).

The broad categories of attributable income are as follows:

- Certain types of dividend that would be taxable if received by a New Zealand resident company.
- Certain interest.
- Certain royalties.
- Certain rents.
- Certain amounts for financial arrangements.
- Income from services performed in New Zealand.
- Income from offshore insurance business and life insurance policies.
- Personal services income.
- Income from the disposal of revenue account property.
- Certain income related to telecommunications services.

Taxpayers must disclose interests in CFCs in their annual tax returns. Failure to disclose CFC interests can result in the imposition of penalties.

Foreign investment funds (FIFs)

The FIF regime is an extension of the CFC regime, which subjects persons with interests in certain foreign entities (which are not CFCs) to New Zealand tax. It also applies when the investor does not have a sufficient interest in a foreign entity to be taxed under the CFC regime.

Common examples of investments classified as FIFs include foreign companies, unit trusts, and life insurance policies issued by foreign entities not subject to New Zealand tax.

The FIF rules can be split into two regimes:

- The portfolio FIF rules, which apply to interests of less than 10% in an FIF.
- The non-portfolio FIF rules, which apply to interests of 10% or more that are outside the CFC rules.

Portfolio FIF rules

The portfolio FIF rules apply to interests of less than 10% in foreign companies, foreign superannuation schemes, and foreign life insurance policies issued by non-resident life insurers (if the CFC rules do not apply). However, a New Zealand resident does not generally have FIF income when:

- the total cost of FIF interests held by the individual does not exceed NZD 50,000
- the income interest is in certain Australian Stock Exchange (ASX) listed companies or certain Australian unit trusts, or
- the CFC rules apply.

There are also exemptions for interests in certain foreign employment-related superannuation schemes. These include interests held by returning residents and new migrants acquired before the person became a New Zealand resident or within the first five years of New Zealand residence.

When an interest is exempt from the FIF rules, distributions are subject to tax on a receipts basis in accordance with normal principles.

The taxable income of a New Zealand resident with an interest in an FIF that does not qualify for one of the exemptions is calculated using one of the following methods:

- Fair dividend rate (FDR).
- Comparative value.
- Cost.
- Deemed rate of return.
- Attributable FIF income.

The nature of the interest held and the availability of information restrict the choice of method.

Taxpayers must disclose interests in certain FIFs in their annual tax returns. Failure to disclose can result in the imposition of penalties.

Non-portfolio FIF rules

The active business exemption (which applies for CFCs) also includes certain non-portfolio FIFs. If the FIF fails the active business test, passive income will be attributed to the New Zealand shareholders. There is also an exemption for shareholders with a 10% or greater interest in an FIF that is resident and subject to tax in Australia.

When investors do not have sufficient information to perform the calculations required under the active business test (or choose not to apply the active business test), they will be able to use one of the attribution methods for portfolio FIF investments (*see above*).

Tax credits and incentives

Foreign tax credits

If a New Zealand resident company derives overseas income that is subject to New Zealand income tax, the company is generally allowed a credit for the foreign income tax paid in respect of that income. Generally, the credit is limited to the lesser of the actual overseas tax paid on the overseas income or the New Zealand tax applicable to the overseas income.

Foreign tax credits can only be used if the taxpayer is in a tax paying position. If foreign tax credits are not claimed in the current year, they are forfeited.

Inbound investment incentives

There are limited, specific tax incentives designed to encourage the flow of investment funds into New Zealand.

Legislation encourages foreign venture capital investment into unlisted New Zealand companies. Gains derived by certain non-residents from the sale of shares (held on revenue account and owned for at least 12 months) in New Zealand unlisted companies that do not have certain prohibited activities as their main activity are exempt from income tax. The rules apply to foreign investors who are resident in all of the countries with which New Zealand has a DTA (except Switzerland) and who invest into New Zealand venture capital opportunities.

Capital investment incentives

Investment allowances on fixed assets are not available.

Trans-Tasman imputation

Elective rules allow trans-Tasman groups of companies to attach both imputation credits (representing New Zealand tax paid) and franking credits (representing Australian tax paid) to dividends paid to shareholders.

The regime allows eligible wholly owned groups of Australian and/or New Zealand companies to group for imputation purposes only. Groups with both Australian and New Zealand members are known as trans-Tasman imputation groups (TTIGs). New Zealand companies within a trans-Tasman group maintain a separate 'resident imputation subgroup' account.

Withholding taxes

Resident corporations paying certain types of income are required to withhold tax on gross income, as shown in the table below.

	WHT (%)		
Recipient	**Dividends**	**Interest**	**Royalties**
Resident corporations	33 (1)	28 (1)	0
Resident individuals	33	max 33	-
Non-resident corporations and individuals		(2)	
Non-treaty	0/15/30 (3)	15 (4)	15
Treaty:			
Australia	0/5/15 (5)	0/10 (5)	5
Austria	15	10	10
Belgium	15	10	10
Canada	5/15 (6)	10	5/10 (6)
Chile	15	10/15 (7)	5
China, People's Republic of	15	10	10
Czech Republic	15	10	10
Denmark	15	10	10
Fiji	15	10 (8)	15
Finland	15	10	10
France	15	10	10
Germany	15	10	10
Hong Kong	0/5/15 (9)	0/10 (9)	5
India	15	10	10
Indonesia	15	10	15
Ireland, Republic of	15	10	10
Italy	15	10	10
Japan	0/15 (10)	0/10 (10)	5
Korea, Republic of	15	10	10
Malaysia	15	15	15

Recipient	WHT (%) Dividends	Interest	Royalties
Mexico	0/5/15 (11)	10	10
Netherlands	15	10	10
Norway	15	10	10
Papua New Guinea	15	10	10
Philippines	15	10	15
Poland	15	10	10
Russian Federation	15	10	10
Samoa	5/15 (12)	10	10
Singapore	5/15 (13)	10	5
South Africa	15	10	10
Spain	15	10	10
Sweden	15	10	10
Switzerland	15	10	10
Taiwan	15	10	10
Thailand	15	10/15 (14)	10/15 (14)
Turkey	5/15 (15)	10/15 (15)	10
United Arab Emirates	15	10	10
United Kingdom	15	10	10
United States	0/5/15 (16)	0/10 (16)	5
Vietnam	5/15 (17)	10	10

Notes

1. Resident WHT applies to both interest and dividends. Unless the recipient corporation holds an exemption certificate, and if the recipient provides a tax file number, the default rate of the interest WHT is 28%. Recipients can elect for the rate of interest withholding to be 28% or 33%. The rate of interest WHT is 33% where the recipient does not provide a tax file number.

   The rate of WHT on dividends paid is 33%, but the tax is reduced by the aggregate imputation and withholding payment credits attached to the dividend or taxable bonus share. Interest and dividends paid between group companies and in certain other limited circumstances are exempt from the WHT.

   Where a fully imputed dividend is paid to a corporate shareholder, there is no requirement to withhold RWT or NRWT.

2. Resident corporations paying interest to non-associated, non-resident corporations and individuals need not withhold tax if they have approved-issuer status and the security under which interest is payable is registered with Inland Revenue. In this case, the resident corporation pays a 2% levy (tax deductible) on the interest payments instead of the WHT otherwise applicable.
3. NRWT is imposed on dividends at the following rates, regardless of the jurisdiction to which the dividends are paid:
   - 0% for fully imputed dividends paid to a shareholder holding 10% or more of the direct voting interests in the company and fully imputed non-cash dividends.
   - 15% for fully imputed cash dividends paid to a shareholder holding less than 10%.
   - 30% in most other cases, subject to any relief available under a DTA.
4. Net interest income is subject to reassessment at the company tax rate where the payer and the recipient are ‘associated persons’, but WHT is the minimum liability. NRWT is not imposed where the recipient of the interest has a fixed establishment in New Zealand.
5. The WHT on dividends is reduced from 15% to 5% for an investing company that has at least a 10% shareholding in the company paying the dividend. The rate reduces to 0% if the investing company holds 80% or more of the shares in the other company and meets other criteria. The WHT rate on interest is 10% but is reduced to 0% if it is payable to eligible financial institutions.
6. The WHT on dividends is reduced from 15% to 5% for an investor who holds at least 10% of the shares in the company that pays the dividend. The WHT rate on royalties is reduced from 15% to 10% generally, with a further reduced rate of 5% for royalties relating to copyright, computer software, and others.
7. The WHT on interest is reduced to 10% if the interest received is derived from loans granted by banks or insurance companies. In all other cases, 15%.

8. The WHT on interest may differ in accordance with the rates prescribed by New Zealand legislation for interest paid to 'associated persons'.
9. The WHT on dividends is reduced from 15% to 5% for an investing company that has at least a 10% shareholding in the company paying the dividend. The rate reduces to 0% if the investing company holds 50% or more of the shares in the other company and meets other criteria. The WHT rate on interest is 10% but is reduced to 0% if it is payable to eligible financial institutions.
10. The WHT rate on dividends is reduced from 15% to 0% for an investor who holds at least 10% of the voting power in the company paying the dividend (subject to certain conditions being met). The WHT rate on interest is 10% generally and 0% if it is payable to eligible financial institutions.
11. The 0% WHT rate applies where the foreign company owns at least 80% of the voting rights in the paying company (directly or indirectly) for 12 months prior to the date the dividend is paid and meets other criteria. The 5% rate applies if the foreign company has a direct interest of at least 10% of the voting rights in the paying company.
12. The WHT rate on dividends will reduce from 15% to a maximum of 5% for an investor who holds at least 10% of the shares in the company that pays the dividend.
13. The standard WHT rate on dividends reduces to 5% for an investing company that has at least a 10% shareholding in the company paying the dividend.
14. The WHT rate on interest is reduced to 10% if it is received by a financial institution or it is paid with respect to debt arising from a sale on credit of any equipment, merchandise, or services. The WHT rate is reduced to 10% for certain types of royalty.
15. The WHT rate on dividends is reduced to 5% if the beneficial owner is a company holding at least 25% of the capital of the company paying the dividends and 15% in all other cases. The WHT rate on interest is reduced to 10% if the interest is paid to a bank and 15% in all other cases.
16. The WHT rate on dividends is 5% for an investor who holds at least 10% of the shares in the company that pays the dividend; 0% if the investor holds 80% or more of the shares in the company and meets other criteria; 15% in all other cases. The WHT rate on interest is 10% but is reduced to 0% if it is payable to eligible financial institutions.
17. The WHT rate on dividends is reduced to 5% if the beneficial owner is a company holding at least 50% of the voting power in the company paying the dividends and 15% in all other cases.

Tax administration

Taxable period

Tax returns are based on the fiscal year ending 31 March, although other fiscal year-ends are possible if permission is obtained.

Tax returns

The system is one of self-assessment, under which the corporation files an income tax return each year. For those not linked to a tax agent, returns must be filed by 7 July for balance dates between 1 October and 31 March, or by the seventh day of the fourth month following a balance date between 1 April and 30 September. The filing date for taxpayers linked to a tax agent is extended to 31 March of the following year.

Payment of tax

Terminal tax payment is due on 7 February for balance dates between 31 March and 30 September. For other balance dates, terminal tax payments are generally due on the seventh day of the 11th month following the balance date. The terminal tax due date is extended by two months for taxpayers linked to a tax agent.

Provisional tax payments are generally due in three instalments: (i) 28th day of the seventh month before the balance date, (ii) 28th day of the third month before the balance date, (iii) 28th day of the month following the balance date.

Calculating provisional tax

For the 2018/19 income year (i.e. year ending 31 March 2019), provisional taxpayers have the following five options:

1. Where the 2017/18 return of income has been filed, 2018/19 provisional tax can be based on 105% of the 2017/18 residual income tax.

2. Where the 2017/18 return of income has not been filed, due to an extension of time for filing, 2018/19 provisional tax can be based on 110% of the 2016/17 residual income tax, but only for the first two instalments. The final instalment must be calculated based on the first option above.
3. Provisional tax can be based on a fair and reasonable estimate of the 2018/19 residual income tax.
4. The GST ratio option.
5. The Accounting Income Method (AIM).

The GST ratio option enables smaller taxpayers to align their provisional tax payments with their cash flow and reduce their exposure to use of money interest. The option is intended to benefit those taxpayers with declining, seasonal, or fluctuating income. This option calculates provisional tax by reference to the taxpayer's GST taxable supplies in the relevant provisional tax instalment period.

With effect from 1 April 2018, a new method for calculating provisional tax payable, the AIM, is available for businesses with gross annual income of less than NSD 5 million. AIM uses accounting information from the business' accounting software for a period as a basis for calculating the tax liability of the business for that period. The resulting amount is payable by the taxpayer as a provisional tax instalment.

Taxpayers can also make voluntary payments. Such payments can be made to minimise exposure to use of money interest. A taxpayer choosing to estimate residual income tax is required to take reasonable care when estimating.

When the taxpayer's return of income for the year is furnished, the provisional tax paid for that year is credited against the tax assessed. This results in either a refund or further tax to pay by way of terminal tax.

For the 2017 year and prior, where provisional tax paid was less than the amount of income tax deemed due on that instalment date, interest was imposed. If provisional tax was overpaid, interest was payable to the taxpayer. Interest was deductible for tax purposes by business taxpayers, and interest earned on overpaid provisional tax was gross income for tax purposes.

From the 2018 year and onwards, there will be no interest charged by or received from Inland Revenue if the first and second instalments are in line with the standard uplift method (described as options 1 and 2 above). A taxpayer will be exposed to full use-of money interest (UOMI) from the point they choose to estimate. 'Provisional tax associates' should use the same method (i.e. standard or estimation).

Use-of-money interest (UOMI)

From 8 May 2017, the interest rate for unpaid tax is 8.22%, while the rate for overpaid tax is 1.02%.

Tax pooling

Taxpayers are able to pool their provisional tax payments with those of other taxpayers through an arrangement with a commercial intermediary. Tax pooling allows underpayments to be offset by overpayments within the same pool and *vice versa*.

Tax penalties

An initial late payment penalty of 1% applies if a tax payment is not made on the due date. A further 4% late payment penalty applies if the payment is not made within seven days of the due date. For the 2017 year and prior, an incremental late payment penalty of 1% was imposed monthly until payment was made. The 1% monthly penalty is no longer being charged on amounts that remain unpaid for the 2018 year onwards.

Inland Revenue is required to notify a taxpayer the first time their payment is late rather than imposing an immediate late payment penalty. If payment is not made by a certain date, a late payment penalty will be imposed. Taxpayers will be entitled to one notification every two years. After receiving a first warning, Inland Revenue will not send further notifications for two years, and an initial late payment penalty will be imposed in the normal manner.

Shortfall penalties

Shortfall penalties, calculated as a percentage of the tax shortfall resulting from the action or position taken by the taxpayer in a tax return, may also apply.

There is a 50% discount on certain penalties where the taxpayer has a past record of 'good behaviour' and, in certain circumstances, a cap of NZD 50,000 on shortfall penalties for not taking reasonable care or for taking an unacceptable tax position.

Tax audit process

Inland Revenue maintains an active audit programme across all tax types and taxpayer profiles and regularly publishes information about their compliance focus. Often, Inland Revenue audits are preceded by a risk review where Inland Revenue requests information in order to evaluate the risk of non-compliance. Where this review detects an issue that requires further inspection, Inland Revenue will then advise that an audit will be commenced.

Statute of limitations

The general rule is that Inland Revenue has four years from the end of the New Zealand income tax year (31 March) in which the return is filed to re-assess the return, unless the return is fraudulent, wilfully misleading, or omits income of a particular nature or source.

Topics of focus for tax authorities

For multinational corporations, Inland Revenue highlights tax avoidance, transfer pricing, CFCs, and international financing arrangements as key risk areas, in tune with the OECD's current dialogue on the BEPS work. In particular, Inland Revenue is focussing on the following:

- Transfer pricing: Lack of transfer pricing documentation, major downwards 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.
- CFCs: Technical compliance, possible New Zealand tax residency of CFCs through local management control or director decision making.
- BEPS concerns: Taxation of digital goods and services provided over the internet, hybrid mismatches occurring 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.
- Non-residents: Transactions with non-residents and non-resident contractors.

For small-to-medium sized enterprises (SMEs), Inland Revenue is focussing on GST errors, employer deductions, NRCT, and other minor filing errors.

Other key focus areas include the following:

- Aggressive tax planning.
- Central and local government.
- Life insurance providers.
- Trusts.
- Fraud and identity theft.
- Charities.
- The property sector.
- Under-reporting income and operating outside the system.

Other issues

Financial reporting standards for SMEs

The Financial Reporting Act 2013, along with the Financial Reporting (Amendments to other Enactments) Act 2013, changed the financial reporting and audit requirements for some New Zealand entities. As of 1 April 2014, entities that do not fall under the definition of 'large' or have 'public accountability' do not have to prepare general purpose financial statements in accordance with NZ GAAP. Entities that no longer have to prepare general purpose financial statements under the Financial Reporting Act 2013 are still required to prepare special purpose financial statements for tax purposes. Inland Revenue has provided the minimum requirements for financial statements in an Order in Council. These include:

- a balance sheet, profit and loss, and supporting notes or schedules
- accounts based on double entry cost-based accrual accounting
- tax values utilised for the determination of income and expenditure and preparation of the balance sheet
- a statement of accounting policies and changes
- a reconciliation of the financial statements to taxable income, and
- a schedule of related-party transactions.

BEPS Multilateral Instrument (MLI)

New Zealand signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI) in June 2017. New Zealand has ratified the MLI. However, to complete the process, New Zealand needs to deposit the instrument of ratification with the OECD.

The MLI will enter into force on 1 July 2018, given five signatories have now completed the ratification process. The MLI will enter into force for relevant New Zealand treaties three months after New Zealand has deposited the instrument of ratification with the OECD, provided the other treaty partner has also completed its ratification process.

Pakistan

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Significant developments

- The generally applicable corporate tax rate of 30% (relevant for tax year 2018) will be reduced by 1% each year until a rate of 25% is applicable for tax year 2023 and onwards.
- The corporate tax rate for 'small companies', presently 25%, will also be reduced by 1% each year until a rate of 20% is applicable for tax year 2023 and onwards.
- Super tax, presently leviable at 3%, is to be gradually phased out in the case of persons (including companies, other than banking companies) by 1% each year, until tax year 2021.
- Tax on 'undistributed reserves' in case of public companies has been reduced from 7.5% to 5%. Previously, no tax was payable where a company distributed at least 40% of after tax profits. Such threshold is now being reduced to 20%. Moreover, issuance of bonus shares shall no longer be considered as distribution of profits for the purposes of these provisions.
- Tax at 5% earlier applicable on issue of bonus shares has been abolished.
- 'Fees for offshore digital services' received by non-resident persons have been made subject to final tax (like royalties and 'fees for technical services') at the rate of 5% of the gross amount.
- Income from turnkey contracts derived by non-resident persons and their affiliates, that form part of an overall arrangement for supply of goods, installation, construction, assembly, commission, guarantee, and supervisory activities, is to be considered as Pakistan-source income.
- Under the domestic law, scope of expression of 'permanent establishment' (PE) has been enhanced to include (i) fixed place of business used by non-resident persons/affiliates for execution of 'composite' contracts and (ii) those persons who are habitually engaged in execution of contracts on behalf of non-residents.
- The concept of controlled foreign company (CFC) has been introduced with the aim to bring into the tax net passive incomes earned by foreign companies, owned by residents, that are not repatriated into Pakistan.
- Gain derived outside Pakistan on disposal of a Pakistani asset, held by a non-resident company, has been included in the ambit of Pakistan-source income.
- Income from services rendered by PEs of non-resident persons have now also been made subject to 'minimum tax' (and thus brought on par with resident corporate service providers).
- Tax authorities have been empowered to disregard an entity/corporate structure having no economic substance or executed as part of a 'tax avoidance scheme'.
- Adjustment of unabsorbed depreciation/amortisation against taxable profits of subsequent years has been restricted to 50% of taxable profits in case of profits of

10 million Pakistani rupees (PKR) or more. The remaining amounts shall, however, remain eligible for carryforward/adjustment in future years.

- Gain on disposal of listed and other securities held for more than five years but less than six years were earlier taxable at 0%; however, now these have been made taxable at 15% (20% for non-filers).
- The rate of tax chargeable/deductible on dividends received by a company from collective investment schemes, real estate investment trust (REIT) schemes, or mutual funds (other than stock funds) has been reduced from 25% to 15%.
- 'Commercial importers', earlier subject to tax on a presumptive basis, have now been made subject to tax under the normal tax regime, with tax at 5% of the import value considered to be a minimum tax on related transaction.
- The exemption on income from export of computer software, information technology (IT) services, or IT-enabled services, has been extended to tax year 2025.
- The tax credit on investment in plant and machinery and newly established undertakings is extended for a period up to 30 June 2021.
- A one-time amnesty scheme has been announced for declaration of undisclosed domestic incomes/assets by 30 June 2018 for companies on the basis of payment of tax at 2% to 5% (depending on the category of such assets).

Taxes on corporate income

A resident company is taxed on its worldwide income. Non-resident companies operating in Pakistan through a branch are taxed on their Pakistan-source income attributable to the branch at rates applicable to a company.

The federal corporate tax rates on taxable income (for tax year 2018) are as follows:

Company type	Tax rate (%)
Banking company	35
Public company other than a banking company	30
Any other company	30
Small company (*see the Tax credits and incentives section for more information*)	25

The tax rates for 'companies' as well as 'small companies' will be reduced gradually from tax year 2019 in the following manner:

Tax year	Company (%)	Small company (%)
2019	29	24
2020	28	23
2021	27	22
2022	26	21
2023 and onwards	25	20

The term 'public company' implies a company listed on any stock exchange in Pakistan or one in which not less than 50% of the shares are held by the federal government or a public trust.

In the case of a *modaraba* (*see the Income determination section for a definition*), income, except relating to trading and manufacturing activities, is exempt from tax, provided that 90% of its profit is distributed to the certificate holders as cash dividends.

The final tax regime (FTR) for resident taxpayers, a presumptive tax scheme where taxes are withheld at the source on the sale of goods and execution of contracts, is considered the final tax liability in respect of income arising from the sale or contract.

In the case of exports, tax collected at the time of realisation of foreign-exchange proceeds is treated as the final tax for that income. The exporters can also opt out of such regime, subject to the condition that tax deducted on exports is offered as minimum tax.

The FTR is also applicable to non-resident taxpayers, at their option. However, it is only applicable in cases of receipts on account of the execution of a contract for construction, assembly, or installation, including a contract for the supply of management activities in relation to such project as well as certain contracts for services and contracts for advertisement services rendered by television satellite channels.

Commercial importers (persons engaged in the import of goods where the goods are sold in the same condition as they were when imported) were subject to tax on presumptive tax basis, though an option was provided for under the law to opt out of FTR. This regime has now been abolished, and commercial imports have been made taxable under the normal tax regime, with tax at 5% of import value (as increased by applicable duties/taxes) considered as a 'minimum tax' on such transaction.

Taxation of a PE

The following principles shall apply in computing taxable income of a PE:

- It is a distinct and separate entity dealing independently with the non-resident of which it is a PE.
- In addition to business expenditure, executive and administrative expenditure, whether incurred in Pakistan or elsewhere, will be allowed as deductions.
- Head office expenditure, including rent, salaries, travelling, and any other expenditure that may be prescribed, shall be allowed as a deduction in proportion to the turnover of the PE in the same proportion as the non-resident's total head office expenditure bears to its worldwide turnover.
- Royalties, compensation for services (including management services), and interest on loans (except in banking business) payable or receivable to or from a PE's head office shall be considered in computing taxable income of the PE.
- No deduction will be allowed for any interest paid on loans acquired by a non-resident to finance the operations of a PE (or for the insurance premium in respect of such loans).
- Income from rendition of services derived by a PE of a non-resident person has been made subject to 'minimum tax' at 8% (of the gross consideration).

Taxation of certain contracts executed by non-resident persons

Income derived by non-resident persons/their affiliates from turnkey contracts that are part of an overall arrangement for supply of goods, installation, construction, assembly, commission, guarantee, and supervisory activities, including offshore supply of goods, now constitutes Pakistan-source income.

Necessary amendments to this effect have also been made in the definition of a PE by way of introduction of the concept of 'cohesive business operations', which includes:

- an overall arrangement for the supply of goods, installation, construction, assembly, commission, guarantees, or supervisory activities, and all or principal activities are undertaken or performed either by the person or the associates of the person, and
- supply of goods include the goods imported in the name of the associate or any other person, whether or not the title to the goods passes outside Pakistan.

The objective of these amendments seems an attempt to tax income of a non-resident arising from transactions wholly undertaken outside Pakistan (such as income relating to supply of goods where the title is passed outside Pakistan) in case the same is part of a 'cohesive business operation'. It is, however, clear that the double tax treaty (DTT) provisions would override these provisions and thus the same would only apply in non-treaty cases.

Minimum tax on turnover

Where the tax payable by a company is less than 1.25% of the turnover, the company is required to pay a minimum tax equivalent to 1.25% of the turnover. Tax paid in excess of normal tax liability can be carried forward for adjustment against tax liability of a subsequent tax year. However, such tax can only be adjusted against tax liability of the five tax years immediately succeeding the tax year for which the amount was paid.

The minimum tax rate for companies providing services is 8% of the turnover, except for certain specified services sectors, which are allowed concessions, subject to fulfilment of certain conditions.

Alternate Corporate Tax (ACT)

Under the ACT, the minimum tax liability of a company is the higher of 17% of accounting income or the corporate tax liability determined under the Ordinance, including minimum tax on turnover. This concept is applicable for all companies except insurance companies, companies engaged in exploration and production of petroleum, banking companies, and companies enjoying a reduced rate of tax.

Exempt incomes, income taxable under the FTR, capital gain on disposal of specified listed securities, income entitled to 100% tax credit on account of equity investment, and income of non-profit organisations, trusts, and welfare institutions are not subject to levy of ACT.

Super tax

The levy of 'super tax' has been extended up to tax year 2021 in the case of banking companies and up to tax year 2020 in the case of other persons. The revised rates of super tax are as follows:

Tax year	Banking company (%)	Persons other than banking company (%)
2018	0	3
2019	4	2
2020	3	1
2021	2	0

Local taxes on income

No provincial or local taxes are payable in respect of income of companies.

Corporate residence

A company is resident in Pakistan if it is incorporated or formed by or under the law of Pakistan or if the control and management of its affairs is situated wholly in Pakistan in that year.

The term 'company' includes a trust, a cooperative society, a finance society, or any other society established or constituted by or under any law; a corporate body incorporated outside Pakistan; and any foreign association, incorporated or unincorporated, that the Central Revenue authorities may declare to be a company.

Permanent establishment (PE)

A PE is a place of business through which the business of a non-resident is wholly or partly carried out, including:

- A place of management, branch, office, factory or workshop, premises for soliciting orders, warehouse, permanent sales exhibition, or sales outlet, except a liaison office.
- An agriculture, pastoral, or forestry property.
- A mine, oil or gas well, quarry, or any other place of extraction of natural resources.
- A building site; a construction, assembly, or installation project; or supervisory activities connected with such site or project if such activity continued for more than 90 days within any 12-month period.
- The furnishing of services, including consultancy services, by any person through employees or other personnel engaged by the person for that purpose.
- A person acting in Pakistan on behalf of the person, other than an agent of independent status (excluding a person acting exclusively/almost exclusively on behalf of such person) in the ordinary course of business.
- Any substantial equipment installed, or other asset or property capable of activity giving rise to income.
- A person who habitually exercises authority to conclude contracts on behalf of another person or plays a principal role in execution of contacts that are concluded without any material variations and these contracts are:
  - in the name of the person
  - for the transfer of the ownership of or for the granting of the right to use property owned by that enterprise or that the enterprise has the right to use, or
  - for the provision of services by that person.
- A fixed place of business that is used or maintained by a person if the person or an associate of a person carries on business at that place or at another place in Pakistan and:
  - that place or other place constitutes a PE of the person or an associate of the person under this sub-clause, or
  - business carried on by the person or an associate of the person at the same place or at more than one place constitutes complementary functions that are part of a cohesive business operation.

The definition of a PE provided in a DTT will prevail in cases where a DTT is executed by Pakistan with the related country of origin of the PE.

Other taxes

Value-added tax (VAT)

VAT (locally termed as 'sales tax') is ordinarily levied at 17% on the value of goods, unless specifically exempt, after allowing related input credits. Export of goods is subject to sales tax at 0%.

Sales tax on services is levied by all four provinces, Islamabad Capital Territory, Gilgit-Baltistan, Azad Jammu, and Kashmir at rates ranging from 13% to 16%. Sales tax paid on services, federal sales tax on goods, and federal excise duty are adjustable against each other, with a few exceptions.

Significant zero-rated goods are as follows:

- Supplies and repair and maintenance of certain ships and aircraft.
- Supplies to diplomatic missions and diplomats.
- Supplies of raw materials, components, and goods for export processing zones.
- Supplies of locally manufactured plant and machinery to export processing zones and supplies of certain specified machinery to the exploration and production sector.
- Supplies to exporters.

Significant exemptions are as follows:

- Live animals and live poultry.
- Live plants.
- Vegetables, pulses, edible fruits (excluding imported fruits), certain spices, sugar cane, edible oils, etc.
- Milk preparations.
- Newsprints, newspapers, journals, periodicals, and books.
- Agricultural produce not subjected to any process.

Customs and import duties

Customs and certain other duties are collected at the import stage at varying rates classified under the Harmonized System (HS) Code.

Excise duty

Federal excise duty (FED) is leviable on certain types of manufacturing, import of goods, and rendering of services at varying rates. Sales tax on services, which is a replacement of FED, under the constitution, is to be levied and collected by the provinces on services rendered within their jurisdictions.

Property taxes

Property owners are required to pay property tax levied and collected by provincial governments through municipal governments at varying rates.

Stamp duty

In the case of sale or transfer of immovable property, stamp duty is payable (with varying rates on the basis of location of the property) on the value of the property.

Payroll taxes

Other than social security contributions (*see below*), employers are not responsible to pay any other tax in respect of their employees or their salaries.

Social security contributions

Nominal social security and Employees Old Age Benefit contribution is collected from the employers and the employees. Employers are responsible to collect and pay on a monthly basis.

Branch income

The rates of tax for a branch of a company incorporated outside Pakistan are the same as those applicable on resident companies, other than public and banking companies. Tax at the rate of 15% is levied on the transfer of after tax profits by a branch to the head office, with an exception for companies engaged in the oil and gas exploration and production business.

Payments to a branch in Pakistan of a non-resident are subject to deduction of tax at source on the same basis as a resident in the case of sale of goods, rendering of professional services, and execution of contracts. In other circumstances, a reduced/0% withholding tax (WHT) certificate can be obtained from the Commissioner of Income Tax.

Pakistan has presently executed agreements for avoidance of double taxation with 65 countries.

Income determination

Inventory valuation

Inventories are to be stated at the lower of cost or market. The first in first out (FIFO) and average methods are accepted. Conformity of methods used for book and tax reporting is desirable, and the method used should be consistently applied.

Capital gains

Capital gain on the sale of immovable property acquired on or after 1 July 2016, on which depreciation is not allowed, is taxed at the rate of 10% if disposed of within one year, 7.5% if disposed of within two years, and 5% if disposed of within three years. However, if the retention period is more than three years, such gain is not taxable. Capital gain on the sale of immovable property acquired before 1 July 2016 is taxed at 5% if disposed of within three years. No tax is payable if the retention period is more than three years.

Gain on the disposal of shares of a resident company or a non-resident company, whose assets wholly or principally consist of immovable property situated in Pakistan or rights to explore/exploit natural resources in Pakistan, shall be Pakistan-source income.

Tax rates on capital gains on the sale of shares of public companies, *modaraba*, and other specified ‘securities’ are exempt from tax if the date of acquisition of shares is before 1 July 2013. Capital gains on such instruments for tax years 2018 and 2019 are taxed as follows:

Holding period	Tax rates - Filers (%) Securities acquired before 1 July 2016	Tax rates - Filers (%) Securities acquired after 1 July 2016	Tax rates - Non-filers (%) Securities acquired before 1 July 2016	Tax rates - Non-filers (%) Securities acquired after 1 July 2016
Less than 12 months	15	15	18	20
12 months or more, but less than 24 months	12.5	15	16	20
24 months or more	7.5	15	11	20

Capital gain on future commodity contracts entered into by members of the Pakistan Mercantile Exchange is 5% for both filers and non-filers.

Capital gain, other than on statutory depreciable assets, realised within one year of acquisition is fully taxed; after one year, 75% of such gains are taxed and 25% are exempt.

Capital gains on statutory depreciable assets (other than immovable property) are chargeable to tax as normal business income in the year of sale. They are measured as the difference between the sale proceeds and the tax written-down value of the relevant asset sold.

In the case of an asset disposal transaction that is on a non-arm's-length basis, fair market value of the asset shall be taken to be the consideration received by the seller, as well as the cost for the buyer.

Where assets are transferred outside Pakistan, the original cost is treated as the sale price, which means that the entire depreciation is recaptured at the time of export, except if the assets are used in oil or gas exploration, in which case only the initial depreciation is recaptured.

No gain or loss shall be taken to arise on disposal of an asset by a resident company to another resident company, provided certain conditions are met. The required conditions include, *inter alia*, that the transferor is 100% owned by the transferee or *vice versa* or both companies are 100% owned by a third company, and the transferee income is not exempt in the year of transfer. The scheme of arrangement is approved by the Securities and Exchange Commission of Pakistan or State Bank of Pakistan.

Any distribution to the shareholders of a company, to the extent that it relates to undistributed profits, is treated as a dividend.

Capital loss can be offset only against capital gains. Unabsorbed capital loss (except that arising on disposal of listed securities) can be carried forward for adjustment against capital gains for six years.

Capital gain derived on disposal of assets by non-residents outside Pakistan

Gain on disposal/alienation of any asset derived outside Pakistan by a non-resident person in respect of any asset located in Pakistan now constitutes Pakistan-source income.

With respect to shares of a company, however, the asset shall be treated to be located in Pakistan if:

- the share or interest derives, directly or indirectly, its value principally or wholly from the assets located in Pakistan
- the share or interest representing 10% or more of the share capital of the non-resident company is disposed or alienated, and
- the share or interest, as mentioned above, derives its value principally from an asset located in Pakistan if on the last day of the preceding tax year the value of such asset exceeds PKR 100 million and represents at least 50% of value of total assets.

Where the entire assets of the non-resident company are outside Pakistan, a share or interest in such company will be treated as located in Pakistan to the extent of reasonable attribution.

The above gain is subject to income tax (with no further incidence of tax under any other provisions of law) at the higher of:

- 20% of the amount representing the difference between fair market value and cost of acquisition of the asset, or
- 10% of the fair market value of the asset.

Dividend income

Dividend income is subject to tax/WHT of 15% or a lower tax treaty rate. A rate of 20% is applicable for persons receiving dividend income but not filing income tax returns (non-filers).

The deduction at source shall be the full and final discharge of tax liability on dividend income. However, in case of non-filers filing a return of dividend income, they will be entitled to a refund of 5% of the 20% tax withheld on dividend income (over and above the applicable tax charging rate of 15% on such dividends).

Interest income

Interest earned by a company is taxed as its income from other sources. Interest earned by a non-resident company without a PE in Pakistan attracts WHT at the rate of 10%, except where a lower rate is provided in the related DTT, which is also the final tax on such income.

Income from royalties and fees for technical services/offshore digital services

Royalties received by non-residents are deemed to accrue or arise in Pakistan and are taxable if paid by a resident in Pakistan or borne by a PE of a non-resident in Pakistan.

Income from 'fees for technical services' and 'fees for offshore digital services' are deemed to accrue or arise in Pakistan if paid by a resident in Pakistan or borne by a PE of a non-resident in Pakistan.

'Fees for technical services' means any consideration for the rendering of any managerial, technical, or consultancy services (including the provision of the services of technical or other personnel), but does not include consideration for any construction, assembly, or like project undertaken by the recipient or consideration that would be income of the recipient chargeable under the head salary.

'Fee for offshore digital services' means consideration for rendering or providing services of online advertising and online collection of data processing or any facility for online sale of services.

Other significant items

Liabilities allowed as a tax deduction in a tax year and remaining unpaid for three subsequent years are deemed to be income in the first tax year following the said three years. Such items are then allowed as a deduction in the year the liability is discharged.

Agricultural income is exempt from income tax.

Foreign income

A resident company is taxed on its worldwide income and on its foreign income as earned. Double taxation of foreign income is avoided by means of foreign tax credits; this relief is allowed to the resident company on the doubly taxed income at the lower of the Pakistan or foreign tax rate.

Foreign loss can only be offset against foreign income and can be carried forward for six years.

Modaraba

Modaraba (profit sharing) is a financing vehicle that enables a management company to control and manage the business of a *modaraba* company with a minimum of 10% equity participation. The management company is entitled to remuneration based on an agreed percentage (but not exceeding 10%) of annual profits of the *modaraba* business. A *modaraba* can be for a specific purpose or many purposes and for a limited or unlimited period. The income of a *modaraba* not relating to trading or manufacturing activity is exempt from tax if 90% of its profits are distributed as cash dividend.

Deductions

Depreciation

Normal depreciation is allowed at the following prescribed rates by applying the reducing-balance method.

Assets	Depreciation rate (%)
Buildings	10
Furniture	15
Machinery and equipment, including motor vehicles and ships	15
Computer hardware, including monitors and printers	30
Aircraft and aero engines	30
Below-ground installations in mineral oil concerns	100
Offshore platform	20

All depreciable assets put into service for the first time in Pakistan during a tax year, other than road transport vehicles not plying for hire, furniture (including fixtures), plant and machinery used previously in Pakistan, or plant and machinery for which a deduction has been allowed under another section of this ordinance, for the entire cost of the asset, shall be entitled to an initial allowance at 25% of the cost of the asset.

Initial depreciation rate for buildings is 15%. First year depreciation allowance is available for specified assets.

Book depreciation need not conform to tax depreciation. Unabsorbed tax depreciation not set off against the income of the year is carried forward and added to depreciation of the assets of the same business in the following year. Tax depreciation can be carried forward for adjustment against income of future years for an unlimited period. However, such deprecation is only allowed to be set off to the extent of 50% of taxable profits of a particular (succeeding) tax year in cases where the same is PKR 10 million or more. The remaining amount can, however, still be carried forward/adjusted in future tax years.

Amortisation of intangibles

The cost incurred on acquisition of a patent, invention, design or model, secret formula or process, copyright, software, quota, licence, intellectual property (IP), or other like property or right, and any expenditure that provides an advantage or benefit for a period of more than one year, is allowed as a deduction on a straight-line basis over the useful life of the asset, but not exceeding a period of ten years.

Any payment made against acquisition of goodwill will also be amortised under these provisions.

Unabsorbed tax amortisation not set off against the income of the year is carried forward and added to amortisation of the assets of the same business in the following year. Tax amortisation can be carried forward for adjustment against income of future years for an unlimited period. However, such amortisation is only allowed to be set off to the extent of 50% of taxable profits of a particular (succeeding) tax year, in cases where the same is PKR 10 million or more. The remaining amount can be carried forward/adjusted in future tax years.

Organisational and start-up expenses

Expenditure incurred before the commencement of a business wholly and exclusively to derive income chargeable to tax can be deducted over a period of five years.

Interest expense

Interest expense is allowed as an expense if required WHT is deducted and deposited in the government treasury.

Bad debt

Bad debts are allowed as deductible expenditure if the following conditions are satisfied:

- Debts are included previously in the income chargeable to tax.
- Debts are written off in the financial statements.
- There are reasonable grounds for believing that the debt is irrecoverable.

Charitable contributions

See Charitable donations credit in the Tax credits and incentives section.

Fines and penalties

Fines or penalties that are not paid or payable for the violation of any law, rule, or regulation are allowable as tax deductible expenses.

Taxes

Taxes on income are not deductible. Sales tax and excise tax are tax deductible where these are to be absorbed by the business; otherwise, these are passed on to the consumer.

Other significant items

Expenditure on scientific research incurred in Pakistan wholly and exclusively for the purpose of deriving income chargeable to tax is an allowable expenditure.

Exchange gains and loss on foreign currency loans specifically obtained for acquiring an asset are adjusted against the depreciable cost of the asset.

Any lease rental incurred by a person in the tax year to a scheduled bank, financial institution, approved *modaraba*, or approved leasing company shall be a deductible expense. However, financial charges paid for the above-mentioned leases are added back into the taxable income of the company.

Net operating losses

Operating losses may be carried forward and set off against the profits of the succeeding six years of the same business in which the losses were incurred. Unabsorbed depreciation can be carried forward indefinitely.

Carried forward losses of an entity in the case of group relief cannot be utilised if the ownership of the holding company is reduced to less than 55% and 75% if one of the companies is a listed company or none of the companies is a listed company, respectively.

Business losses can be carried forward up to a period of six years in the case of the amalgamation of two companies, with the condition that the same business is continued for a minimum period of five years.

The carrying back of losses is not permitted.

Payments to foreign affiliates

The deductibility of a head office expenditure of a non-resident taxpayer is limited to the same proportion of total head office expenditure as the Pakistan turnover has with the total world turnover. However, such domestic rules are overridden if the branch is a tax resident of a country having an agreement for avoidance of double taxation (treaty) and that treaty provides a different basis.

Group taxation

A locally incorporated holding company and subsidiary of a 100% owned group may be taxed as one group by giving an irrevocable option for taxation as one fiscal unit. The relief is not available for losses prior to formation of the group. The group is available if the companies are designated as entitled to avail group relief by the Securities and Exchange Commission of Pakistan. Inter-corporate dividends are, however, exempt from levy of tax in case of entities availing group taxation and filing consolidated group returns.

Any company that is the subsidiary of a holding company may surrender its assessed loss for the year to its holding company or its subsidiary (in the proportion of the shareholding held by the holding company in the subsidiary), or between another subsidiary of the holding company, provided that the holding company directly holds 55% or more capital of the subsidiary if one of the companies is a listed company. However, if none of the companies is a listed company, the holding requirement is 75% or more. The loss can be surrendered for a maximum of three years, and the required holding is for at least five years.

Transfer pricing

The tax authorities have the power in respect of a transaction between associates to distribute, apportion, or allocate income, deductions, or tax credits between such associates to reflect the income that would have been realised in an arm's-length transaction. Companies are required to maintain specified records and documents for transactions between associates, and tax authorities can require information and documents for such transactions.

Transfer pricing documentation and country-by-country (CbC) reporting

Transfer pricing documentation requirements have also recently been introduced in law in order to comply with the requirements of various international Conventions/ Agreements executed by the government (*see Base Erosion and Profit Shifting [BEPS] in the Other issues section*), *inter alia*, including the following:

- Every taxpayer, being a constituent entity of a multinational entity (MNE) group having turnover of more than PKR 100 million, is required to keep, maintain, and make available a 'Master File', containing certain prescribed information.
- Every taxpayer entity in Pakistan that has undertaken transactions exceeding the monetary limit of PKR 50 million with related parties is required to keep, maintain, and make available a 'Local File', containing the prescribed information/details.

Every ultimate parent entity or surrogate parent entity in Pakistan that is part of an MNE group resident in Pakistan and whose consolidated group revenue is 750 million euros (EUR) or more during a fiscal year is required to file a CbC report for each country wherein the constituent entities of the MNE group operates.

A constituent entity (including a PE of a company) of an MNE group (not being the ultimate parent or surrogate parent) is also required to furnish a CbC report in case:

- The ultimate parent is not obligated to file such report in its country of residence (other than in cases where its consolidated group revenue is EUR 750 million or below).
- The ultimate parent is required to file a CbC report in its country of residence, but such country does not have any Competent Authority Agreement in place with Pakistan.
- There has been a systemic failure due to which such information cannot be exchanged.

The CbC report should contain the following information for each country wherein the constituent entities of the MNE group operates:

- Revenues from related and unrelated parties.
- Profit/loss before income tax.
- Income tax paid.
- Income tax accrued.
- Stated capital.
- Accumulated earnings.
- Number of employees.
- Tangible assets other than cash.
- Main business activities.

Thin capitalisation

Where a foreign-controlled resident company (other than a financial institution or a banking company) or a branch of a foreign company operating in Pakistan has a foreign-debt-to-foreign-equity ratio in excess of 3:1 at any time during a year, a deduction shall be disallowed for the profit on debt (interest) paid by the company in that year on that part of the debt that exceeds the 3:1 ratio.

Controlled foreign companies (CFCs)

The concept of taxation of incomes of CFCs has been introduced whereby attributable incomes of CFC that are retained and not repatriated to Pakistan have been brought into tax ambit and subjected to tax on the basis of the tax rate applicable to dividends (i.e. 15%).

A company shall be classifiable as a CFC if:

- more than 50% of its capital or voting rights are directly or indirectly held by Pakistani resident persons or if more than 40% of such capital or voting rights is held by a single Pakistani resident person
- tax paid in respect of income derived or accrued in a foreign tax year is less than 60% of tax payable on the said income under this Ordinance
- the non-resident company does not derive active business income (as defined in the provisions), and
- the shares of the company are not traded on any recognised stock exchange in the relevant jurisdiction.

There will be no tax incidence under these provisions in case the voting rights or capital held by the resident person is less than 10% or income of the CFC is less than PKR 10 million. Moreover, no further tax is payable at the time of actual distribution.

Tax credits and incentives

Tax credits are available to corporate taxpayers for employment generation, enlistment on a stock exchange, and making of investments in newly established undertakings, as well as those for extensions, expansion, balancing, modernisation, and replacements carried out in existing undertakings.

Tax exemptions

Profits and gains derived from an electric power generation project set up in Pakistan are exempt from tax.

Profits and gains derived by a company from the export of computer software, IT services, or IT-enabled services are exempt from tax up until 30 June 2025.

Profits and gains derived by refineries, which are setup between 1 July 2018 and 30 June 2023, have been granted exemption from tax for a period of 20 years, upon fulfilment of certain conditions.

Low-cost housing projects have been incentivised by allowing a reduction in tax liability (arising on profits and gains) by 50%, subject to fulfilment of certain conditions.

Profits and gains from new manufacturing units set up in Khyber Pakhtunkhwa and Baluchistan are exempt from tax for five years if set up between 1 July 2015 and 30 June 2018.

Profits and gains from electricity transmission projects are exempt from tax for ten years if set up between 1 July 2015 and 30 June 2018.

Income derived by an enterprise set up in 'special economic zones' is exempt from tax for a period of ten years, starting from commencement of commercial operations/ production, subject to certain conditions. These 'special economic zones' have been established in different territories of the country.

Profits and gains derived by liquefied natural gas terminal operators and terminal owners are exempt from tax for a period of five years beginning from the date of commercial production.

Small companies

Activities of small companies are encouraged with a reduced income tax rate of 25% (*see the Taxes on corporate income section*).

A small company has been defined to mean a company that:

- is registered on or after 1 July 2005 under the Companies Ordinance, 1984
- has a paid-up capital plus undistributed reserves not exceeding PKR 50 million
- has employees not exceeding 250 at any time during the year
- has an annual turnover not exceeding PKR 250 million, and
- is not formed by splitting up or the reconstitution of business already in existence.

Charitable donations credit

Companies are allowed a tax credit equivalent to 20% of their taxable income in respect of donations to:

- any board of education or university in Pakistan, established by or under federal or provincial law
- any educational institution, hospital, or relief fund established or run in Pakistan by federal government, provincial government, or local government, and
- any non-profit organisation.

Companies are also allowed a straight deduction against taxable income (up to 20% of taxable income) in case of donations made to certain approved institutions.

Foreign tax credit

Where a resident taxpayer derives foreign-source income on which foreign income tax is paid within two years from the year in which it is derived, the taxpayer is allowed a tax credit equal to the lower of (i) the foreign income tax paid or (ii) the Pakistan tax payable in respect of that income. However, foreign tax paid is not refundable.

Withholding taxes

WHT on payments of royalty and FTS, when royalty or FTS is not attributable to a PE in Pakistan, is 15% or a lower treaty rate of royalty or gross fees. The tax withheld is deemed to be the final tax liability of the non-resident. In the case of a non-resident where royalty or FTS is attributable to a PE in Pakistan, the amount of royalty/FTS shall be chargeable to tax as normal income, and withholding on payments can be avoided, subject to approval of the commissioner. If a reduced rate is available in a tax treaty, such rate would be applicable.

Resident corporations making certain types of payments must withhold tax as follows:

	WHT (%)		
Recipient (1, 2, 3)	**Dividends**	**Interest**	**Royalties**
Resident individuals	15	10	N/A
Resident corporations	15	10	0
Non-resident individuals:			
Non-treaty	15 (9)	10	15
Treaty	15 (9)	(4)	(4)
Non-resident corporations:			
Non-treaty	12.5	10	15
Treaty:	(5)	(6)	
Austria	10/15 (10)	15	10
Azerbaijan	10	10	10
Bahrain	10	10	10
Bangladesh	15	15	15
Belarus	10/15 (10)	10	15
Belgium	10 (11)/15	15	15/20 (12)
Bosnia and Herzegovina	10	20	15
Brunei Darussalam	10	15	15
Canada	15 (11)/20 (10)	25	15/20 (12)
China	10	10	12.5
Czech Republic	5/15 (10)	10	10
Denmark	10/15 (10)	15	12
Egypt	15/30 (20)	15	15
Finland	12/15/20 (10)	10 (13)/15	10
France	10/15 (10)	10	10
Germany	10/15 (10)	10 (13)/20	10
Hong Kong	10	10	10
Hungary	10/15/20 (10)	15	15
Indonesia	10/15 (10)	15	15
Iran	5	10	10

	WHT (%)		
Recipient (1, 2, 3)	**Dividends**	**Interest**	**Royalties**
Ireland, Republic of	5 (10)/10	10	10
Italy	15/25 (10, 11)	30	30
Japan	5/7.5/10 (10)	10	10
Jordan	10	10	10
Kazakhstan	12.5/15 (10)	12.5	15
Korea, Republic of	10 (11)/12.5 (10)	12.5	10
Kuwait	10	0 (21)/10	10
Kyrgyzstan Republic	10	10	10
Lebanon	10	10	7.5
Libya	(7)	(7)	(7)
Malaysia	15 (11)/20 (11)/10	15	15
Malta	15 (10)	10	10
Mauritius	10	10	12.5
Morocco	10	10	10
Nepal	10 (10)	10 (19)/15	15
Netherlands	10/20 (10)	10 (13)/15/20 (10)	5/15 (16)
Nigeria	10/12.5/15 (10)	15	15
Norway	15	10	12
Oman	10/12.5 (10)	10	12.5
Philippines	15/25 (10)	15	15 (14)/25
Poland	15 (10, 11)	(7)	15/20 (12)
Portugal	10/15 (10)	10	10
Qatar	5/10 (10)	10	10
Romania	10	10	12.5
Saudi Arabia	5 (15)/10	10	10
Serbia	10	10	10
Singapore	10 (11)/12.5/15	12.5	10
South Africa	10/15 (10)	10	10
Spain	5/7.5/10 (10)	10	7.5
Sri Lanka	15 (10)	10	20
Sweden	10/15 (10)	15	10
Switzerland	10/20 (10)	10	10
Syria	10	10	10/15/18 (17)
Tajikistan	5/10 (10)	10	10
Thailand	15 (11)/25 (10)	10 (13)/25	10/20 (18)
Tunisia	10	13	10
Turkey	10 (11)/15 (10)	10	10
Turkmenistan	10	10	10
Ukraine	10/15 (10)	10	10
United Arab Emirates	10/15 (10)	10	12
United Kingdom	10 (11)/15/20 (10)	15	12.5
United States	8.75	(7)	(8)
Uzbekistan	10	10	15
Vietnam	15	15	15
Yemen	10	10	10

Notes

1. This table is a summary only and does not reproduce all the provisions that may be relevant in determining the application of WHT in each tax treaty.

2. Resident and non-resident imply tax status.
3. Individuals and companies are required to render annual returns of income and pay tax at the applicable rates. Credit is given for WHT deducted.
4. WHT rates for interest and royalties given to non-resident corporations (treaty countries) also apply to non-resident individuals.
5. The following remarks for dividends should be noted:
   - The inter-corporate rate of tax on dividends received by a foreign corporation is 15%; corresponding treaty WHT rates in excess of 15% have been specified.
   - The rates given in the table for treaty countries relate to recipient corporations. The maximum rate, as stated above, in respect of inter-corporate dividends is 15%.
6. Certain treaties provide for tax exemption of interest paid to the government or the central bank of the contracting state and on foreign loans specifically approved by the federal government.
7. No concession is provided under the treaty.
8. Royalties are exempt from tax, provided the recipient does not have a PE in Pakistan.
9. Inter-corporate dividend where companies are entitled to group relief is exempt.
10. WHT rate depends on percentage of holding in the company.
11. This rate applies if the paying company is engaged in the industrial undertaking.
12. Consideration for technical know-how or information concerning industrial, commercial, or scientific experience.
13. This rate applies if the beneficial owner is a bank.
14. This rate applies if the paying company operates in preferred areas.
15. This rate applies if the company is owned by the government.
16. 5% is applicable for royalties payable for copyright of a literary, artistic, or scientific work, but excluding cinematograph films and tapes for television or broadcasting. All other royalties are taxable at 15%.
17. 18% is applicable for royalties payable for patent, trademark, design or model, plan, secret formula, or process of any industrial or scientific equipment, or for information concerning industrial and scientific experience; 15% for copyright of literary, artistic, or scientific work; and 10% for copyright of cinematograph films or tapes for television or radio broadcasting.
18. 10% is applicable for royalties payable for copyright of literary, artistic, and scientific work. All other royalties are taxable at 20%.
19. The rate applies if the beneficial owner is a financial institution, an insurance company, or investment company.
20. 15% applies if the beneficial owner of dividends is a company.
21. 0% applicable in case interest is being earned by the government, a company 51% or more shares of which are held by the government, or the loan is guaranteed by the government or any of its institutions.

Tax administration

Taxable period

The tax year is 1 July through 30 June. However, tax authorities are empowered to approve a special year-end.

Tax returns

All companies are required to file an income tax return each year by 31 December for the preceding financial year (1 July through 30 June) by accounting for business income on an accrual basis. If the special year granted by the tax authorities ends between 1 July and 31 December, then the tax return is required to be filed by 30 September following the year-end.

An across-the-board self-assessment scheme is in place whereby assessment is taken to be finalised upon filing of the return. The Commissioner, however, has powers to amend the assessment if it is believed that the Ordinance has been incorrectly applied or there is definite information that the assessment made is incorrect. These powers are to be exercised within a prescribed time frame. In the case of transactions between associates, the Commissioner can substitute the transaction value with the fair market consideration. The Commissioner is also empowered to determine tax liability according to the substance of the transaction, disregarding formal arrangements between the parties.

Tax authorities can require a non-filer to file income tax return for any of the last ten years.

Payment of tax

Companies are required to pay advance tax on the basis of tax liability of the immediately preceding tax year in respect of their income (excluding capital gains and presumptive income). The advance tax is to be paid after adjusting the taxes withheld at source (other than the tax withheld relating to FTR).

Advance tax is required to be paid in four quarterly instalments on or before 25 September, 25 December, 25 March, and 15 June in each financial year. Credit for tax paid in a tax year shall be allowed against tax liability of that year. However, in case of banking companies, such advance tax is payable on a monthly basis.

The total tax liability is to be discharged at the time of filing the return of income.

Advance taxes and taxes withheld are adjustable against the tax payable with the return of income.

Tax audit process

The Federal Board of Revenue (FBR) is authorised to prescribe criteria for selection of audit of taxpayers who have filed their returns for a tax year. Based on such criteria, cases are selected through computer ballot separately for income tax, sales tax, and federal excise duty (though recently, the concept of a composite tax audit has also been introduced). The returns are examined by tax authorities, and related documents and information are requisitioned. Show cause notices are then raised and, on receipt of explanations from taxpayers, income or loss is assessed. In case of disagreement with assessments, the taxpayer has the right to agitate the issues before appellate forums.

A taxpayer shall not be selected by the FBR and the Commissioner of Inland Revenue for a tax audit where its income tax affairs were already audited in any of the preceding three tax years. The Commissioner may, however, still select a taxpayer for audit with the approval of the FBR.

Statute of limitations

An audit of the tax return filed by a taxpayer can be conducted by the tax authorities within five years of the end of the financial year in which the return is filed.

Advance rulings

A non-resident not operating in Pakistan through a PE can apply to the FBR to issue an advance ruling setting out the Board's position regarding application of the provisions of the Income Tax Ordinance to a transaction proposed or entered into by the taxpayer. The tax ruling, once issued, is binding on tax authorities.

Topics of focus of tax authorities

Tax authorities focus on the following issues:

- WHT.
- Transfer pricing.
- Relationship of expenditure with the business of the taxpayer.
- Advance tax.
- Payment of tax due within the time prescribed.

- Audit of returns filed.
- Compliance by taxpayers.
- Collection of arrears.

Other issues

Special rules

Special rules are applicable for computation of income from exploration and production of petroleum, mineral deposits, insurance, and banking business.

United States (US) Foreign Account Tax Compliance Act (FATCA)

Pakistan is under active negotiation with the United States for executing an agreement for compliance with FATCA; however, banks and other entities affected by FATCA are required to register with the US Internal Revenue Service (IRS).

Base Erosion and Profit Shifting (BEPS)

On 12 September 2016, Pakistan signed the Multilateral Convention on Mutual Administrative Assistance in Tax Matters ('Convention') under the aegis of the Organisation for Economic Co-operation and Development (OECD), as part of prevention of BEPS. BEPS refers to tax planning strategies that exploit gaps and mismatches in national tax laws to shift profits to low or no tax locations. Accordingly, on the recommendations of the BEPS Action Plan, amendments have also been introduced in the relevant fiscal laws in order to fulfil its obligations under the Convention.

Pursuant to the above Convention, the following agreements were signed by Pakistan:

- Automatic Exchange of Tax Related Information (dated 7 June 2017).
- Multilateral Competent Authorities Agreement (dated 21 June 2017).

Keeping in view these Conventions/Agreements, relevant fiscal laws have been amended/enacted to provide for the following:

- Transfer pricing documentation and country-by-country (CbC) reporting (*see Transfer pricing in the Group taxation section for more information*).
- Controlled foreign companies (*see Controlled foreign companies [CFCs] in Group taxation section for more information*).
- Treaty abuse/shopping (*see below*).
- Common Reporting Standard (*see below*).

Treaty abuse/shopping

Tax authorities have been empowered to disregard an entity or a corporate structure not having any economic substance or that entered into such as a part of a 'tax avoidance scheme', such expression being defined to mean a transaction entered into with the primary purposes of tax avoidance or 'reduction in tax liability'. 'Reduction in tax liability', *inter alia*, includes within its scope that achieved as a result of availing benefit under a DTT.

Further, provisions of law granting an overriding status to treatment provided for in DTTs have also been accordingly amended to the effect that any re-characterisation of income/transactions would not be ineffective on account of such provisions.

This amendment signifies that the substance of the transaction will form the basis of taxation and no rescue would be available on the basis of structure designed to avail treaty benefits.

Common Reporting Standard (CRS)

In order to implement the directives contained in the Convention, the FBR was earlier empowered to obtain information from banks/financial institutions regarding non-resident persons for the purposes of automatic exchange of information under bilateral agreements. Now, in exercise of these provisions, the CRS has also been made part of the income tax law, by way of insertion in the relevant Income Tax Rules.

Under the CRS, tax authorities of countries that are signatory to the Convention/Information Exchange Agreements will share information with the FBR with respect to financial accounts (broadly meaning accounts maintained by banks/financial institutions, including custodial and depository accounts) in their jurisdiction held by Pakistani residents. Pakistan will also provide corresponding information to the foreign tax authorities on accounts held by residents of jurisdiction in Pakistan.

The CRS requires the banks and other financial institutions to provide certain information or to undertake certain due diligence with respect to certain financial accounts. The CRS is aimed to reduce tax evasion by taxpayers using offshore financial accounts held both directly and indirectly through enhanced information sharing and collaboration.

Papua New Guinea

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Significant developments

The 2018 National Budget was handed down in November 2017 and introduced a number of tax changes, including:

- removal of training levy and double deduction for staff training costs
- implementation of a pay now and litigate later policy
- the introduction of transitional provisions for exiting projects in respect of additional profits tax (rent tax), which, following an amended last year, is applicable to all resource projects in Papua New Guinea (PNG)
- making registering taxpayer identification numbers a legal requirement for operating a business
- removing the right to claim certain goods and services tax (GST) input tax credits for educational institutions
- simplifying the administration of non-resident insurer's tax, and
- making shareholders liable for tax liabilities of companies.

In some cases, the changes in the 2017 National Budget produced seemingly unintended consequences, and corrections of these unintended consequences were included in the 2018 Budget.

A comprehensive review of the tax system in Papua New Guinea was completed at the end of 2015, and Treasury continues to assess the recommendations from the review. It is expected that further reform of the tax system will be undertaken in the next few years.

Taxes on corporate income

PNG resident companies are liable for income tax on their worldwide income. Companies that are not resident in Papua New Guinea are only required to remit tax on income sourced in Papua New Guinea. A non-resident's PNG-sourced passive income, including dividends, interest, and royalties, may be subject to withholding tax (WHT). It is ordinarily the case that the payer of the dividend, interest, or royalty must withhold the relevant amount of the tax and remit this to PNG's Internal Revenue Commission (IRC).

Papua New Guinea levies corporate income tax (CIT) on companies on a flat rate basis.

Generally, trading profits and other income (except income that is specifically exempt) of resident companies in Papua New Guinea are assessed tax at a rate of 30%, whereas non-resident companies operating in Papua New Guinea are assessed tax at a rate of 48%.

Overseas shippers

Income derived by overseas shippers or charterers carrying passengers, livestock, mail, or goods out of Papua New Guinea is taxable in Papua New Guinea. The tax is calculated on a deemed taxable income equal to 5% of the gross income, which is taxable at the non-resident rate of 48% in the case of companies. The IRC may exempt the overseas shipper from tax if the shipper's home country exempts PNG shippers from a similar tax.

Local income taxes

There are no provincial or local income taxes in Papua New Guinea.

Corporate residence

A company will be deemed a resident for CIT purposes if it meets either the (i) incorporation test or (ii) the management and control test.

Incorporation test

A company incorporated in Papua New Guinea is automatically regarded as a PNG tax resident. However, the operation of the law of another country and a relevant double taxation treaty (DTT) may result in a company also being treated as resident in another country.

Management and control test

A company is a PNG tax resident if it is managed and controlled in Papua New Guinea, regardless of where it is incorporated. Generally, a company is managed and controlled in Papua New Guinea if key decisions affecting the company are made at directors' meetings held in Papua New Guinea. This also includes a company incorporated outside Papua New Guinea that trades in Papua New Guinea and has its voting power controlled by resident shareholders.

Dual residence

An entity may be a tax resident of both Papua New Guinea and another country by application of domestic legislation. A DTT entered into between Papua New Guinea and another country may contain a tiebreaker test to determine the country of residence for the purposes of the DTT.

Permanent establishment (PE)

The concept of 'permanent establishment' has limited significance in the domestic taxation law of Papua New Guinea and is defined to mean a place at or through which a person carries on any business. Under domestic taxation law, Papua New Guinea will seek to tax the PNG-sourced income of a non-resident irrespective of whether or not that income is derived at or through a PE in Papua New Guinea.

Where PNG has entered into a DTT, the concept of PE becomes more important as it will then be one of the factors determining Papua New Guinea's taxing rights over income sourced in Papua New Guinea, particularly with respect to the business profits of a non-resident company. In general terms, Papua New Guinea's DTTs:

- define a PE to be a fixed place at or through which the business of an enterprise is wholly or partly carried on, and
- deem a PE to exist in various circumstances, including those relating to the presence of substantial equipment in the contracting state and the time spent by personnel of an enterprise furnishing services in a contracting state.

Other taxes

Goods and services tax (GST)

The GST rate is 10% and applies to most goods and services supplied in Papua New Guinea. Exported goods and services attract a zero rate of GST. Goods and services, other than motor cars, supplied to mining, petroleum, or gas companies are also zero-rated. Some goods and services are exempt, including medical, educational, and financial services. Land is excluded from GST, but buildings and other improvements are subject to the tax.

An import GST deferral scheme is also available. Taxpayers wishing to participate in the import deferral scheme are required to apply for approval by the IRC and must have a good history of tax compliance in order to qualify.

Directors of companies that fail to comply with GST obligations are personally liable for a penalty equal to the outstanding tax liability that the company ought to have remitted to the IRC.

Customs duties

The majority of manufacturing inputs (including plant and machinery) attract no customs duties, and other customs duty rates are being progressively reduced. The remaining rates for customs duties vary depending on the nature of the good being imported and are assessed on the total value of the goods imported, including cost, insurance, and freight (CIF). Customs bonds may be issued for the temporary importation of goods that are to be re-exported within 12 months.

Excise taxes

Although customs duties are now minimal in many cases, some goods, most notably motor vehicles, now attract excise tax. Private motor vehicles generally attract excise tax at the rate of 60%, whereas work vehicles attract excise tax of 10%. Excise taxes can also apply to some domestically produced goods, including refined fuel products, alcohol, and tobacco. The tobacco excise tax is levied at 5% biannually (10% annually).

Land tax

Land tax is imposed annually by provincial governments on the unimproved value of the land, and the power to levy land tax is vested exclusively with the provincial governments. In Papua New Guinea, land tax is difficult to implement and faces major geographical and social problems.

Stamp duties

Stamp duty applies at varying rates on documents and certain transactions. Of particular note is duty charged on the conveyance of property, which rises to a maximum of 5% where the value of the property being transferred exceeds 100,000 PNG kina (PGK). The duty is payable by the purchaser, and a 5% duty on the unencumbered value of land may also be payable where there is a transfer of shares in certain landholding companies.

Other dutiable transactions include share transfers (including some share buy-backs), which are subject to a rate of 1%. The Collector of Stamp Duties has the power to amend assessments and refund overpayments of stamp duty.

The Stamp Duties Act was amended to implement a rental income compliance system. The amendment effectively makes it compulsory for a landlord to provide their Taxation Identification Number (TIN) on lease documents, as lease documents will not otherwise be stamped.

Stamp duty is payable on documents executed outside Papua New Guinea that relate to property or matters done or to be done in Papua New Guinea.

Export duties

Timber

Export duty on timber logs (not sawn timber or plantation logs) is calculated with reference to the freight on board (FOB) value per cubic metre of exported logs and rates that increase as the value of the exported logs increase.

Spices

Levies are imposed from time to time on the export of specified spices (e.g. vanilla).

Payroll taxes

Salary or wages tax (SWT)

Businesses paying salary or wages to employees are required to withhold SWT (calculated at the prescribed marginal rates) and remit to the IRC on the seventh day of the month following the month of payment.

Salary or wages is defined as remuneration paid to employees in cash or kind, including benefits such as accommodation and transportation.

Normal employment-related receipts and benefits also include any remuneration paid as consultancy fees or fees for professional services, where the remuneration is paid wholly or substantially for personal services performed in Papua New Guinea.

Directors are personally liable for any unpaid SWT obligations of their companies. Directors who fail to ensure their company complies with its SWT reporting obligations may be penalised at a rate of 20% of the unpaid tax liability *per annum*. After three months of non-payment of outstanding SWT, directors will not be able to obtain a remission of penalties imposed.

Contributions to employee superannuation funds

Contributions to employee superannuation funds are compulsory for entities with 15 or more permanent employees. The employer's compulsory contribution is 8.4% of each employee's gross basic salary. The employee's minimum contribution is 6.0%.

Membership is generally compulsory for citizens. Non-citizens are currently exempt; however, this is under continuing review.

Contributions must be paid to an authorised superannuation fund. Contributions paid to an authorised fund are tax-deductible to the extent that they do not exceed 15% of the relevant employee's gross taxable salary. Contributions to non-resident funds are not tax-deductible.

Training levy

The training levy is abolished effective from 1 January 2018.

Previously, all businesses whose annual payroll exceeded PGK 200,000 were subject to a 2% training levy, calculated on the sum of the taxable salaries, including benefits, of all personnel. Qualifying expenses incurred in training PNG citizen employees were creditable up to the actual amount of the levy. The training levy, if payable, was not tax-deductible.

Departure tax

A departure tax is collected by airlines issuing tickets for persons departing Papua New Guinea.

Gaming machine tax

Papua New Guinea imposes a 74% tax on gross revenue from gaming machines.

Resource project production levies

Production royalties of 2% are payable to the national government on the net smelter return from mining operations. These royalties are tax-deductible. A royalty, at the rate of 2% of the wellhead value, is also payable from the production of petroleum and gas operations. Holders of new petroleum development licences are entitled to treat royalties as income tax paid. However, new petroleum projects will also pay a tax-deductible development levy calculated at the same rate of 2% of the wellhead value.

Mining projects are also required to pay a production levy to the Mineral Resources Authority calculated at a rate between 0.25% and 0.5% of the assessable income from production.

Branch income

Income derived by a non-resident contractor for services in Papua New Guinea is usually subject to a WHT at the rate of 15% of gross income. The provisions extend to payments for the following:

- The installation, maintenance, and use in Papua New Guinea of substantial equipment or machinery.
- Construction projects.
- For the lease or charter of any industrial, commercial, or scientific equipment or any machinery or vehicle.
- Consultancy or management services.

Where the non-resident contractor rules do not apply, the non-resident company will be subject to income tax at the non-resident tax rate of 48% on its PNG-sourced taxable income (*see the Income determination section for a definition of taxable income*).

PNG branch remittances are not liable for dividend WHT or any branch profits or similar tax.

Income determination

Taxable income is defined as the sum of assessable income minus allowable deductions. In practice, profits are calculated for tax purposes by reference to the profits reported in the financial accounts. Accounts must be prepared in accordance with PNG accounting principles, which follow the International Financial Reporting Standards (IFRS).

Inventory valuation

There is no form of stock relief or trading stock valuation adjustment to recognise the effects of inflation in Papua New Guinea. There is a once-only option to adopt the lowest of the cost amount, the market selling value, or the replacement value (which, in practice, may mean that book and tax valuations for trading stock are not aligned). Where the option is not exercised, the value of the stock is deemed to be the cost price; however, neither the income tax law nor the associated regulations provide detailed guidance on what constitutes 'cost price' (the Commissioner General of Internal Revenue has not produced any related guidance to date). It will generally be the case that where a taxpayer has determined a cost price in accordance with IFRS, that cost price will also be accepted for income tax purposes.

In special circumstances, the Commissioner General of Internal Revenue may accept a lower valuation.

Capital gains

There is no general capital gains tax in Papua New Guinea. However, profits arising on the sale of property acquired for the purpose of resale at a profit, or from the carrying out of a profit-making scheme, are taxable as ordinary income.

Dividend income

Unless otherwise exempt from CIT, dividends are included in the assessable income of a shareholder.

Inter-company dividends

Dividends received by a resident company from other companies, whether resident or non-resident, while being assessable to tax, are generally subject to a full tax rebate and are effectively received tax-free. However, where a company has losses on other activities or losses carried over from earlier years, those losses are applied against dividend income before the calculation of the dividend rebate.

Stock dividends

In most cases, the payment of a dividend by way of the issue of shares is subject to the same taxation treatment as the payment of a dividend by way of cash or the distribution of other property. However, dividends paid by the issue of shares wholly and exclusively out of profits arising from the sale or revaluation of assets not acquired for the purpose of resale at a profit are exempt from income tax and dividends WHT.

Interest income

Unless exempt under specific provisions, interest paid or credited by a financial institution, the Central Bank, or a company to a person resident in Papua New Guinea is includable in income, and the person making the payment of or crediting interest in the account is liable to withhold and pay tax upon the amount.

Royalty income

Tax is imposed on royalties and similar payments made to non-residents who do not have a PE in Papua New Guinea. The tax must be withheld by the payer on behalf of the payee and remitted to the IRC. The tax payable on royalties paid to a party who is not an 'associated person' is the lesser of:

- 48% of the net royalty (i.e. gross royalty, less applicable expenses), and
- 10% of the gross royalty.

Royalty payments to a non-resident 'associated person' are liable for a WHT of 30% of gross payments (subject to any DTT), with no option to adopt the net income basis.

The definition of 'associated person' is detailed and widely drawn. Broadly, it encompasses relatives, partners, companies under effective common control, and related trust interests.

There is also a 5% WHT on mining, petroleum, timber, and fishing royalties to landowners.

Partnership income

A partner's share of the assessable income of the partnership less all allowable deductions to the partnership is includable in the partner's assessable income for the year of income. Likewise, the partner's individual interest in a partnership loss incurred in the year of income is an allowable deduction. Further, if income is exempt income to the partnership, this income will be exempt income to the individual partner relative to their individual interest.

Unrealised exchange gains/losses

Generally, foreign exchange gains realised and derived from debts made on or after 11 November 1986 or denominated in a currency other than the Papua New Guinea kina are included in assessable income.

Foreign income

PNG resident companies are liable for CIT on their income from all sources (i.e. including foreign-sourced income). A foreign tax credit may be available to offset foreign tax paid against PNG tax payable (*see the Tax credits and incentives section for more information*).

There are no provisions in Papua New Guinea that permit the deferral of the taxation of income derived outside Papua New Guinea. Subject to the operation of a DTT, foreign-sourced income derived by a resident of Papua New Guinea is subject to tax in Papua New Guinea in the year in which it is derived, irrespective of whether or not that income is repatriated to Papua New Guinea.

Deductions

General deduction provisions provide that all losses and expenditures, to the extent incurred in gaining or producing the assessable income or necessarily incurred in carrying on a business for the purpose of gaining or producing that income, are allowable deductions. However, the general deduction provisions do not allow a deduction to the extent a loss or expenditure is an outgoing of capital, or of a capital, private, or domestic nature, or incurred in relation to the gaining or production of exempt income.

Depreciation

Depreciation is allowed for equipment and other assets at prescribed rates. A taxpayer must use the diminishing-value method unless an election is made to use the prime-cost method. The applicable diminishing-value rates are 150% of the prime-cost rates.

Plant, machinery, and equipment

Plant, machinery, and equipment (including buildings) are depreciable at rates according to their estimated lives. A taxpayer other than a taxpayer who derives income from mining, petroleum, or gas operations may elect to claim special accelerated depreciation rates for certain capital items. For example, flexible depreciation rates (up to 100%) may be claimed on new industrial plant with a life exceeding five years that is used for manufacturing purposes. Other new plant and articles used in manufacturing, construction, transport, storage, communication, and agricultural production are eligible for an accelerated deduction equal to 20% of cost in the year of purchase. New plant and articles used for tourism are eligible for an accelerated deduction equal to 55% of cost in the year of purchase.

Motor vehicles

Motor vehicles are generally depreciable at 20% of prime cost. There is no upper limit in value for depreciation purposes.

Buildings

Buildings forming an integral part of plant, machinery, and equipment are depreciable at a prime-cost rate of up to 7.5%, depending on the construction materials. Buildings housing plants eligible for the one-year write-off deduction (*see comments on new industrial plant under Plant, machinery, and equipment above*) can be written off in the year of construction. Other income-producing buildings may qualify for the accelerated deduction of 20% in the year of purchase.

Agricultural and fishing plants

Most items of new agricultural and commercial fishing plants qualify for 100% depreciation, as do boats and ships, including ancillary equipment, used solely as dive boats or for scuba diving by accredited tour operators. Other new items having a life exceeding five years used by a person carrying on agricultural operations are eligible for accelerated depreciation in the initial year of use.

Goodwill

A deduction is not available for goodwill or the amortisation of goodwill in Papua New Guinea (this being an amount not deductible under ordinary concepts and an item for which there is no specific deduction provision).

Start-up expenses

It will generally be the case that start-up expenses will not be deductible in Papua New Guinea. Such expenses are generally either capital, or of a capital nature, or incurred prior to the derivation of assessable income. There is no specific deduction provision for the deductibility of start-up expenses.

Interest expenses

A deduction is generally available for interest incurred on an arm's-length basis, subject to meeting the general principles for deductibility and the requirements under the thin capitalisation rules (*see Thin capitalisation in the Group taxation section*). Where interest is incurred in connection with the construction or acquisition of a plant or capital asset, that interest is not immediately deductible. Rather, such interest is deemed to form part of the cost of that asset (and in the case of a plant will then form part of the base from which future depreciation deductions may be claimed).

Bad debt

Bad debts are deductible if they have previously been included in assessable income and written off by year-end or if the bad debt was in respect of money lent in the ordinary course of the taxpayer's business of money lending.

Double deductions

An additional amount equal to the actual amount of expenditure incurred is deductible in respect of certain expenditures (e.g. export market development costs, certain donations). In other words, a 'double deduction' is available with respect to these items.

Donations

It is considered that donations made by a corporate taxpayer meet the general principles for deductibility and hence will generally be deductible (notwithstanding the specific provision dealing with gifts to charitable bodies has no current effect as there are no charitable bodies approved by the Commissioner General of Internal Revenue for this purpose). There are specific provisions in Papua New Guinea's taxation law dealing with the deductibility of certain donations, some of which provide a deduction for up to 200% of the value of the amount donated.

Pension expenses

Contributions paid to an authorised superannuation fund are tax-deductible to the extent that they do not exceed 15% of the relevant employee's gross taxable salary. Contributions to non-resident funds are not tax-deductible. *See the Other taxes section for more information*.

Taxes

A deduction is not allowable in respect of payments of income tax. Other taxes may be deductible, subject to meeting the general principles for deductibility.

Net operating losses

Domestic

Trading losses may be offset against all income received in the same accounting period or carried forward and offset against future trading profits. The limitation period on the carryforward of losses is generally 20 years. Losses may not be carried back against prior years' profits. Primary production losses and resource project losses may be carried forward without a time limitation, although, again, they may not be carried back (*see the Tax credits and incentives section for more information*).

Note that the carryforward of losses is subject to a 50% or more continuity of shareholding and control test, or a continuity of business test where there is a breach of the ownership test.

Foreign

Losses incurred by a resident taxpayer from a source outside Papua New Guinea (other than in relation to export market development) are not deductible against assessable income derived within Papua New Guinea. In practice, overseas losses can be carried forward and offset against overseas income for up to 20 years.

Payments to foreign affiliates

The deduction available to a taxpayer for management fees paid to an associated person is limited to the greater of:

- 2% of assessable income derived from PNG sources by the taxpayer or
- 2% of the total allowable deductions, excluding management fees incurred by the taxpayer in Papua New Guinea.

The limitation applies to both resident and non-resident taxpayers. Special rules apply to mining, petroleum, and gas companies. These limits may not apply where the recipient of the management fee is resident in a country with which Papua New Guinea has a DTT or where it can be demonstrated that the management fee arrangements do not have the purposes or effect of avoiding or altering the income tax payable in Papua New Guinea.

Group taxation

Companies are assessed for CIT separately, regardless of whether they are part of a group of associated or related companies. Losses of one company within a group cannot be offset for tax purposes against the profits of another company within that group.

The Companies Act allows two or more companies to amalgamate and continue as one, and provisions are in place to allow this to occur without any adverse CIT consequences.

Transfer pricing

Papua New Guinea has transfer pricing provisions that require transactions with foreign affiliates to be conducted on an arm's-length basis. Disclosure of such transactions is done through an international dealings schedule (IDS). Corporate taxpayers (including companies, superannuation funds, and unit trusts) that have transactions or dealings with international affiliates that exceed PGK 100,000 in an income year or have aggregate loan balances with international affiliates in excess of PGK 2 million at any time during an income year are required to prepare and lodge an IDS with their income tax return for that year of income.

Thin capitalisation

Thin capitalisation rules apply to prevent taxpayers from incurring excessive levels of debt. By excessively gearing their investments, companies are able to claim greater tax deductions through the interest expense charged on such debt. Thin capitalisation rules typically feature a debt-to-equity ratio that governs the ratio by which companies can borrow from related parties relative to their equity. Any interest charged on debt that exceeds this ratio will not be deductible for CIT purposes.

Papua New Guinea's thin capitalisation rules apply a debt-to-equity ratio of 3:1 to PNG resource companies and 2:1 to all other PNG companies.

These rules do not apply to licensed financial institutions and do not apply to interest paid under domestic debt for non-resource companies. If the ratio is breached, a proportion of the interest on foreign debt will be denied as a tax deduction. For resource companies, a proportion of interest on all debt will be denied.

Controlled foreign companies (CFCs)

Papua New Guinea does not have CFC rules.

Tax credits and incentives

In this section, we comment on the more significant tax credits and incentives available in Papua New Guinea, followed by a summary of those with more limited application.

Foreign tax credit

A foreign tax credit may be available to offset foreign tax paid against PNG tax payable. The foreign tax credit is limited to either the foreign tax paid or the average PNG tax payable on that foreign income, whichever is less. There is no mechanism to carry forward excess foreign tax credits for utilisation in a subsequent year.

Primary production incentives

Key incentives that are available with specific application to primary production activities include:

- Outright deductions for certain capital expenditures, including clearing, preparing, or conserving land for agriculture; eradicating pests; providing labourers' accommodation; and for the conservation and conveyance of water.
- A 100% deduction is available for a new plant used directly for the purposes of agricultural production, and an initial 20% accelerated depreciation deduction is allowed for a new plant with a life exceeding five years.
- Losses incurred in carrying on a primary production business can be carried forward indefinitely; they are not restricted to the 20-year limit that generally applies to company tax losses.
- Agricultural companies may transfer to their shareholders the benefit of the outright tax deduction available for many types of capital expenditures. The total deduction available to shareholders may not exceed the amounts paid on their shares.
- As part of promoting investment in primary production, a 20% tax rate is prescribed in respect of 'incentive rate primary production income' derived by a company (as opposed to the normal 30% tax rate for a resident company or 48% for a non-resident company) for up to ten years.

Agricultural production extension services deduction

A 150% deduction is available for expenditure on services provided free of charge to smallholder growers, including the provision of advice, training, and technical assistance in relation to primary production to assist growers with production, processing, packaging, and marketing issues.

Double deduction for export market development costs

Expenditure incurred in the promotion for sale outside Papua New Guinea of goods manufactured in Papua New Guinea or tourism promotion is eligible for double deduction. The total tax saving cannot exceed 75% of the expenditure incurred.

Export incentives

Prior to 1 January 2015, the net export income from the export sale of certain types of goods was exempt for the first four years of income, with a partial exemption in the following three years. This exemption is not applicable from 1 January 2015 (except in respect of goods that qualified for the exemption prior to that date).

Tax credit for infrastructure development by agricultural, mining, petroleum, and gas companies

A tax credit is available to agricultural, mining, petroleum, gas, and certain tourism companies that incur expenditure on a prescribed infrastructure development. In the case of taxpayers engaged in mining, petroleum, and gas operations, the credit is limited to 0.75% of the assessable income or the amount of tax payable for the year (in respect of that mining, petroleum, or gas project), whichever is less. Excess expenditure over the 0.75% or tax payable may be included in the following year's rebate claim.

Unutilised credits or excess expenditure can generally only be carried forward for two years. In the case of taxpayers engaged in agricultural production, the credit is limited to 1.5% of the assessable income or the amount of tax payable for the year, whichever is less.

A prescribed infrastructure development includes a school, aid post, hospital road, and other capital assets that have been approved as such by the Department of National Planning and the IRC. It cannot be an expenditure required under the Mining Act or the Oil and Gas Act.

Other tax incentives in Papua New Guinea

Other tax incentives available in Papua New Guinea include:

- Manufacturers' wage subsidy.
- Immediate deduction for the costs of acquiring and installing solar heating plant.
- A ten-year tax exemption for qualifying new business located in prescribed remote areas of Papua New Guinea.
- A specific deduction for environmental protection and clean-up costs.

Incentives for petroleum, mining, and gas operations

Special incentives and rules apply to mining, petroleum, and gas exploration, extraction, and production activities. The main aspects are as follows:

Project basis of assessment

A project basis of assessment (ring-fencing) is adopted for all resource projects. This means losses from other operations, regardless of whether or not they are resource related, cannot generally be offset against resource project income from a particular ring-fenced project. However, there are some concessions to the ring-fencing principle in respect of exploration expenditure and expenditure in respect of discontinued projects and losses arising from site restoration costs.

In general, all costs incurred in the exploration and development phases of the project are accumulated and amortised over the life of the project. Once production starts, an immediate deduction is allowed for 'normal' operating and administration expenses. Capital expenditure incurred after the start of production are capitalised and amortised over the life of the project.

Rate of tax

A standardised rate of 30% applies to all companies resident in Papua New Guinea.

Interest deductions

Interest is not deductible prior to the commencement of a resource project. Following the issue of a resource development licence, a person carrying on a resource project or exploration in relation to a resource project may claim a deduction against resource income for interest on money borrowed for carrying on the relevant operations or exploration. This is subject to a number of conditions, including the resource company maintaining a debt-to-equity ratio of 3:1 (*see Thin capitalisation in the Group taxation section*).

Capital allowances

Allowable exploration expenditures (AEE) are amortised over the life of the resource project. The deduction is calculated by dividing the unamortised balance by either the remaining life of the project or four, whichever is less. The amount of the deduction is limited to the amount of income remaining after deducting all other deductions, other than deductions for allowable capital expenditure. In other words, the deduction cannot create a tax loss.

Allowable capital expenditures (ACE) are amortised over the life of the resource project. The ACE is split into two categories: capital expenditures with an estimated effective life of more than ten years (long-life ACE) and capital expenditures with an estimated effective life of less than ten years (short-life ACE).

The annual deduction for long-life ACE is claimed on a straight-line basis over ten years.

Where the remaining life of the project is less than ten years, the rate at which the deduction is allowed is calculated by referring to the remaining life of the project. For short-life ACE, the annual deduction is calculated by dividing the unamortised balance by either the remaining life of the project or four, whichever is less. For new mining projects, the deductions for both long-life ACE and short-life ACE are calculated by dividing the unamortised balance by either the remaining life of the project or four, whichever is less.

The amount of the deduction for ACE is limited to the amount of income remaining after deducting all other deductions. In other words, the deduction cannot create a tax loss.

Off-licence exploration expenditure

A major easing of the ring-fencing principle applies to taxpayers that are involved in a producing project where the taxpayer or a related party incurs exploration expenditure outside the area of the productive project. In this situation, the taxpayer can elect (whether or not it is currently involved in a producing project) to add such exploration expenditure to an exploration pool that can be amortised against income from the producing project.

The amount allowable as a deduction from this exploration pool in respect of resource operations carried on by the taxpayer or a related corporation is the lesser of:

- 25% of the total undeducted balance of expenditure in the exploration pool or
- such amount as reduces CIT (other than additional profits tax [*see below*]) that would, but for this deduction, be payable by the taxpayer and its related corporations in respect of those resource operations for that year of income, by 10% (or 25% for mining projects).

Management fees

Once a resource project derives assessable income, the deduction for management fees is restricted to 2% of operating expenses other than management fees. During the exploration phase of a project, the amount of management fees that can be treated as allowable exploration expenditure is limited to 2% of the exploration expenditure other than management fees. Furthermore, during the development phase, the amount of management fees that can be treated as allowable capital expenditure is limited to 2% of the allowable capital expenditure other than management fees.

Transfer of expenditure

When interests are transferred from one taxpayer to another, the vendor and purchaser can agree to transfer deduction entitlements for the unamortised balances of allowable exploration expenditure and allowable capital expenditure to the purchaser.

Liquefied natural gas (LNG) project

A number of provisions with specific application to the PNG LNG project have been included in the Income Tax Act, Stamp Duties Act, Goods and Services Tax Act, Customs Act, and Excise Act.

Additional profits tax

A modified additional profits tax applies to all resource projects (mining, petroleum, and gas). The additional profits tax applies a tax rate of 30% to returns in excess of a 15% hurdle rate.

Withholding taxes

Dividends, interest, royalties, and technical/management fees

The following WHT rates apply to dividends, interest, royalties, and technical fees under PNG domestic law and tax treaties. PNG domestic legislation provides an exemption from WHT for dividends and interest in certain circumstances. The higher rates quoted are the maximum rates allowable under the treaties.

	WHT (%)			
Recipient	**Dividends**	**Interest (1)**	**Royalties**	**Technical fees**
Resident company	0	15	0	0
Resident individual	15	15	0	0
Non-resident corporations and individuals	15	15	10/30 (2)	17
Treaty:				
Australia	15	10	10	0
Canada	15	10	10	0
China	15	10	10	0
Fiji	15	10	15	15
Germany (3)	15	10	10	10
Indonesia	15	10	10	10
Korea, Republic of	15	10	10	0
Malaysia	15	15	10	10
New Zealand	15	10	10	0
Singapore	15	10	10	0
United Kingdom	15	10	10	10

Notes

1. There is no WHT on interest when:
   - interest is paid or credited to a licensed financial institution in Papua New Guinea, the Bank of Papua New Guinea, or the state, or
   - the interest income is otherwise exempt income in the hands of the recipient.
2. A royalty paid to a non-resident associate of the payee will suffer a 30% WHT. Where the non-resident is not an associate of the payee, the WHT rate will be 10% (or 48% of the taxable income derived from the royalty if the non-resident chooses to lodge an income tax return in Papua New Guinea).
3. The treaty with Germany has not yet been ratified by Germany.

Business income WHT

Income derived by local contractors in certain industries is covered by the business income WHT regime. The industries affected include:

- Building and construction.
- Road transport.
- Motor vehicle repairs.
- Security.
- Equipment hire.

Businesses affected are required to have a certificate of compliance and to produce it when entering into contracts with their customers. Payers are required to file an annual income reporting statement where they make either an eligible payment of PGK 500 or more in relation to one contract or eligible payments for several contracts exceeding PGK 5,000 in the year of income in relation to a single payee. Payers are required to deduct a 10% WHT if payees do not produce a certificate of compliance.

Non-resident insurer WHT

Premiums paid to non-resident insurers in respect of insurance contracts on property situated in Papua New Guinea or insured events that can only occur in Papua New

Guinea are subject to tax in Papua New Guinea. The tax is calculated on a deemed taxable income equal to 10% of the gross premium, which is taxed at the non-resident tax rates of 48% (companies) or 30% (unincorporated associations). Tax treaties may limit the rate of tax applied.

Tax administration

Taxable period

The tax year is generally the period 1 January to 31 December; however, application may be made for a substituted tax year-end. These will normally be granted where the substituted tax year-end coincides with the accounting year-end of an overseas holding company. A company's tax year does not need to be the same as its accounting period.

Tax returns

Papua New Guinea operates on a full assessment basis, and companies are required to lodge an annual CIT return showing the calculation of taxable income for the year. In addition, the return must provide detailed disclosures in relation to income derived and expenses incurred during the year of income.

A company must file a tax return by 28 February in the year following the year of income to which the return relates. However, the following automatic extensions apply where the company lodges its return through a registered tax agent:

- Six months from the taxpayer's year-end for taxable returns and partnership returns.
- Eight months from the taxpayer's year-end for resource company returns in a tax payable position.
- Ten months from the taxpayer's year-end for non-taxable returns.

Payment of tax

CIT is collected under a provisional tax system. Under this system, tax is paid in respect of a company's current year profits (i.e. payments made in the year of income are in respect of income derived in the same year as the payment is due).

Provisional tax is assessed by the IRC based on the last return lodged. In the event that no tax was payable on the previous year's return, the Commissioner General has the right to estimate the amount of tax based on any other information available.

Provisional tax is payable in three equal instalments by 30 April, 31 July, and 31 October.

Applications may be made to reduce provisional tax assessed if the tax due for the year in question is expected to be lower than the provisional tax assessed. Where estimated provisional tax is less than 75% of the income tax ultimately assessed, additional tax may be levied. Additional tax at a rate of 20% will be assessed, based on the difference between the estimate lodged and the provisional tax originally determined, or the actual tax payable, whichever is less. The Commissioner General has the discretion to require payment of additional tax.

Mining, petroleum, and gas companies are subject to advance payments tax, a system that broadly mirrors the provisional tax system in place for non-resource companies. The main difference for resource companies is they have the option to lodge an estimate of their taxable income for the year prior to 30 April, 31 July, and 31 October each year, which the IRC uses to assess each advance payments tax instalment.

Following the lodgement of the CIT return, the IRC will serve a notice of assessment on the company. The balance of tax payable for a year of income, after the application of provisional tax (or advance payments tax in the case of a resource company) and other tax credits or rebates, is due to be paid within 30 days of the date of service of the notice of assessment.

Tax audit process

There is no prescribed tax audit process in Papua New Guinea, and resource constraints have limited the IRC's audit activities.

Period for amendment of assessments

Where the IRC considers that a taxpayer made a full and true disclosure of all the material facts necessary for assessing their returns as originally assessed, the IRC may only amend an assessment that increases the tax liability of the taxpayer within three years from the date that tax became due and payable under the original assessment.

Where the IRC considers that a taxpayer did not make a full and true disclosure of all the material facts necessary for the assessment of their returns, and there has been an avoidance of tax, then:

- the IRC may amend any assessments previously issued to the participants if the IRC is of the opinion that the avoidance of tax was due to fraud or evasion (i.e. no time limit applies), or
- in cases of tax avoidance due to reasons other than fraud or evasion, the IRC may amend an assessment within six years from the date that tax became due and payable under the original assessment.

Topics of focus for the Internal Revenue Commission (IRC)

In late 2011, the IRC issued Taxation Circular No 2011/2, which provided guidance on transfer pricing matters in Papua New Guinea. The IRC continues to consider transfer pricing as an area of focus.

The IRC has indicated an increased focus on the effective collection of taxes and tax compliance through the implementation of a new Standard Integrated Tax Accounting System (SIGTAS).

The IRC has not otherwise publicly announced areas of focus for audit programs.

Philippines

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Significant developments

Tax Reform for Acceleration and Inclusion (TRAIN)

On 19 December 2017, the President signed into law Republic Act No. 10963, otherwise known as the Tax Reform for Acceleration and Inclusion (TRAIN) law. The law amends several provisions of the National Internal Revenue Code of 1997 on individual income taxation, passive income taxation for corporations, estate tax, donor's tax, value-added tax (VAT), excise tax, and documentary stamp tax, among others.

The TRAIN law took effect on 1 January 2018, following its complete publication in the Official Gazette on 27 December 2017. The affected sections of this summary were updated accordingly.

Reinstatement of Notice of Informal Conference in the tax audit process

Revenue Regulation No. 7-2018 reinstated the issuance of a Notice of Informal Conference during tax audits.

Under this Revenue Regulation, the taxpayer shall be informed, in writing, by the concerned tax office of the discrepancy in the taxpayer's payment of one's internal revenue taxes for the purpose of an Informal Conference to afford the taxpayer with an opportunity to present one's side.

The Informal Conference must be held within 30 days from receipt of the notice. If it is found that the taxpayer is still liable for deficiency taxes, and the taxpayer is not amenable, the tax office shall proceed to issue a deficiency tax assessment.

Reversion of authority to accredit and register customs brokers and importers to the Bureau of Customs (BOC)

This Order was issued to revert the authority to accredit and register customs brokers and importers to the Bureau of Customs (BOC) for purposes of simplifying the process. The Importer's Clearance Certificates (ICC) and Broker's Clearance Certificates (BCC) are no longer pre-requisites in securing accreditation from the BOC since the Bureau of Internal Revenue (BIR) will no longer accept ICC and BCC applications effective 1 March 2018.

Pending legislation

Please note this information is current as of 1 June 2018. Any changes in current legislation will be announced after 1 June 2018. Please visit the Worldwide Tax

Summaries website at *www.pwc.com/taxsummaries* to see any significant corporate tax developments that occurred after 1 June 2018.

Taxes on corporate income

A domestic corporation is subject to tax on its worldwide income. On the other hand, a foreign corporation is subject to tax only on income from Philippine sources (*see the descriptions of Resident foreign corporations and Non-resident foreign corporations below*).

Domestic corporations

The following corporate income tax (CIT) rates apply to domestic corporations:

Income	CIT rate (%)
In general, on net income from all sources.	30
Minimum corporate income tax (MCIT) on gross income, beginning in the fourth taxable year following the year of commencement of business operations. MCIT is imposed where the CIT at 30% is less than 2% MCIT on gross income.	2
Proprietary educational institutions and non-profit hospitals, on net income if gross income from unrelated trade, business, and other activities does not exceed 50% of the total gross income from all sources.	10
Non-stock, non-profit educational institutions (all assets and revenues used actually, directly, and exclusively for educational purposes) and other non-profit organisations.	Exempt

Certain passive income from domestic sources is subject to final tax rather than ordinary income tax (*see the Income determination section*).

Improperly accumulated earnings tax

An improperly accumulated earnings tax of 10% is imposed on improperly accumulated income. The tax applies to every corporation formed or used for the purpose of avoiding income tax with respect to its shareholders, or the shareholders of any other corporation, by permitting earnings and profits to accumulate instead of being divided or distributed. Exceptions are made for publicly held corporations, banks and non-bank financial intermediaries, and insurance companies.

Resident foreign corporations

Resident foreign corporations (i.e. foreign corporations engaged in trade or business in the Philippines through a branch office) are taxed in the same manner as domestic corporations (except on capital gains on the sale of buildings not used in business, which are taxable as ordinary income), but only on Philippine-source income.

International carriers are subject to an income tax of 2.5% on their gross Philippine billings unless a lower rate is available under an existing tax treaty. Exemption from this tax is also available under international agreements to which the Philippines is a signatory or on the basis of reciprocity in cases where the home country of the international carrier grants income tax exemption to Philippine carriers.

Income of offshore banking units (OBUs) and foreign currency deposit units (FCDUs) of depository banks from foreign currency transactions with non-residents, other OBUs, or FCDUs and local commercial banks (including branches of foreign banks) authorised by the *Bangko Sentral ng Pilipinas* (BSP; central bank) to transact business with OBUs and FCDUs are exempt from all taxes except net income specified by the Secretary of Finance upon recommendation of the Monetary Board. Interest income from foreign currency loans granted to residents other than OBUs or local commercial banks shall be subject to a 10% final income tax.

Regional or area headquarters of multinational corporations that do not earn or derive income from the Philippines, and that act as supervisory, communications, and coordinating centres for their affiliates, subsidiaries, or branches in the Asia-Pacific region and other foreign markets are not subject to CIT.

Regional operating headquarters (ROHQ) pay a tax of 10% on their taxable income. An ROHQ is a branch established in the Philippines by a multinational company that is engaged in any of the following services: general administration and planning, business planning and coordination, sourcing and procurement of raw materials and components, corporate finance advisory services, marketing control and sales promotion, training and personnel management, logistic services, research and development services and product development, technical support and maintenance, data processing and communication, or business development.

Non-resident foreign corporations

In general, non-resident foreign corporations are taxed on gross income received from sources within the Philippines at 30%, except for reinsurance premiums, which are exempt. Interest on foreign loans is taxed at 20%. Dividends from domestic corporations, however, are subject to a final withholding tax (WHT) at the rate of 15% if the country in which the corporation is domiciled does not impose income tax on such dividends or allows a tax deemed paid credit of 15%.

Lower rates or exemption on the above income may be available under an applicable tax treaty.

Rentals and charter fees payable to non-resident owners of vessels chartered by Philippine nationals are subject to a final tax of 4.5%. Rentals, charters, and other fees derived by non-resident lessors of aircraft, machinery, and other equipment are subject to a final tax of 7.5%.

Local income taxes

See Local government taxes in the Other taxes section for a description of local taxes on sales or receipts.

Corporate residence

A domestic corporation is a corporation that is created or organised under Philippine laws. A foreign corporation that is duly licensed to engage in trade or business within the Philippines is referred to as a ‘resident foreign corporation’.

Permanent establishment (PE)

The business profits provision in most Philippine treaties permits the Philippines to tax only those profits attributable to a PE. While Philippine treaties adopt the United Nations (UN) Model Convention, Organisation for Economic Co-operation and Development (OECD) commentaries have often been cited by tax authorities to support their interpretation of treaty provisions. The main implication is that most

Philippine treaties contain a rule deeming a PE to arise when services are performed in the Philippines for a specified period of time.

Other taxes

Value-added tax (VAT)

VAT applies to practically all sales of services and imports, as well as to the sale, barter, exchange, or lease of goods or properties (tangible or intangible). The tax is equivalent to a uniform rate of 12%, based on the gross selling price of goods or properties sold, or gross receipts from the sale of services. On importation of goods, the basis of the tax is the value used by the Bureau of Customs (BOC) in determining tariff and customs duties plus customs duties, excise taxes, if any, and other charges. Where the valuation used by the BOC is by volume or quantity, the VAT basis is the landed cost plus excise taxes, if any.

Certain transactions are zero-rated or exempt from VAT. Export sales by VAT-registered persons are zero-rated.

Certain sales of services exempt from VAT, including services provided by financial intermediaries, are subject to percentage taxes based on gross sales, receipts, or income. A 3% percentage tax also applies to persons who are not VAT-registered because their annual sales or receipts do not exceed the VAT threshold of 3 million Philippine pesos (PHP), as increased by the TRAIN law.

Some of the VAT rules that were amended under the TRAIN are as follows:

- VAT exemption for lease of a residential unit increased from PHP 12,800 to PHP 15,000 and is no longer subject to automatic adjustment.
- Beginning in 2021, the threshold of the VAT-exempt sale of a house and lot and other residential dwellings will be reduced to PHP 2 million and sale of a residential lot will be subject to VAT.
- Upon establishment of an enhanced VAT refund system, 12% VAT will apply on:
  - Sales of raw materials or packaging materials to a non-resident buyer for delivery to resident local export-oriented enterprises.
  - Sales of raw materials or packaging materials to export-oriented enterprises whose export sales exceed 70% of total annual production.
  - Those considered export sales under Executive Order No. 226, otherwise known as the Omnibus Investment Code of 1987, and other special laws.
  - Processing, manufacturing, or repacking goods for other persons doing business outside the Philippines which goods are subsequently exported, where the services are paid for in acceptable foreign currency and accounted for in accordance with the rules and regulations of the BSP.
  - Services performed by subcontractors and/or contractors in processing, converting, or manufacturing goods for an enterprise whose export sales exceed 70% of total annual production.
- Additional VAT exemptions:
  - Sale or lease of goods and services to senior citizens and persons with disabilities as provided under relevant laws.
  - Sale of drugs and medicines for diabetes, high cholesterol, and hypertension starting in 2019.
  - Sale of gold to the BSP (previously VAT zero-rated).

- Transfers of property pursuant to Section 40(C)(2) of the Tax Code.
- Association dues, membership fees, and other assessments and charges collected by condominium corporations.

Customs duties

Applicable customs duties are determined based on the tariff classification of the import product. As with the rest of the Association of South East Asian Nations (ASEAN) countries, tariff classification in the Philippines is based on the ASEAN Harmonised Tariff Nomenclature (AHTN), which is patterned after the Harmonised Commodity Classification and Coding System (HS) Convention and its 2002 revisions. The latest edition, HS Code 2012, entered into force on 1 January 2012. With HS Code 2012, the overall AHTN tariff lines were reduced by 247, or an approximately 4% cut in the number of AHTN tariff lines in 2010. Although 267 classification rulings were issued to address commonly raised valuation and tariff classification, it is still advisable that tariff classification rulings from the Philippine Tariff Commission be secured prior to importation into the Philippines in case of uncertainty as to the correct classification of a product. Note that while the tariff classification rulings issued by the Philippine Tariff Commission do not prevent the BOC from conducting its own verification, these rulings carry persuasive reference in support of the classification and duty rate used by an importer.

The Philippines adopts the World Trade Organization (WTO) Valuation Agreement, where the declared invoice price is used as the basis for determining customs duties.

As a protective measure, the Philippines retains higher tariff rates (20% to 50%) on sensitive agricultural products, such as grains, livestock and meat products, sugar, certain vegetables, and coffee. A few agricultural commodities are subject to minimum access volumes, but these represent less than 1% of all tariff lines.

In view of the existing free trade agreements in the region, such as the ASEAN Free Trade Area (AFTA), the ASEAN-China Free Trade Area (ACFTA), the ASEAN-Korea Free Trade Area (AKFTA), the ASEAN-Australia-New Zealand Free Trade Area (AANZFTA), the ASEAN-Japan Comprehensive Economic Partnership Agreement (AJCEPA), the ASEAN-INDIA Free Trade Area (AIFTA), the European Free Trade Association (EFTA), and the Philippine-Japan Economic Partnership Agreement (PJEPA), the Philippines has taken steps to progressively eliminate tariffs. Tariff reductions for the Philippines range from 10% to 35% for most products included in the Normal Track list.

Excise taxes

Excise taxes apply to services and to goods manufactured or produced in the Philippines for domestic sales, consumption, or for any other disposition and to things imported.

Below is the new excise tax schedule under the TRAIN law:

Manufactured oils and other fuels

Description	Units	2018 (PHP)	2019 (PHP)	2020 (PHP)
Lubricating oils and greases	Per litre	8.00	9.00	10.00
Processed gas	Per litre	8.00	9.00	10.00
Waxes and petrolatum	Per kilo	8.00	9.00	10.00
Denatured alcohol	Per litre	8.00	9.00	10.00

Description	Units	2018 (PHP)	2019 (PHP)	2020 (PHP)
Naphtha	Per litre	7.00	9.00	10.00
Unleaded premium gasoline	Per litre	7.00	9.00	10.00
Aviation turbo jet fuel	Per litre	4.00	4.00	4.00
Kerosene	Per litre	3.00	4.00	5.00
Diesel fuel oil	Per litre	2.50	4.50	6.00
Liquefied petroleum gas	Per kilo	1.00	2.00	3.00
Asphalts	Per kilo	8.00	9.00	10.00
Bunker fuel oil	Per litre	2.50	4.50	6.00
Petroleum coke	Per ton	2.50	4.50	6.00

Automobiles

Automobile (PHP)		
Over	**Up to**	**Excise tax rate (%)**
0	600,000	4
600,000	1,000,000	10
1,000,000	4,000,000	20
4,000,000		50

Hybrid vehicles shall be subject to 50% of the applicable excise tax rates.

Purely electric vehicles and pick-ups shall be exempt from excise tax.

Sweetened beverages

Description	Excise tax (PHP/litre)
Using purely caloric sweetener, purely non-caloric sweetener, or mixture of both	6.00
Using purely high-fructose corn syrup	12.00
Using purely coconut sap sugar / purely steviol glycosides	Exempt

Cigars and cigarettes

Effective date	Excise tax (PHP/pack)
1 January 2018	32.50
1 July 2018	35.00
1 January 2020	37.50
1 January 2022	40.00

Cosmetic procedures

5% excise tax is imposed on gross receipts from invasive cosmetic procedures and surgeries directly and solely towards altering or enhancing the patient's appearance for aesthetic purposes. However, this will not cover procedures necessary to ameliorate a deformity arising from, or directly related to, a congenital or developmental defect or abnormality, a personal injury resulting from an accident or trauma, or disfiguring disease, tumour, virus or infection.

Documentary stamp tax (DST)

DST is payable at varying rates on various documents and transactions. The following table contains selected examples as revised under the TRAIN law:

Taxable document/transaction (tax base)	DST rate
Original issue of shares	PHP 2.00 for every PHP 200 of the par value or actual consideration for no-par shares
Sale, barter, or exchange of shares of stock listed and traded through the local stock exchange	Exempt
Other sales agreement, agreement to sell, memoranda of sales, delivery or transfer of shares or certificates of stock	PHP 1.50 for every PHP 200 of the par value or 50% of the DST paid upon original issuance of no-par shares
Certificate of profits, interest in property or accumulations	PHP 1.00 for every PHP 200 of the face value
Non-exempt debt instruments	PHP 1.50 for every PHP 200 of the issue price.
Bank check, draft, certificate of deposit not bearing interest, other instruments	PHP 3.00 for each instrument
Deed of sale, conveyance of real property	PHP 15 for each PHP 1,000 of consideration/ value or fractional part thereof
Bills of exchange or drafts	PHP 0.60 on each PHP 200 of the issue price
Acceptance of bills of exchange and others	PHP 0.60 on each PHP 200 of the face value
Foreign bills of exchange and letters of credit	PHP 0.60 on each PHP 200 of the face value
Policies of annuities or other instruments	PHP 1.00 on each PHP 200 of premium or instalment payment
Pre-need plans	PHP 0.40 on each PHP 200 of the premium or contribution collected
Certificates	PHP 30.00 per certificate
Warehouse receipts	PHP 30.00 per warehouse receipt (valued at PHP 200 or more)
Jai-alai, horse race tickets, lotto, or other authorised number games	PHP 0.20 on every PHP 1.00 cost of the ticket
Bills of lading or receipts	Exempt if bill/receipts not exceeding PHP 100; PHP 2.00 for bill/receipts not exceeding PHP 1,000; or PHP 20.00 for bill/receipts exceeding PHP 1,000
Proxies	PHP 30.00 on each proxy of voting
Powers of attorney	PHP 10.00 on each power of attorney; except acts connected with claims due to/from the government
Leases and other hiring agreements	PHP 6.00 for the first PHP 2,000 + PHP 2.00 for every PHP 1,000 thereafter
Mortgages, pledges, and deeds of trust	PHP 40.00 for the first PHP 5,000 + PHP 20.00 on every PHP 5,000 thereafter

DST on life insurance policies

Life insurance policy (PHP)	DST (PHP)
Does not exceed 100,000	Exempt
Exceeds 100,000 but does not exceed 300,000	20.00
Exceeds 300,000 but does not exceed 500,000	50.00
Exceeds 500,000 but does not exceed 750,000	100.00
Exceeds 750,000 but does not exceed 1,000,000	150.00
Exceeds 1,000,000	200.00

DST on charter party and similar instruments

Registered tonnage	DST rate
Does not exceed 1,000 tons	PHP 1,000 + an additional tax of PHP 100 for each month or fraction of a month in excess of 6 months

Registered tonnage	DST rate
Exceeds 1,000 tons and does not exceed 10,000 tons	PHP 2,000 + an additional tax of PHP 200 for each month or fraction of a month in excess of 6 months
Exceeds 10,000 tons	PHP 3,000 + an additional tax of PHP 300 for each month or fraction of a month in excess of 6 months

Capital gains tax

Capital gains arise from the sale or exchange of 'capital assets'. Capital assets are property held by the taxpayer (whether or not connected with its trade), other than the following:

- Inventories or property held primarily for sale to customers in the ordinary course of business.
- Real property or depreciable property used in trade or business.
- Property of a kind that would be included in the inventory of the taxpayer if on hand at the close of the taxable year.

Capital losses are deductible only to the extent of capital gains.

There are no holding period requirements for capital assets of corporations.

A 6% final tax is imposed on the higher of the gross selling price or fair market value upon the sale, exchange, or disposition of land or buildings not actually used in the business of a corporation. The tax is withheld by the buyer at the time of sale.

Net capital gains derived from the sale, exchange, transfer, or similar transactions of shares of stock not traded through a local stock exchange are now taxed at a flat 15% rate under the TRAIN law. This new rate only applies to domestic corporations. For foreign corporations, the old rates are applicable (i.e. 5% on the first PHP 100,000 of gains, and 10% on gains in excess of PHP 100,000). Sales of shares of stock listed and traded on a local stock exchange, other than the sale by a dealer in securities, are subject to a stock transaction tax of 0.5% based on the gross selling price, provided the listed corporation observes a minimum public ownership of at least 10% based on the company's issued and outstanding shares, exclusive of any treasury shares or such percentage as may be prescribed by the Securities and Exchange Commission (SEC) or Philippine Stock Exchange (PSE), whichever is higher; otherwise, the 5%/10% tax shall apply.

Capital gains from the sale of bonds, debentures, or other certificates of indebtedness with a maturity of more than five years are exempt from tax.

A tax is levied on every sale, barter, exchange, or other disposition through an initial public offering (IPO) of shares of stock in closely held corporations. A 'closely held corporation' is any corporation of which at least 50% in value of the total outstanding capital stock, or at least 50% of the total combined voting power of all classes of stock entitled to vote, is owned directly or indirectly by, or for, not more than 20 individuals. The tax rates provided hereunder are based on the proportion of the gross selling price, or gross value in money, of the shares of stock sold, bartered, exchanged, or otherwise disposed of to the total outstanding shares of stock after listing on the local stock exchange.

Proportion of sale to total shares	Tax rate (%)
25% or less	4
Over 25% but not over 33.33%	2
Over 33.33%	1

Payroll taxes

There are no payroll taxes other than social security contributions (*see below*).

Social security contributions

Corporations doing business in the Philippines must be registered with social institutions, such as the Social Security System (SSS), Home Development Mutual Fund (HDMF), and Philippine Health Corporation (PHIC), upon employment of any employee and prior to the due date of the remittance of any social contributions.

Employee contributions for social security are deducted from the employee's salary payments. For 2018, the maximum monthly deductions remain at PHP 581.30 for SSS, PHP 100 for HDMF, and PHP 550.00 for PHIC.

Employers are also required to make contributions. Employers' maximum contribution for each employee is PHP 1,178.70 per month for SSS. Employer contributions for HDMF and PHIC are generally of the same amount as the employee contributions.

Fringe benefits tax

Under the TRAIN law, a final tax of 35%, payable by the employer, is imposed on the grossed-up monetary value of fringe benefits (e.g. housing, expense accounts, vehicles of any kind, household personnel, interest on loans at lower than market rates [the current benchmark rate is 12%], membership dues for social and athletic clubs, foreign travel expenses, holiday and vacation expenses, educational assistance, insurance) furnished or granted to managerial or supervisory personnel by the employer. An exception is for fringe benefits required by the nature of or necessary to the trade, business, or profession of the employer, or when the fringe benefit is for the convenience or advantage of the employer.

The following fringe benefits are not subject to the tax:

- Those authorised and exempted from tax under special laws.
- Contributions of the employer for the benefit of the employee to retirement, insurance, and hospitalisation benefit plans.
- Those granted to rank-and-file employees (however, the employees may be subject to WHT on compensation).
- Those of relatively small value or *de minimis* benefits.

The fringe benefits tax is payable on a calendar quarter basis and is an additional deductible expense for the employer. Fringe benefits already subjected to fringe benefits tax will no longer form part of the employee's taxable income.

The grossed-up monetary value of the fringe benefit is generally computed by dividing the actual monetary value of the benefit by 65%.

Donor’s taxes

Donor’s tax is a tax on a donation or gift, and is imposed on the gratuitous transfer of property. It shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Under the TRAIN law, the donor’s tax rate is fixed at 6% based on total gifts in excess of PHP 250,000 made during the calendar year whether the donee is a stranger or not.

Local government taxes

Local government units impose local business taxes, which are generally based on the gross sales or gross receipts of the prior year, and real property taxes, which are levied annually on the basis of a fixed proportion of the value of the real property (taxable value). The local business tax rate varies depending on the location of the business, but generally shall not exceed 3%. Real property located in a province may be subject to real property tax of not more than 1% of its taxable value, while real property in a city (or municipality in Metro Manila) may be subject to real property tax of not more 2% of its taxable value.

Branch income

The income tax rate on branch profits is the same as on corporate profits. In general, profits remitted abroad by a branch office are subject to a 15% tax rate, based on the total profits applied or earmarked for remittance, without any deduction for the tax component thereof. A lower rate may apply under certain tax treaties. Profits from qualified activities remitted by a branch registered with the Philippine Economic Zone Authority (PEZA) are tax exempt.

Income determination

Inventory valuation

Inventories are generally stated at cost or at the lower of cost or market. Last in first out (LIFO) is not allowed for tax purposes. Generally, the inventory valuation method for tax purposes must conform to that used for financial reporting purposes.

Capital gains

Capital gains are not generally subject to CIT, but may be subject to capital gains tax. *See Capital gains tax in the Other taxes section for more information.*

Dividend income

Dividends received by a domestic or resident foreign corporation from another domestic corporation are not subject to tax. These dividends are excluded from the taxable income of the recipient.

Dividends received by a non-resident foreign corporation from a domestic corporation are subject to a general final WHT at the rate of 30%. A lower rate of 15% applies if the country in which the corporation is domiciled either does not impose income tax on such dividends or allows a tax deemed paid credit of 15%. Treaty rates ranging from 10% to 25% may also apply if the recipient is a resident of a country with which the Philippines has a tax treaty (*see the Withholding taxes section*).

Stock dividends

A Philippine corporation can distribute stock dividends tax-free, proportionately to all shareholders.

Interest income

Interest on bank savings, time deposits, deposit substitutes, and money market placements received by domestic or resident foreign corporations from a domestic corporation are subject to a final tax of 20%, while interest income derived from FCDU deposits is subject to a final tax of 15% under the TRAIN law. Such income is excluded from gross income reportable in CIT returns.

Interest income of OBUs and FCDUs from foreign currency loans granted to residents other than OBUs or local commercial banks shall be subject to 10% tax.

Royalty income

Royalties received by domestic or resident foreign corporations from a domestic corporation are subject to a final tax of 20%.

Other significant items

Other items exempt from CIT include the following:

- Proceeds of life insurance policies.
- Return of policy premium.
- Gifts, bequests, and devises.
- Interest on certain government securities.
- Income exempt under a treaty.
- Gains from sale, exchange, or retirement of bonds.
- Gains from redemption of shares of stock in mutual fund companies.

Foreign income

A Philippine (domestic) corporation is taxed on its worldwide income. A domestic corporation is taxed on income from foreign sources when earned or received, depending on the accounting method used by the taxpayer.

Income earned through a foreign subsidiary is taxed only when paid to a Philippine resident shareholder as a dividend. Meanwhile, income earned through a foreign branch is taxed as it accrues. The losses incurred by the foreign branch are deductible against other income earned by the Philippine corporation.

Double taxation is generally relieved through a credit for foreign taxes. However, a taxpayer can take a deduction for foreign taxes instead, if that leads to a more favourable outcome.

Deductions

Corporate taxpayers can avail themselves of the optional standard deduction computed at 40% of gross income. The optional standard deduction is *in lieu* of the itemised operating expenses.

Depreciation and depletion

Depreciation is generally computed on a straight-line basis, although any reasonable method may be elected if the aggregate amount of depreciation, plus salvage value at the end of the useful life of the property, will equal the cost of the property. Gain on the sale of depreciated property is taxable as ordinary income. Generally, tax depreciation should conform to book depreciation, unless the former includes incentives.

Properties used in petroleum operations may be depreciated over a period of ten years using the straight-line or declining-balance method, at the option of the service contractor. Properties used in mining operations with expected life of more than ten years may be depreciated over any number of years between five years and their expected life.

A cost depletion allowance is available as follows:

- For oil and gas wells, depletion is based on actual reduction in flow and production ascertained, not by flush flow, but by the settled production or regular flow.
- For mines, depletion is allowable up to an amount not to exceed the market value, as used for purposes of imposing the mining *ad valorem* taxes, of the products mined and sold during the year.

Goodwill

Goodwill is not deductible for tax purposes.

Start-up expenses

Start-up expenses are deductible when incurred.

Interest expenses

The allowable deduction for interest expense is reduced by an amount equal to 33% of interest income that is subject to final tax.

Bad debts

Bad debts are deductible expenses when written-off, subject to certain requirements.

Charitable contributions

The deduction for charitable contributions ordinarily may not exceed 5% of taxable income. However, contributions to certain institutions are 100% deductible, subject to certain conditions.

Entertainment expenses

Entertainment, amusement, and recreation expenses should not exceed 0.5% of net sales for taxpayers engaged in the sale of goods or properties, or 1% of net revenue for taxpayers engaged in the sale of services, including professionals and lessors of properties.

Special deductions

Special deductions are allowed for certain businesses (e.g. insurance, mining, petroleum, and real estate investment trust).

Fines and penalties

Fines and penalties are deductible as necessary and ordinary business expenses. Surcharge and compromise penalty imposed for non-payment or late payment of taxes is not deductible for tax purposes.

Taxes

Corporate taxpayers can claim a deduction for all taxes paid or accrued within the taxable year in connection with their trade or business, except for the following:

- Philippine CIT.
- Income taxes imposed by authority of any foreign country, unless the taxpayer elects to take a deduction *in lieu* of a foreign tax credit.
- Donor's taxes.
- Taxes assessed against local benefits of a kind tending to increase the value of the property assessed.

In the case of a foreign corporation, deductions for taxes are allowed only if they are connected with income from sources within the Philippines.

Net operating losses

A net operating loss for any taxable year immediately preceding the current taxable year, which had not been previously offset as a deduction from gross income, may be carried over as a deduction from gross income for the next three consecutive taxable years immediately following the year of this loss (except losses during the period when the taxpayer was tax-exempt), provided there has been no substantial change in the ownership of the business or enterprise.

For mines, other than oil and gas wells, a net operating loss calculated without the benefit of incentives provided for under Executive Order (EO) No. 226, or the Omnibus Investments Code of 1987, as amended, incurred in any of the first ten years of operation may be carried over as a deduction from taxable income for the next five years immediately following the year of such loss.

Loss carrybacks are not allowed.

Payments to foreign affiliates

A Philippine corporation can claim a deduction for royalties, management service fees, and interest charges paid to foreign affiliates, provided such amounts are equal to what it would pay an unrelated entity, and the appropriate WHTs are withheld and remitted.

The registration of licensing and management agreements, now known as technology transfer arrangements (TTAs), has been liberalised. Only TTAs not conforming to certain provisions of the Intellectual Property Code require approval by, and registration with, the Documentation, Information, and Technology Transfer Bureau of the Intellectual Property Office (formerly Bureau of Patents, Trademarks, and Technology Transfer) to render the contracts enforceable.

Head office expense allocations

A resident foreign corporation is allowed to claim allocated head office expenses as a deduction, subject to certain requirements.

Group taxation

There is no group taxation in the Philippines.

Transfer pricing

Transfer Pricing Regulations govern the cross-border and domestic transactions between associated enterprises. The Regulations state that the 'arm's-length principle' shall be adopted in determining the transfer price in related-party transactions. The application of the arm's-length principle may follow a 'three-step' approach prescribed by the BIR under the Regulations, to wit: (i) the conduct of a comparability analysis, (ii) the identification of the tested party and the appropriate transfer pricing method, and (iii) the determination of the arm's-length results.

Taxpayers must keep adequate documentation supporting their transfer prices so that they can defend their transfer pricing analysis, mitigate the risk of transfer pricing adjustments arising from tax examinations, and support their applications for Mutual Agreement Procedure (MAP). There is also a 'contemporaneous' requirement that transfer pricing documents must exist or be brought into existence at the time the taxpayers develop or implement any arrangements that may raise transfer pricing issues. This can generally mean that while transfer pricing documentation is not required to be submitted together with the tax returns, such documents should be retained and submitted to the BIR when required or requested. There is no prescribed period within which such documentation may be made available, but it should be available in cases of audit/investigation.

An Advance Pricing Arrangement (APA) is an agreement entered into between the taxpayer and the BIR to determine in advance an appropriate set of criteria (e.g. method, comparables, appropriate adjustments thereto) to ascertain the transfer prices of controlled transactions over a fixed period of time. It is currently available to taxpayers, but the BIR is still in the process of drafting more detailed guidelines. The APA is not mandatory, but may be advisable since the purpose of the APA is to reduce the risk of transfer pricing re-examination and double taxation.

Transactions entered into prior to the Transfer Pricing Regulations becoming effective in February 2013 shall be governed by the laws and other administrative issuances prevailing at the time the controlled transactions were entered into.

Thin capitalisation

There are generally no thin capitalisation rules in the Philippines.

Controlled foreign companies (CFCs)

There are no CFC rules in the Philippines.

Tax credits and incentives

Foreign tax credit

Domestic corporations are allowed to claim a credit for any income taxes paid to a foreign country, provided that the taxes are not claimed as deductions. Foreign corporations are not allowed foreign tax credits.

Credits for foreign taxes are determined on a country-by-country basis. The amount of foreign tax credit in respect of the tax paid in a country shall not exceed the same proportion of the tax against which the tax credit is taken, which the taxpayer's income from the country bears to its entire taxable income. There is, however, a further limitation based on the total amount of foreign-sourced income that the taxpayer earns. The total amount of foreign tax credits shall not exceed the same proportion of the tax against which the tax credit is taken that the taxpayer's foreign-sourced income bears to its entire taxable income.

Export incentives

Tax incentives available to export enterprises registered with the Board of Investments (BOI) are as follows:

- Income tax holiday (ITH) giving full exemption from CIT for six years for pioneer firms and those locating in less-developed areas and four years for non-pioneer firms. The ITH period starts to run from the date of commercial operation, or target date of operation, whichever is earlier. If prescribed conditions are met, the ITH period may be extended by up to three years. In no case, however, can the total ITH period exceed eight years. Expanding export-oriented firms are also allowed a three-year ITH on the incremental income. Subject to certain exceptions, new and expansion projects located in the National Capital Region (NCR) or Metro Manila are no longer entitled to ITH.
- Tax and duty exemption on imported spare parts and supplies for export producers with a customs bonded manufacturing warehouse exporting at least 70% of annual production, if foreign-owned, or 50%, if Filipino-owned.
- Full deduction of the cost of major infrastructure undertaken by enterprises in less-developed areas.
- Additional deduction of 50% of the incremental labour expense if the prescribed ratio of capital assets to annual labour is met and 100% of the incremental labour if located in less-developed areas within five years from date of registration (this incentive cannot be availed of simultaneously with the ITH).
- Ten-year exemption from taxes and duties on importation of breeding stock and genetic materials.
- Tax credit on domestic breeding stocks and genetic materials (ten years).
- Exemption from wharfage, any export tax, duty, impost, or fees.
- Tax credits equivalent to taxes and duties paid on purchases of raw materials, supplies, and semi-manufactured products forming part of the products for export.

Other incentives

Export and free-trade enterprises, information technology (IT) enterprises, and special economic zone developers/operators (including IT buildings located in Metro Manila and IT parks) registered with PEZA are entitled to an ITH of six years for pioneer firms and four years for non-pioneer firms. Foreign articles brought into the zones will be exempt from import duties and taxes. Local purchases of goods from VAT-registered suppliers outside the economic zones are zero-rated. After the lapse of the ITH period, enterprises registered and operating within special economic zones/export processing zones will pay only a 5% special tax on gross income earned from registered activities *in lieu* of all local and national taxes.

A regional or area headquarters established in the country as a supervisory, communications, and coordination centre for a corporation's subsidiaries, affiliates, and branches in the Asia-Pacific region, and whose headquarters do not derive income from the Philippines, are not subject to any CIT nor VAT and are entitled to certain non-tax incentives.

An ROHQ that is allowed to derive income in the Philippines by performing qualifying business services to its affiliates, subsidiaries, or branches in the Philippines, in the Asia-Pacific Region, and other foreign markets may avail itself of the following incentives:

- Income tax at the preferential rate of 10% of its taxable income.
- Exemption from all kinds of local taxes, fees, or charges imposed by a local government unit, except real property tax on land improvements and equipment.
- Tax and duty-free importation of equipment and materials for training and conferences that are needed and used solely for its functions as an ROHQ and are not locally available, subject to the prior approval of the BOI.
- Importation of new motor vehicles, subject to the payment of corresponding duties and taxes.
- Exemption from travel tax, specific immigration fees, and requirements, subject to certain conditions.

The following are the incentives granted to exporters under the Export Development Act (Republic Act [RA] No. 7844):

- Exemption from Presidential Decree No. 1853 (requiring 100% of Letter of Credit), provided that the importation shall be used for the production of goods and services for export.
- Tax credit for incremental export performance. The tax credit for increase in current export revenues shall be computed as a percentage to be applied on the incremental export revenue converted to pesos at the current rate. The percentages or rates are as follows:
  - For the first 5% increase in annual export revenues over the previous year: 2.5%.
  - For the next 5% increase: 5.0%.
  - For the next 5% increase: 7.5%.
  - In excess: 10%.

  Note that this incentive is not available for exporters enjoying ITH or VAT exemption or whose local VAT is below 10%.

- In addition to the above incentives, all existing incentives being enjoyed by the enterprise if registered with the BOI, PEZA, Subic Bay Metropolitan Authority (SBMA), Clark Development Corporation (CDC), or other ecozone regulating agencies.

Withholding taxes

Corporations and individuals engaged in business are required to withhold the appropriate tax on income payments to non-residents, generally at the rate of 30% in the case of payments to non-resident foreign corporations or 25% for non-resident aliens not engaged in trade or business. *For WHT on resident corporations, see the discussions in the Income determination section*.

Tax treaty rates

For countries with which the Philippines has concluded tax treaties, the maximum rates of taxes to be withheld are as follows:

As of 16 March 2018:

	WHT (%)		
Recipient	**Dividends (1)**	**Interest (2)**	**Royalties**
Non-treaty	15/30 (12)	30	30
Treaty:			
Australia	15/25 (3, 4)	10/15 (5)	15/25 (6)
Austria	10/25 (7)	10/15 (5, 8)	10/15 (6, 9)
Bahrain	10/15 (7)	10	10/15 (10)
Bangladesh	10/15 (11)	15	15
Belgium	10/15 (7)	10	15
Brazil	15/25 (25)	10/15 (5)	15/25 (6)
Canada	15/25 (3, 7)	10/15 (5)	25 (9)
China, People's Republic of	10/15 (7)	10	10/15 (13)
Czech Republic	10/15 (7)	10	10/15 (14)
Denmark	10/15 (11)	10	15
Finland	15 (3, 7)	10/15 (5)	15/25 (15)
France	10/15 (3, 7)	10/15 (5)	15
Germany	5/10/15 (11, 24)	10	10
Hungary	15/20 (3, 11)	15	15 (9)
India	15/20 (3, 7)	10/15 (5, 17)	15/30 (6)
Indonesia	15/20 (3, 11)	10/15 (5)	15/25 (6)
Israel	10/15 (7)	10	15 (9)
Italy	15	10/15 (5)	15/25 (6, 18)
Japan	10/15 (3, 7)	10	10/15 (19)
Korea, Republic of	10/25 (11)	10/15 (5)	10/15 (6)
Kuwait	10/15 (7)	10	20
Malaysia	15/25 (26)	15	15/25 (6, 18)
Netherlands	10/15 (7)	10/15 (5, 16, 17)	10/15 (6)
New Zealand	15	10 (5)	15
Nigeria	12.5/15 (7)	15	20
Norway	15/25 (3, 7)	15	7.5/10/25 (9, 20)
Pakistan	15/25 (3, 11)	10/15 (5)	15/25 (6)
Poland	10/15 (11)	10	15
Qatar	10/15 (7)	10	15
Romania	10/15 (11)	10/15 (5, 16, 17)	10/15/25 (21)
Russia	15	15	15
Singapore	15/25 (3, 22)	10/15 (5)	15/25 (6, 18)
Spain	10/15 (7)	10/15 (5, 16)	10/15/20 (23)
Sweden	10/15 (11)	10	15
Switzerland	10/15 (7)	10	15
Thailand	15	10/15/25 (5)	15/25 (6, 18)
Turkey	10/15 (11)	10	10/15 (13, 19)
United Arab Emirates	10/15 (7)	10	10
United Kingdom	15/25 (3, 7)	10/15 (5)	15/25 (6, 19)
United States	20/25 (3, 7)	10/15 (5)	15/25 (6, 9)
Vietnam	10/15 (11)	15	15

Notes

1. The lower rate generally applies if the beneficial owner of the dividends is a company with a substantial ownership in the dividend paying company.
2. Interest derived by a foreign government or its agencies is typically exempt from Philippine tax. Many treaties also contain special rules for both Philippine and home country taxation of interest paid on instruments secured by a government agency of one of the countries. Such provisions have been excluded from the analysis.
3. A 15% rate applies under domestic law if the home country exempts the dividend from tax or permits a 15% or greater credit for corporate taxes paid by the company paying the dividend.
4. Entitlement to the lower rate depends on how the dividend will be taxed in Australia.
5. The 10% rate applies to interest paid in respect of the public issues of bonds, debentures, or similar obligations.
6. The lower rate applies to royalties paid by an enterprise registered with the Philippine BOI and engaged in preferred areas of activity.
7. The threshold for substantial ownership is 10%.
8. The 10% rate also applies to interest paid by a company registered with the BOI and engaged in preferred pioneer areas of investment in the Philippines.
9. The treaty also contains a most-favoured-nation rule, limiting the Philippine tax on royalties to the lowest rate of Philippine tax that may be imposed on royalties of the same kind paid in similar circumstances to a resident of a third state.
10. The 15% rate applies to royalties arising from the use of, or the right to use, any copyright of literary, artistic, or scientific work including cinematograph films or tapes for television or broadcasting.
11. The threshold for substantial ownership is 25%.
12. *For a description of when each rate applies, see Dividend income in the Income determination section.*
13. The 10% rate applies to the use of, or the right to use, any patent, trademark, design or model, plan, secret formula or process, or from the use of, or the right to use, industrial, commercial, or scientific equipment, or for information concerning industrial, commercial, or scientific experience. Strictly, application of the rate is generally at the discretion of the Philippine Competent Authorities, but the BIR has never raised this as an issue.
14. The 10% rate applies to royalties arising from the use of, or the right to use, any copyright of literary, artistic, or scientific work (other than copyright of cinematograph films), any patent, trademark, design or model, plan, secret formula or process, or from the use of, or the right to use, industrial, commercial, or scientific equipment, or for information concerning industrial, commercial, or scientific experience.
15. The 15% rate applies to royalties paid by an enterprise registered and engaged in preferred areas of activities, and to royalties in respect of cinematographic films or tapes for television or broadcasting, and for the use of, or the right to use, any copyright. The 25% rate applies to other royalties.
16. The 10% rate also applies to interest paid in connection with the sale on credit of any industrial, commercial, or scientific equipment.
17. The 10% rate also applies to interest paid on any loans granted by a bank.
18. The 15% rate also applies to royalties in respect of cinematographic films or tapes for television or broadcasting.
19. The 15% rate applies to royalties paid for the use of, or the right to use, cinematographic films and films or tapes for radio or television broadcasting.
20. The 7.5% rate applies to the lease of containers. The 10% rate applies to royalties paid by an enterprise registered with the BOI. The 25% rate applies to other royalties.
21. The 10% rate applies to royalties paid by an enterprise registered with the BOI and engaged in preferred pioneer areas of activity. The 15% rate applies to rentals from cinematographic films and tapes for television or broadcasting. The 25% rate applies to all other royalties.
22. The threshold for substantial ownership is 15%.
23. The 10% rate applies to royalties paid by an enterprise registered with the BOI and engaged in preferred pioneer areas of activity. The 20% rate applies to rentals from cinematographic films and tapes for television or broadcasting. The 15% rate applies to all other royalties.
24. The threshold for substantial ownership is 70% for the 5% rate to apply.
25. The 15% rate applies if the recipient is a company, including a partnership.
26. The 15% rate applies if the recipient is a company.

Tax administration

Taxable period

The accounting period must follow a 12-month fiscal period but may or may not follow the calendar year. Most Philippine companies have a fiscal year that ends in December or March.

Tax returns

Corporations should file their returns and compute their income on the basis of an accounting period of 12 months.

Corporate taxpayers file self-assessed returns. Electronic filing and payment of taxes are available under the Electronic Filing and Payment System (eFPS) of the BIR.

The following corporate taxpayers who are not covered by eFPS are required to use Electronic BIR Forms (eBIRForms) in filing their tax returns:

- Accredited tax agents/practitioners and all their client-taxpayers who authorised them to file on their behalf.
- Accredited printers of principal and supplementary receipts/invoices.
- One-time transaction taxpayers.
- Those who shall file a 'No Payment' return, except senior citizens or persons with disabilities filing their own return, employees deriving purely compensation income and the income tax of which has been withheld correctly, employees qualified for substituted filing but opted to file for an income tax return and are filing for purposes of promotion (Philippine National Police and Armed Forces of the Philippines), loans, scholarships, foreign travel requirements, etc.
- Government-owned or controlled corporations.
- Local government units, except barangays.
- Cooperatives registered with the National Electrifications Administration and Local Water Utilities Administrations.

Taxpayers who are required to file their returns using eFPS or eBIRForms but fail to do so shall be subject to a penalty of PHP 1,000 per return and civil penalties equivalent to 25% of the tax due.

A domestic or resident foreign corporation is required to file income tax returns on a quarterly basis. Within 60 days from the close of the first three quarters of its taxable year, the corporation must file a return summarising its gross income and deductions for the year to date. A final annual income tax return must be filed on or before the 15th day of the fourth month following the close of the taxable year.

Corporate taxpayers must file their income tax returns using one of three different forms, depending on their tax regime (i.e. subject only to the regular income tax, tax exempt, or with mixed income subject to multiple tax rates or special/preferential rates).

Payment of tax

Every corporation files cumulative quarterly income tax returns for the first three quarters and pays the tax due within 60 days after each quarter. A final adjustment return covering the total taxable income of the preceding taxable year must be filed on the 15th day of the fourth month following the close of the taxable year. The balance of the tax due after deducting the quarterly payments must be paid, while the excess may be claimed as a refund or tax credit. Excess estimated quarterly income taxes paid may be carried over and credited against estimated quarterly income tax liabilities for succeeding taxable years. Once the option to carry over has been made, such option is irrevocable, and no cash refund or tax credit certificate (TCC) is allowed, except upon liquidation of the company.

Since additional modes of payment of taxes are now available through credit, debit, and prepaid cards under recently issued Revenue Regulations, taxpayers may choose from the available online payment facilities provided by the Electronic Payment Service Provider (EPSP) to process tax payments. However, only accredited Authorised Agent Banks (AABs) may accept such payments, and accreditation of AABs is subject to compliance with certain conditions under existing Regulations.

Payment of taxes through the Card Payment Facility shall be deemed made on the date and time appearing in the system-generated payment confirmation receipt issued to the taxpayer-cardholder by the AAB-acquirer, provided that the payment was actually received by the BIR. The taxpayer is not relieved of, and has a continuing liability for, such taxes until the payment is actually received by the BIR.

Annual statutory audit

An annual statutory audit is required for all corporations with authorised capital stock or paid-up capital exceeding PHP 50,000, including branches of foreign corporations. It is also required for any corporation whose gross sales or earnings exceed PHP 150,000 in any quarter.

Statute of limitations

There is no statutory obligation on the Tax Commissioner to make an assessment for internal revenue taxes, and most taxes are collected based on the taxpayer's self-calculation. If an assessment is to be issued, however, it must be done within three years from the deadline or the date of actual filing of the return, whichever is later. The taxpayer and the Commissioner can, however, agree in writing to extend this period.

In the case of a false or fraudulent return or of failure to file a return, the tax may be assessed or a proceeding in court for collection may be commenced without assessment at any time within ten years from the discovery of the falsity, fraud, or omission.

Any internal revenue tax that has been assessed within the period of limitation may be collected by distraint or levy or by a proceeding in court within five years following the assessment of the tax.

The prescription periods are suspended in certain circumstances, such as when the offender is absent from the Philippines, when the Commissioner grants a taxpayer's request for a reinvestigation, or when the taxpayer and the BIR agree to extend the prescriptive period for assessment through a written waiver.

In the case of overpayment of tax, a claim for refund or credit may be filed with the BIR within two years from the date of erroneous payment of the tax. If the claim is denied or no decision is received from the BIR, a petition for review may be filed with the Court of Tax Appeals (CTA). This must be filed before the two-year period expires, and in the case of a denied claim, within 30 days from the receipt of the denial.

Topics of focus for tax authorities

During audits, the BIR generally covers all applicable internal revenue taxes. With the issuance of certain regulations in recent years, assessment issues involving transfer pricing, inter-company advances, donor's tax, and improperly accumulated earnings tax have become more prevalent.

Other issues

United States (US) Foreign Account Tax Compliance Act (FATCA)

Under FATCA, financial institutions outside the United States shall report each year to the US Internal Revenue Service (IRS) information about accounts held by US citizens. The said financial institutions that fail to comply with FATCA are subject to a 30% WHT on US-sourced 'fixed, determinable, annual, or periodic income', which shall be withheld by their counterparties in the United States.

In the absence of an intergovernmental agreement (IGA), participating foreign financial institutions (FFIs) in the Philippines individually signed an FFI Agreement with the IRS.

Under Model 1 of the IGA, FFIs will provide information on US accounts to the BIR, which information will be relayed to the IRS.

Currently, Model 1 of the IGA is treated as 'in effect' by the US Treasury as of 30 November 2014. The United States and the Philippines have reached an agreement in substance, and the Philippine government has consented to disclose this status. In accordance with this status, the text of such IGA has not been released and financial institutions in the Philippines are allowed to register on the FATCA registration website consistent with the treatment of having an IGA in effect, provided that the jurisdiction continues to demonstrate firm resolve to sign the IGA as soon as possible.

On 1 December 2016, President Duterte ratified the agreement that was then transmitted to the Senate on 6 December 2016 for concurrence but with no available status to date.

Singapore

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Significant developments

The 2018 Budget was announced on 19 February 2018. Corporate tax changes include the following:

Key corporate tax changes include:

- Enhancement of the tax rebate for year of assessment 2018 (income year 2017) to 40% of tax payable, capped at 15,000 Singapore dollars (SGD), and extension of the rebate to year of assessment 2019 at 20% of tax payable, capped at SGD 10,000.
- Adjustments to the Partial Tax Exemption and Start-up Tax Exemption schemes from year of assessment 2020, which reduce the maximum exempt income to SGD 102,500 (previously SGD 152,000) and SGD 125,000 (previously SGD 200,000), respectively.
- Introduction of a 250% tax deduction for qualifying research and development (R&D) projects performed in Singapore, and 200% tax deductions for the first SGD 100,000 of qualifying intellectual property (IP) registration costs and the first SGD 100,000 of qualifying IP licensing costs.
- Introduction of investment allowances for submarine cable systems landing in Singapore.
- Higher cap for double deduction for prescribed travelling expenses (for which no prior approval is needed) under the Double Tax Deduction for Internationalisation scheme.
- Introduction of a tax framework for Singapore Variable Capital Companies (S-VACC).
- Tax transparency for specified income of Singapore-listed Real Estate Investment Trusts Exchange-Traded Funds (REIT-ETFs).
- Extension of the Enhanced-Tier Fund scheme to all forms of fund vehicles.
- Rationalisation of the withholding tax (WHT) exemptions for the financial sector.

Other Budget changes include the following:

- Introduction of a goods and services tax (GST) reverse charge on services imported by businesses that make exempt supplies or those that do not make any taxable supplies with effect from 1 January 2020.
- Requirement for overseas vendors providing digital services to register for GST with effect from 1 January 2020 if their global turnover is more than SGD 1 million annually and their online sales to Singapore consumers exceed SGD 100,000.
- Increase GST rate from 7% to 9% sometime between 2021 and 2025.
- Increase in buyer's stamp duty for residential property purchases.
- Introduction of carbon tax of SGD 5 per tonne of greenhouse gas emissions.

For details of the 2018 Budget proposals, refer to our 2018 Budget Commentary at *https://www.pwc.com/sg/en/publications/budget-commentary.html*

Taxes on corporate income

Companies (resident and non-resident) that carry on a business in Singapore are taxed on their Singapore-sourced income when it arises and on foreign-sourced income when it is remitted or deemed remitted to Singapore. Non-residents are subject to WHT on certain types of income (e.g. interest, royalties, technical service fees, rental of movable property) where these are deemed to arise in Singapore (*for details, see the Withholding taxes section*).

Tax on corporate income is imposed at a flat rate of 17%.

A partial tax exemption and a three-year start-up tax exemption for qualifying start-up companies are available.

Partial tax exemption (income taxable at normal rate):

Years of assessment 2018 to 2019			Year of assessment 2020 onwards		
Chargeable income (SGD)	Exempt from tax	Exempt income (SGD)	Chargeable income (SGD)	Exempt from tax	Exempt income (SGD)
First 10,000	75%	7,500	First 10,000	75%	7,500
Next 290,000	50%	145,000	Next 190,000	50%	95,000
Total		152,000	Total		102,500

Start-up tax exemption (income taxable at normal rate):

Years of assessment 2018 to 2019			Year of assessment 2020 onwards		
Chargeable income (SGD)	Exempt from tax	Exempt income (SGD)	Chargeable income (SGD)	Exempt from tax	Exempt income (SGD)
First 100,000	100%	100,000	First 100,000	75%	75,000
Next 200,000	50%	100,000	Next 100,000	50%	50,000
Total		200,000	Total		125,000

The start-up exemption is not available to property development and investment holding companies.

In addition, for the year of assessment 2018, there is a 40% corporate tax rebate. This rebate is capped at SGD 15,000. There is also a rebate of 20% of tax payable for year of assessment 2019, which is capped at SGD 10,000.

Singapore adopts a one-tier taxation system, under which all Singapore dividends are tax-exempt in the shareholder's hands.

Corporate residence

In Singapore, the tax residence of a corporation is determined by the place where the central management and control of its business is exercised. This is taken generally to mean the place where the directors meet to exercise *de facto* control. The Inland Revenue Authority of Singapore (IRAS) has also set out further guidance.

Permanent establishment (PE)

The presence of a PE is largely irrelevant, except for treaty purposes, as Singapore taxes with reference to the source of income rather than the presence of a PE.

However, a PE is a clear indication of source.

The definition of a PE in Singapore's double taxation agreements (DTAs) is largely based on the Organisation for Economic Co-operation and Development (OECD) Model Tax Convention definition.

It is generally taken to be a fixed place through which the business of an enterprise is wholly or partly carried on, and normally includes a place of management, a branch, an office, a factory, a workshop, and a place of extraction of natural resources, etc.

In addition, and subject to the terms of the relevant agreements, a non-resident may have a PE in Singapore if one:

- has a building site or a construction, assembly, or installation project that lasts longer than a specified period, or supervisory activities connected with the building site or construction project
- furnishes services (including consultancy services) through employees in Singapore for more than a specified period, or
- has an agent in Singapore who has, and habitually exercises, a general authority to negotiate and conclude contracts on behalf of the enterprise.

The Singapore tax legislation defines a PE more broadly than most of the DTAs; however, as mentioned above, this is largely irrelevant where a treaty can take precedence.

Other taxes

Goods and services tax (GST)

GST is charged at 7% on the supply of goods and services made in Singapore by a taxable person in the course or furtherance of one's business. It was announced in the 2018 Budget that this rate would be increased to 9% sometime between 2021 and 2025.

The only exemptions from GST are prescribed financial services (including life insurance), the sale or rental of residential properties, and the import and local supply of investment precious metals (IPM). Zero-rating only applies to the export of goods and international services.

GST is also levied on imports of goods, at the time of importation. However, there are reliefs available to ease the cash-flow burden of import-export traders by suspending GST at the time of importation. GST is not currently charged on imports of services, although this will change from 1 January 2020 with the introduction of a reverse-charge on local businesses that make exempt supplies, and those which do not make any taxable supplies, to account for GST on the services they import. A non-registered business that imports services exceeding SGD 1 million in a year and is not entitled to full input tax credit if it were GST-registered will be required to register for GST to account for the reverse charge under the new rules. These businesses can in turn claim the GST accounted for as their input tax, subject to the normal rules for input tax recovery. In addition, overseas suppliers and electronic marketplace operators that make significant supplies of digital services to local consumers will be required to register for GST in Singapore.

A taxable person is one who is, or is required to be, registered for GST. GST registration is required if one's taxable turnover exceeds SGD 1 million per year. Voluntary registration is permitted if the taxable turnover is below the registration threshold, subject to conditions.

A supply of goods is made in Singapore if the goods are in Singapore at the time of supply, and a supply of services is made in Singapore if the supplier belongs in Singapore. Generally, a person belongs in Singapore if one's business establishment (including carrying on a business through a branch or agency) or fixed establishment is in Singapore.

A taxable person is allowed to credit the input GST paid on taxable purchases against the output GST chargeable on taxable supplies made. However, certain purchases are specifically denied an input GST deduction. These include supplies of goods and services such as non-business expenses, club subscription fees, family benefits, car rental expenses, motor vehicle expenses, medical expenses, and transactions involving betting, sweepstakes, lotteries, fruit machines, or games of chance.

A non-resident is not entitled to GST refunds except by appointing a resident business that is registered for GST to act on one's behalf. The resident tax agent can then recover import GST paid on behalf of the non-resident business but will be required to account for output GST on any subsequent supply of the non-resident's goods in Singapore.

Customs and excise duties

Singapore is essentially a free port with minimal import restrictions. Customs and excise duties are imposed on intoxicating liquors, tobacco products, motor vehicles, and petroleum products.

Property tax

Property tax is levied annually on the annual value of houses, land, buildings, or tenements.

For residential properties, owner-occupier tax rates range from 0% to 16% and non-owner occupier tax rates range from 10% to 20%. The tax rates depend on the annual value bands.

For non-residential properties, such as commercial and industrial buildings and land, the tax rate is 10%.

Stamp duties

Stamp duties are levied on written documents relating to immovable properties, leases, and stocks and shares.

Immovable properties

Stamp duties are typically payable by the buyer (i.e. buyer's stamp duty or BSD); however, seller's stamp duty (SSD) and additional buyer's stamp duty (ABSD) have been introduced as measures to cool the residential property market.

There is BSD of up to 4% on the purchase price or market value, whichever is the higher. There is an ABSD of up to 15% and an SSD of up to 15% on the price or market value of the property, whichever is the higher, depending on the type of property (residential or industrial), the residency status of the buyer, the holding period of the property, and the number of properties owned.

Foreigners of certain nationalities who fall within the scope of the respective free trade agreements will be accorded the same treatment as Singaporeans.

Certain transfers of equity interest in property holding entities (PHEs) that own (directly or indirectly) primarily Singapore residential properties could attract additional conveyance duty (ACD) for buyers and sellers who are significant owners (as defined) of PHEs, as well as for a buyer who would become a significant owner after acquiring an equity interest in the PHEs. For acquisition of equity interest in a company, share duty remains payable in addition to the ACD.

Leases

Leases attract duty at 0.4% of the total rent (for leases of up to four years) or 0.4% of four times the average annual rent for the period of the lease (for leases longer than four years), but leases with average annual rents not exceeding SGD 1,000 are exempt from stamp duty.

Stocks and shares

Instruments effecting the transfer of stocks and shares are subject to stamp duty of 0.2% on the purchase price or market value of the shares transferred, whichever is higher.

Foreign Worker Levy (FWL)

The FWL is a monthly levy of up to SGD 950 that employers are liable to pay for each foreign employee (Work Permit or S Pass holders) hired. The levy rate depends on the employee's qualifications, the employer's industry, and the ratio of foreigners to Singaporeans and permanent residents employed in the company. The government has announced that levy increases for Work Permit holders in the marine and process sectors that were originally proposed for 1 July 2016 will be deferred for yet another year till 1 July 2019.

Payroll taxes

Singapore does not have payroll withholding. When a non-Singapore citizen employee ceases employment in Singapore, leaves Singapore for an overseas posting, or leaves Singapore for a period exceeding three months, the employer needs to notify the Singapore tax authorities once the fact of cessation/departure is known to the employer, unless the employer is bearing full Singapore taxes for the employee, and withhold all monies due until tax clearance is issued. The notification must be made no later than one month prior to the date of cessation/departure, or two months from the date of cessation/departure where the employer is bearing full Singapore taxes for the employee. Non-Singapore citizen employees are also subject to tax on unexercised/

unvested stock options/awards on a deemed gain basis when they cease employment or leave Singapore.

Social security contributions

Central Provident Fund (CPF)

The CPF is Singapore's national pension scheme. Contributions are payable by Singapore citizens and permanent residents only. Generally, employers and employees contribute 17% and 20%, respectively, of ordinary monthly wages up to an income ceiling of SGD 6,000. Their respective maximum contributions are therefore SGD 1,020 and SGD 1,200. The rates are applicable to employees aged 55 years and below.

These rates also apply to additional wages (e.g. year-end bonus), up to a maximum contribution of:

If: Annual ordinary wages	And: Total wages	Maximum contribution
Not more than the ordinary wage ceiling of SGD 72,000	Not more than the maximum contribution of SGD 102,000	Actual additional wages
Not more than the ordinary wage ceiling of SGD 72,000	Exceed the maximum contribution of SGD 102,000	Difference between the maximum contribution of SGD 102,000 and annual ordinary wages
Exceed the ordinary wage ceiling of SGD 72,000	Not more than the maximum contribution of SGD 102,000	Actual additional wages
Exceed the ordinary wage ceiling of SGD 72,000	Exceed the maximum contribution of SGD 102,000	Difference between the maximum contribution and the ordinary wage ceiling (SGD 30,000)

Reduced rates apply for employees who are earning less than SGD 750 per month and those above 55, although these rates are being gradually increased.

Foreign nationals and their employers are precluded from making CPF contributions. Foreign employees who become Singapore permanent residents, and their employers, may contribute at reduced rates for the first two years.

Supplementary Retirement Scheme (SRS)

The SRS is a voluntary scheme to encourage employees and the self-employed to save for retirement over and above their CPF savings. The maximum amount to be contributed is subject to an income cap of SGD 102,000. Employers are allowed to contribute to their employees' SRS accounts. This is subject to a 15% contribution limit (capped at SGD 15,300) for Singapore citizens and permanent residents, and a 35% cap for foreigners (maximum SGD 35,700). Employees will be taxable on these employer contributions, but will be allowed corresponding tax relief. Relief is subject to a personal income tax (PIT) relief cap of SGD 80,000 that applies to the total amount of all tax reliefs claimed, including any SRS relief. There is no refund for SRS contributions already made, in the event the overall PIT relief cap is exceeded.

Carbon tax

Carbon tax at a rate of SGD 5 per tonne of carbon dioxide-equivalent (tCO2e) of emissions will be applied on the total greenhouse gas emissions of facilities that produce 25,000 or more tCO2e of emissions per year. The carbon tax will apply uniformly to all sectors, without exemption, and will take the form of a fixed-price credits-based mechanism. The first payment of the carbon tax will be in 2020, based on emissions in 2019.

Branch income

Tax rates on branch profits are the same as on corporate profits. There is no branch profits remittance tax on the repatriation of profits to the head office.

Income determination

Inventory valuation

There are no special rules as to which valuation basis should be adopted for inventories (stock-in-trade) in the case of a continuing business, as long as the basis is consistent from one year to another. However, a last in first out (LIFO) basis of valuation is not permitted for tax purposes. Generally, tax reporting conforms to book reporting.

Capital gains

There is no tax on capital gains. Where there is a series of transactions or where the holding period of an asset is relatively short, the tax authorities may take the view that a business is being carried on and attempt to assess the gains as trading profits of the corporation. The United Kingdom (UK) Badges of Trade, which are used in judicial decisions to distinguish capital and revenue transactions, are generally applied in determining this issue. They include the existence of a profit-seeking motive, the number of transactions, the nature of the asset, the existence of similar trading transactions or interests, the way the sale was carried out, the source of finance, the interval of time between purchase and sale, and the method of acquisition.

Gains derived by a company from the disposal of ordinary shares that take place between 1 June 2012 and 31 May 2022 will not be taxed if the company has held at least 20% of the ordinary shares in the investee company for a continuous period of at least 24 months prior to the disposal. This protection does not apply to gains derived by an insurance company or disposal of shares in certain companies that trade or hold immovable properties.

Dividend income

Singapore dividends are exempt in the hands of the recipient.

Interest income

Singapore-sourced interest income is taxable when it arises, and foreign-sourced interest is taxable when it is remitted or deemed to be remitted to Singapore. *For further details on foreign-sourced interest income and the availability of foreign tax credit, refer to Foreign income below*.

Royalty income

Singapore-sourced royalty income is taxable when it arises, and foreign-sourced royalty income is taxable when it is remitted or deemed to be remitted to Singapore. *For further details on foreign-sourced royalty income and the availability of foreign tax credit, refer to Foreign income below*.

Foreign income

A corporation, whether resident in Singapore or not, is taxed on foreign income when it is received in Singapore. Legislative provisions govern the basis of treating foreign income as received in Singapore. There are no special rules for taxing the undistributed income of foreign subsidiaries.

Where income is earned from treaty countries, double taxation is avoided by means of foreign tax credit granted under those treaties. For non-treaty countries, unilateral tax credit is given in respect of foreign tax on all foreign-sourced income. These foreign tax credits may be pooled, subject to certain conditions.

Foreign dividends, foreign branch profits, and foreign service fee income remitted to Singapore may be exempt from tax if they fulfil certain conditions.

Deductions

Depreciation

Tax depreciation is allowable at specified rates on buildings used in qualifying industry sectors, subject to conditions. In 2010, industrial building allowances were replaced by a Land Intensification Allowance. The latter provides for faster depreciation but is subject to approval as it is allowed as a tax incentive. Transitional provisions for industrial building allowances are available for taxpayers who committed to qualifying capital expenditure on or before 22 February 2010.

Tax depreciation is available on machinery and equipment on a straight-line basis over their specified working life for all types of business. In lieu of the straight-line basis, accelerated tax depreciation allowances can be claimed by all businesses on all machinery and equipment in equal instalments over three years.

A 100% depreciation allowance is available on capital expenditure incurred on computers, robots, standby generators, pollution control equipment, and prescribed automation equipment.

Writing down allowances on a straight-line basis over five years are allowable on the cost of acquisition of IP, subject to certain conditions. Taxpayers acquiring IP in the 2016 to 2019 income years may make an irrevocable election to claim the writing down allowances over 10 or 15 years instead of five.

In addition, enhanced allowances may be available for the acquisition of automation equipment and IP up to the year of assessment 2018 (*see Productivity and Innovation Credit [PIC] in the Tax credits and incentives section*).

Gains on tax depreciable property (i.e. the excess of proceeds over tax base) are taxed as ordinary income to the extent that tax depreciation has been allowed; that is, there is a clawback of tax depreciation on the disposal of the asset.

Goodwill

Payments for the acquisition of goodwill are generally capital in nature and not deductible.

Start-up expenses

Generally, expenses incurred prior to the commencement of business are not tax deductible. However, most businesses are allowed to deduct expenses incurred in the 12 months immediately preceding the accounting year in which the business earned its first dollar of trading income. Deductible expenses are those that would have been allowed a deduction had they been incurred after the business commenced operations.

In addition, deductions and writing down allowances are available for certain types of pre-commencement expenditure (acquisition of plant and machinery, R&D, etc.) that are deemed to be incurred on the first day on which the taxpayer carries on one's business.

Interest expenses

Interest incurred on capital employed in the production of income, and prescribed borrowing costs that are incurred as a substitute for interest or to reduce interest costs, will be allowed as a tax deduction.

Research and development (R&D) expenses

The following deductions are available for qualifying R&D expenditure, subject to conditions:

	Year of assessment 2018	Years of assessment 2019 to 2025
R&D carried out in Singapore	150% of qualifying R&D expenditure	250% of qualifying R&D expenditure
R&D carried out overseas	100% of qualifying R&D expenditure	

Expenditure incurred in relation to R&D cost-sharing arrangements are accorded the same tax treatment as R&D expenses.

Enhanced deductions may also be available under the PIC scheme up to the year of assessment 2018 (*see Productivity and Innovation Credit [PIC] in the Tax credits and incentives section*).

Bad debts

Bad trade debts and provisions for trade debts are deductible to the extent that they are incurred in the business and previously included as trading receipts. Doubtful debts are deductible if they are properly estimated and specific. General provisions for bad debts are not deductible.

Businesses that have elected to align their tax treatment of financial instruments with the accounting treatment prescribed by SFRS 39 (Financial Instruments: Recognition and Measurement) will be allowed a tax deduction for impairment losses on trade debts when they are incurred (regardless of whether they are general or specific provisions). Correspondingly, any reversal will be taxed. Businesses that have adopted SFRS 109 (Financial Instruments) will be allowed a tax deduction for impairment losses on trade debts when recognised in the profit and loss account, to the extent that the debts are credit impaired. Correspondingly, any reversal will be taxed.

Charitable contributions

Donations are deductible only if they are made in cash or another prescribed form and to an approved recipient. The deduction allowed for qualifying donations is generally 250% of the value of the donation. Businesses that send employees to volunteer and provide services to approved charitable institutions from 1 July 2016 to 31 December 2021 will be allowed to deduct 250% of the wages and incidental expenses incurred, subject to certain conditions.

Fines and penalties

Fines and penalties imposed for violations of the law are not deductible.

Taxes

Income taxes are generally not deductible in determining corporate income. However, irrecoverable GST is deductible under certain circumstances. The FWL and property taxes are deductible to the extent they are incurred wholly and exclusively in the production of income.

Other significant items

Private automobile expenses are not deductible.

The tax deduction for medical expenses is limited to 2% of total payroll if the employer implements certain portable medical insurance or benefit schemes. Otherwise, the amount deductible will be limited to 1% of total payroll. Where the company is exempt or taxed at a reduced rate, the excess expenses will be taxed at the prevailing corporate rate.

A tax deduction for employee share-based remuneration (stock awards or stock option schemes) is allowed only if treasury shares in the company or its holding company are purchased to fulfil such obligations. A company may also claim a tax deduction when the share-based remuneration scheme is administered by a special purpose vehicle (SPV). The deduction is restricted generally to the lowest of the actual outlay incurred by the company, its holding company, or the SPV.

Net operating losses

Loss carryover, including unutilised tax depreciation allowance, is unlimited, provided shareholdings in the loss-making corporation have not changed beyond 50% of the total number of issued shares. Additionally, for tax depreciation allowances to be carried forward, the same trade needs to be continued. The tax authorities may exercise discretion to allow carryover of tax losses and unutilised tax depreciation even when there has been a change in shareholding beyond 50%, absent any tax avoidance motives. Losses and tax depreciation of up to SGD 100,000 incurred by the company in the current year can be carried back for one year. The carryback of losses and tax depreciation is subject to the continuity of shareholding test and the same trade test for carryback of tax depreciation.

Payments to foreign affiliates

Payments to non-residents, including foreign affiliates, are deductible, provided they are fair and reasonable, are revenue in nature, and can be seen to be relevant to earning the payer's income.

Group taxation

A company is allowed to transfer excess current year trade losses, current year tax depreciation, and current year approved donations to another company within the same group if certain conditions are satisfied.

Broadly, to qualify for group relief, companies must be incorporated in Singapore, belong to the same group of companies where, among other things, there must be at least a 75% ownership relationship between claimant and transferor, and have the same accounting year-end. In addition, a group must comply with certain prescribed offset and apportionment rules.

Transfer pricing

The Income Tax Act contains specific transfer pricing provisions that define the arm's-length principle and provide the tax authorities with a right to make transfer pricing adjustments in cases where taxpayers do not comply with the arm's-length principle.

In 2017, these transfer pricing provisions were enhanced to introduce mandatory contemporaneous documentation requirements, penalties for non-compliance, and a surcharge to be imposed at 5% of the transfer pricing adjustment value. In general, businesses with turnover exceeding SGD 10 million are required to maintain contemporaneous transfer pricing documentation with effect from the year of assessment 2019, subject to certain exemptions as defined. Failure to comply with these requirements (including contemporaneous transfer pricing documentation) could result in a penalty not exceeding SGD 10,000. The tax authorities are also given the power to disregard the form of a transaction where the substance of it is inconsistent with the form.

The tax authorities have issued revised transfer pricing guidelines to supplement the provisions in the Income Tax Act. Guidance is also provided on matters relating to mutual agreement procedures (MAPs) and advance pricing arrangements (APAs).

Country-by-country (CbC) reporting

On 21 June 2017, Singapore signed the Multilateral Competent Authority Agreement on the exchange of CbC Reports. For income years beginning on or after 1 January 2017, Singapore-headquartered multinational enterprises with global revenues exceeding SGD 1,125 million have to submit to the IRAS an annual CbC report containing the income, taxes paid, and other indicators of level of economic activities in every tax jurisdiction where they operate. The IRAS will exchange CbC reports with jurisdictions with which Singapore has entered into bilateral agreements for the exchange of CbC reports.

Thin capitalisation

There are no formal thin capitalisation rules in Singapore. However, general anti-avoidance and transfer pricing provisions may operate in cases of abuse.

Controlled foreign companies

There are no CFC rules in Singapore.

Tax credits and incentives

There are various tax incentives available to taxpayers involved in specified activities or industries identified as being beneficial to Singapore's economic development.

Tax incentive applications are typically subject to an approval process during which the administering agency evaluates the applicant's business plans in detail. Successful applicants are required to satisfy rigorous requirements and are expected to make significant economic commitments in Singapore.

Generally, applicants are expected to carry out substantive, high value activities in Singapore, and will be required to commit to certain levels of local business spending and skilled employment. Some factors that will be considered include the use of Singapore as a base from which to implement regional growth strategies; introduction and anchoring of leading-edge skills, technology, and activities in Singapore; contributions to the growth of R&D and innovation capabilities; and potential spin-off to the rest of the economy.

Pioneer tax incentive

Corporations manufacturing approved products with high technological content or providing qualifying services may apply for tax exemption for five to 15 years for each qualifying project or activity under the pioneer tax incentive. Corporations may apply for their post-pioneer profits to be taxed at a reduced rate under the Development and Expansion Incentive, *as discussed below*.

Development and Expansion Incentive

Under the Development and Expansion Incentive, corporations engaging in new high-value-added projects, expanding or upgrading their operations, or undertaking incremental activities after their pioneer period may apply for their profits to be taxed at a reduced rate of not less than 5% for an initial period of up to ten years. The total tax relief period for each qualifying project or activity is subject to a maximum of 40 years (inclusive of the post-pioneer relief period previously granted, if applicable).

Investment allowance

Under the investment allowance, a tax exemption is granted on an amount of profits based on a specified percentage (of up to 100%) of the capital expenditure incurred for qualifying projects or activities within a period of up to five years (up to eight years for assets acquired on hire-purchase). Capital expenditure incurred for productive equipment placed overseas on approved projects may likewise be granted integrated investment allowances. Investment allowances of 100% of capital expenditure (net of grants) may be granted to businesses seeking to make substantial investment in automation, subject to a cap of SGD 10 million per project.

Incentives for internationalisation

The double tax deduction scheme for internationalisation allows companies expanding overseas to claim a double deduction for eligible expenses for specified market expansion and investment development activities. This includes manpower expenses incurred when Singaporeans are deployed to overseas entities.

Intellectual Property Development Incentive (IDI)

The IDI is a new incentive scheme that was introduced to encourage the exploitation of IP arising from R&D activities of the taxpayer. Income from the commercialisation of certain IP will be taxed at a concessionary rate. This incentive scheme is expected to be modelled after the modified nexus approach set out in the Action 5 report of the OECD base erosion and profit shifting (BEPS) project.

Productivity and Innovation Credit (PIC)

The PIC scheme provides for an enhanced 400% deduction for qualifying expenditure incurred in respect of six qualifying activities during the accounting periods that ended between 2010 and 2017 (i.e. years of assessment 2011 to 2018). The six qualifying activities are:

- The acquisition or leasing of prescribed IT and automation equipment.
- Staff training.
- The acquisition of IP.
- The registration of IP rights.
- R&D.
- Design.

The enhanced deduction is available only on the first SGD 400,000 of qualifying expenditure incurred each year on each of the qualifying activities, although, for the years of assessment 2015 to 2018, qualifying small and medium enterprises may claim PIC benefits for up to SGD 600,000 of such expenditure for each qualifying activity a year. The cap may be combined for certain years of assessment. Certain activities are subject to approval or minimum ownership requirements.

For the years of assessment 2013 to 2018, the acquisition of IP rights includes licensing of those rights, other than trademarks and any rights to the use of software.

With the expiry of the PIC scheme, the following further deductions have been introduced for the years of assessment 2019 to 2025:

- 250% deduction for qualifying expenditure incurred for R&D carried out in Singapore.
- 200% deduction for the first SGD 100,000 of qualifying expenditure incurred to register qualifying IP.
- 200% deduction for the first SGD 100,000 of expenditure incurred to license qualifying IP.

Mergers and acquisitions allowance

The mergers and acquisitions allowance allows a write-off, over five years, of 25% of the value of qualifying mergers or acquisitions deals executed between 1 April 2015 and 31 March 2020, subject to a cap of SGD 5 million (SGD 10 million for deals executed from 1 April 2016 to 31 March 2020) per year of assessment. This incentive is available to companies that are incorporated, tax resident, and carrying on a business in Singapore; however, this requirement may be waived for companies under the headquarters schemes (further details below) and the Maritime Sector Incentive (MSI) (further details below) for shipping-related supporting services (for share acquisitions completed from 17 February 2012 to 31 March 2020). A 200% tax allowance is also granted on transaction costs (capped at SGD 100,000 per year of assessment) incurred on qualifying deals.

Financial services incentives

Financial Sector Incentive (FSI) scheme

The FSI scheme covers a broad range of financial institutions, including bond intermediaries, Asian currency units, derivative traders, fund managers, equity capital market intermediaries, operational headquarters, providers of high-value-added processing services supporting financial activities, providers of trustee and custodian services, and trust management or administration services. Financial institutions that plan to expand their Singapore operations and are prepared to meet various strict qualifying conditions may apply for this incentive.

Under the FSI scheme, income from certain high growth, high-value-added activities, such as services and transactions relating to the bond market, derivatives market, equity market, and credit facilities syndication, may be taxed at 5%, while a broader range of financial activities will qualify for a 12% tax rate. This rate has been increased to 13.5% for awards granted or renewed from 1 June 2017, and the scope of qualifying income has been expanded (broadly speaking, certain currency, counterparty, and investment instrument restrictions have been removed). The tax incentive period may last for five, seven, or ten years, subject to certain conditions being met.

Finance and treasury centre (FTC)

Income derived by an FTC from approved FTC activities is taxed at a reduced rate of 8%. Approved activities include international treasury and fund management activities, corporate finance and advisory services, economic and investment research and analysis, and credit control and administration.

Interest payments to overseas banks and approved network companies are also exempt from WHT where the funds borrowed are used for approved activities.

Debt securities incentives

A package of tax concessions is available to various players in the Singapore bond market, including those involved in certain Islamic financing arrangements.

Insurance Business Development (IBD) scheme

The IBD scheme is an umbrella incentive for the insurance sector. Incentives offered under this scheme include a 10% concessionary tax rate for qualifying income of life, general, and composite insurers from carrying on insurance businesses from Singapore, and income derived from the provision of insurance broking and advisory services. This includes income from marine hull and liability insurance, captive insurance businesses, and qualifying specialised insurance.

Real Estate Investment Trusts (REITs)

Distributions made to foreign non-individual investors by a listed REIT out of rental income from Singapore real estate are subject to a reduced tax rate of 10%, subject to certain conditions being met. Listed REITs investing in foreign properties can apply for tax exemption for certain foreign income received in Singapore. Distributions out of this income similarly are exempt.

From 1 July 2018 to 31 March 2020, tax transparency treatment will be accorded for specified income of Singapore-listed REIT Exchange-Traded Funds (REIT-ETFs) so that there will be parity in tax treatments between investing in individual S-REITs and via REIT-ETFs with investments in S-REITs.

As a concession, Singapore-listed REITs are allowed to claim GST on expenses incurred for their business and for their special purpose vehicles, regardless of whether the REIT is eligible for GST registration, subject to a specified formula and certain conditions.

Islamic financing arrangements

The income tax, stamp duty, and GST treatment of prescribed Islamic financing arrangements and Islamic debt securities (*Sukuk*) are aligned with that of the conventional financing contracts to which they are economically equivalent, subject to certain conditions.

Infrastructure project finance incentives

Tax exemption is available for interest income earned from qualifying investments in qualifying infrastructure projects/assets. FSI companies that provide project finance advisory services related to qualifying projects/assets may enjoy certain tax concessions for their qualifying income, and companies that provide management services to qualifying business trusts and funds pay tax at 10% on their qualifying income.

Sovereign wealth funds

Tax exemption is available for income derived by a sovereign fund entity and an approved foreign government-owned entity from funds managed in Singapore.

Singapore Variable Capital Companies (S-VACC)

An S-VACC will be treated as a company and a single entity for tax purposes. The tax exemptions for income from funds managed in Singapore and the existing GST remission for funds will be extended to qualifying S-VACC. A 10% concessionary tax rate under FSI incentive for fund managers will be extended to approved fund managers managing an incentivised S-VACC. This tax framework will take effect when or after the regulatory framework for S-VACC comes into effect.

Headquarters schemes

Approved regional headquarters in Singapore are taxed at a concessionary rate of tax of 15% on qualifying overseas income. Depending on their level of economic commitments to Singapore, international headquarters can apply for various tax incentives, including tax exemption or concessionary tax rates on qualifying income.

Maritime Sector Incentive (MSI) scheme

The MSI scheme is the umbrella incentive for the maritime sector. Incentives offered include tax exemption for shipping companies and a 10% concessionary tax rate for international freight and logistics operators. Approved ship investment managers are also taxed at 10% on qualifying management-related income. The scheme also includes approved ship investment vehicles, which are tax exempt on their qualifying vessel lease income; approved container investment enterprises, which are taxed at 5% or 10% on qualifying income from container-leasing; and approved container investment management companies, which are taxed at 10% on qualifying management fees.

Qualifying ship operators and lessors under the MSI scheme also enjoy automatic tax exemption on gains from the disposal of vessels, vessels under construction, and new building contracts.

Global Trader Programme (GTP)

International traders are taxed at concessionary rates of 5% or 10% on qualifying income from physical trading, brokering of physical trades, and derivative trading income.

Other incentives

Other incentives include tax exemptions for not-for-profit organisations and a concessionary tax rate of 8% for approved aircraft lessors.

Foreign tax credit

See Foreign income in the Income determination section for a description of the foreign tax credit regime.

Withholding taxes

Domestic corporations paying certain types of income to non-residents are required to withhold tax.

Unless a lower treaty rate applies, interest on loans and rentals from movable property are subject to WHT at the rate of 15%. Royalty payments are subject to WHT at the rate of 10%. The tax withheld represents a final tax and applies only to non-residents who are not carrying on any business in Singapore and who have no PE in Singapore. Technical assistance and management fees for services rendered in Singapore are taxed at the prevailing corporate rate. However, this is not a final tax. Royalties, interest, rental of movable property, technical assistance, and management fees can be exempt from WHT in certain situations or subject to a reduction in tax rates, usually under fiscal incentives or DTAs.

Payments made to public entertainers and non-resident professionals who perform services in Singapore are also subject to a final tax of 15% on their gross income. For public entertainers, this appears to be a final tax unless they qualify to be taxed as Singapore tax residents. However, non-resident professionals may elect to be taxed at the prevailing tax rate for non-resident individuals of 22% on net income if this results in a lower tax cost. The WHT rate on payments to non-resident entertainers was reduced to 10% from 22 February 2010 to 31 March 2020.

Ship charter fee payments are not subject to WHT.

The WHT rates are shown in the following table.

	WHT (%)		
Recipient	**Dividends (1)**	**Interest (2)**	**Royalties (2)**
Resident individuals	0	0	0
Resident corporations	0	0	0
Non-resident corporations and individuals:			
Non-treaty	0	15	10
Treaty:			
Albania	0	5 (3b)	5
Australia	0	10	10 (4a)
Austria	0	5 (3b, d)	5

Recipient	WHT (%) Dividends (1)	Interest (2)	Royalties (2)
Bahrain	0	5 (3b)	5
Bangladesh	0	10	10 (4a)
Barbados	0	12 (3b)	8
Belarus	0	5 (3b)	5
Belgium	0	5 (3b, d)	3/5 (4b)
Bermuda (5a)	0	15	10
Brazil (5c)	0	15	10
Brunei	0	5/10 (3a, b)	10
Bulgaria	0	5 (3b)	5
Cambodia (5d)	0	10 (3b)	10
Canada	0	15 (3e)	10
Chile (5b)	0	15	10
China, People's Republic of	0	7/10 (3a, b)	6/10 (4b)
Cyprus	0	7/10 (3a, b)	10
Czech Republic	0	0	0/5/10 (4b, 4c)
Denmark	0	10 (3b)	10
Ecuador	0	10 (3a, b)	10
Egypt	0	15 (3b)	10
Estonia	0	10 (3b)	7.5
Ethiopia (5d)	0	5	5
Fiji Islands, Republic of	0	10 (3b)	10
Finland	0	5 (3b)	5
France	0	0/10 (3b, k)	0 (4a)
Georgia	0	0	0
Germany	0	8 (3b)	8
Guernsey	0	12 (3b)	8
Hong Kong (5c)	0	15	10
Hungary	0	5 (3b, d)	5
India	0	10/15 (3a)	10
Indonesia	0	10 (3b, e)	10
Ireland	0	5 (3b)	5
Isle of Man	0	12 (3b)	8
Israel	0	7 (3b)	5
Italy	0	12.5 (3b)	10
Japan	0	10 (3b)	10
Jersey	0	12 (3b)	8
Kazakhstan	0	10 (3b)	10
Korea, Republic of	0	10 (3b)	10
Kuwait	0	7 (3b)	10
Lao People's Democratic Republic	0	5 (3b)	5
Latvia	0	10 (3b)	7.5
Libya	0	5 (3b)	5
Liechtenstein	0	12 (3b)	8
Lithuania	0	10 (3b)	7.5
Luxembourg	0	0	7
Malaysia	0	10 (3b, f)	8
Malta	0	7/10 (3a, b)	10
Mauritius	0	0	0
Mexico	0	5/15 (3a, b)	10

Singapore

Recipient	WHT (%) Dividends (1)	Interest (2)	Royalties (2)
Mongolia	0	5/10 (3a, b)	5
Morocco	0	10 (3b)	10
Myanmar	0	8/10 (3a, b)	10
Netherlands	0	10 (3b)	0 (4a)
New Zealand	0	10 (3b)	5
Norway	0	7 (3b)	7
Oman	0	7 (3b)	8
Pakistan	0	12.5 (3b)	10 (4a)
Panama	0	5 (3b, d)	5
Papua New Guinea	0	10	10
Philippines	0	15 (3e)	10
Poland	0	5 (3b)	2/5 (4b)
Portugal	0	10 (3b, f)	10
Qatar	0	5 (3b)	10
Romania	0	5 (3b)	5
Russian Federation	0	0	5
Rwanda	0	10 (3a)	10
San Marino	0	12 (3b)	8
Saudi Arabia	0	5	8
Seychelles	0	12 (3b)	8
Slovak Republic	0	0	10
Slovenia	0	5 (3b)	5
South Africa	0	7.5 (3b, j, l)	5
Spain	0	5 (3b, d, f, g)	5
Sri Lanka (5d)	0	10 (3a, b)	10
Sweden	0	10/15 (3b, c)	0 (4a)
Switzerland	0	5 (3b, d)	5
Taiwan	0	15	10
Thailand	0	10/15 (3a, b, h)	5/8/10 (4d)
Turkey	0	7.5/10 (3a, b)	10
Ukraine	0	10 (3b)	7.5
United Arab Emirates	0	0	5
United Kingdom	0	5 (3a, b, i)	8
United States (5c)	0	15	10
Uruguay (5d)	0	10 (3b, d, j, k)	5/10 (4e)
Uzbekistan	0	5	8
Vietnam	0	10 (3b)	5/10 (4f)

Notes

1. Singapore has no WHT on dividends over and above the tax on the profits out of which the dividends are declared. However, some treaties provide for a maximum WHT on dividends should Singapore impose such a WHT in the future.
2. The non-treaty rates (a final tax) apply only to non-residents who do not carry on business in Singapore and who do not have a PE in Singapore. This rate may be further reduced by tax incentives.
3. Interest:
   a. Lower rate or exemption if received by a financial institution.
   b. Exempt if paid to the government.
   c. Lower rate or exemption if paid by an approved industrial undertaking.
   d. Exempt if paid by a bank and received by a bank.
   e. Exempt if paid to a bank but linked to a government loan agreement or paid to specific financial institutions/banks.
   f. Exempt if paid in respect of an approved loan or indebtedness.

g. Exempt if paid to an approved pension fund.
h. Lower rate if paid to a financial institution or insurance company or paid with respect to indebtedness arising from a sale on credit of any equipment, merchandise, or services.
i. Exempt if paid by a financial institution.
j. Exempt if paid by the government.
k. Exempt if paid in respect of a loan, debt-claim, or credit that is guaranteed or insured by the government.
l. Exempt if paid in respect of any debt instrument listed on a recognised stock exchange.

4. Royalties:
   a. Royalties on literary or artistic copyrights, including film royalties, are taxed at the non-treaty rate.
   b. Lower rate for payments in connection with industrial, commercial, or scientific equipment.
   c. Royalties on literary, artistic, or scientific work, except computer software, but including film royalties, are exempt.
   d. Lower rate of 5% for royalties on copyright of literary, artistic, or scientific work, including cinematograph films, or films or tapes used for radio or television broadcasting, and 8% for royalties in connection with patents, trademarks, designs or model, plan, secret formula, or process, or industrial, commercial, or scientific equipment.
   e. Lower rate on copyright of literary, artistic, or scientific work, including cinematograph films, or films or tapes used for radio or television broadcasting.
   f. Lower rate for payments in connection with patents, designs, secret formulas/processes, or industrial, commercial, or scientific equipment/experience.
5. Treaties:
   a. Treaty with Bermuda covers only the exchange of information.
   b. Treaty with Chile covers only international ship operations.
   c. Treaties with Brazil, Hong Kong, and the United States cover only shipping and air transport activities.
   d. Treaty or lower rate applies from 1 January 2018.

Tax administration

Taxable period

The tax basis period is the calendar year; however, for business profits, the accounting period will generally be adopted.

Tax returns

Tax is computed for each tax year based on the income earned in the preceding year (the tax basis period). The corporation files an estimate of its income within three months of the end of the accounting period followed by a return of income by 30 November of the tax year, and the tax is assessed by the Comptroller of Income Tax. Mandatory electronic filing of tax returns will be introduced gradually. Certain companies will be required to file electronically from year of assessment 2018 (income year 2017). By year of assessment 2020 (income year 2019), all companies are expected to have adopted electronic filing. There is no fixed date for the issue of assessments.

Payment of tax

Assessed tax is payable within one month after the service of the notice of assessment, whether or not a notice of objection to the assessment has been lodged with the tax authorities. Application may be made to the Comptroller to pay estimated tax liabilities on a monthly basis. However, the Comptroller is under no obligation to grant such an application.

Late payment of tax will attract penalties, up to a maximum of 17% of the outstanding tax.

Tax audit process

The IRAS adopts a risk-based approach to identifying compliance risk, with a focus on improving the behaviour of taxpayers who pose a higher risk of non-compliance. It also prioritises and tailors specific compliance programmes that aim to identify taxpayers who have made mistakes in their tax returns, create an audit presence in the community to deter non-compliance by other taxpayers, educate taxpayers on their tax obligations and how to comply with these, and identify areas of tax law, policies, and processes where the tax system can be simplified.

Statute of limitations

The statute of limitations is four years from the year of assessment, but does not apply where there has been fraud or wilful default by the taxpayer.

Topics of focus for tax authorities

In the past, the IRAS has focussed its compliance efforts on:

- the timely filing of corporate tax returns
- PIC claims
- the classification of income and expenses for income taxable at concessionary and prevailing corporate tax rates
- group relief claims
- tax exemption for foreign-sourced dividends, and
- the recognition of income from construction contracts and provisions claimed by construction companies.

The IRAS has announced that, in addition to the above, it will be focussing on:

- wholesale of chemicals and chemical products, and
- travel agencies and ticketing agents.

Other issues

Exchange of information (EOI)

Generally, Singapore's tax treaties and EOI arrangements include provisions for the exchange of information for tax purposes. Treaty partners may make a request to the Comptroller of Income Tax for information, or the exchange may take the form of spontaneous EOI or automatic EOI.

Spontaneous EOI

Singapore has committed to spontaneously exchange certain rulings under the agreed framework for the compulsory spontaneous EOI set out in the BEPS Action 5 Report 'Countering Harmful Tax Practices More Effectively, taking into Account Transparency and Substance'.

International Tax Compliance Agreements

Singapore has also concluded the following international tax compliance agreements and will exchange information pursuant to those agreements as follows:

Foreign Account Tax Compliance Act (FATCA)

Singapore has a Model 1 FATCA intergovernmental agreement (IGA) with the United States in place to help ease the compliance burden of Singapore-based financial institutions (SGFIs). All Reporting SGFIs must submit a FATCA Return to the IRAS, setting out the required information in relation to every US Reportable Account.

Common Reporting Standard (CRS)

SGFIs are required to establish the tax residency of all their account holders. Further, they will need to report to the IRAS the requisite information for each Reportable Account relating to tax residents of jurisdictions with which Singapore has a Competent Authority Agreement to exchange information. The IRAS is expected to make the first exchange of CRS information in September 2018.

Adoption of International Financial Reporting Standards (IFRS)

Companies incorporated in Singapore and Singapore branches of foreign companies are required by the Companies Act to prepare and present financial statements that comply with the Singapore Financial Reporting Standards (SFRS). In Singapore, the Accounting Standards Council (ASC) has the statutory authority to issue SFRS for adoption.

The SFRS is principally based on and substantially similar to IFRS that are issued by the International Accounting Standards Board (IASB). Full convergence of the SFRS with IFRS for Singapore-listed companies was the strategic direction of the ASC set in 2009, and, on 29 December 2017, the ASC issued Singapore Financial Reporting Standards (International) (SFRS(I)s), Singapore's equivalent of the IFRS. Singapore-incorporated companies that have issued, or are in the process of issuing, equity or debt instruments for trading in a public market in Singapore are required to apply SFRS(I)s for annual periods beginning on or after 1 January 2018. Non-listed companies may voluntarily apply the new framework.

Companies are required to submit financial statements as part of their tax return filing. The IRAS generally accepts financial statements prepared for statutory filing, although companies that have been allowed to prepare their financial statements using standards other than SFRS, such as IFRS or the Generally Accepted Accounting Principles (GAAP) adopted by the United States, may be required to explain and/or account for any differences and make the necessary tax adjustments, if any.

In relation to financial instruments, the Income Tax Act has been amended to align the tax treatment with the accounting treatment prescribed by SFRS(I) 9 (Financial Instruments) and SFRS(I) 15 (Revenue from Contracts with Customers), and to allow tax adjustments to be made when the SFRS(I) is first applied. As a concession, the IRAS allows taxpayers to elect to align their tax reporting of lease income to the accounting treatment prescribed by SFRS 17 (Leases), which requires operating lease income to be recognised using the 'effective rent method'.

Sample corporate tax calculation

Accounting period ended 31 December 2017 (year of assessment 2018).

	SGD	SGD
Net profit before tax per accounts		5,857,500
Less:		
Singapore dividend (exempt)	1,500	
Foreign-sourced dividend (exempt)	2,200	
Foreign-sourced interest (unremitted)	1,600	
Profit on sale of fixed assets	34,000	
Capital exchange gain	6,750	(46,050)

	SGD	SGD
		5,811,450
Add:		
Depreciation	650,485	
Foreign pension contribution	100,000	
Medical expenses (non-deductible)	500	
Legal fees (capital in nature)	15,500	
Automobile expenses	33,500	
Donations	9,000	
Penalties and fines	2,000	810,985
Adjusted profit before capital allowances		6,622,435
Less:		
Unutilised capital allowances brought forward	1,152,000	
Capital allowances (current year)	3,000,000	
Balancing charge	(7,700)	(4,144,300)
Adjusted profit after capital allowances		2,478,135
Less: Unutilised losses brought forward		(67,500)
Adjusted profit after capital allowances and unutilised losses brought forward		2,410,635
Less: Approved donations (250% deduction)		(22,500)
Chargeable income before partial exemption		2,388,135
Less: Partial exemption		
75% of first SGD 10,000	7,500	
50% of the next SGD 290,000	145,000	(152,500)
Chargeable income after partial exemption		2,235,635
Tax thereon at 17%		380,057.95
Corporate tax rebate (capped at SGD 15,000)		(15,000.00)
Tax payable after tax rebate		365,057.95

Sri Lanka

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Significant developments

The significant development in the Sri Lanka tax scene is the enactment of the New Inland Revenue Act, No. 24 of 2017, which took effect from 1 April 2018. The New Inland Revenue Act is aimed at simplifying the tax system, make the tax system more equitable and efficient, and help generate more revenue for social and economic development purposes. The New Act deports from the hitherto practice of granting liberal tax exemptions and concessions, provides tax relief for a limited category of investment incentives, eliminates multiplicity of corporate tax rates by introducing a three tier corporate rate structure, and simplifies the expense deductibility rule. It seeks to enhance revenue generation by broadening the tax base, in particular by eliminating the vast range of tax holidays, partial tax holidays, reliefs, and other concessions; introducing taxation of capital gains; and expanding the coverage of withholding taxes (WHTs).

The rules and procedures in relation to corporate income tax (CIT), which are set out in sections that follow, are based on the provisions of the New Inland Revenue Act, No. 24 of 2017.

Taxes on corporate income

Resident companies and public corporations are liable for CIT on their worldwide taxable income. Further, a friendly society, building society, pension fund, provident fund, retirement fund, superannuation fund, or similar fund or society are also deemed a company. A partnership having more than 20 partners who have limited liability for the debts of the partnership also treated as a company. Similarly, a unit trust or a mutual fund that does not conduct an eligible investment business is also treated as a company, and in all such cases corporate tax is applicable. Non-resident companies are liable for CIT in respect of any business, investment, or other source to the extent that the income arises in or is derived from a source in Sri Lanka.

Prior to year of assessment 2018/19, CIT rates are based on the nature of the income and the institution earning the income, as provided in the following table.

Income/Institution	2017/18 CIT rate (%)
Undertaking for manufacture of any product for export or for supply to an exporter for export, being a product having domestic value addition over 65% and a Sri Lanka brand name with patent rights received in Sri Lanka	10
Undertaking for operation and maintenance of facilities for storage, local development of software, or supply of labour	10

Income/Institution	2017/18 CIT rate (%)
Agricultural undertakings referred to in Section 16 of the Act	10
Educational services	10
Undertaking (not being a holding company, subsidiary company, or any associate company of a group of companies) with an annual turnover not exceeding 750 million Sri Lankan rupees (LKR), other than buying and selling activities	12
Undertaking (not being a holding company, subsidiary company, or any associate company of a group of companies) with an annual turnover not exceeding LKR 500 million, other than buying and selling activities	-
Unit trusts and mutual funds *	10
Unit trust management companies	10
Profits on poultry farming	10
Shipping agents approved by the Director of Merchant Shipping in respect of profits attributable to agency fees connected to transhipment activity and received in foreign currency	12
Companies engaged in non-traditional export (other than exempt), including deemed exporters and suppliers of specified services to garment exporters; performance of any service of ship repair, ship breaking, and refurbishment of marine cargo containers; and provision of computer software, programmes, systems, or recording of computer data paid for in foreign currency	12
Undertakings engaged in agriculture, manufacture of animal feed, promotion of tourism, or construction work carried on by a resident person	12
Venture capital companies	12
Petroleum exploration	12
Local manufacture of handloom products	12
Healthcare services	12
Joint venture between a grower cum manufacturer or a manufacturer of tea with a tea exporter for exporting Sri Lanka tea in value added form, on the manufacturing income attributable to the quantum of tea purchased	12
Profits from operating any mini hydropower project or other alternative energy source	12
Profits on supply of goods manufactured in Sri Lanka or provision of services to foreign ships for payment in foreign currency	12
Profits on sale of any product manufactured in Sri Lanka for payment in foreign currency through a foreign exchange earning account	12
Profits on export of organic tea in bulk	12
Undertaking for the manufacture of sugar	12
Sale of goods manufactured in Sri Lanka by an export-oriented Board of Investment (BOI) enterprise, up to the quantity approved by the BOI, to: • any BOI enterprise enjoying tax holiday under Section 16C, 16D, or 17A of the Inland Revenue Act or the Strategic Development Projects Act that is permitted to import project-related goods or raw materials on a duty-free basis during the project implementation period, or • any person eligible to import specific goods on a duty-free basis under any government authority. (Treated as deemed export of the manufacturer.)	12
Profits and income of any company listing its shares on or after 1 April 2013 and issuing more than 20% of its shares to the general public for the tax year in which such shares are listed and for two years of assessment immediately succeeding that year of assessment	50% of the applicable rate
Research and development (R&D) activities	20
Branch of commercial bank dedicated to development banking	24
Banking and financial services, insurance industries, trading activities (including any primary preparation for the adapting for sale of any article)	28
Manufacture and sale, or import and sale, of liquor or tobacco products	40

Income/Institution	2017/18 CIT rate (%)
Business of lottery, betting, or gaming activity	40
Profit and income from business, other than stated above	28
Other sources (e.g. dividends, interest income, royalties)	28

* Unit trusts and mutual funds are treated as resident companies for CIT purposes if such unit trust or mutual fund does not conduct eligible investment business. Eligible business means a business or investment comprising predominantly of owning, investing, or trading in capital assets, financial instruments, or other similar assets.

Commencing from the year of assessment 2018/19, companies are taxed only under three income tax rates: 14%, 40%, and 28%, as listed below. In order to apply a lower tax rate for an undertaking, it should have more than 80% from such identified undertaking which is considered predominant.

Income/ Institution	CIT rate (%)
Small and medium enterprises (SMEs) that conduct business in Sri Lanka, which do not have an associate that is an entity and with an annual turnover less than LKR 500 million	14
Predominantly conducting of a business of exporting goods and services (exports includes specified undertakings *)	14
Predominantly conducting of a business of an agricultural business	14
Business consisting of betting and gaming, liquor, and tobacco	40
Companies predominantly providing educational services	14
Companies predominantly engaged in an undertaking for the promotion of tourism	14
Companies predominantly providing information technology services	14
Profits and income from business other than stated above (including unit trusts and mutual funds)	28
Gains from the realisation of investment assets	10

* Specified undertaking means an undertaking that is engaged in:

- Entrepot trade involving import, minor processing, and re-export.
- Offshore business where goods can be procured from one country or manufactured in one country and shipped to another country without bringing the same into Sri Lanka.
- Providing front-end services to clients abroad.
- Headquarters operations of leading buyers for management of financial supply chain and billing operations.
- Logistic services such as bonded warehouse or multi-country consolidation in Sri Lanka.
- Transhipment operations.
- Freight forwarding.
- Supply of services to any exporter of goods or services or to any foreign principal of such exporter directly, being services which could be treated as essentially related to the manufacture of such goods or provision of such services exported by such exporter either directly or through any export trading house, including any service provided by an agent of a ship operator to such agent's foreign principal, and the payment for such services are made by such exporter or foreign principal to such person in Sri Lanka in foreign currency.
- Production or manufacture and supply to an exporter of non-traditional goods.
- The performance of any service of ship repair, ship breaking repair, and refurbishment of marine cargo containers, provision of computer software, computer programmes, computer systems or recording computer data, or such other services as may be specified by the Minister by notice published in the Gazette, for payment in foreign currency.
- Sale for foreign currency of any gem or jewellery, being a sale made in Sri Lanka by any person authorised by the Central Bank of Sri Lanka to accept payment for such sale in foreign currency.

Dividend tax

A dividend tax is payable at 14% (prior to 1 April 2018, it was at 10%) on the gross dividends distributed by a resident company, other than such dividends distributed out of any dividend received from another resident company. Any dividend distributed prior to 1 April 2019 out of dividends from which WHT has been deducted at 10% prior to 1 April 2018 will not be subject to dividend tax under the new Inland Revenue Act No. 24 of 2017.

Remittance tax

Where profits of a non-resident company are remitted in a tax year, a remittance tax of 14% of the remittances is payable (prior to 1 April 2018, it was at 10%).

Local income taxes

There is no local or provincial income tax applicable to corporates in Sri Lanka.

Corporate residence

A company is treated as resident for tax purposes in Sri Lanka for a year of assessment if it is incorporated or formed under the laws of Sri Lanka, registered or the principal office is in Sri Lanka, or at any time during the year the management and control of the affairs of the company are exercised in Sri Lanka.

Permanent establishment (PE)

PE is a treaty concept in Sri Lanka. If a non-resident company creates a PE in Sri Lanka in terms of a double tax treaty (DTT), then such company is liable to Sri Lanka CIT. In the absence of a DTT, the domestic tax laws will apply. However, the New Inland Revenue Act, No. 24 of 2017 incorporates the concept of a 'permanent establishment', which is defined to mean a place in Sri Lanka where a non-resident person carries on business or that is at the disposal of the person for that purpose and includes:

- a place in Sri Lanka where a person has, is using, or is installing substantial equipment or substantial machinery
- a place in Sri Lanka where a person is engaged in a construction, assembly, or installation project for 90 days or more, including a place where a person is conducting supervisory activities in relation to such a project
- the provision of services in Sri Lanka, but only if activities of that nature continue (for the same or a connected project) for a period of 183 days or more in any 12-month period, and
- a place in Sri Lanka where an agent performs any function on behalf of the business of a non-resident person:
  - including, in the case of an insurance business, the collection of premiums or the insurance of risks situated in Sri Lanka, but
  - excluding a case involving a general agent of independent status acting in the ordinary course of business as such.

Further, under the transfer pricing provisions of the New Act, 'permanent establishment' is defined:

- in relation to a country with which an agreement has been entered into on avoidance of double taxation means, a permanent establishment defined in an agreement for the relief of double taxation where an agreement is in force between the government of Sri Lanka and the government of any territory in which any person and their agencies, branches, or establishments in Sri Lanka is resident, or

- in relation to a country with which an agreement has not been entered into on avoidance of double taxation, includes any business connection or a fixed place of business through which the business of the enterprise is wholly or partly carried out irrespective of the number of days of such business carried out in Sri Lanka.

Other taxes

Value-added tax (VAT)

VAT is payable on imported goods and on the supply of goods (including wholesale and retail trade where the turnover liable supplies per quarter is not less than LKR 3 million) and services in Sri Lanka. Provisions are made for filing returns monthly or quarterly, based on specified criteria. Even where returns can be filed quarterly, the tax payments are required to be made on a monthly basis by manufacturers and on a half-monthly basis by others. Certain specified imports and domestically supplied goods and/or services are exempt.

VAT is payable on the prescribed valuations of imports and domestic supplies at a standard rate of 15%. Exports and certain specified international services are zero-rated.

Registration for VAT arises only if the quarterly value of taxable supplies exceeds LKR 3 million or the annual value of taxable supplies exceeds LKR 12 million, except for supplies from wholesale and retail activities unless the total supplies (whether taxable, excluded, or exempted) exceed LKR 12.5 million per quarter.

The input tax paid on the imports and supplies of goods (including capital goods) and services in a month, and used in the business of making taxable supplies in that month, can be deducted from the tax payable (output tax) on such supplies, subject to a limitation of the lesser of 100% of output tax or the actual input tax paid.

Refunds of excess VAT paid are available to zero-rated supplies and to new businesses registered under Section 22 (7) of the VAT Act. A simplified VAT scheme is in place to relieve zero-rated suppliers and other qualified suppliers from the burden of paying input VAT, thereby obviating the need for the issue of refunds.

Customs duties

Customs duty is levied on the value for customs duty (i.e. transaction value). World Trade Organization (WTO) rules on customs valuations are implemented. Sri Lanka has a simplified three-tier tariff structure. The rates are published in the government gazettes. The current rates are 15%, 30%, and 0% (applies to few goods).

Special Commodity Levy

Special Commodity Levy is imposed on certain commodity items at the rate specified by the Minister by order published in the gazette at the point of importation of such commodities. The collection of Special Commodity Levy is undertaken by the Director General of Customs.

Special Commodity Levy is a composite levy, and no other tax, duty, levy, cess, or other charge is imposed in terms of any other laws specified as applicable in respect of the commodities specified in any such order.

Excise duties

Excise duties and special excise levies are charged on tobacco, cigarettes, liquor, motor vehicles, selected petroleum products, paints, air conditioners, dishwashers, household washing machines, and other products at various rates and at unit rates.

Stamp duty

Stamp duty is payable on specified instruments and documents at rates prescribed in the Gazette.

Payroll taxes

Employees Provident Fund (EPF)

Employers and employees are required to contribute specified percentages (employer 12%, employee 8%) of each employee's monthly emoluments/salary to the EPF established by the government. Alternatively, employers and employees can contribute to certain private provident funds approved by the labour authority.

Employees Trust Fund

Employers are also required to contribute a specified percentage (currently 3%) of each employee's monthly emoluments/salary to the Employees Trust Fund established by the government.

Share transaction levy

Share transaction levy at the rate of 0.3% is chargeable from both the buyer and the seller on the sale value of listed shares transacted through the Colombo Stock Exchange (CSE).

Economic Service Charge (ESC)

ESC is payable quarterly by all businesses at 0.5% of the aggregate turnover of the trade, business, profession, or vocation if the total turnover exceeds LKR 12.5 million for that quarter. ESC so paid is deductible from the CIT payable for that tax year. ESC is not refundable but can be carried forward for two immediately succeeding tax years to be set off against CIT payable.

Nation Building Tax (NBT)

NBT is chargeable at 2% from every person (a person includes a company) who imports any article on the 'liable turnover' from such importation, who carries on the business of manufacture of any article, who provides a service of any description, or on the wholesale or retail sale of any article (other than such sale by the manufacturer of that article) on the liable turnover of the relevant quarter. Certain specified articles or services are exempt from NBT.

The threshold for NBT is LKR 3 million per quarter, or LKR 12 million *per annum*.

Liable turnover means:

- In the case of importers, the value of any article ascertained under Section 6 of the VAT Act for the purpose of importation.
- In the case of manufacturers, the proceeds receivable, whether received or not, from the manufacture and sale of goods in Sri Lanka.
- In the case of service providers, the proceeds receivable, whether received or not.

- In the case of wholesale or retail traders, the proceeds receivable, whether received or not, other than pharmaceuticals, gems and jewellery sold for payment in foreign currency, and any article subject to the Special Commodity Levy sold by an importer.

In case of wholesale and retail traders, 50% of the liable turnover will be taxed at a zero rate and the remaining 50% will be taxed at 2%. In the case of a distributor as defined in the ESC Act, 75% of the liable turnover will be taxed at a zero rate and the remaining 25% will be taxed at 2%.

Bad debts, VAT, excise duty (other than such excise duty paid on importation) rebate under export development, or services in relation to an international event should not be included in the liable turnover.

Tourism development levy

Tourism development levy is payable by tourist hotels and institutions licensed under the Tourist Development Act on the turnover of such institutions at the rate of 1%.

Local taxes

Taxes (more usually called rates) are currently assessed and collected annually from the owners of land and premises by the local authorities of the areas in which the properties are located. These authorities also charge and collect annual licence fees from certain businesses.

Branch income

Foreign companies are permitted to register a place of business as an 'overseas company' in Sri Lanka under local company law, where the business carried on conforms to the stipulations made under the Foreign Exchange Act, No. 12 of 2017.

An overseas company registered under the Companies Act may also carry on in Sri Lanka any non-commercial, non-trading, or non-industrial activities, such as the activities undertaken or carried on by a liaison office, representative office, regional office, or other similar office, provided such activities do not directly or indirectly provide any income to the company.

In addition to paying the standard CIT, a trading branch is also subject to the 14% remittance tax on remittance of its after tax profits to its foreign head office.

The Sri Lanka-source income of foreign companies from a local 'place of business' is taxed at the CIT rate. However, under most DTTs that Sri Lanka has entered into, the income of a project carried out will not be liable for CIT if its duration is less than the period specified in the treaty concerned.

Further approval granted under the Inland Revenue Act No. 10 of 2006 for ascertainment of profits of a project as a percentage of receivables can be continued from year of assessment 2018/19 until the project is completed.

Income determination

Business accounting for CIT purposes should, unless otherwise specified by the tax statute, conform to Sri Lanka Financial Reporting Standards.

Inventory valuation

Inventories should be measured at the lower of cost and market value.

Capital gains

A gain made by a company on the realisation of an investment asset or liability (which is the amount by which the sum of the consideration received for the asset or liability exceeds the cost of the asset or liability) is subject to tax at 10%. Gains made on realisation of shares quoted in any official list published by any stock exchange licensed by the Securities and Exchange Commission of Sri Lanka are exempt from income tax. Such gains are subject to the share transaction levy chargeable at 0.3% on the seller as well as the buyer on the transaction value.

Dividend income

Resident company dividends paid on shares held by resident or non-resident persons are not assessable to the recipients if income tax is withheld on such dividends (*see the Withholding taxes section*) or the dividends are paid out of dividends received from resident companies.

Stock dividends

A capitalisation of profits, whether by way of a bonus share issue, increase in the amount paid-up on shares, or otherwise, whether distributed or not, is treated, by definition, as a dividend and is subject to the WHT of 14%.

Interest income

Interest income forms part of the total assessable income.

Interest accruing to any non-resident person or to any licensed commercial bank in Sri Lanka, on moneys invested in any sovereign denominated in foreign currency, issued on or after 21 October 2008, by or on behalf of the government of Sri Lanka, is exempt from income tax.

Royalty income

Royalty income can be business income or investment income that forms part of the total assessable income, which is liable to income tax at the standard rate of 28%.

Foreign income

Foreign income of a resident person forms part of the total assessable income.

Deductions

In calculating the income from a business or investment for a year of assessment, expenses incurred during the year, in the production of income from the business or investment, are permitted to be deducted.

Depreciation

Capital allowance for depreciation of assets acquired/constructed is granted based on the number of years applicable to the relevant depreciable asset as follows:

Depreciable assets	Number of years
Computers and data handling equipment, together with peripheral devices	5
Buses and minibuses, goods vehicles; construction and earthmoving equipment, heavy general purpose or specialised trucks, trailers, and trailer-mounted containers; plant and machinery used in manufacturing	5
Railroad cars, locomotives, and equipment; vessels, barges, tugs, and similar water transportation equipment; aircraft; specialised public utility plant, equipment, and machinery; office furniture, fixtures, and equipment; any depreciable asset not included in another class	5
Buildings structures and similar works of a permanent nature	20
Intangible assets, excluding goodwill	20 or the actual useful life

The allowance for depreciation for capital assets (e.g. plant and machinery) and qualified buildings constructed/acquired before 1 April 2018 can be computed and deducted as per the respective provision of the Inland Revenue Act No. 10 of 2006.

Goodwill

Capital allowance is not granted on the acquisition of goodwill.

Formation or liquidation expenses of a company

Expenses incurred in the formation or liquidation of a company are not allowed in computing the taxable income, as such expenses are not incurred in the production of income during the year.

Interest expenses

Interest paid or payable on borrowings for purposes of business are deductible, subject to the thin capitalisation rules (*see the Group taxation section*).

Bad debts and doubtful debts

A sum equal to the bad debts incurred in any business or investment that have become bad debts during the period for which the profits are being ascertained is allowed for tax purposes.

In the case of a bank or a financial institution, deductibility of a specific bad debt provision as may be specified by the Commissioner General of Inland Revenue (CGIR) would be allowed.

Charitable contributions

Relief is available as a deduction from taxable income for contributions in money to an approved charity, provided the charity is established for the provision of institutionalised care for sick or the needy, and contributions in money or in kind to the government of Sri Lanka. The deduction for the former is subject to a ceiling of one-fifth of the taxable income of the company or LKR 500,000, whichever is less. In the case of the latter, there is no limit to the deduction; however, and any un-recouped excess of such contributions over the taxable income cannot be carried forward and deducted from the following year's taxable income.

Investment and other allowances

Any balance allowance as at 31 March 2018 deductible from taxable income under the Inland Revenue Act, No. 10 of 2006 can be deducted in accordance with provisions of the new Inland Revenue Act No. 24 of 2017 (subject to conditions) from the year of assessment 2018/19.

Finance lease allowances

Any profit, loss, receipt, or payment of a finance lease agreement entered into prior to 1 April 2018 can be computed in accordance with the respective provisions of the Inland Revenue Act, No. 10 of 2006.

According to the provisions of Inland Revenue Act No. 24 of 2017, payments made under finance lease agreements entered into after 1 April 2018 shall be treated as interest and a repayment of capital under a loan made by a lessor to lessee, and accordingly interest payments on a finance lease are deductible from profits and income while capital allowances are claimed for capital repayments of leased assets.

Termination gratuities

Termination gratuities paid to employees on cessation of business and contributions made by an employer to an employee's account with a pension, provident, or savings fund or savings society approved by the CGIR are deductible.

Royalties and ground rents

Any royalty or ground rent payable is deductible, subject to the general rule of being incurred in the production of income during the year, and, if WHT has been deducted, it has been remitted to the CGIR.

Interest, fines, and penalties

Interest, fines, and penalties paid or payable to a government or a political subdivision of a government of any country for breach of any written law are not deductible for tax purposes.

Taxes

Sri Lanka income tax payable and taxes or other levies specified by the CGIR are not deductible.

Non-deductible expenses

In ascertaining the total income liable to CIT from the financial accounts filed by a company, the following deductions, including any expense of a capital nature (other than repairs and improvement expenses subject to certain restrictions, R&D, and agricultural start-up expenses), are not be allowed:

- Domestic expenses incurred by the person.
- Income tax payable.
- Interest, fines, and penalties payable to a government or a political subdivision of a government of any country for breach of any written law.
- Expenditure to the extent incurred by a person in deriving exempt amounts or final withholding payments.
- Retirement contributions, unless they are included in calculating the income of an employee or consist of a contribution by an employer to a pension, provident,

or savings fund or a savings society that is approved by the CGIR, subject to any specified conditions.
- Dividends of a company.
- Outlays or expenses for entertainment.
- An amount that a person has transferred, in one's financial accounts, to a reserve or provision for expenditures or losses not yet incurred but expected to be incurred in a future year of assessment.
- Amounts incurred on lotteries, betting, or gambling, other than amounts incurred from conducting a business of lotteries, betting, or gambling.
- Taxes or other levies specified by the CGIR.

Also, no deduction is allowed where a person is required to withhold tax from certain payments until the tax withheld has been paid to the CGIR.

Net operating losses

In calculating the income from a business for a year of assessment, the following shall be deducted:

- an unrelieved loss of the person for the year from any other business, and
- an unrelieved loss of the person for any of the previous six years of assessment from the business or any other business.

However, the loss can be deducted only in calculating income taxed at the same rate, a lower reduced rate, or exempt amounts.

Unrelieved losses from a business may be deducted in calculating income from an investment, whereas unrelieved losses from an investment can be deducted only in calculating income from an investment.

Any balance loss as at 31 March 2018 shall be deemed to be a loss incurred in the year of assessment 2018/19 and be deductible in accordance with provisions of the new Inland Revenue Act No. 24 of 2017 (within six years without being subject to the 35% of the statutory income limitation but subject to other restrictions).

A gain from the realisation of an investment asset cannot be set off against any loss on the disposal of another investment asset.

Payments to foreign affiliates

Any payment made to an affiliate is allowed for tax purposes, provided such payment is in the nature of revenue and is incurred in the production of income.

Group taxation

There are no special provisions for taxation of companies in a group in Sri Lanka. Each company is taxed independently of others in the group.

Transfer pricing

Any income, gains, and profits arising, derived, or accruing from, or any loss incurred in, any transaction entered into between two associated enterprises shall be ascertained with regard to the arm's-length price.

Thin capitalisation

Interest payments (financial cost) made to any person are restricted to the debt-to-equity ratio of 3:1 for manufacturing companies and 4:1 for other companies. Any excess amount of finance costs arising due to this restriction can be carried forward and treated as incurred during any of the following six years of assessment, subject to the above limitation.

Controlled foreign companies (CFCs)

There are no provisions in the tax statute regarding CFCs.

Tax credits and incentives

The following exemptions and incentives granted under the provision in another law or an agreement that is in force on date of commencement (1 April 2018) of the New Inland Revenue Act, No. 24 of 2017 will continue to be in force:

- Any unexpired part of the exemptions as at 31 March 2018 granted under sections 16C, 16D, 16E, 17, 17A, 18, 20, 24A of the Inland Revenue act No. 6 of 2010 will continue to be exempt under the new Inland Revenue Act No. 24 of 2017.
- Fully or partly exempt profits or profits taxed at reduced rate of income tax under the provisions of previous Inland Revenue Acts of an enterprise/company that has entered into an agreement with the Board of Investment of Sri Lanka under section 17 of the Board of Investment of Sri Lanka Law will continue to be exempt or be liable to tax at the rate provided in the agreement under the new Inland Revenue Act No. 24 of 2017 as well.

  Any unexpired part of the profits and income liable for concessionary rates under 59D, 59I, 59J, 59K, 59L, 59M of the Inland Revenue Act, No. 10 of 2006 as at 31 March 2018 will continue as specified in those provisions under the new Inland Revenue Act No. 24 of 2017 as well.

Further, the carried forward notional tax credit relating to treasury bills and treasury bonds, as per the Inland Revenue Act, No. 10 of 2006, can be carried forward to be set off against the income tax liability within three consecutive years from the year of assessment 2018/19.

Enhanced depreciation allowance

A person who invests in Sri Lanka (other than the expansion of an existing business) during a year of assessment shall be granted enhanced depreciation allowances in addition to the depreciation allowances, computed on the expenses incurred during the year of assessment on depreciation assets, other than intangibles assets.

Investment amount during the year of assessment	Place of investment	Rate of depreciation (%)
Exceeds 3 million United States dollars (USD) but does not exceed USD 100 million	Any part of Sri Lanka other than Northern Province	100
Exceeds USD 100 million	Any part of Sri Lanka other than Northern Province	150
Exceeds USD 250 million by a state-owned company	On the assets and liabilities of a state-owned company in any part of Sri Lanka	150
Exceeds USD 3 million	Northern Province	200

Exemption of certain dividends from WHT

If a company has incurred more than USD 1,000 on depreciable assets (other than intangible assets) in Sri Lanka, the dividends paid by such company to a non-resident member does not attract WHT in Sri Lanka.

Exemption of employment income from WHT

If a company that pays dividends has incurred more than USD 1,000 on depreciable assets (other than intangible assets) in Sri Lanka, where the number of expatriate employees is not exceeding 20, the rate of tax to be withheld from a payment made by that company (employer) to an expatriate employee shall be zero.

Foreign tax credit

A foreign tax credit is to be granted in respect of any foreign income tax paid or payable in respect of foreign income, which should be calculated separately for each year of assessment, separately for assessable foreign income from each employment, business, investment, or other source, and further separately for each gain from the realisation of an investment asset. Such credit should not exceed the average rate of Sri Lankan income tax of the person for the year, applied to the person's assessable foreign income.

A foreign tax credit shall be allowed only if the foreign income tax is paid within two years after the end of the year in which the foreign income to which the tax relates was derived by the resident person or within such further time as the CGIR may allow.

Withholding taxes

Resident companies are required to withhold tax at 14% on interest, discount, charge, natural resource payment, rent, royalty, premium or retirement payment, or pay amounts as winnings from a lottery, reward, betting, or gambling, and where the payment or allocation has a source in Sri Lanka.

Every bank and financial institution is required to withhold income tax at 5% on the amount of any interest paid to a company on any sum of money deposited with it. The depositor is entitled to receive a certificate setting out the gross amount of interest, the amount of tax withheld, and the net amount of interest paid. With respect to Treasury bills and Treasury bonds issued by the Central Bank, no WHT is deductible at the time of the sale of the Treasury bills and Treasury bonds by the Central Bank in the primary market.

Payment	WHT rate (%)
Dividends:	
Paid by a resident persons	14
Non-resident company on remittance of profits (remittance tax)	14
Interest	14
Interest or discount paid by banks and financial institutions to resident and non-resident persons (WHT will not apply to interest or discount paid to any person on security or Treasury bond or Treasury bill)	5
Rent:	
Paid to a resident person	10
Paid a non-resident person	14
Service fee and contract payments:	
Royalty premium	14

Sri Lanka

Payment	WHT rate (%)
Payments to resident individuals exceeding LKR 50,000 (no deduction if such payments are chargeable with ESC)	5
Winnings from a lottery, reward, betting, and gambling	14
Service fee or an insurance premium with a source in Sri Lanka to a non-resident person (no deductions if such payments are chargeable with ESC), subject to rates specified in DTTs	14
Payments made by a person to a non-resident person who is in the business of transport or telecommunication	2

Treaty WHT rates

Currently, Sri Lanka has entered into 44 DTTs as set out below:

	WHT (%)		
Recipient	**Dividends**	**Interest**	**Royalties**
Non-resident	14	20	20
Treaty (9):			
Australia	15	10	10
Bangladesh	15	15	15
Belarus	7.5/10 (7)	10	10
Belgium	15	10	10
Canada	15	15	10
China	10	10	10
Denmark	15	10	10
Finland	15	10	10
France	15	10	0/10 (1)
Germany	15	10	10
Hong Kong (4)	-	-	-
India	7.5	10	10
Indonesia	15	15	15
Iran	10	10	8
Italy	15	10	10
Japan	10	15 (2)	0/7.5 (1, 3)
Korea, Republic of	10/15 (5)	10	10
Kuwait (4)	-	-	-
Luxembourg	7.5/10 (7)	10	10
Malaysia	15	10	10
Mauritius	10/15 (6)	10 (2)	10
Nepal	15	10/15 (8)	15
Netherlands	10/15 (5)	10 (2)	10
Norway	15	10	0/10 (1)
Oman (4)	-	-	-
Pakistan	15	10	20
Palestine	10	10	10
Philippines	10	10	10
Poland	15	10	10
Qatar	10	10	10
Romania	12.5	10	10
Russia	10/15 (5)	10	10
Saudi Arabia	-	-	-
Seychelles	7.5/10 (7)	10	10

Recipient	WHT (%) Dividends	Interest	Royalties
Singapore	7.5/10 (7)	10	10
Sweden	15	10	10
Switzerland	10/15 (5)	10	10
Thailand	15	10	15
United Arab Emirates	10	10	10
United Kingdom	15	10	10
United States	15	10	10
Vietnam	10	10	15

Notes

1. 0% for copyright royalties.
2. 0% in certain circumstances.
3. 50% of normal tax, which is 7.5%.
4. These treaties are limited to the avoidance of double taxation of income from international transport by air.
5. 10% applies if the beneficial owner is a company that directly holds at least 25% of the capital of the company paying the dividends. In all other cases, the rate is 15%.
6. 10% applies if the beneficial owner is a company that directly holds at least 10% of the capital of the company paying the dividends. In all other cases, the rate is 15%.
7. 7.5% of the gross amount of the dividends if the beneficial owner is a company that directly holds at least 25% of the capital of the company paying the dividends.
8. 10% applies to banking business only.
9. When the treaty rate is higher than the rate specified by the domestic tax statute, the lower rate can be applied subject to obtaining a confirmation from the International Tax Branch of the tax authority.

Tax administration

Taxable period

A tax year is any period of 12 consecutive months reckoned from 1 April in any calendar year to 31 March of the following year.

Tax returns

Return of income is due within eight months from the end of the year of assessment.

Payment of tax

Sri Lanka has a pay-and-file system under which the CIT payable for each tax year is required to be paid in four instalments. In the case of companies with year ended 31 March, CIT instalments should be paid respectively for the first, second, third, and fourth quarters, on or before 15 August, 15 November, and 15 February of the tax year and 15 May immediately following the end of the tax year. In the case of companies with year ended other than 31 March, each tax instalment is due on or before the 15th day after each three-month period.

Tax audit process

The tax authority may select tax files for an audit on a random basis or if there is any specific information relating to a taxpayer that warrants investigation.

Statute of limitations

No assessment on income tax payable can be raised on a taxpayer who has duly filed a return of income after the expiry of a period of 30 months from the date the taxpayer filed the return.

Topics of focus for tax authorities

Tax authorities, in their audit, primarily focus on whether disallowable expenses have been added back to taxable profits and on profit margins reported. With the requirement to obtain tax clearance for remittance of fees and other payments abroad, increasing attention is paid to remittance of royalties, fees, and other payments to non-resident persons. Transfer pricing audits are also now taking place.

Taiwan

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Significant developments

Change to the corporate income tax (CIT) rate, profit retention tax rate, and dividend withholding tax (WHT) rate

On 18 January 2018, the Legislative Yuan passed amendments to the Income Tax Act, increasing the CIT rate from the previous 17% to 20% and reducing the profit retention tax on undistributed earnings from the previous 10% to 5% for income earned from taxable year 2018 onwards. For companies having taxable income less than 500,000 new Taiwan dollars (TWD), the CIT rate will increase gradually by 1% per year from 2018 onwards up till 20%.

Further, the dividend WHT rate for foreign shareholders is increased from 20% to 21%. For dividends distributed to foreign shareholders, the profit retention tax on undistributed earnings can no longer be credited against dividend WHT, with the exception of 2018 (i.e. dividends distributed in 2018 can still utilise the tax credit).

New income tax system for provision of cross-border electronic services after 1 January 2017

A new tax system has been implemented to address income tax treatment of remuneration derived by foreign enterprises from provision of cross-border electronic services to Taiwanese consumers (including individuals and profit-seeking enterprises and organisations). This new tax system provides rules governing determination of Taiwan-sourced revenues, calculation of taxable income, and methods of taxation, and is effective from 1 January 2017 onwards.

Depending on the business model and situation of the taxpayer, costs/expenses can be deducted and the taxable income can be further reduced via use of a ‘contribution ratio’. Therefore, going forward there may be annual compliance requirements that need to be fulfilled.

Three tier transfer pricing documentation

Starting from 2017, in addition to the already required transfer pricing report, corporations will also need to provide a Master File and a Country-by-Country Reporting (CBCR) file. *See the Group taxation section for more information.*

Common Reporting Standard (CRS)

The Legislative Yuan passed amendments to Articles 5-1 and 46-1 of the Tax Collection Act on 26 May 2017, establishing the legal basis for implementation of Automatic Exchange of Information (Including Financial Account Information) for Tax Purposes. Subsequently, on 16 November 2017, the Ministry of Finance (MoF) announced

Regulations Governing Common Reporting for Financial Institutions. Under the announced Regulations, the CRS will be implemented in 2019 and exchange of information with foreign countries will start in 2020.

Anti-tax avoidance rules

The Income Tax Act was amended in July 2016 to include anti-tax avoidance rules in Article 43-3 (Controlled Foreign Company [CFC]) and Article 43-4 (Place of Effective Management [PEM]) of the Income Tax Act.

In general, profits retained at the CFC level, which is located in a low tax rate jurisdiction and without commercial substance, will be taxed in advance at the Taiwan parent company level. In the past, taxation of foreign investment income was deferred until the Taiwan parent company received dividend income. Going forward, qualified investment income will be deemed distributed and taxable in Taiwan in advance. As of 31 May 2017, the Ministry of Finance has announced draft Regulations Governing Controlled Foreign Companies, but the final version has yet to be promulgated.

For PEM rules, under this new tax regime, if a foreign company meets all three criteria triggering the PEM definition, including (i) decision making location, (ii) record keeping and maintenance location, and (iii) actual operating location are all in Taiwan, the foreign enterprise will be deemed as having its head office in Taiwan and will be subject to tax assessment in accordance with the Taiwan Income Tax Act and other tax regulations. The Regulations Governing Places of Effective Management were announced by the Ministry of Finance in May 2017.

However, the CFC and PEM taxation mechanisms have yet to take effect. The actual effective date is to be determined by the Executive Yuan.

Tax treaties

Recently, Taiwan's tax treaty network has increased to include treaties with Canada, Japan, Poland, and the Czech Republic. Apart from Czech Republic, the treaties have all come into effect as of 1 January 2018. The treaty with the Czech Republic will become effective after necessary domestic procedures are completed. Taiwan has also signed a treaty with China; however, this tax treaty has not yet come into effect.

Taxes on corporate income

With effect from 1 January 2018, the CIT rate in Taiwan is 20%. However, for profit-seeking entities with less than TWD 500,000 in taxable income, the CIT rate is 18% in 2018, 19% in 2019, and 20% in 2020 if taxable income exceeds TWD 120,000.

Resident companies in Taiwan are taxed on their worldwide income as follows:

Taxable income (TWD)	Tax thereon
Up to 120,000	Exempt
120,001 and over	20% of total taxable income*

* Note: If taxable income is less than TWD 500,000, the tax rate is 18% in 2018 and 19% in 2019.

A non-resident company is taxed on income derived from Taiwan sources. A non-resident company with a fixed place of business (FPOB) or business agent in Taiwan is taxed similarly to a resident company (i.e. subject to filing of an annual CIT return based on the same CIT rate provided above). A non-resident company having no FPOB or business agent in Taiwan is subject to WHT at source on its Taiwan-sourced income. WHT rates on dividends, interest, and royalties may be reduced if the recipient is a tax resident of a tax treaty country and the relevant treaty provides for a reduced rate. *See the Withholding taxes section for more information*.

Tonnage tax system

A qualifying enterprise having its head office in Taiwan engaged in maritime transportation may elect to be taxed under the tonnage tax system, where a lump sum tax is calculated on the net tonnage of their fleet. Once the application is approved, the enterprise must remain under the tonnage tax system and cannot switch to the regular tax system at its discretion for ten consecutive years. Furthermore, loss carryforwards and tax incentives are not eligible under the tonnage tax system.

Profit retention tax

An additional profit retention tax is imposed on any current earnings of a corporation that remain undistributed by the end of the following year. With effect from 1 January 2018, profit retention tax is 5% (previously 10%). Taiwan branches of foreign companies are not subject to profit retention tax.

Imputation tax system

Beginning 1 January 2018, Taiwan no longer operates an imputation system. Imputed tax credits can no longer be used by resident individuals or non-resident shareholders to offset their income tax liabilities or dividend WHT. However, an exception is granted for non-resident shareholders for 2018, whereby dividends distributed in 2018 can still utilise the profit retention tax credit. The profit retention tax credit is calculated based on a prescribed formula and subject to a ceiling, with only 50% of the credit from profit retention tax paid to be used to offset the dividend WHT.

Income basic tax (IBT)

All Taiwan resident companies, as well as non-resident companies with an FPOB or business agent in Taiwan, should calculate IBT if they earn certain income that is tax-exempt. The basic income of a company is the amount calculated in accordance with a formulae stipulated by the government, with a deduction of TWD 500,000. The IBT rate is 12%. If the IBT amount is greater than the regular CIT amount, taxpayers must pay income tax based on the regular CIT amount plus the difference between the IBT amount and the regular CIT amount. On the other hand, if the regular CIT amount is greater than the IBT amount, no special action is required.

Corporate residence

A company is a resident of Taiwan for CIT purposes if it is incorporated in Taiwan. A non-resident company that has an FPOB or business agent in Taiwan is obligated to file a CIT return in Taiwan on its Taiwan-sourced income.

Permanent establishment (PE)

The term ‘permanent establishment’ only exists in the underlying double tax agreements (DTAs) signed with Taiwan. Taiwan domestic tax regulations only refer to an FPOB and business agent, which generally follows the definitions of an FPOB and agency PE in the Organisation for Economic Co-operation and Development (OECD) Model Tax Convention.

Other taxes

Business tax

All sales of goods and services in Taiwan, as well as the importation of goods into Taiwan, are subject to business tax. There are two types of business tax systems: value-added tax (VAT) and gross business receipts tax (GBRT).

Sellers and service providers are generally obligated to pay business tax for the sales of goods or services within Taiwan unless the law provides otherwise. For importation of goods, the business tax will be paid by the goods receivers or buyers via customs. For importation of services sold by foreign companies to Taiwanese buyers, business tax shall be paid by the service buyers. However, the service buyer (corporate entity) will not be required to pay business tax if it is exclusively engaged in taxable transactions subject to either 5% or 0% VAT.

Despite the above, Taiwan has formally implemented a new VAT mechanism starting 1 May 2017 for cross-border sales of business-to-consumer (B2C) electronic services. Under the new mechanism, sales of cross-border electronic services by corporate sellers to individual buyers require the foreign companies to register for VAT purposes in Taiwan, file VAT returns, and pay VAT if their annual sales exceed the promulgated threshold of TWD 480,000.

Value-added tax (VAT)

VAT is applicable to general industries, and the VAT rate is 5%. Under the VAT system, each seller collects output VAT from the buyer at the time of sale, deducts input VAT paid on purchases from output VAT, and remits the balance to the tax authority.

Gross business receipts tax (GBRT)

GBRT is applicable to specified industries (e.g. financial institutions, small businesses). For investment trust companies, securities and futures firms, short-term commercial paper enterprises, and pawnshops, the rate is 2%. The GBRT rate on revenues derived from the core business operations of banks and insurance enterprises is 5%. For re-insurance enterprises, the rate is 1%.

Customs duties

Taiwan uses the Customs Cooperation Council Nomenclature (CCCN) to classify goods and set duty rates. The customs duty is payable by the consignee or the holder of the bill of lading for imported goods, and is based on the dutiable value or the volume of goods imported.

Commodity tax

Commodity tax (excise duty) is levied on certain commodities, as specified in the Commodity Tax Act (including rubber tyres, beverages, cement, plate glass, oil and gas, electrical appliances, and vehicles), at the time when such goods are dispatched from a factory or when imported. Tax rates vary from 8% to 30% and are applicable to different types of commodities based on the value of the goods or its volume in specific circumstances.

Type of commodity	Tax rate
Rubber tyres	10% or 15%
Beverages	8% or 15%
Cement	TWD 280 to TWD 600 per ton
Plate glass	10%
Oil and gas	TWD 110 to TWD 6,830 per kilolitre or TWD 690 per ton
Electrical appliances	10% to 20%
Vehicles	15% to 30%

Property tax

Land and buildings are annually assessed for tax based on their officially assessed values as determined by the government authorities at the applicable rate. The land value tax rate ranges from 1% to 5.5% of the assessed land value. The building tax rate for commercial properties is 3% to 5% of the assessed value, and the rate for non-commercial properties is 1.2% to 3.6% of the assessed value.

Land value increment tax (LVIT)

The sale of land is currently subject to LVIT and payable by the seller. The tax is levied on the increase in the government-assessed value of the land during the ownership period, adjusted for inflation, at regular progressive rates ranging from 20% to 40%, or a special rate of 10%.

Real property transfer tax

The new real property transfer tax regime is applicable to all properties acquired on or after 1 January 2016, as well as those bought on or after 2 January 2014 if held for less than two years. The taxable base is the market value of the properties reduced by related costs, expenses, and the increase in government-assessed land value for LVIT purposes. A rate of 17% will apply on Taiwanese corporate taxpayers; whereas, a tax rate of 35% or 45% will apply on profit-seeking enterprises with foreign head offices located outside of Taiwan (i.e. Taiwan branch), depending on whether the property is held for more than or less than one year.

LVIT will remain unchanged by the implementation of the new real property transfer tax regime on property transactions. The total amount of land value increment is deducted from real estate transaction income to avoid double taxation. The old property tax regime still applies to properties purchased prior to 2 January 2014, or those bought on or after 2 January 2014 if held for more than two years, where only gain from sale of buildings is subject to CIT assessment, while gain from sale of land is exempt from CIT assessment, and LVIT applies to increment in government-assessed value of land instead.

Deed tax

Currently, transactions of immovable property involving sale, creation of *Dien*, exchange, bestowal, partition, or acquisition of ownership by virtue of possession are subject to deed tax. The deed tax rates range from 2% to 6%, depending on the types of transactions involved.

Stamp tax

Stamp taxes are imposed on each copy of the following documents executed within the territory of Taiwan (with the following respective tax rates):

- Monetary receipts must have a revenue stamp of 0.4% of the amount received per piece. However, a receipt for the money deposited by the bidder requires a revenue stamp of 0.1% of the amount received per piece.
- Contract or deed for the sale or purchase of movable property must have a revenue stamp of TWD 12 per piece.
- Contractual agreement under which one party agrees to complete a specific piece of work for the other party for consideration must have a revenue stamp of 0.1% of the contract price.
- Contract for the sale, transfer, and partition of real estate must have a revenue stamp of 0.1% of the contract price.

Securities transaction tax

Tax is levied on securities transactions at the rate of 0.3% on gross proceeds from the sale of domestic shares. Trading in corporate bonds and financial bonds issued by Taiwan companies is temporarily exempt from securities transaction tax assessment.

Luxury tax

A 10% luxury tax applies to the sale of passenger cars, private jets, and helicopters valued at TWD 3 million or more, as well as to the sale of yachts that are at least 30.48 metres (100 feet) long. Preserved wildlife products (including turtle shells, hawksbill, coral, ivory, furs, and their products), high-end furniture, and non-refundable memberships worth TWD 500,000 or more are also taxed at 10%.

As of 1 January 2016, luxury tax is no longer levied on sales of real estate properties.

Payroll taxes

There are no payroll taxes other than those for social security contributions (*see below*).

Social security contributions

There are compulsory social security programs that require contributions from employers and employees based on monthly insured salary, which is capped at various amounts for labour insurance, health insurance, and pensions. Taiwan social security programs include the following:

- Labour Insurance Program: Where a company hires five or more employees, it is obligated to insure all employees (including domestic and foreign employees) under the labour insurance program run by the government. Companies with less than five employees may also apply for labour insurance coverage for their employees. The premium rate for ordinary insurance is 9.5% on the employee's monthly insured salary up to TWD 45,800, with an additional 1% levied for unemployment insurance. The employer is required to contribute 70% of this premium.
- National Health Insurance Program: The premium rate for each insured person is set at 4.69% of a domestic/foreign employee's monthly insured salary, up to TWD 182,000. The employer is required to contribute 60% of this premium. Further, the employer bears the cost of both the employee itself and that of the average dependant, which amounts to 1.61 headcount per employee. Moreover, under the Second Generation National Health Insurance Program, the employer needs to bear a supplementary premium (at the rate of 1.91%) where the monthly pay (including both regular and non-regular pay) exceeds the monthly insured salary range, which is capped at TWD 182,000 for any individual.
- Labour Pension Program: An employer needs to make monthly contributions to a domestic employee's individual pension account set up with the Labour Insurance

Bureau. The monthly contribution rate borne by the employer should be at least 6% of the employee's monthly insured salary up to TWD 150,000.

Branch income

A non-resident company whose head office is located outside of Taiwan must keep separate books for its branch in Taiwan. A head office or regional headquarters' general and administrative expenses may be allocated to the branch under certain conditions. CIT is assessed only on the branch's profits. A Taiwan branch should complete an annual CIT return.

A Taiwan branch of a foreign company may remit after-tax profits to its foreign head office without further tax due.

Motion picture leasing

A foreign motion picture's branch in Taiwan can deem 45% of its revenue from leasing of motion pictures as cost. However, if a foreign enterprise with no branch office in Taiwan leases motion pictures through agents, 50% of the revenues can be deemed as taxable income.

Deemed-profit method

A non-resident company that is engaged in international transportation, construction contracting, provision of technical services, or machinery and equipment leasing within Taiwan, and where the cost and expenses are proven to be difficult to calculate, may apply for advance approval from the National Tax Administration (NTA) to adopt the deemed-profit method to determine the taxable income as 10% or 15% of the gross revenues. This will effectively reduce the WHT rate to 2% or 3% on gross revenues once the approval is obtained from the NTA.

For non-resident enterprises providing cross-border electronic services to Taiwanese buyers (including individuals and profit-seeking enterprises and organisations), the non-resident company may apply to the NTA to adopt a deemed-profit method based on its business model and industry.

Income determination

A Taiwan resident company is taxed on its net income, which is defined as gross annual income after deduction of costs, expenses, losses, and taxes. Except for certain exempt items, income from all sources, including offshore and onshore, is subject to CIT.

A non-resident company is only taxed on its Taiwan-sourced income. Article 8 of the Income Tax Act and the related Guideline defines the types of income that should be regarded as sourced from Taiwan. For example, fees received by a non-resident company for service performed entirely outside of Taiwan are exempt from income tax assessment, subject to supporting evidentiary documents.

Inventory valuation

Inventory must be valued at cost. If cost exceeds the net realisable value, the latter may be used as the valuation basis. Cost may be determined by the first in first out (FIFO), moving average, weighted average, specific identification, or any other method approved by the tax authorities. Conformity between financial and tax reporting is not required.

Capital gains

Gains on the disposal of fixed assets are taxable as current-year income of the company, with the exception of gains on the sales of land under the old real estate taxation regime. Capital gains on disposal of Taiwanese marketable securities and futures by resident companies and non-resident companies with an FPOB or business agent in Taiwan are exempt from CIT assessment, but are liable for IBT of 12%, with an exemption amount of TWD 500,000. Capital losses may be deducted against capital gains and carried forward for five years. 50% of capital gains can be tax exempt should the securities be held for more than three years. In addition, securities transaction tax is levied on the sales proceeds (*see the Other taxes section*).

Dividend income

Dividends received from resident investee companies by a resident corporate shareholder are not included in taxable income. However, dividends received from foreign subsidiaries are taxable, but credits are given for the WHT paid offshore, limited to the incremental tax liability that would result if the dividends were added to the Taiwan corporate shareholder's taxable income and taxed at the Taiwan CIT rate.

Interest income

Interest received on commercial paper and certain other interest-bearing financial instruments is subject to WHT of 10% and 15%/20% for resident and non-resident taxpayers, respectively (*see the Withholding taxes section*). This income should be reported as current-year income, and the WHT paid can be deducted against the income tax payable.

Royalties and technical service fees

Non-resident companies who receive royalties for licensing patents both registered in Taiwan and overseas, trademarks registered in Taiwan, and computer software copyright licensed to Taiwan companies, or who receive technical service fees in relation to construction of factories/plant/power plants to Taiwan companies incorporated as companies limited by shares, can apply for income tax exemption by obtaining advance approval from both the Industrial Development Bureau and the tax authorities. For licensing of patents and technical service fees, the Taiwan licensee company needs to be engaged in designated industries. The amendments to the relevant regulation governing the applicable criteria are effective retroactively for contracts concluded after 1 January 2011.

Foreign income

Taiwan adopts a worldwide tax system to tax its resident companies (including the Taiwan subsidiaries of foreign companies). In theory, taxation on foreign investment income of a Taiwanese company is deferred until cash is repatriated to Taiwan. However, given Taiwan also taxes undistributed profits based on net income shown on the income statement (*see Profit retention tax in the Taxes on corporate income section*), foreign investment income may still be taxed in Taiwan before cash is repatriated back to Taiwan.

Deductions

Depreciation

Depreciation on all fixed assets other than land, including premises, plants (buildings), and equipment, which are used to generate income, is allowed as a deduction. The straight-line, fixed percentage on diminishing book value, sum-of-years-digit, unit-of-production, and working-hour methods are acceptable depreciation methods to the tax office. The useful lives of typical assets are shown below:

Asset category	Useful life (years)
Computer equipment	3
Furniture and fixtures	5
Automobile	5
Building	50

With the approval of the tax authority, a company may revalue its fixed assets each time the government's wholesale price index increases by 25% over the base period. A company's base period is established at the time of purchase of fixed assets or at such time when a company revalues its fixed assets. Any increase in fixed assets may then be depreciated for tax purposes.

Goodwill

Goodwill is commonly realised from merger and acquisition, which should follow the purchase method as defined under Taiwan Generally Accepted Accounting Principles (GAAP) or International Financial Reporting Standards (IFRS). Goodwill should be amortised for 15 years if a valuation report is issued by a creditable professional valuation firm and the net identifiable assets are valued separately. However, in practice, the amortisation of goodwill is frequently challenged by the Taiwan tax authority.

Start-up expenses

Start-up expenses during the start-up period can be deducted in the year incurred. The start-up period is from the preparatory stage to the date the business starts to generate significant revenue from its primary business operation.

Interest expenses

Interests on loans that are used for business purposes are deductible in the year incurred. However, for a loan from a non-financial institution, the interest rate shall not exceed 15.6% *per annum*. As for interest on inter-company loans, the deductible amount is subject to the thin capitalisation rule and transfer pricing regulations (*see the Group taxation section*).

Bad debt

Actual losses on bad debts are allowed for deduction when certain legal proceedings or time requirements have been satisfied. The loss should first be charged against the bad debt provision, which should not exceed either 1% of accounts receivable and notes receivable outstanding, or the actual average bad debt ratio for the past three years.

Charitable contributions

Charitable contributions to support national defence, troop morale, contribution to government of any level, and donation made with special approval of the MoF are not subject to any tax limit. Donations to other parties are subject to prescribed limits under the relevant regulations.

Fines and penalties

Fines and penalties arising from violation of various tax laws are generally not deductible.

Taxes

All taxes, other than income tax, are generally deductible, unless where such taxes are related to tax-exempt income. The tax associated with the acquisition of real estate should be included in the cost of the land or building.

Net operating losses

A company's net operating losses can be carried forward for ten years. Losses cannot be carried back.

Payments to foreign affiliates

Royalties, interest, and service fees paid to a foreign affiliate are subject to WHT. Royalties or service fees paid to a foreign entity may be tax-exempt if certain requirements are met and prior approval is obtained.

Group taxation

Group enterprises meeting certain criteria under the Financial Holding Company Act and Business Mergers & Acquisitions Act may file consolidated tax returns for the Taiwan parent and its first tier Taiwan subsidiaries. For other enterprises, group taxation is not permitted. The Taiwan parent is eligible to file consolidated tax returns if it continuously holds over 90% of the shares of the subsidiaries for 12 months in a tax year.

Transfer pricing

Transfer pricing regulations were established to constrain multinational corporations from leaving their profits in countries with lower tax rates. For applicable companies, the disclosure of related-party transactions in the CIT return and the preparation of a transfer pricing report is required. Upon request, the transfer pricing report will have to be submitted to the Taiwan tax authority within one-month of notice. The transfer pricing report must demonstrate the company's good faith effort to comply with the assessment rules. Without proper reason, failure to comply with such rules will result in additional tax payable and financial penalties. The types of transactions governed by these regulations include the following: transfer of tangible assets, use of tangible assets, transfer of intangible assets, use of intangible assets, rendering of services, use of funds, business restructuring, and other types of transactions prescribed by the MoF.

If related-party transaction amounts exceed certain thresholds laid out below, an advance pricing agreement (APA) with the tax authority may be obtained to eliminate risk of inter-company prices being challenged. The criteria for applying for an APA are as follows:

- The total amount of the controlled transaction covered under the APA is at least TWD 500 million or the annual amount of such controlled transaction is at least TWD 200 million.
- There has been no significant act of tax evasion in the past three years.
- The required documentation for the APA application has been well prepared, including the transfer pricing report.
- Other criteria specified by the MoF are satisfied.

Three tier transfer pricing documentation

In addition to a transfer pricing report, corporations also need to provide a Master File and a Country-by-Country Reporting (CBCR) file.

The Master File is to contain information on the corporation's group's value chain analysis, description of intangible assets, and financing activities. The threshold for being exempted from needing to prepare a Master File is each individual Taiwan local entity's total net operating revenues and non-operating income being less than TWD 3 billion, or over TWD 3 billion but with total absolute value of cross-border controlled transaction(s) amounting to less than TWD 1.5 billion in the current year.

The CBCR file is to contain information relating to the allocation of the corporation's group's profit/loss, resources, taxes paid, and primary activities performed by each entity. The threshold for being exempted from preparing a CBCR file is the corporation's group's consolidated group revenues and non-operating income being less than TWD 27 billion (approximately equal to the OECD's threshold of 750 million euros [EUR]) in the preceding year.

Thin capitalisation

Deductible interest expense on inter-company loans is capped at a prescribed debt-to-equity ratio of 3:1. The thin capitalisation rule generally applies to profit-seeking enterprises, except banks, credit cooperatives, financial holding companies, bills finance companies, insurance companies, and securities companies.

Controlled foreign companies (CFCs)

Currently, profits of overseas subsidiaries held by Taiwan companies are not subject to 20% CIT in Taiwan until such profits are repatriated to Taiwan as dividend income. However, under the new CFC mechanism expected to take effect in the future, qualified investment income will be deemed distributed and taxable in Taiwan in advance, even if profits have not actually been distributed.

Place of effective management (PEM)

Under the new tax regime, if a foreign company meets all three criteria triggering PEM definition, including (i) decision making location, (ii) record keeping and maintenance location, and (iii) actual operating location are all in Taiwan, the foreign enterprise will be deemed as having its head office in Taiwan and will be subject to tax assessment in accordance with Taiwan Income Tax Act and other tax regulations. A foreign enterprise may voluntarily apply to be subject to the PEM taxation mechanism, or the tax authorities may determine whether the PEM taxation mechanism should apply after conducting appropriate audits.

Tax credits and incentives

Certain tax incentives are provided to investors if they are located in prescribed areas, such as science parks, economic processing zones, free-trade-zones, etc. Other tax credits are granted to qualifying companies that invest in specific businesses or industries promoted by the government, such as biotech.

Research and development (R&D) tax incentives

Under the Statute for Industrial Innovation (SII), R&D credits are available for up to 15% of qualified R&D expenses incurred, with the maximum amount of tax credit capped at 30% of the tax payable for the year in which the expenses were incurred, including the 5% profit retention tax.

Effective from 1 January 2016 to 31 December 2019, amendments to the SII provide another alternative for companies to claim an 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. In addition, to facilitate the circulation and application of innovative R&D results, and to promote industrialisation of innovative technologies, 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 of up to 200% (capped at corresponding income received) within the current year or claim R&D tax credits against income tax payable.

Moreover, according to the Statute for Development of Small and Medium Enterprises (SMEs), enterprises qualifying as SMEs may elect one of the following methods to calculate R&D credits, subject to the 30% cap mentioned above:

- 15% of qualified R&D expenses for the current year, with credits limited to the same year, or
- 10% of qualified R&D expenses for the current year, which can be carried forward for two ensuing years.

According to Regulation Governing R&D Investment Tax Credit (ITC) Available to Profit-seeking Enterprises, a single annual application for R&D ITC should be made with the central competent authorities within four months prior to the CIT return filing due date. Information relating to R&D ITC should be provided with the CIT return.

Tax concessions on merger

A number of tax incentives are available under the Mergers and Acquisitions (M&A) Act to encourage M&A activities in Taiwan. Certain taxes, including business tax, deed tax, LVIT, securities transaction tax, and stamp tax, may be exempted or deferred in case of acquisitions, mergers, or corporate divisions (including spin-offs) that meet certain conditions.

After the merger, spin-off, or acquisition, any tax concession previously enjoyed by the merged entities will continue to be applicable to the surviving or newly-created company. However, it is required to manufacture the same products or provide the same services that were originally approved for tax concessions by the merged entities in order to continue the concessions obtained previously.

The unexpired and unutilised net operating losses of the participating entities prior to the merger or spin-off may be carried over to the surviving or newly-created entity according to the percentage of shareholding in the surviving or newly-created company held by all shareholders of the participating entities.

Income tax exemption is available if the shares acquired by a company as a result of transfer of its entire or substantial portion of business or assets to another company, or due to spin-off, is greater than 80% of the consideration of the entire transaction, and all the shares so acquired have been transferred to the shareholders of the transferor.

Free-trade-zones

According to the Statute for the Establishment and Management of Free-trade-zones, foreign companies or their branch offices in Taiwan that apply for establishment in the free-trade-zone or delegate companies already established in the free-trade-zone to store and/or perform simple processing in the free-trade-zone and sell goods to customers within and outside of Taiwan shall be exempted from CIT. However, in the event that the annual domestic sales exceed 10% of the total annual domestic and foreign sales, the portion in excess shall not be exempted from CIT.

Foreign tax credit

Taiwan uses the credit method to avoid double taxation of income. Foreign taxes paid on foreign-sourced income may be credited against a company's total Taiwan income tax liability. However, the credit is limited to the incremental taxes derived from the foreign-sourced income.

Withholding taxes

Resident corporations paying certain types of income are required to withhold tax as follows:

	WHT (%)		
Recipient	**Dividends**	**Interest**	**Royalties**
Resident corporations and individuals	N/A	10	10
Non-treaty	21	15/20 (1)	0/20 (2)
Treaty:			
Australia	10/15 (3)	10	12.5
Austria	10	10	10
Belgium	10	10	10
Canada	10/15 (15)	0/10 (16)	10
Denmark	10	10	10
France	10	10	10
Gambia	10	10	10
Germany	10	0/10/15 (10)	10
Hungary	10	10	10
India	12.5	10	10
Indonesia	10	10	10
Israel	10	7/10 (4)	10
Italy	10	10	10
Japan	10	0/10 (14)	10
Kiribati	10	10	10
Luxembourg	10/15 (13)	10/15 (13)	10
Macedonia	10	10	10
Malaysia (5)	12.5	10	10

Taiwan

Recipient	WHT (%) Dividends	Interest	Royalties
Netherlands	10	10	10
New Zealand	15	10	10
Paraguay	5	10	10
Poland	10	0/10 (17)	3/10 (18)
Senegal	10	15	12.5
Singapore	(6)	Not prescribed	15
Slovakia	10	10	5/10 (8)
South Africa	5/15 (7)	10	10
Swaziland	10	10	10
Sweden	10	10	10
Switzerland	10/15 (9)	10	10
Thailand	5/10 (11)	0/10/15 (12)	10
United Kingdom	10	10	10
Vietnam	15	10	15

Notes

1. For non-resident enterprises, a 15% WHT applies to interest income derived from short-term bills, securitised certificates, corporate bonds, government bonds, or financial debentures, as well as interest derived from repurchase transactions involving these bonds or certificates. The rate in all other cases is 20%, unless reduced under a tax treaty.
2. Royalties received by foreign enterprises that are specially approved in advance by the government are exempt from income tax.
3. A rate of 10% applies for shareholders that are companies (other than partnerships) with at least a 25% shareholding.
4. 7% of the gross amount of the interest arising in a territory and paid on any loan of whatever kind granted by a bank of the other territory.
5. The WHT rate on technical service fees is reduced to 7.5%.
6. The total tax burden of CIT and dividends tax is not to exceed 40% of the total profits of the company.
7. A rate of 5% applies for shareholders with at least a 10% shareholding.
8. A rate of 5% applies for the use of (or the right to use) industrial, commercial, or scientific equipment.
9. A rate of 10% applies for shareholders with at least a 20% shareholding.
10. A rate of 10% applies to all types of interests, except a rate of 15% applies for interest derived from real estate investment trusts and real estate asset trusts in Taiwan. Tax exemption applies to interests paid to public institutions of the other territory as mutually agreed between the competent authorities of both territories.
11. A rate of 5% applies for shareholders with at least a 25% shareholding.
12. A rate of 15% applies to all types of interests, except a rate of 10% applies for interest received by any financial institution (including an insurance company). Tax exemption applies to interests paid to the authority of the other territory as mutually agreed between the competent authorities of both territories.
13. A rate of 15% applies for shareholders/creditors that are a collective investment vehicle and treated as a body corporate for tax purposes.
14. A rate of 10% applies to all types of interests; however, tax exemption applies to certain interests paid to public institutions of the other territory or paid with respect to debt-claims guaranteed, insured, or indirectly financed by government institutions.
15. A rate of 10% applies for shareholders that are companies with at least a 20% shareholding percentage.
16. A rate of 10% applies to all types of interests; however, tax exemption applies to certain interests paid to public institutions of the other territory or paid in respect of a loan made, guaranteed, or insured by certain institutions.
17. A rate of 10% applies to all types of interests; however, tax exemption applies to certain interests paid to public institutions of the other territory or paid in respect of a loan granted, guaranteed, or insured by certain institutions.
18. A rate of 3% applies to royalties paid as a consideration for the use of industrial, commercial, or scientific equipment.

Tax treaties

Tax treaties entered into with Australia, Austria, Belgium, Canada, Denmark, France, Gambia, Germany, Hungary, India, Indonesia, Israel, Italy, Japan, Kiribati, Luxembourg, Macedonia, Malaysia, Netherlands, New Zealand, Paraguay, Poland, Senegal, Singapore, Slovakia, South Africa, Swaziland, Sweden, Switzerland, Thailand, the United Kingdom, and Vietnam relate to corporate and individual income tax.

Treaties with Canada, the European Union, Germany, Israel, Japan, Korea, Luxembourg, Macau, Netherlands, Norway, Sweden, Thailand, and the United States (US) relate to certain earnings from the operation of ships and/or aircraft.

Tax administration

Taxable period

The tax year in Taiwan runs from 1 January to 31 December. Businesses may request approval from the local collection authority to file CIT returns using a fiscal year-end other than 31 December.

Tax returns

Tax returns are filed on a self-assessment basis. CIT returns are due no later than five months after the end of the tax year.

Payment of tax

Tax is paid on a self-assessment basis in two instalments. The first payment is based on 50% of the tax liability of the prior year's tax return and is made in the ninth month of the enterprise's fiscal year. However, if the taxpayer meets certain requirements, it may self-assess the provisional tax based on the taxable income of the first half of the current fiscal year and deduct income taxes paid overseas against the provisional income tax payable if corresponding income is consolidated in the provisional tax return. The second payment is made at the time of filing the annual tax return. The returns are subsequently reviewed by the tax authorities, and a final assessment is issued.

Any overpaid tax as a result of the tax collection authority's mistake shall be refunded to the taxpayer within two years of the tax authority's acknowledgement of such mistake, and shall not be subject to the original five-year period for applying for refund where the taxpayer is responsible for the mistake.

Tax audit process

Taiwan does not have a fixed audit cycle. Tax audit can be carried out any time prior to the expiration of the statute of limitations. Companies may be selected for audit if certain criteria are met.

Statute of limitations

The statute of limitations in Taiwan is five years from the tax return filing date if the return is filed on time. Where a taxpayer fails to file an annual tax return within the statutory deadline or evades tax by fraud or any other unrighteous means, the statute of limitations is extended to seven years.

Tax ruling system

Corporate taxpayers may file an advance tax ruling application with the tax authorities, together with the relevant supporting documents, to clarify their tax position before initiating the specific transaction. The tax authorities are obligated to issue a response within six months after submitting the application.

Recent focus of Taiwan tax authorities

The tax authorities have developed sophisticated and comprehensive tax audit techniques and approaches over the years. The following sets out some of the common items frequently challenged or audited by the tax authorities:

- Management fees allocated from the foreign parent company or affiliates: The tax authorities frequently question the economic substance of the services rendered, the allocation method, and the availability of sufficient documents to support the tax deduction claim.
- Amortisation of goodwill: The tax authorities frequently challenge the valuation report supporting the calculation of goodwill and whether the transaction itself should give rise to goodwill.
- Amortisation of business rights: The tax authorities have taken a more conservative view, which limits 'business rights' to those explicitly authorised by laws (e.g. those regulated under certain public utilities act).
- Eligibility for R&D tax credits.
- WHT compliance.
- Transfer pricing compliance.
- Business tax audit.

Other issues

US Foreign Account Tax Compliance Act (FATCA)

A Model 2 Intergovernmental Agreement (IGA) was signed in December 2016. As such, financial institutions are to make relevant registration with and disclosure to the US tax authority.

Tajikistan

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Significant developments

The Tax Code was amended as follows:

- Laws establishing new taxes and new tax liabilities for taxpayers that worsen the position of taxpayers should not have retrospective force.
- Laws excluding or mitigating liability or obligation for violation of tax law and providing additional guarantees to protect the rights of taxpayers, tax agents, and their representatives could have retrospective force.
- All ambiguities/unclear provisions of the Tax Code are to be interpreted in favour of the taxpayer.

The first planned tax audit of a small-size business entity, which applies the simplified tax regime, is carried out not earlier than three years from the date of registration, instead of two years.

The planned tax audit of a taxpayer whose gross income is less than 25 million Tajikistan somoni (TJS) should be carried out not more than once every two years. Previously, the threshold for gross income was TJS 15 million.

Late payment interest has been decreased from 0.08% to 0.05% per day.

Taxes on corporate income

All Tajik legal entities are subject to CIT in Tajikistan. Tajik residents are taxed on their worldwide income. Non-residents are subject to CIT in Tajikistan only on Tajikistan-source income. Non-residents operating through a permanent establishment (PE) are generally subject to the same CIT provisions.

CIT is computed by applying the statutory 23% rate to taxable income (13% for enterprises producing goods), which is calculated based on gross income decreased by allowed deductions and losses carried forward from previous periods. CIT liability may not be less than 1% of aggregate income.

Simplified tax system

The simplified tax system for small business entities (hereinafter 'tax under the simplified system') is a special tax regime under which income tax for small business legal entities or income tax for individual entrepreneurs shall be paid under a simplified procedure. The simplified tax regime is applied by small businesses with aggregate annual income that does not exceed TJS 1 million.

Taxpayers who pay the tax under the simplified system are not liable for:

- Income tax, except for withholding tax (WHT).
- Road tax.
- Income tax from revenues of the individual entrepreneur, functioning according to the certificate, except for WHT.
- VAT, except for the import VAT and reverse-charge VAT.

The tax base for applying tax under the simplified system is the aggregate income. For activities related to production of goods, the tax rate is 5%; for other activities, the tax rate is 6%.

Local income taxes

There are no provincial or local income taxes in Tajikistan.

Corporate residence

Legal entities formed under Tajik law, as well as legal entities whose effective control (management) is in Tajikistan, are recognised as residents for CIT purposes.

Permanent establishment (PE)

Under general provisions of the Tax Code, any activity carried out through a fixed place on the territory of Tajikistan, including activity performed through a dependent agent, regardless of duration of such activities, will create a PE of a non-resident.

Further, a non-resident legal entity having business activities in Tajikistan may also create a PE in the following cases:

- 'Services PE': A non-resident enterprise renders services in Tajikistan through employees or other personnel engaged by the non-resident for such purposes, provided that these activities continue for more than 90 calendar days within any consecutive 12-month period.
- 'Construction PE': A construction site, assembly facility, performance of supervisory activities (connected with such objects), or project works/design works.
- 'Agency PE': A non-resident will be considered as having a PE in cases where a resident or non-resident has the contractual authority to represent the non-resident's interests in Tajikistan (i.e. act and/or sign contracts on behalf of the non-resident).

Other taxes

Value-added tax (VAT)

VAT is generally assessed on taxable turnover, which includes goods and services. The VAT rate is 18%. Individuals and businesses are required to register as VAT payers if the taxpayer's taxable turnover exceeds a threshold of TJS 1 million for the preceding 12-month period.

Generally, the Tax Code exempts the following from VAT: goods and services that are not provided in Tajikistan under the place of supply rules; sale, transfer, or rent of real property; financial services; certain medical services; and certain other goods and services.

Additionally, professional participants who carry out activity on the Tajikistan stock exchange are exempt from VAT.

For goods, the place of supply is determined as the initial point of transportation. Services are generally considered to be provided at the place of business of the service provider or the actual place where services are rendered. However, certain types of services are considered to be provided at the location of the buyer. Such services include legal, marketing, consulting, accounting, etc.

A VAT refund is generally available for qualified exporters if input VAT exceeds assessed VAT.

VAT returns, together with issued and received invoices, are filed monthly, not later than the 15th day of the month following the reporting month. Payments are due by the same date.

Customs duties

The tariff rates established by the government, ranging from 0% to 15%, are applied on an *ad valorem* basis, at a specific rate, or via a combination of the two. The tax rate of 0% is granted to certain types of goods (e.g. some types of printed publication, unwrought wool, gaseous hydrocarbons, electricity).

Note that Tajikistan is signatory to several free trade agreements, primarily among the following Commonwealth of Independent States (CIS) countries: Russia, Belarus, Kazakhstan, and Kyrgyzstan.

Customs fees

Customs clearance can’t be performed without certification of goods, for which the importer should pay a fee based on the time spent by a certification specialist. Fees for customs clearance range from approximately 10 United States dollars (USD) to USD 450, depending on customs value.

Excise taxes

Excise tax is assessed on beverages, tobacco products, fuel, tyres, passenger automobiles, jewellery, and mobile communications. Excise tax rates are established by the government.

Property taxes

Property tax is divided into two taxes, which are paid based on the taxable base.

Land tax

A tax on land plots is paid annually based on the rates established by the Tajikistan government applied to the area of the land plot, which vary depending on the location of the land plot.

Real estate tax

Tax on real estate is paid annually and applies to immovable real property, such as buildings, houses, and flats. The real estate tax rate varies from 3% to 15% and depends on territory coefficients.

Transfer taxes

There are no transfer taxes in Tajikistan.

Stamp taxes

There are no stamp taxes in Tajikistan.

Payroll taxes

There are no payroll taxes borne by an employer other than social tax (*see below*).

Social tax

An employer is obligated to make social tax payments at the rate of 25% of salary. In addition to an employer's portion, 1% social tax is withheld from employee's income.

Road tax

The formula for calculating road tax is total deductions of the reporting year multiplied by the 1% tax rate (0.25% for trade companies). If actual deductions do not exceed 70% of gross income, the tax base for road tax is 70% of gross income. It is contemplated that the tax will be eliminated in 2020.

Vehicle tax

Vehicle tax is computed as a percentage of the calculation index applied for horsepower of the vehicle engine. The percentage ranges from 2.5% to 15%.

Branch income

In addition to CIT, PEs are subject to branch profit tax at the rate of 15% of net profit after CIT, unless a lower rate is prescribed by an applicable double tax treaty (DTT).

Income determination

Income tax is assessed on taxable income, which is the difference between gross income and allowed exemptions and deductions.

Professional participants who carry out activity on the Tajikistan stock exchange are exempt from income tax.

Inventory valuation

Inventory accounting for tax purposes follows inventory accounting for financial reporting purposes. Public companies are required to apply International Financial Reporting Standards (IFRS). Other legal entities may apply IFRS or National Accounting Standards.

For tax purposes, the following inventory methods are permitted: last in first out (LIFO), first in first out (FIFO), and weighted average. For public companies, there can be a mismatch between the tax method and the book method, as LIFO is not permitted under IFRS. For other legal entities, the tax method will match the book method if the tax accounting follows National Accounting Standards.

Capital gains

In general, capital gains on securities are taxed as business profits.

Exemption is available for capital gains on the sale of securities on the Tajikistan stock exchange.

Dividend income

In general, dividends are subject to 12% income tax withheld at source. WHT exemption can only be applied to dividends paid as part of net income distribution to the government budget. Dividends withheld at source are not included in aggregate annual income.

In case dividends were not taxed at source, then such dividends should be included in annual aggregate income of a person receiving the dividends and taxed at the standard CIT rate.

Dividends received by residents and non-residents (investors) from securities listed on the Tajikistan stock exchange are exempt from taxation.

Interest income

The Tax Code defines interest income as income received from any fees associated with a debt obligation, including tax liability, payments for any loans, and contributions on deposit (accounts). Interest income is subject to CIT in Tajikistan and should be included in annual aggregate income.

Royalty income

Royalty income received by a resident entity should be included in the aggregate annual income and taxed at the standard CIT rate.

Royalty income received by a non-resident from a Tajikistan source is subject to WHT at the rate of 15%.

Foreign income

Tajik residents are taxed on their worldwide income. Non-residents are subject to CIT in Tajikistan only on Tajikistan-source income. There are no provisions in the Tax Code for tax deferral.

For information about Controlled foreign company (CFC) provisions, see the Group taxation section.

Deductions

In general, all business expenses (e.g. materials, payroll) are allowed as a deduction if the expenses are connected with the earning of income, not of a capital nature, and supported by proper documentation.

Depreciation

The deduction for costs related to fixed assets generally is made through depreciation at rates ranging from 7% to 20% using the declining-balance method.

Goodwill
There are no special provisions for goodwill deduction in the Tax Code; however, goodwill is not deductible in accordance with the general rules on intangible assets amortisation.

Start-up expenses
Start-up expenses are not deductible. However, in case of registration of a branch, the head office can deduct expenses related to the creation of such branch.

Interest expenses
Interest deductibility is generally limited to three times the refinancing rate of the National Bank of Tajikistan (currently 8%). For certain entities, additional limitations may apply.

Bad debt
A taxpayer is allowed a bad debt deduction in cases where the income associated with such bad debt is already recognised for CIT purposes. Bad debts are deductible when they are written-off in the accounting books. Special provisions apply for banks and other financial institutions.

Charitable contributions
Charitable contributions are limited to 10% of taxable income.

Fines and penalties
Fines and penalties paid to the budget of Tajikistan and other states are not deductible.

Taxes
Taxes paid to the budget of Tajikistan and other states are deductible, except for CIT and individual income tax.

Other significant items
Among other deductions specifically mentioned in the Tax Code are research and development (R&D), repair expenses, and geological and geophysical expenses.

Non-deductible expenses
Non-deductible expenses specifically mentioned by the Tax Code include meals and entertainment, personal expenses, passenger vehicles, and non-business expenses.

Net operating losses
Net operating losses may be carried forward for three years but may not be carried back.

Payments to foreign affiliates
No special provisions for deduction of payments to foreign affiliates exist in the Tax Code; consequently, general rules for deductibility of expenses should apply.

Group taxation

There are no rules permitting grouping for tax purposes in Tajikistan.

Transfer pricing

Under Tajikistan market pricing (transfer pricing) provisions, tax authorities have the right to adjust prices. The following transactions are subject to control and further feasible (potential) adjustment:

- Transactions between related parties.
- Barter transactions.
- Foreign trade agreements (contracts) where one of the parties is resident of a tax haven.
- Transactions where one of the participants receives tax benefits or tax incentives.
- Where the price of goods (services, works) deviates by more than 15% from the market price for identical (homogeneous) goods (services, works).

Thin capitalisation

There are no thin capitalisation rules in Tajikistan; however, interest deductibility is limited *as described in the Deductions section*.

Controlled foreign companies (CFCs)

The Tax Code contains CFC provisions, according to which, income received by the resident's subsidiary (more than 10% ownership) registered in countries with privileged taxation should be included in the income of the resident.

Tax credits and incentives

Foreign tax credit

Taxes paid outside Tajikistan may be credited against the same types of taxes in Tajikistan if appropriate supporting documents are provided. The amount of credit may not exceed the amount of tax assessed in respect of such income at the rates applicable in Tajikistan.

Free Economic Zones (FEZs)

Four FEZs were established by the government of Tajikistan to offer reduced taxes and customs fees to both foreign and domestic businesses located in these zones. Tax incentives include FEZs of Sogd, Panj, Ishkoshim, and Dangara. The legislation for the FEZs has been modified several times since the start of the process, but current law requires a minimum investment of USD 500,000 for manufacturing companies, USD 50,000 for trading companies, and USD 10,000 for consulting and service companies, before being eligible for the preferential tax treatment.

CIT exemptions

An exemption from CIT is available for taxpayers that have made a certain amount of investments into chartered capital of a production company, as follows:

- Two-year exemption if volume of investments is from USD 200,000 up to USD 500,000.
- Three-year exemption if volume of investment is from USD 500,000 up to USD 2 million.
- Four-year exemption if volume of investment is from USD 2 million up to USD 5 million.
- Five-year exemption if volume of investment exceeds USD 5 million.

Professional participants who carry out activity on the Tajikistan stock exchange are exempt from CIT for five years.

Tax benefits for specified taxpayers

Tax benefits for poultry farms and combined feed producers

Tax benefits are available for poultry farms and producers of combined feed for birds and animals if such producers will attract foreign investments of not less than USD 16 million. Tax benefits include a 12-year exemption from:

- Income taxes.
- VAT.
- Road tax.
- Property tax.
- Import VAT and customs duties.

The statute of limitation period is extended for the period of use of tax benefits.

Tax benefits for construction of a hydroelectric power plant

Under certain conditions, the construction project owner and the general contractor of a hydroelectric power plant can enjoy tax exemptions from the following taxes:

- VAT.
- Road tax.
- Income taxes.
- Vehicle tax.
- Property tax.
- Social tax with respect to foreign citizens involved in construction.
- Import VAT and customs duties.

Tax benefits for enterprises operating in full-cycle processing of raw cotton

Newly established enterprises operating in full-cycle processing of raw cotton can obtain tax exemptions from the following taxes if certain conditions are met:

- VAT.
- Income taxes.
- Property tax.

Tax benefits under production sharing agreements

An investors that satisfies the conditions of a production sharing agreement concluded with the government of Tajikistan Republic can enjoy the following tax benefits during the period when such production sharing agreement is effective:

- VAT (under certain conditions).
- Excise tax.
- Income taxes.

Tax exemptions for income derived from tourism services

Effective from 1 January 2017, a five-year CIT exemption is available on income derived from tourism services from the moment of state registration. In addition, import of equipment and construction materials for tourist objects are exempt from VAT. The list of tourist objects, titles, and amounts of imported equipment and construction materials is approved by the government of Tajikistan.

Withholding taxes

New requirements on tax residency certificates have been introduced and are effective from 1 January 2016. Thus, the tax residency certificates should be apostilled and legalised for the purpose of application of the DTTs.

Tajikistan-source income of non-residents is subject to WHT at its source at the rates shown in the following table:

Types of income at source of payment	Tax rate (%)
Dividends and interest	12
Insurance and reinsurance premiums	6
International transport and telecommunications	5 to 6
Royalties, rent, lease income, management fees, and other income	15

The information outlined in the table below is provided for application by business entities. Foreign legal entities that do not carry on activities in Tajikistan through a PE are subject to WHT on income from sources in Tajikistan, subject to the terms of a relevant DTT. Tajikistan has enforced DTTs with 29 countries and 3 DTTs that are pending. In cases where certain DTTs envisage the tax rates applying for taxation of dividends/interest that exceed the rates envisaged by the Tajikistan domestic tax legislation, we believe that such income is subject to taxation at rates envisaged by the above-mentioned domestic tax legislation. The below table does not represent tax provisions provided by respective DTTs for government-owned legal entities, governmental institutions, or governmental organisations (central/national banks).

	WHT (%)		
Recipient	**Dividends**	**Interest**	**Royalties**
Non-treaty	12	12	15
Treaty:			
Armenia	10	10	10
Austria	5 (1a)/10	0 (2a)/8	8
Azerbaijan	10	10	10
Bahrain	8	8 (2b)	8
Belarus	15	0 (2c)/10	15
Belgium (pending)	0 (1b)/15	0 (2d)/10	10
Brunei (pending)	5 (1c)/10	10	10
China	5 (1d)/10	8	8
Czech Republic	5	0 (2e, 2f)/7	10
Finland	5 (1d)/15	0 (2e, 2f)/10	5
Germany	5 (1c)/15	0	5 (3a)
India	5 (1d)/10	0 (2g)/10	10
Iran	10	10	8
Kazakhstan	10 (1e)/15	10	10
Kuwait (pending)	5 (1f, 1g)	10	10
Kyrgyzstan	5 (1h)/15	10	10
Latvia	0 (1i)/5 (1d)/10	0 (2f)/7	5 (3b)/10

Tajikistan

	WHT (%)		
Recipient	**Dividends**	**Interest**	**Royalties**
Luxembourg	0 (1b)/15	0 (2h)/12	10
Moldova	5 (1d)/10	5	10
Pakistan	5 (1d)/10	10	10
Poland	5 (1d)/15	10	10
Romania	5 (1d)/10	10	10
Russia	5 (1j)/10	0 (2i)/10	0
Saudi Arabia	5 (1d)/10	8 (2b)	8
South Korea	5 (1d)/10	0 (2j, 2k)/8	10
Switzerland	5 (1k)/15	0 (2j, 2k, 2f)/10	5
Thailand	10	0 (2e, 2f)/10	5 (3c)/10
Turkey	10	10	10
Turkmenistan	10	10	10
Ukraine	10	10	10
United Arab Emirates	0	0	10
United Kingdom	5 (1l)/10/15 (1m)	0 (2l)/10	7

Notes

1. Where one of the following conditions is met:
   a. Beneficial owner is a company (other than a partnership) that directly holds at least 15% of the capital of the company paying the dividends.
   b. Beneficial owner is a company resident of another contracting state and directly holds for an uninterrupted period of at least 12 months at least 10% of the capital of the company paying the dividends.
   c. Beneficial owner is a company (other than a partnership) that directly holds at least 10% of the capital of the company paying the dividends.
   d. Beneficial owner is a company (other than a partnership) that directly holds at least 25% of the share capital of the company paying the dividends.
   e. Beneficial owner is a legal entity and directly holds no less than a 30% stake in the company paying the dividends.
   f. Beneficial owner is a company that directly holds at least 20% of the capital of the company paying the dividends.
   g. Beneficial owner is an individual.
   h. Beneficial owner is a company that holds at least 50% of the share capital of the company paying the dividends.
   i. Beneficial owner is a company (other than a partnership) that directly holds at least 75% of the capital of the company paying the dividends.
   j. Beneficial owner is a person who directly holds at least 25% of the share capital of the company paying the dividends.
   k. Beneficial owner is a company (other than a partnership) that directly holds at least 20% of the capital of the company paying the dividends.
   l. Beneficial owner is a pension scheme or a company that directly holds at least 10% of the capital of the company paying the dividends.
   m. Beneficial owner is a resident of another contracting state and such dividends are paid out of income (including gains) derived directly or indirectly from immovable property by an investment vehicle that is resident of a contracting state whose income from such immovable property is exempt from tax and which distributes most of that income annually.
2. Where one of the following conditions is met:
   a. Recipient is beneficial owner of the interest and such interest is paid: (i) with respect to indebtedness arising as a consequence of the credit sale of any equipment, merchandise, or services, and (ii) to a financial institution.
   b. Interest applied to income is deemed as income from debt-claims. The term ‘income from debt-claims” means income from debt-claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor’s profits, and in particular, income from government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds, or debentures. Penalty charges for late payment should not be considered as income from debt-claims for the purpose of the corresponding DTT.
   c. Interest arising in a contracting state could be exempt from taxation at a certain amount approved by a government in such state if the recipient and beneficial owner of interest is resident of another contracting state and transaction resulting in a debt-claim was approved by a government of a contracting state.

  d. Interest is paid with respect to a loan given or a credit granted by an enterprise to another enterprise.
  e. Recipient is beneficial owner of the interest and such interest is paid in respect to credit sales of any merchandise or equipment.
  f. Recipient is beneficial owner of the interest and such interest is paid in respect to a loan or credit of any kind granted by a bank.
  g. Recipient and beneficial owner of the interest is an institution that could be agreed between the competent authorities of the contracting states.
  h. Recipient and beneficial owner is a financial institution or a collective investment vehicle in a contracting state.
  i. Interest is paid to supplier by customer on commercial credits on deferred payments basis for purchased goods, equipment, performed works, rendered services.
  j. Recipient is beneficial owner of the interest and such interest is paid in connection with the credit sale of any industrial, commercial, or scientific equipment.
  k. Recipient is beneficial owner of the interest and such interest is paid in connection with credit sale of any goods by an enterprise to another enterprise.
  l. Beneficial owner of the interest is a bank.
3. Where one of the following conditions is met:
  a. The term 'royalties' as used in the corresponding DTT means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic, or scientific work, including cinematograph films, any patent, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial, or scientific experience. The term 'royalties' shall also include payments of any kind received as a consideration for the use of, or the right to use, a person's name, picture, or any other similar personality rights, or the recording of entertainers' or sportsmens' performances by radio or television.
  b. Royalties are paid for the use of, or the right to use, software or industrial, commercial, or scientific equipment.
  c. Royalties are paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work.

Tax administration

Maintaining of accounting documentation

The Tax Code stipulates the requirements for maintaining of accounting documentation in the Tajik language.

Taxable period

The Tax Code prescribes a calendar year as the tax year.

Tax returns

Annual CIT declarations are due by 1 April in the year following the tax year-end.

Taxpayers are required to submit their estimated calculation of monthly advance payments of CIT.

Payment of tax

With respect to CIT, advance payments are due every 15th day of the month. Payment of any outstanding CIT liabilities is required not later than 10 April following the reporting tax period.

The settlement of minimum income tax should be made by 10 April following the reporting tax period in cases where it exceeds CIT liability.

Fines and interest penalties

The fine for failure to file a tax return ranges from a minimum amount of 1 calculation index (CI), which is currently TJS 50, to a maximum fine of 100 CI, or TJS 4,000. The amount of the fine depends on the taxpayer's category and should be assessed based on each ten days of delay. In the absence of tax returns, the tax authorities are entitled to assess taxes based on any information available.

Fines may be assessed in the amount of 10% to 20% of the understated tax liabilities. In severe cases, a violation may be considered a criminal offence.

A fine for failure to withhold and remit tax may be assessed in the amount of 3 to 200 CI (approximately TJS 120 to TJS 8,000) of the tax not withheld.

Interest penalties may apply to late tax payments in the amount of 0.05% of the underpaid tax amount for each day of tax underpayment.

Tax audit process

Tajikistan tax authorities have the right to conduct regular tax audits (once per year for planned tax audits). Generally, there are two types of audits:

- Planned tax audits. Planned tax audits are conducted according to the list of entities that fall under tax audit, published by the competent authority.
- Unplanned tax audits. Reorganisation or liquidation of a legal entity, the expiration of the contract on subsoil use, validation of the VAT amount that is charged for a return, etc., may trigger an unplanned tax audit.

Documentary tax audits may be further subdivided into comprehensive (i.e. covering all taxes), thematic (covering only specific type of taxes), or cross-check (covering only transactions with a particular counterparty). Comprehensive and thematic audits may be conducted once a year.

The first planned documentary tax audit of a small business, implementing the simplified tax system, can be carried out only after 36 full calendar months from the date of its registration.

The tax authority sends or presents a notice of a tax audit to a taxpayer no later than ten working days before the start of the documentary tax audit unless otherwise provided in the Tax Code.

The period of tax audits, specified in issued orders, shall not exceed 30 working days from the date of receipt of the order, unless otherwise provided in the Tax Code.

Statute of limitations

Taxpayers are allowed to make changes to prior period tax returns within the statute of limitations (three years). No fines should apply to corrections in this case.

Topics of focus for tax authorities

The tax authorities are currently paying particular attention to deals involving sale of shares and participation interests.

Other issues

Accounting and reporting requirements

In accordance with the governmental Resolution of the Republic of Tajikistan concerning International Standards of Financial Statements, the Ministry of Finance of the Republic of Tajikistan shall adopt IFRS through a step-by-step approach. Starting from 2011, juridical legal entities should apply IFRS; however, National Accounting Standards may still be applicable by companies, except for public companies.

Accounting policies and practices are being revised in light of the legal requirement that companies adopt IFRS and International Accounting Standards. Such revised accounting policies should be adopted by companies' boards of directors and disseminated to all the accounting units with clear instructions on how to introduce and follow the new policies and procedures.

Thailand

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Significant developments

The Eastern Economic Corridor (EEC) project, which is an area-based development aiming to promote high technology and innovation in targeted industries, is expected to become a major factor helping to accelerate the future growth of the country.

The Eastern Economic Corridor Act (2018) became effective on 15 May 2018. Projects wishing to take advantage of the benefits under the Act must be located in certain zones within the EEC, which consists of the three Eastern provinces of Rayong, Chonburi, and Chachoengsao.

Further details are noted in the Tax credits and incentives section.

Taxes on corporate income

Companies incorporated in Thailand are taxed on worldwide income. A company incorporated abroad is taxed on its profits arising from or in consequence of the business carried on in Thailand.

The corporate income tax (CIT) rate is 20%.

A foreign company not carrying on business in Thailand is subject to a final withholding tax (WHT) on certain types of assessable income (e.g. interest, dividends, royalties, rentals, and service fees) paid from or in Thailand. The rate of tax is generally 15%, except for dividends, which is 10%, while other rates may apply under the provisions of a double tax treaty (DTT).

Rates for companies with low paid-in capital and income

For accounting periods beginning on or after 1 January 2017, companies and juristic partnerships with paid-in capital not exceeding 5 million Thai baht (THB) at the end of any accounting period and income from the sale of goods and/or the provision of services not exceeding THB 30 million will be subject to tax at the following rates:

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

Reduced rates for certain banking transactions

Banks are subject to tax at the rate of 10% on their profits derived from lending to non-Thai residents from foreign currency funds obtained from non-Thai sources (so-called 'out-out' business).

Petroleum income tax

International oil companies can engage in exploration and production activities in Thailand under a concession, a production sharing contract, or a service contract.

Taxation on income from petroleum operations is imposed on petroleum concessionaire companies and production sharing producers by the Petroleum Income Tax Acts (PITA). Petroleum companies under a service contract are not taxed under the PITA but under the Revenue Code.

Companies taxed under the PITA are exempt from taxes and duties on income imposed under the Revenue Code and under any other laws. The exemption applies provided that the company pays taxes and duties on income subject to the PITA or on dividends paid out of income subject to the PITA.

Petroleum companies under a concession are taxed at the rate of 50% of their annual net profit from petroleum operations, including profit from the transfer of their concession interests and other activities incidental to the petroleum operations. Deductions are allowed for 'ordinary and necessary' business expenses, as well as depreciation of capital expenditure, petroleum royalties, and other charges. Certain types of expenses are specifically disallowed for deduction, including interest.

A production sharing producer is taxed at the rate of 20% of its annual net profit derived from its petroleum business, including profits derived from the transfer of interests in the nature of rights, annuity, or any other recurring income as a consequence of such transfer.

Local income taxes

There are no local government taxes on income in Thailand.

Corporate residence

Corporate residence is determined by the place of incorporation. A company incorporated under the laws of Thailand is a resident company.

A company incorporated abroad is subject to CIT in Thailand if it is considered to be carrying on business in Thailand. The term 'carrying on business in Thailand' is broad and, subject to the provisions of a DTT, includes the presence of an employee, representative, or go-between that results in the foreign company deriving income or gains in Thailand.

Other taxes

Value-added tax (VAT)

The standard rate of VAT is 10%, but the rate is currently reduced to 7% until 30 September 2018 (unless further extended by the government). VAT is levied on the sale of goods and the provision of services. Exports are zero-rated, while a number of goods and services are exempt (e.g. basic groceries, education, healthcare, interest, leasing of immovable property, sale of real estate).

Customs duties

Basis of taxation

Customs duties are imposed under the Customs Act and the Customs Tariff Decree. Customs duties are collected on both imports and a limited number of exports. Classification of imports is based on the Harmonised Commodity Description and Coding System (the so-called 'Harmonised System'). Thailand has adopted the Association of Southeast Asian Nations (ASEAN) Harmonised Tariff Nomenclature (AHTN) 2017, which is based on the Harmonised System 2017, as its import tariff nomenclature.

Duties are levied on a specific or an *ad valorem* basis, whichever is higher, and the applied *ad valorem* duties range between 0% and 80%. Exemptions from import duties are available on particular items of goods as prescribed in the Customs Tariff Decree. Preferential duty rates are available on imported goods from countries that have a preferential free trade agreement (FTA) with Thailand.

Currently, Thailand has FTAs with the following countries:

- ASEAN member states (Singapore, Vietnam, Malaysia, Indonesia, Philippines, Cambodia, Laos, Myanmar, and Brunei)
- Australia
- Chile
- India
- Japan
- New Zealand
- Peru

Also, as a member of ASEAN, Thailand has preferential trade agreements with the following countries:

- Australia and New Zealand
- China
- India
- Japan
- Korea

The ASEAN - Hong Kong Free Trade Agreement (AHKFTA) was signed in November 2017. It is expected to be enforced on 1 January 2019.

Generally, the value of imports is based on their cost, insurance, and freight (CIF), whereas exported goods are based on their free on board (FOB) amount.

Thailand has implemented the World Trade Organisation (WTO) Valuation Agreement. The primary basis for the customs value is the transaction value, which is the price actually paid or payable for the goods when sold for export, subject to adjustments for certain elements that are considered to form a part of the value for customs purposes or that can be deducted from the value of the imported goods (e.g. the cost of transportation after the importation, duties, and taxes associated with the import).

Elements that may need to be added include royalties and licence fees that are related to the goods and paid as a condition of sale, proceeds from subsequent resale in the importing country, and the value of goods or services supplied by the buyer, such as design or development fees related to the imported goods. If the declared price is evidently low or is unlikely to be the true value of such goods, Thai Customs will likely dispute the declared price.

Customs controls and procedures

Customs procedures for goods arriving in Thailand in any manner are similar to those existing in most other countries. An importer is required to file an entry form together with other requisite documents, including a bill of lading, invoice, and packing list via the e-Customs system.

Customs duties are due upon the arrival of the vessel carrying the imported goods, and goods may be stored in a Customs bonded warehouse for up to 45 days with no submission of an import entry and 60 days in the case of submission of an import entry. Landing and storage charges must be paid before the goods are released.

Customs incentives schemes

Various customs incentives schemes, each with its own specific conditions and duty privileges, are available, including the following:

- Duty and tax compensation (tax coupons).
- Duty drawback for imported raw materials used in export production.
- Duty drawback for re-export in the same state.
- Free zones (Customs or Industrial Estate Authority of Thailand Free Zones).
- Manufacturing bonded warehouses.
- General bonded warehouses.
- Board of Investment (BOI) promotion.
- Preferential import duties under FTAs.

Offences and penalties

Although, technically, an offence against the customs law is a criminal offence, in practice, legal procedures are usually concerned with the recovery of tax arrears and fines. Offences include non-compliance with customs procedures, false declarations, and the most serious offence of smuggling and evasion of customs duties. Statutory penalties are as prescribed by the relevant provisions of the Customs Act. Where Customs and the offender agree to settle the case at the Customs level (i.e. waiver of prosecution), the penalties would be in accordance with the settlement criteria as prescribed by the Director-General of the Customs Department. Currently, we understand that a duty evasion offence would typically be settled with a fine of from 50% to 200% based on the duty shortfall per the import entry. The VAT penalty would also be applied proportionally based on the duty fine. Duty and VAT surcharges (capped at the amount of the shortfall) are applied in this respect as well.

For import licensing errors, the settlement criteria would be the surrendering of the goods or a fine in lieu thereof based on the value of the goods plus the duty and tax payable. For offences related to smuggling, the penalties are based on a multiple of the value of the goods.

Excise tax

Basis of taxation

Excise tax (ET) is a form of consumption tax that is imposed on the sale of a selected range of services and goods (whether manufactured locally or imported) that are considered 'luxuries'. The tax liability arises on locally manufactured goods when leaving the factory and at the time of importation for imported goods.

The excise tax calculation is based on both *ad valorem* rates (a percentage of the suggested retail price [SRP]) and/or specific rates (based on the quantity or weight of the goods). The excise tax formula varies depending on type of excise taxable products, for example:

- (SRP x ET rate) is applicable for motor vehicles, motor cycles, and cosmetic products.
- (Specific rate x quantity) is applicable for petroleum oil products.
- (SRP x ET rate) + (specific rate x quantity) is applicable for non-alcoholic beverages and tobacco products.
- (SRP x ET rate) + (specific rate x quantity x degree of pure alcohol) is applicable for alcoholic beverages.

Taxable goods and services

Goods/services	Ad valorem rate (%)	Specific rate
Petroleum and petroleum products	0	THB 0 to THB 6.5 per litre or kilogram
Certain non-alcoholic beverages	0 to 14	THB 0 to THB 44 per litre
Certain electrical appliances	0	-
Batteries	0 to 8	-
Crystal glassware	0	-
Motor vehicles	0 to 40	-
Motorcycles	0 to 17	-
Boats	0	-
Perfume products and cosmetics	0 to 8	-
Woollen carpets	0	-
Marble and granite	0	-
Ozone depleting substances/ CFCs	0 to 30	-
Alcoholic beverages	0 to 22	THB 0 to THB 1,500 per litre of pure alcohol
Cigarettes containing tobacco	0 to 40	THB 0.005 to THB 1.2 per piece or gram
Playing cards	0	THB 2 to THB 30 per 100 cards
Entertainment services	0 to 10	-
Race courses and lotto	0 to 20	-
Golf courses	0 to 10	-
Telecommunications business	0	-

In addition to the excise tax, an interior tax is also levied by the Excise Department at the rate of 10% of the excise tax payable. Other taxes, such as the health tax and Thai Public Broadcasting Service tax (TPBS tax or TV tax), may apply to certain specified products in the categories of cigarettes and alcoholic beverages.

The manufacturer of the products must file a return and remit the tax due prior to taking the goods from the factory or bonded warehouse. If a VAT liability arises before the goods are taken out of such locations, the manufacturer must file a return and remit the excise tax to the Excise Department within 15 days from the end of the month.

Stamp duty

Stamp duty is levied on 28 different types of documents and instruments, including contracts for hire of work, loans, share transfers, leases of land or buildings, and insurance policies. The rate of stamp duty varies depending on the type of document, but ranges from THB 1 per THB 1,000 of value on most contracts and agreements to a fixed amount per instrument on most commercial and other documents.

Stamp duty is generally paid by way of affixing stamps on the instrument and crossing them out. However, certain instruments now require the stamp duty to be paid in cash to the Revenue Department instead, such as agreements for the lease of land and buildings, other construction or floating rafts with a rental of THB 1 million or more, and hire of work agreements with a remuneration of THB 1 million or more.

Unstamped documents are not admissible as evidence in a civil lawsuit, and the surcharge can be as high as 600% of the duty for failure to pay the stamp duty on a timely basis.

Specific business tax

Specific business tax is collected at fixed rates on the gross revenue of certain businesses not subject to VAT, such as commercial banking, similar financial businesses, and the sale of immovable property, which are taxed at 3%, and life insurance, which is taxed at 2.5%.

The rate of specific business tax has been reduced to 0.01% for certain revenue derived by commercial banks and finance, securities, and credit foncier businesses, as well as businesses that have regular transactions similar to commercial banking.

An additional 10% of the tax is levied as municipality tax.

Capital taxes

There are no capital taxes in Thailand.

Payroll taxes

An employer is responsible for withholding personal income tax (PIT) from all salaries and benefits paid to or on behalf of an employee and remitting such tax to the Revenue Department within seven days from the end of the month in which the salaries and benefits were paid.

Social security contributions

Contributions are levied at the rate of 5% of the monthly salary of each employee, subject to a maximum levy per employee of THB 750 per month. These contributions are payable by both the employer and employee.

Local taxes

There are currently three major local taxes. However, the house and land tax and the local development tax below are planned to be revoked and replaced by a new land

and building tax. A draft of the new law is under the consideration of the National Legislative Assembly (NLA). The taxes currently in effect are as follows:

House and land tax

House and land tax is levied annually at the rate of 12.5% of the assessed economic rental income.

Local development tax

Local development tax is levied annually at rates ranging between 0.25% and 0.95% of the value of land assessed by local authorities. This tax does not apply if the property is subject to the house and land tax.

Signboard tax

Signboard tax is levied annually on certain commercial signs or billboards at varying rates according to size and language used. The rates per 500 square centimetres are THB 3 if all words are in Thai, THB 20 if both Thai and foreign words are used, and THB 40 if only foreign words are used or if the Thai words are below the foreign words.

Branch income

Branches of foreign corporations are subject to CIT on locally earned profits only. Branch profits remitted to the foreign head office are subject to an additional tax at the rate of 10%. However, this is a tax on the disposition of profits abroad and is not limited to remittances. For example, a credit of profit to the head office account in the books is held to be a disposition of profit abroad even though no remittance of funds takes place.

Income determination

Inventory valuation

Inventory is valued at the lower of cost or market price. Any recognised method of ascertaining the cost price may be used, but a change in the method may only be made with the prior approval of the Director-General of the Revenue Department.

Capital gains

There is no specific legislation governing capital gains. All capital gains earned by a Thai company are treated as ordinary revenue for tax purposes. Capital gains on the sale of investments derived from or in Thailand by a foreign company not carrying on business in Thailand are subject to a tax of 15%, withheld at source by the purchaser, unless otherwise exempt under a DTT.

The following income earned by a foreign company not carrying on business in Thailand is also subject to 15% WHT:

- Interest on bonds/debentures issued by state enterprises.
- Difference between the redemption price and the initial sale price of bonds issued by the government, state enterprises, and specified institutions.
- Gains on the transfer of bonds issued by the government, state enterprises, and specified institutions.

Dividend income

Dividends received from a Thai company by a company listed on the Stock Exchange of Thailand are exempt from tax. Dividends received by a non-listed company from other Thai companies are also exempt from tax, provided that the company receiving the dividends holds at least 25% of the total voting shares without any cross-shareholding in the company paying the dividend and that the shares have been held for at least three months before and three months after the dividends were received.

In other cases, where one Thai company receives dividends from another Thai company, one-half thereof is exempt from tax also on the condition that the shares have been held for at least three months before and three months after the dividends were received.

Dividends received from a company incorporated abroad are exempt from tax if the Thai company receiving the dividends holds at least 25% of the shares with voting rights of the company paying the dividends for a period of not less than six months before the date on which the dividends are received and the dividends are derived from the net profit in the foreign country taxed at a rate of not less than 15%. In the event that a 'special law' in a particular foreign country provides a reduced tax rate or exemption for the net profit, the limited company that receives the dividends is still eligible for the tax exemption.

The share of profits received by a Thai company or a foreign company carrying on business in Thailand from an unincorporated joint venture carrying on business in Thailand is exempt from tax.

Stock dividends

Stock dividends are taxable to the recipient as ordinary income.

Interest income

Interest is taxable as income on the accrual basis.

Royalty income

Royalties are taxable as income on the accrual basis.

Foreign income

Companies incorporated in Thailand are taxed on worldwide income. The foreign income received by a company incorporated in Thailand is taxable on the accrual basis. Double taxation is relieved by way of a credit against the tax chargeable in Thailand (*see Foreign tax credit in the Tax credits and incentives section*).

Deductions

Depreciation, amortisation, and depletion

Deductions for depreciation are allowed as a percentage of cost. If the rate of deduction adopted by a company under its own accounting method is lower than the maximum percentage of cost permitted, a deduction will be allowed only at the rate adopted by the company. The straight-line basis is the method most commonly used by companies, but any generally accepted basis, such as sum-of-the-years-digits or double-declining method, is permitted. The maximum permitted rates are shown below:

Asset	Maximum permitted rate (%)
Buildings:	
Durable buildings	5
Temporary buildings	100
Cost of acquisition of depletable natural resources	5
Cost of acquisition of lease rights:	
If there is no written lease agreement or if there is a written lease agreement containing a renewal clause whereby continual renewals are permitted	10
If there is a written lease agreement containing no renewal clause or containing a renewal clause but restricting renewable periods to a definitely limited duration	Percentage rate equals 100 divided by the sum of years of the original and renewable lease periods
Cost of acquisition of the right in a process, formula, goodwill, trademark, business licence, patent, copyright, or any other right:	
If the period of use is unlimited	10
If the period of use is limited	Percentage rate equals 100 divided by the number of years of use
Other assets not mentioned above, excluding land and inventory	20

Special depreciation methods for certain assets

- Machinery and equipment for research and development (R&D) may initially be depreciated at 40% of cost, with the remaining balance being depreciated at the above maximum rate of 20% *per annum*.
- Computer hardware and software may be depreciated within three accounting periods.

Special depreciation method for small companies

Companies and juristic partnerships with fixed assets, excluding land, with a value of no more than THB 200 million and with no more than 200 employees are entitled to use the following special depreciation methods:

- Machinery and equipment may initially be depreciated at 40% of cost, and the remaining balance will then be depreciated at the maximum rate of 20%.
- Computer hardware and software may initially be depreciated at 40% of cost, and the remaining balance can then be depreciated within three accounting periods.
- Factory buildings may initially be depreciated at 25% of cost, and the remaining balance will then be depreciated at the maximum rate of 5%.

Start-up expenses

Start-up expenses, such as incorporation expenses and registration fees, are deductible when incurred.

Interest expenses

Interest on money borrowed for the purpose of acquiring profit or for the purpose of the business is deductible. Interest incurred in respect of the construction or installation of fixed assets that require a period of time before they are ready for their intended use is considered to be capital expenditure and deductible in the form of depreciation.

Bad debts

Bad debts written off are deductible, provided that they are consistent with the rules, procedures, and conditions prescribed by the Ministerial Regulations.

Charitable contributions

Donations to specified charities or for public benefit are deductible in the amount actually paid but not exceeding 2% of net profit. Donations for education or sport are also deductible in the amount actually paid but not exceeding 2% of net profit.

Donations to support certain educational or recreational programmes are allowed a double deduction for tax. Donations made to educational institutions and to sports entities from 1 January 2016 to 31 December 2018 are also allowed a double deduction for tax.

Fines and penalties

Fines, penalties, and surcharges imposed under all tax laws are not deductible.

Taxes

In general, all taxes are deductible except CIT and VAT (in certain cases).

Other significant items

Non-deductible expenses include, but are not limited to, the following:

- Expenses in the nature of provisions.
- Contributions to any fund (except for registered provident funds).

Net operating losses

Losses may be carried forward to offset against the profits of the following five accounting periods. The carryback of losses is not permitted. A change in control of a loss-making company does not impact its loss carryforward status.

Payments to foreign affiliates

A Thailand-incorporated company may claim a deduction for royalties, management service fees, and interest charges, provided they are expended exclusively for the purpose of generating profit or for the purpose of the business in Thailand and are determined on an arm's-length basis.

Group taxation

Group taxation is not permitted in Thailand.

Transfer pricing

Thailand is in the process of introducing specific transfer pricing provisions into the income tax law. Among the expected provisions are the definition of the arm's-length principle and the mandatory transfer pricing disclosure in the form of a transfer pricing declaration at the time of tax filing as well as the full transfer pricing documentation upon request.

There will also be additional subordinate regulations, currently being written by the Revenue Department, to provide further details of the transfer pricing requirements. At the earliest, the provisions, and the subordinate regulations, are expected to be applicable for accounting periods beginning on or after 1 January 2018.

At present, related-party transactions are governed under the general provisions of the income tax law, which require companies to transact on an arm's-length basis, as well as the transfer pricing guidelines issued by the Revenue Department.

The transfer pricing guidelines are in the form of a Departmental Instruction (no. Paw 113/2545), which does not have the status of legislation. This instruction provides internal directives to Revenue officials to adhere to when conducting transfer pricing reviews. It also provides guidelines to taxpayers on setting arm's-length prices for their transactions with related parties.

The instruction authorises the use of both traditional transaction methods (i.e. comparable uncontrolled price, resale price, and cost plus methods), as well as transactional profit methods, in order to determine the market price of a transaction. Although taxpayers are technically expected to consider using traditional transaction methods before resorting to using a transactional profit method, no one method is preferred in practice.

The instruction also defines the term 'market price', describes the transfer pricing documentation requirements, and allows taxpayers to apply for advance pricing agreements (APAs) in respect of any related-party transaction.

To address the APA process, the Revenue Department has issued separate APA guidelines. At present, Thailand accepts only bilateral APAs and limits the period covered to three to five accounting periods. Only a company or partnership incorporated in Thailand, which enters into intra-group transactions with affiliates who are residents of Thailand's treaty partners, may apply for an APA.

The main concepts under the current transfer pricing guidelines and the APA guidelines are expected to remain, in one form or another, once the specific transfer pricing provisions are enacted.

Thin capitalisation

There are no thin capitalisation rules. However, for certain businesses or as part of the conditions for granting tax incentives, a certain debt-to-equity ratio may be required.

Controlled foreign companies (CFCs)

There are no tax provisions in respect of CFCs.

Tax credits and incentives

Board of Investment (BOI) tax incentives

The BOI, by virtue of the Investment Promotion Act of 1977 (including its amendment no. 4 (2017)) and the Competitive Enhancement Act (2017), provides tax incentives for certain activities within the following categories:

- Agriculture and agricultural products.

- Mining, ceramics, and basic metals.
- Light industry.
- Metal products, machinery, and transportation equipment.
- Electronic industry and electrical appliances.
- Chemicals, paper, and plastics.
- Services and public utilities.
- Technology development and innovation.

The tax incentives available include the following:

- Exemption from import duties on imported machinery.
- Exemption from import duties on raw and essential materials imported for manufacturing for export.
- Reduction of import duties on raw and essential materials by up to 90% for use in manufacturing for domestic sale.
- Exemption from import duties on items used for R&D.
- Exemption from CIT equal to or more than the amount of the investment, excluding the cost of land and working capital, for up to 15 years, depending on the promoted activity.
- 50% reduction in the CIT rate for five years from the date on which the tax holiday expires.
- Exclusion of dividends received from promoted enterprises from taxable income during the period of exemption from CIT and within six months from the date of expiry of any tax holiday period.
- THB 10 billion subsidy under the Competitiveness Enhancement Fund, provided that certain criteria are fulfilled, without any conditions.

Incentives by category

Under the 2018 BOI promotion scheme, the focus is placed on the activities and the importance of the activities. Tax incentives are under four categories (A1 to A4) and non-tax incentives under two categories (B1 and B2), as below:

Group	CIT exemption	Import duty exemption on machinery	Import duty exemption on raw materials for export	Non-tax incentives
A1	8 years (without cap) + merit*	Yes	Yes	Yes
A2	8 years + merit *	Yes	Yes	Yes
A3	5 years + merit	Yes	Yes	Yes
A4	3 years + merit	Yes	Yes	Yes
B1	Merit (3 years) **	Yes	Yes	Yes
B2	Merit (3 years) **	No	Yes	Yes

* Exemption from CIT will be up to 13 years in total.

** Only some activities are available.

The following tax incentives are granted for certain eligible activities categorised as B1 or B2:

- 50% CIT reduction for a maximum of ten years.
- Deduction from net profit for ten years of up to 70% of the investment amount in addition to the normal depreciation deductions.

In addition, tax incentives are granted to the following new categories of activities:

Targeted core technologies and enabling services

CIT exemption	Import duty exemption on machinery	Import duty exemption on raw materials for export	Non-tax incentives
10 years (without cap) + merit (but not exceeding 13 years in total)	Yes	Yes	Yes

Strategic based activities

CIT exemption	Import duty exemption on machinery	Import duty exemption on raw materials for export	Non-tax incentives
15 years	Yes	Yes	Yes

Additional incentives based on the value of a project (merit-based incentives) have been launched in order to motivate investors to invest or spend on activities that will benefit the country or the industry as a whole.

Merit on research and development (R&D)

R&D merit-based incentives will depend on the investment made or expenses incurred by investors in R&D for their business, the provision of advance training to employees, or the development of local suppliers. The investment or expenses permitted are as follows:

Investment in	Additional investment cap (% of investment or expenses incurred)
R&D, whether in-house, outsourced in the country, or in cooperation with educational or research institutions abroad	300
Donations to the Technology and Human Resources Development Fund as approved by the BOI	100
Licence fees paid for technology developed in the country	200
Training in advanced technology	200
Development of local suppliers with not less than 51% Thai shareholding in advance technology training or technical assistance	200
Product or packaging design, whether in-house or outsourced in the country as approved by the BOI	200

Additional years of tax exemption will be added to the standard tax incentives received as follows:

Investment/expenditure based on the sales revenue in the first 3 years	Additional period of tax exemption with cap based on amount of investment (in total, maximum period is 13 years)
1% or ≥ THB 200 million	1 year
2% or ≥ THB 400 million	2 years
3% or ≥ THB 600 million	3 years

Merit on decentralisation

As the previous zoning scheme has been abolished, investment promotion zones have been included as a decentralisation merit to businesses that have operations in any of the following 20 provinces with low average income:

Kalasin, Chaiyaphum, Nakhon Phanom, Nan, Bung Karn, Buriram, Phrae, Maha Sarakham, Mukdahan, Mae Hong Son, Yasothon, Roi Et, Sisaket, Sakhon Nakhon, Sa Kaew, Sukhothai, Surin, Nong Bua Lamphu, Ubon Ratchatani, and Amnatcharoen.

Additional incentives for enterprises located in these 20 provinces include the following:

- Three additional years of CIT exemption. However, a reduction of 50% of CIT for five years after the end of the tax holiday will be granted to projects with activities in Groups A1 and A2.
- Double deduction from taxable income of the cost of transportation, electricity, and water supply for ten years from the date on which revenue was first derived from the promoted activity.
- Deduction from net profit of 25% of the project's infrastructure installation or construction costs in addition to normal depreciation; such deduction can be made from the net profit of one or several years within ten years from the date on which revenue was first derived from the promoted activity.

Merit on industrial area development

One additional year of CIT exemption will be granted to Group A projects located within an industrial estate or promoted industrial zone. However, the total period of CIT exemption will not exceed eight years, except for the activities under targeted core technologies and enabling services.

Research and development (R&D) incentives

Tax incentives given to R&D contractors

R&D is a promoted activity under the Investment Promotion Act, which prescribes the criteria and conditions to be followed by an R&D contractor.

Tax incentives given are as follows:

- CIT exemption on income derived from the provision of R&D services as stated in the investment promotion certificate (qualified R&D services) for up to 13 years with no cap.
- Exemption from import duty on imported machinery and raw materials for manufacturing for export.
- Exclusion of dividends derived from promoted enterprises from taxable income during the period of CIT exemption and within six months from the date of expiry of any tax holiday period.

The R&D services must be of the following description:

- Basic research: Activities that are conducted to explore new knowledge from basic natural phenomena and factual observation.
- Applied research: The application of basic knowledge to solve or develop a concept for commercial purposes.

- Pilot development: Activities performed to magnify a production scale from basic research and applied research.
- Demonstration development: To verify a technology and production process and to demonstrate the level of integrity of such process and viability on a commercial scale production in both quality control and cost estimation.

Tax benefits under the Revenue Code

The Revenue Code provides for an additional 100% deduction for tax in respect of expenditure incurred in Thailand on R&D for technology and innovation (including product and process innovation) when hiring government agencies or the private sector, as approved by the Director-General of the Revenue Department.

In addition to the above, a further 100% tax deduction is granted for R&D expenses paid from 1 January 2015 to 31 December 2019 with threshold amounts depending on the revenue of the company.

Eastern Economic Corridor (EEC)

The Eastern Economic Corridor Act (2018) (EEC Act) has been announced in the Government Gazette and became effective on 15 May 2018. An EEC project must be located in certain zones within the EEC, which consists of the three Eastern provinces of Rayong, Chonburi, and Chachoengsao. An EEC project will be promoted only if it is engaged in a target industry.

An EEC promoted company will be granted CIT exemption and/or reduction privileges according to the criteria prescribed by the EEC committee. Currently, the CIT privileges under the EEC Act have not yet been announced.

Nevertheless, the BOI, under the Investment Promotion Act, has already issued criteria and incentives for promoted activities located in the EEC. The tax incentives are categorised under three zones, as follows:

- Special industry promotion zone:
  - Eastern Airport City (EEC-A).
  - Eastern Economic Corridor of Innovation (EECi).
  - Digital Park Thailand (EECd).
- Target industry promotion zone.
- Industrial estate or industrial area within the EEC.

The incentives will be granted only to eligible activities in certain zones, and a bilateral cooperation plan between the company and an academic or research institution or centre of excellence must be made.

Tax incentives provided by the BOI are as follows:

- Special industry promotion zone:
  - BOI standard incentives.
  - CIT exemption for an additional two years.
  - CIT reduction of 50% for five years after the end of the tax holiday.
- Target industry promotion zone:
  - BOI standard incentives.
  - CIT reduction of 50% for five years after the end of the tax holiday.
- Industrial estate or industrial area within the EEC:

- BOI standard incentives.
- CIT reduction of 50% for three years after the end of the tax holiday.

* EEC incentives cannot be utilised together with those under the merit of industrial area development (an additional one-year CIT exemption).

The EEC Act also grants a PIT reduction for employees with special knowledge/abilities who work or operate a business in certain zones within the EEC.

Since 11 July 2017, qualified expatriates and Thai employees have been granted a flat rate of 17% PIT on their income derived from working for companies carrying on target activities within the EEC.

Regional operating headquarters (ROH)

ROH means a company organised under the Thai law providing administrative, technical assistance, or supporting services to its domestic or overseas affiliated enterprises or branches in at least three countries other than Thailand.

Tax incentives available to ROH are under two packages. However, the privileges under the second package are no longer available to new applicants.

The criteria for ROH are:

- Company formed under Thai law with a minimum paid-up capital of THB 10 million.
- Provision of qualified services to qualified affiliates (companies with at least 25% common group ownership) in at least three countries other than Thailand.
- Income from services provided to, or royalties received from, overseas affiliates must be at least 50% of the total income of the ROH company (reduced to one-third for the first three years).

The following tax incentives are still available to existing and new applicants under the first package, provided all of the criteria are met:

- 10% CIT on net profit from ROH services provided to foreign and domestic affiliates.
- 10% CIT on net profit from qualified royalties and interest income from lending borrowed funds to domestic and foreign affiliates.
- Corporate and domestic WHT exemptions on dividends received from affiliates.
- Exemption from WHT on dividends paid to foreign corporate shareholders on net profit arising from ROH qualified income.
- Expatriates employed by the ROH can choose to be taxed at a flat rate of 15% for four consecutive years.

International headquarters (IHQ)

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. This includes carrying on a business as an international trade centre (*see International trade centre below*), which has been approved as an IHQ.

The criteria for an IHQ are:

- A company formed under Thai law with minimum paid-up capital of THB 10 million.

- Managerial, technical, or supporting services (and financial management in the case of treasury centres, *as stated below*) must be provided to foreign affiliates (companies with at least 25% common group ownership, directly or indirectly).
- Operating expenses related to IHQ activities of at least THB 15 million per year.

The tax concessions are:

- 10% CIT on the net profit from qualified services provided to domestic affiliates and royalties derived from domestic affiliates.
- Full CIT exemption on the 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 (under conditions).
- WHT exemption on dividends paid to foreign corporate shareholders from the net profit derived from the income exempt from tax.
- Expatriates employed by the IHQ can choose to be taxed at a flat rate of 15% from the date on which the IHQ becomes qualified until the date on which the IHQ is no longer qualified or the employment is terminated.

Please note the following:

- A qualified IHQ will be granted 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 that are both exempt from tax.
- If an IHQ lacks any of the qualifications in any accounting period, the right to the tax privileges will be suspended only for that accounting period.

Treasury centre (TC)

An IHQ that has obtained a TC licence from the Bank of Thailand can request approval from the Revenue Department for the tax concessions available when carrying on the business of financial management for its associated enterprises or branches situated in Thailand or abroad.

Financial management includes:

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

The tax concessions are:

- WHT 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 all remuneration received from financial management services provided to affiliates.
- Other tax concessions available for the TC activities are the same as for IHQ noted above.

A qualified IHQ will be granted tax privileges for 15 accounting periods.

The criteria are the same as noted above for an IHQ.

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

International trade centre (ITC)

An ITC is defined as a company established under the law of Thailand and engaged 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 advice, including 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 approval to carry on a business as an ITC and enjoy the same tax concessions.

The criteria for ITC are:

- Company formed under Thai law with a minimum paid-up capital of THB 10 million.
- Operating expenses related to ITC activities of at least THB 15 million per year.

The tax concessions are:

- Exemption from CIT 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.
- WHT exemption on dividends paid to foreign corporate shareholders from the net profit derived from the income exempt from tax.
- Expatriates employed by the ITC can choose to be taxed at a flat rate of 15% from the date on which the ITC becomes qualified until the date on which the ITC is no longer qualified or the employment is terminated.

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

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

Foreign tax credit

A Thai company can use foreign tax paid on business income or dividends as a credit against its CIT liability. However, the credit cannot exceed the amount of Thai tax on the income.

Withholding taxes

WHT rate schedule

	WHT (%)		
Recipient	**Dividends**	**Interest**	**Royalties**
Resident corporations	0/10 (1)	0/1 (2)	3
Resident individuals	10	15	Progressive rates (3)
Non-resident corporations and individuals:			

Recipient	WHT (%) Dividends	Interest	Royalties
Non-treaty	10	15	15
Treaty:			
Armenia	10	10/15 (4)	15
Australia	10	10/15 (4)	15
Austria	10	10/15 (4)	15
Bahrain	10	10/15 (4)	15
Bangladesh	10	10/15 (4)	15
Belarus	10	10/15 (5)	15
Belgium	10	10/15 (4)	5/15 (6)
Bulgaria	10	10/15 (4)	5/15 (7)
Cambodia (39)	10	10/15 (4)	10
Canada	10	10/15 (4)	5/15 (8)
Chile	10	10/15 (4)	10/15 (9)
China	10	10/15 (4)	15
Cyprus	10	10/15 (10)	5/10/15 (11)
Czech Republic	10	10/15 (4)	5/10/15 (12)
Denmark	10	10/15 (4)	5/15 (6)
Estonia	10	10	8/10 (13)
Finland	10	10/15 (4)	15
France	10	3/10/15 (14)	0/5/15 (15)
Germany	10	0/10/15 (16)	5/15 (6)
Hong Kong	10	10/15 (17)	5/10/15 (18)
Hungary	10	10/15 (4)	15
India	10	10	10
Indonesia	10	10/15 (4)	15
Ireland	10	10/15 (17)	5/10/15 (19)
Israel	10	10/15 (4)	5/15 (20)
Italy	10	0/10/15 (21)	5/15 (6)
Japan	10	0/10/15 (22)	15
Korea, Republic of	10	10/15 (17)	5/10/15 (23)
Kuwait	10	10/15 (4)	15
Laos	10	10/15 (4)	15
Luxembourg	10	10/15 (4)	15
Malaysia	10	10/15 (4)	15
Mauritius	10	10/15 (4)	5/15 (7)
Myanmar	10	10	5/10/15 (24)
Nepal	10	10/15 (4)	15
Netherlands	10	10/15 (4)	5/15 (6)
New Zealand	10	10/15 (17)	10/15 (25)
Norway	10	10/15 (4)	5/10/15 (26)
Oman	10	10/15 (27)	15
Pakistan	10	10/15 (4)	0/10/15 (28)
Philippines	10	10/15 (29)	15
Philippines (new) (40)	10	10/15 (4)	15
Poland	10	10/15 (4)	0/5/15 (30)
Romania	10	10/15 (4)	15
Russia	10	10/15 (31)	15
Seychelles	10	10/15 (4)	15
Singapore	10	10/15 (17)	5/8/10 (32)

Thailand

Recipient	WHT (%) Dividends	Interest	Royalties
Slovenia	10	10/15 (4)	10/15 (33)
South Africa	10	10/15 (4)	15
Spain	10	10/15 (4)	5/8/15 (34)
Sri Lanka	10	10/15 (4)	15
Sweden	10	10/15 (4)	15
Switzerland	10	10/15 (4)	5/10/15 (35)
Taiwan	5/10 (36)	10/15 (4)	10
Tajikistan	10	10	5/10 (6)
Turkey	10	10/15 (4)	15
Ukraine	10	0/10/15 (37)	15
United Arab Emirates	10	10/15 (4)	15
United Kingdom	10	10/15 (4)	5/15 (6)
United States	10	10/15 (17)	5/8/15 (38)
Uzbekistan	10	10/15 (4)	15
Vietnam	10	10/15 (4)	15

Notes

1. The zero rate applies to a recipient company listed on the Stock Exchange of Thailand and any other limited company that holds at least 25% of the total shares with voting rights in the company paying the dividend without any cross shareholding.
2. The 1% rate applies to interest paid to all resident corporations other than banks or finance companies, except where interest arises from bonds or debentures.
3. The progressive rates refer to the PIT rates.
4. The 10% rate applies to interest paid to a recipient that is a bank or financial institution (including an insurance company).
5. The 10% rate applies to interest paid (i) to a recipient that is a bank or financial institution (including an insurance company) or (ii) with respect to indebtedness arising as a consequence of a sale on credit of any equipment, merchandise, or services.
6. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work.
7. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work, excluding cinematograph films and films, tapes, or discs for radio or television broadcasting.
8. The 5% rate applies to copyright royalties and other like payments in respect of the production or reproduction of any literary, dramatic, musical, or artistic work, excluding royalties with respect to motion picture films and works on film or videotape for use in connection with television.
9. The 10% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work, or for the use of, or the right to use, industrial, commercial, or scientific equipment.
10. The 10% rate applies to interest paid (i) to a recipient that is a bank or financial institution (including an insurance company); (ii) in connection with the sale on credit of any industrial, commercial, or scientific equipment; or (iii) in connection with the sale on credit of any merchandise by one enterprise to another enterprise.
11. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, dramatic, musical, artistic, or scientific work, including software, cinematograph films or films, or tapes used for radio or television broadcasting; and the 10% rate applies to royalties paid for the use of or the right to use industrial, commercial, or scientific equipment or for information concerning industrial, commercial, or scientific experience.
12. The 5% rate applies to royalties paid for the alienation or the use of or the right to use any copyright of literary, artistic, or scientific work, excluding cinematograph films or films or tapes used for radio or television broadcasting, and the 10% rate for the alienation of any patent, trademark, design, or model, plan, secret formula, or process.
13. The 8% rate applies to royalties paid for the use of, or the right to use, industrial, commercial, or scientific equipment. The 10% rate applies to royalties paid in all other cases.
14. The 3% rate applies to interest paid on loans or credits granted for four years or more with the participation of a financing public institution to a statutory body or to an enterprise in relation to the sale of any equipment or to the survey, the installation, or the supply of industrial, commercial, or scientific premises and of public works. The 10% rate applies to interest paid to any financial institution.

15. The zero rate applies to royalties paid to a contracting state or state-owned company with respect to films or tapes, and the 5% rate to royalties for the alienation or the use of or the right to use any copyright of literary, artistic, or scientific work.
16. The zero rate applies to interest paid to any financial institution wholly owned by the other contracting state, a 'land', a political subdivision, a local authority, or a local administration thereof, and in particular, in the case of the Federal Republic, by the Deutsche Bundesbank or the Kreditanstalt für Wiederaufbau, and in the case of Thailand, by the Bank of Thailand. The 10% rate applies to interest paid to a recipient that is a bank or financial institution (including an insurance company).
17. The 10% rate applies to (i) interest paid to any financial institution (including an insurance company) and (ii) interest paid with respect to indebtedness arising as a consequence of a sale on credit of any equipment, merchandise, or services, except where the sale was between persons not dealing with each other at arm's length.
18. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work and the 10% rate for the use of, or the right to use, any patent, trademark, design, or model, plan, secret formula, or process.
19. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work, including software, and motion pictures and works on film, tape, or other means of reproduction for use in connection with radio or television broadcasting, and the 10% rate for the use of, or the right to use, industrial, commercial, or scientific equipment or any patent.
20. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work, excluding cinematograph films or films or tapes used for radio or television broadcasting.
21. The zero rate applies to interest paid to any financial institution wholly owned by the other contracting state, an administrative subdivision, or a local authority thereof. The 10% rate applies to interest paid to a recipient that is a bank or financial institution (including an insurance company).
22. The zero rate applies to interest paid to any financial institution wholly owned by the government. The 10% rate applies to interest paid to a recipient that is a bank or financial institution (including an insurance company).
23. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work, including software and motion pictures and works on film, tape, or other means of reproduction for use in connection with radio or television broadcasting, and the 10% rate for the use of or the right to use any patent, trademark, design, or model, plan, secret formula, or process.
24. The 5% rate applies to royalties paid for the use of, or the right to use, any copyrights of literary, artistic, or scientific work, while the 10% rate applies to royalties for the consideration for any services of a managerial or consultancy nature, or for information concerning industrial, commercial, or scientific experience.
25. The 10% rate applies to royalties paid for the use of, or the right to use, any copyright; or the use of, or the right to use, any industrial, scientific, or commercial equipment; or the use of, or the right to use, any motion picture film, or film or videotape or any other recording for use in connection with television, or tape or any other recording for use in connection with radio broadcasting; or the reception of, or the right to receive, visual images or sounds, or both, transmitted to the public by satellite or, cable, optic fibre, or similar technology; or the use in connection with television or radio broadcasting, or the right to use in connection with television or radio broadcasting, visual images or sounds, or both, transmitted by satellite or cable, optic fibre, or similar technology.
26. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work, and the 10% rate applies to royalties paid for the use of or the right to use industrial, commercial, or scientific equipment.
27. The 10% rate applies to (i) interest paid to a bank or financial institution (including an insurance company) and (ii) interest from a loan or debt claim that is guaranteed by the government.
28. The zero rate applies to royalties paid to a contracting state or a state-owned company with respect to films or tapes, and the 10% rate applies to royalties paid for the alienation or the use of or the right to use any copyright of literary, artistic, or scientific work.
29. In case of interest arising in Thailand, the 10% rate applies to interest paid to a Philippines financial institution (including an insurance company). In the case of interest arising in the Philippines, the 10% rate applies in respect of public issues of bonds, debentures, or similar obligations.
30. The zero rate applies to royalties paid to a contracting state or a state owned company with respect to films or tapes. The 5% rate applies to royalties paid for the alienation or the use of or the right to use any copyright of literary, artistic, or scientific work, excluding cinematograph films or tapes used for television or broadcasting.
31. The 10% rate applies to interest paid to the following recipients (i) in the case of a resident of Russia, any institution having a licence to carry on banking operations; and (ii) in the case of a resident of Thailand, any financial institution (including an insurance company).
32. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work, including cinematograph films, or films or tapes used for radio or television broadcasting. The 8% rate applies to royalties paid for the use of, or the right to use, any patent, trademark, design or model, plan, secret formula or process, or for the use of, or the right to use, industrial, commercial, or scientific equipment.
33. The 10% rate applies to royalties paid for the use of, or the right to use, any copyright of literary or artistic work, including motion pictures, live broadcasting, film, tape, or other means of the use or reproduction in connection with radio and television broadcasting, and for the use of, or the right to use industrial, commercial, or scientific equipment.

34. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, dramatic, musical, artistic, or scientific work, excluding cinematograph films or films or tapes used for radio or television broadcasting. The 8% rate applies to royalties in consideration of financial leasing for the use of, or the right to use, industrial, commercial, or scientific equipment.
35. The 5% rate applies to royalties paid for the alienation or the use of, or the right to use, any copyright, artistic, or scientific work, excluding cinematograph films or films or tapes used for radio or television broadcasting, and the 10% rate for the alienation of any patent, trademark, design or model, plan, secret formula, or process.
36. The 5% rate applies if the recipient holds at least 25% of the capital of the company paying the dividend.
37. The zero rate applies to interest paid to any other financial institution established and owned by the government to promote trade and investment. The 10% rate applies to interest paid to a recipient that is a bank or financial institution (including an insurance company).
38. The 5% rate applies to royalties paid for the use of, or the right to use, any copyright of literary, artistic, or scientific work, including software, motion pictures, and works on film, tape, or other means of reproduction for use in connection with radio or television broadcasting. The 8% rate applies to royalties paid for the use of, or the right to use, industrial, commercial, or scientific equipment.
39. The treaty entered into force on 26 December 2017 and is effective from the tax year commencing on 1 January 2018.
40. A new DTT between Thailand and the Philippines entered into force on 5 March 2018 and will be effective from the tax year commencing on 1 January 2019.

Tax administration

Taxable period

The tax year for a company is its accounting period, which must be of 12 months' duration. However, it may be less than 12 months in the case of the first accounting period after incorporation, the accounting period of dissolution, or after approval for a change in the accounting period has been received from the Revenue Department and the Business Development Department.

Tax returns

The tax system is one of self-assessment. A company prepares and files its tax returns by the due dates and at the same time pays the taxes calculated to be due. The annual CIT return is due 150 days from the closing date of the accounting period.

Payment of tax

CIT is paid twice in each year. A half-year return must be filed within two months after the end of the first six months of an accounting period. The tax to be paid is computed on one-half of the estimated profit for the full accounting period, except for listed companies, banks, certain other financial institutions, and other companies under prescribed conditions where the tax is based on the actual net profit for the first six months. The balance of the tax due is payable within 150 days from the closing date of the accounting period, together with the annual tax return. Credit is given for the amount of tax paid at the half-year.

Tax audit process

If, within a period of two years from the date of filing a tax return, the assessment officer has reason to believe that false or inadequate information has been declared in a return, the assessment officer has the power to issue a summons requesting the presence of the person responsible, or a witness, for examination, and to order either of them to produce accounts or other relevant evidence, provided that advance notice of seven days is given. The subsequent examination of the books and records is normally carried out at the company's offices if it is inconvenient to transfer all the documents to the tax office. After completion of the examination, the assessment officer has the power to adjust the amounts previously assessed or included in a return on the basis of the evidence, and issue a further assessment for tax together with penalties and surcharges, or adjust the amount of losses available for carryforward.

Tax audits may cover the previous five accounting periods from the date of filing a tax return with the approval of the Director-General if the assessment officer has evidence of an intention to evade tax or in the case of a claim for a refund of tax. However, under the Civil and Commercial Code, the Revenue Department can assess tax for up to ten years.

Statute of limitations

The statute of limitations for tax is ten years.

Topics of focus for tax authorities

Topics of focus for tax authorities currently include the following:

- Deductibility of management service fees or expenses allocated to Thailand by foreign affiliates.
- International inter-company transactions and transfer pricing.

Other issues

United States (US) Foreign Account Tax Compliance Act (FATCA)

The intergovernmental agreement (IGA) between the United States and Thailand regarding the US FATCA was signed on 4 March 2016. The agreement will enter into force on the date of Thailand's written notification to the United States that Thailand has completed its necessary internal procedures for entry into force.

The US Treasury has previously treated the IGA to be 'in effect' since 30 June 2014 when the United States and Thailand reached an agreement in substance and Thailand consented to disclose this status. In accordance with this status, financial institutions in Thailand were allowed to register on the FATCA registration website consistent with the treatment of having an IGA in effect.

Timor-Leste

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Significant developments

On 6 March 2018, Timor-Leste and Australia signed a treaty (subject to ratification) permanently agreeing certain maritime boundaries in the Timor Sea ('the Boundary Treaty'). The Boundary Treaty succeeds the Timor Sea Treaty (TST) and the International Unitisation Agreement (IUA). The Boundary Treaty will result in the former Joint Petroleum Development Area (JPDA), as well as territory covering a number of non-JPDA fields (e.g. Buffalo, parts of Greater Sunrise), falling under exclusive Timor-Leste control. As a result Timor-Leste's taxing rights in relation to the effected upstream activities will be increased.

The Boundary Treaty, once ratified should:

- permanently deal with the maritime boundaries between Timor-Leste and Australia (although not necessarily third countries, such as Indonesia), and
- establish a Special Regime for the Greater Sunrise gas field. This includes revenue-sharing arrangements on the upstream revenue allocation, which will vary according to the development concept (essentially the location of the liquefaction facilities) ultimately chosen for the Greater Sunrise gas resource.

As of the writing of this summary, both the Timor-Leste and Australia governments have not yet ratified the Boundary Treaty.

Taxes on corporate income

Timor-Leste residents are subject to income tax on worldwide taxable income, where taxable income is essentially the difference between gross income and allowable deductions. Non-residents are generally subject to income tax on Timor-Leste-source income attributed to a permanent establishment (PE) (*see the Branch income section for more information*). Non-residents without a PE may be subject to a 10% withholding tax (WHT) (*see the Withholding taxes section for more information*).

The income of companies is generally subject to corporate income tax (CIT) at a flat rate of 10%.

Industry-specific CIT rates

The rate of CIT for oil and gas contractors is 30%, while sub-contractors are subject to CIT at the flat rate of (generally) 6%.

Supplemental Petroleum Tax (SPT) also applies for oil and gas contractors and is imposed on 'accumulated net receipts' using a specific formula. SPT is deductible for CIT calculation purposes.

Separate tax arrangements apply for petroleum activities in the Joint Petroleum Development Area (JPDA) (*see the Other issues section*).

Local income taxes

There are no municipal or local taxes on income in Timor-Leste.

Corporate residence

The definition of a corporate resident (resident legal person) covers a wide range of entities, such as companies, partnerships, trusts, governmental institutions, and unincorporated associations incorporated, formed, organised, or established in Timor-Leste.

Permanent establishment (PE)

A PE is defined as a fixed place of business through which the business of a person is wholly or partly carried on, including:

- A place of management.
- A branch.
- A representative office.
- An office.
- A factory.
- A workshop.
- A mine, an oil or gas well, a quarry, or any other place of extraction of natural resources, including any place of drilling for mineral exploration.
- A fishery, place where animal husbandry is conducted, farm, plantation, or forest.
- A construction, installation, or assembly project.
- The furnishing of a service through employees or other personnel if conducted for more than 60 days in any 12-month period.
- A natural or legal person acting as a dependent agent.
- An agent or employee of a non-resident insurance company if the agent or employee collects premiums or insures risks in Timor-Leste.

Other taxes

Sales tax

Sales tax is imposed on the sales tax value of:

- taxable goods imported into Timor-Leste and
- taxable goods sold or taxable services provided in Timor-Leste on or after the date specified by Parliament.

Taxpayers liable for sales tax include the following:

- A taxpayer who imports taxable goods into Timor-Leste.
- A taxpayer who sells taxable goods in Timor-Leste.
- A taxpayer who provides taxable services in Timor-Leste.

The rates of sales tax are 2.5% for taxable goods imported into Timor-Leste and 0% for the sale of taxable goods and provision of taxable services in Timor-Leste.

Services tax

Services tax is imposed at 5% on any gross consideration of more than 500 United States dollars (USD) received by a taxpayer for the provision of hotel, restaurant and bar, or telecommunication services.

Import duties

Import duty applies to imported goods (except for specifically exempted goods) at 2.5% of the 'customs value' of the goods. Customs value is the fair market value, including cost, insurance, and freight (CIF), as stated in the General Agreement on Tariffs and Trade (GATT) rules.

The following goods are exempted from import duty:

- Goods accompany a person arriving in Timor-Leste from another territory (limitations apply).
- Imports of the type exempted under specific international conventions.
- Goods re-imported in the same condition as when they were exported.
- Goods, other than alcohol or tobacco, imported by registered charitable organisations, registered under any law of Timor-Leste, provided the goods are to be used for charitable purposes of humanitarian assistance and relief, education, or health care.
- Other goods for temporary admission if the importer has provided security for the import duty in the prescribed manner.
- Goods for consumption by international staff of the United Nations Integrated Mission in East Timor or members of peace keeping forces from contingent countries, provided the goods are sold in conformity with prescribed rules of sale.
- Certain infant and female hygiene products.
- Other goods imported into Timor-Leste as personal goods accompanying a traveller and where the import duty that would be imposed on the import would be USD 10 or less.

Excise tax

Excise tax is imposed on excisable goods where removed from a warehouse by a registered manufacturer for consumption in Timor-Leste or imported into Timor-Leste.

Below is the list of excisable goods and the respective rates of excise tax:

Goods	Excise tax rate
Beer	USD 1.90/litre
Wine, vermouth, fermented beverages (such as cider)	USD 2.50/litre
Ethyl alcohol (other than denatured) and other alcoholic beverages	USD 8.90/litre
Gasoline, diesel fuel products, and other petroleum products	USD 0.06/litre
Tobacco and tobacco products	USD 19.00/kg
Cigarette lighters	12% of the excise value
Smoking pipes	12% of the excise value
Arms and ammunition	200% of the excise value
Motor cars and small passenger vehicles (with an excise value exceeding USD 70,000)	35% of the excise value
Private boats and aircraft	20% of the excise value

Note that the excise value of excisable goods imported into Timor-Leste is the total of the customs value and any import duty imposed. The excise value of excisable goods manufactured in Timor-Leste is their fair market value at the time of removal from the manufacturer's warehouse.

Goods on the above list are excisable goods, other than:

- goods imported into Timor-Leste that are exempt from import duty, or
- goods exported from Timor-Leste within 28 days after their production or import, as long as the taxpayer liable to excise tax submits to the Banking and Payments Authority documentary proof of the export of goods.

Property taxes
There are no taxes on property in Timor-Leste.

Transfer taxes
There are no transfer taxes in Timor-Leste.

Stamp duties
There is no stamp duty in Timor-Leste.

Payroll taxes
An employer paying taxable wages shall withhold Wage Income Tax (WIT) at a rate of 10% from those wages and remit the WIT on a monthly basis.

An annual WIT return is due by the last day of the March following the end of the relevant tax year. Information on WIT withheld must also be provided to each employee on an annual basis or on termination of employment.

Social security contributions
A Social Security scheme was introduced in November 2016, with both employers and employees required to make contributions. The scheme provides cover for loss of income/benefits due to work-related accidents, maternity, old age, and death. It would appear that Social Security contributions should be deductible to employers. Implementing regulations for this scheme are still outstanding.

Branch income

The taxable income of a non-resident carrying out business activities through a PE is calculated by reference to:

- the income attributable to the PE
- any sales of goods or merchandise of the same or similar kind as those sold through the PE, and
- any other business activities carried on in Timor-Leste of the same or similar kind as those effected through the PE.

Other principles for determining the taxable income of a PE in Timor-Leste include the following:

- Profit is calculated as if the PE was a Timor-Leste entity engaged in the same or similar activities under the same or similar conditions and dealt with wholly independently from the non-resident person of which it is a PE.
- Subject to this, deductions may be claimed for expenses incurred for the purposes of the business activities of the PE, including head office expenditures, whether incurred in Timor-Leste or elsewhere.
- No deductions may be claimed for amounts paid or payable by the PE to its head office or to another PE of the non-resident person, other than towards the reimbursement of actual expenses incurred by the non-resident person to third parties, by way of:
  - royalties, fees, or other similar payments
  - compensation for any services (including management services) provided to the PE, and
  - interest on money lent to the PE (except for banking businesses).

Income determination

Taxable business profits are determined on the basis of net profit for financial accounting purposes in accordance with International Financial Reporting Standards (IFRS), subject to certain modifications in the Tax and Duties Act (TDA). In general, income is assessable when 'receivable', while expenses are deductible when 'payable'. A taxpayer with turnover of less than USD 100,000 may, however, elect to pay tax on a cash basis.

Gross income is defined widely to mean "any realised increase in economic capacity in whatever name or form which can be used for consumption or to increase the wealth of the taxpayer other than wages that are subject to Wages Income Tax (WIT)".

The gross income for a tax year is the total amount earned by the taxpayer, including, but not limited to, business income, property income, lottery prizes or awards, and refunds of tax payments previously deducted as an expense.

Inventory valuation

There are no specific provisions dealing with inventory valuation in Timor-Leste. This is because a deduction is allowed for the cost of inventory incurred during the tax year even if the inventory is on hand at the end of the year.

Capital gains

Gains and losses arising from the alienation of assets are generally assessable and deductible as ordinary income and subject to tax at the standard CIT rate.

Dividend income

Dividends are tax exempt in the hands of Timor-Leste residents.

Interest income

Interest income is generally assessable as ordinary income and subject to tax at the standard CIT rate.

Royalty income

Royalty income is subject to a 10% WHT.

If the royalty payment is to a resident non-individual, the WHT is creditable for income tax purposes.

If the royalty payment is to an individual, the 10% WHT constitutes a final income tax.

Exempted income

The following income is tax exempt:

- Any aid or donations, provided that the donor and recipient do not have any business or control relationship.
- Gifts received by a religious, educational, or charitable organisation, provided that the donor and recipient do not have any business or control relationship.
- Assets (including cash) received by a resident in exchange for shares or a capital contribution.
- Any amount paid by an insurance company to a resident in connection with accident or life.

Foreign income

Under the worldwide income principle, a resident taxpayer is required to calculate income that is not only Timor-Leste sourced but also foreign sourced. In the case that the foreign-sourced income is taxed at source, Timor-Leste allows a foreign tax credit for the particular tax year (*see Foreign tax credit in the Tax credits and incentives section*).

With regard to profits retained in controlled foreign companies (CFCs), Timor-Leste does not currently have any arrangements to otherwise deem the repatriation of the profit.

Deductions

The taxable income of residents and non-residents who have a PE in Timor-Leste shall be determined on the basis of gross income reduced by:

- expenditure and losses incurred from the alienation of assets or the discharge of debt in the conduct of a taxable business activity
- expenditure incurred in deriving any other amounts included in gross income
- any loss on disposal of an asset other than assets held on personal account
- contributions to an approved pension fund, and
- bad and doubtful debts (subject to various tests - *see Bad debts below*).

Depreciation and amortisation

'Depreciable assets' include any tangible movable property with a useful life exceeding one year that is wholly or partly used for taxable business activities. 'Intangible assets' include property, other than tangible movable property or immovable property, with a useful life exceeding one year that is used for taxable business activities.

There are provisions for election of either straight-line or double-declining methods, the pooling of assets, and *de minimis* exceptions. However, the rate of tax depreciation/amortisation (for non-petroleum operations) is set at 100%, meaning that taxpayers are, in effect, entitled to a full and up-front deduction. In circumstances where the asset is only partly used for the conduct of taxable business activities, the deduction is reduced by the proportion of its non-taxable business use.

Goodwill

There are no specific provisions dealing with the treatment of goodwill. We expect that the treatment should follow that under IFRS.

Start-up expenses

There are no specific provisions dealing with the treatment of start-up expenses. However, assuming that the start-up expense is incurred to derive income, we expect that start-up expense should be deductible.

Interest expenses

Interest expenditure is not deductible unless incurred by a financial institution.

Bad debts

Bad debts are not deductible without passing all of the following tests:

- The debt was previously included in taxable income.
- The debt was written off in the accounts during the relevant tax year.
- There are reasonable grounds for believing that the debt will not be recovered.

The above tests do not apply to banks, which are entitled to deduct provisions for doubtful debt where determined in accordance with the prudential requirements prescribed by instruction of the Banking and Payments Authority.

Charitable contributions

Donations are not deductible if the donations are exempt from income tax in the hands of the recipient.

Fines and penalties

Penalties for violation of law and regulation are not deductible.

Taxes

Timor-Leste or foreign income tax is not deductible.

Deductions not allowed or conditional deductions

The following expenses are also not deductible to a resident or non-resident with a PE in Timor-Leste:

- The distribution of profits in whatever name or form.
- Expenses incurred for the personal benefit of a taxpayer, a taxpayer's dependents, shareholders, partners, or members.
- Reserves, other than as provided for under the TDA.
- Excessive compensation paid by a legal person to a member of the legal person, or paid between associates.
- Salaries paid to a partner in a partnership.
- A bribe, or any similar payment.
- Expenditure or losses incurred to the extent recoverable under an insurance policy or a contract of indemnities.

Net operating losses

Losses from previous years may be carried forward indefinitely. However, the carried forward loss from the disposal of assets may only be utilised against gains arising from the disposal of assets. Foreign-sourced losses may only be offset against foreign-sourced income of that particular country.

The carryback of losses is not allowed.

Payments to foreign affiliates

Excessive payments or compensation to 'members of a legal person' or payments between associates for work performed should not be deductible. The TDA, however, does not elaborate on the meaning of 'excessive'.

Group taxation

Companies, etc. are taxable on a stand-alone basis (i.e. there is no grouping or ability to transfer tax losses).

Transfer pricing

Excessive payments or compensation to 'members of a legal person' or payments between associates for work performed should not be deductible. The TDA, however, does not provide specific guidance on how to determine arm's-length pricing on related-party transactions or any other general transfer pricing principles.

Thin capitalisation

Currently, there are no 'thin capitalisation' or similar rules in Timor-Leste (noting that interest is not deductible, except for financial institutions).

Controlled foreign companies (CFCs)

Timor-Leste does not have any CFC regulations.

Tax credits and incentives

Foreign tax credits

A resident taxpayer is entitled to a credit for any foreign income tax paid in respect of foreign-source income. The foreign tax credit is calculated separately for each foreign country from which income is derived by a taxpayer. The value of such tax credits is limited to the value of the Timor-Leste income tax payable on that income. There is no deduction or carryforward of any excess foreign tax credit.

Withholding taxes

WHT is imposed on the following payments by residents to a resident:

Type of payment	WHT rate (%)	Final/non-final tax
Dividends	0	Final
Interest	0	Not final
Royalties	10	Not final, except where paid to an individual
Rent (land and building)	10	Not final, except where paid to an individual
Prize and winnings	10	Final
Construction/building activities	2	Final *

Type of payment	WHT rate (%)	Final/non-final tax
Construction consulting services	4	Final *
Air and sea transportation	2.64	Final *
Mining and mining support services	4.5	Final *

* The default position is that such amounts will be a final tax. The income recipient can elect to have these payments for services not subjected to final tax by submitting a notification letter to the Timor-Leste Revenue Service.

Payments of Timor-Leste-source income made by a resident to a non-resident are subject to WHT at 10%. Timor-Leste has entered into a double taxation treaty (DTT) with Portugal (although elements of DTT relief are also embedded in the Timor Sea Treaty [TST], *see Taxation of petroleum operations in the Other issues section*).

Where WHT is applied as a final tax, the taxed income is not included in the recipients' taxable income for income tax purposes. Accordingly, expenses incurred in deriving income that is subject to final tax are not deductible for income tax purposes.

Tax administration

Taxable period

The standard tax year is the calendar year, although different accounting year-ends can be granted upon application.

Tax returns

CIT returns are to be filed annually by the 15th day of the third month following the year end.

Service tax, excise tax, sales tax, and WHT are to be filed monthly by the 15th day of the following month.

Payment of tax

CIT due shall be settled to the Banking and Payments Authority or another entity nominated by the Timor-Leste Revenue Service by the date of filing (*see above*).

Service tax, excise tax, sales tax, and WHT should be settled to the Banking and Payments Authority or another entity nominated by the Timor-Leste Revenue Service by the 15th day after the end of the following month.

Penalties

If a taxpayer fails to deliver the tax form on time, it shall be liable to an additional tax of USD 100. If a taxpayer fails to deliver all or part of any tax due by the due date, that taxpayer shall be liable to an additional tax of 5% of the amount due plus an additional 1% of the tax due on the 15th day of each month following the due date and:

- if the failure was due to gross carelessness on the part of the person, further additional tax of 25% of the tax that remains unpaid, or
- if the failure was due to a deliberate attempt to avoid payment of tax, further additional tax of 100% of the tax that remains unpaid.

If a taxpayer has understated the tax due in the tax form, that taxpayer shall be liable to an additional tax of 15% and:

- if the understatement was due to gross carelessness on the part of the taxpayer, further additional tax of 25% of the tax understated, or
- if the understatement was due to a deliberate attempt to avoid payment of tax, further additional tax of 100% of the tax understated.

Tax audit process

Assessments may occur upon the following:

- The delivery of a tax return form and payment.
- After receipt of a return where the Commissioner believes a return is incorrect.
- Where a taxpayer fails to file a return.

Assessments may be amended according to the following events:

- By the taxpayer upon delivery to the Commissioner of an amended assessment.
- Via a taxpayer request to the Commissioner.
- Via specific amendment by the Commissioner.

Statute of limitations

The Timor-Leste Revenue Service may issue an assessment notice or amend an assessment notice only within five years from the date of filing of the return. In the event of a deliberate tax evasion or fraud, there is no time limit for the issuance of an assessment notice.

Topics of focus for tax authorities

Based on our experience, the Timor-Leste tax authorities are focussing on the timely remittance of the tax obligations. From an industry perspective, the oil and gas sector continues to be a focus. Finally, there have been numerous challenges of tax concessions granted on a contractual basis, including by government agencies.

Other issues

Taxation of petroleum operations

The taxation of petroleum operations in Timor-Leste is partly covered by the TDA. However, the TDA operates only to modify the taxation of petroleum activities pursuant to a number of legacy tax regimes. These modifications apply to contractors, sub-contractors, and any other parties receiving income from the supply of goods or services to a contractor or sub-contractor.

A contractor is defined as a person with whom the responsible Ministry or Designated Authority, as the case may be, has made a petroleum agreement. A sub-contractor includes any person supplying goods or services directly or indirectly to a contractor in respect of petroleum operations.

Specific provisions for the taxation of petroleum operations include:

- A CIT rate for contractors of 30% on taxable income, while sub-contractors will generally be taxed on a final WHT basis at a rate of 6% (*although see JPDA below*).

- No tax on branch profit remittances (*although see JPDA below*).
- Where 'net receipts' exceed specified levels, an SPT can apply.
- The 'ring fencing' of income and expenditure within the contract area.
- Modified deductibility rules, including around the deductibility of interest for contractors and a modified depreciation regime.
- A specific WHT regime.
- A specific transfer pricing and associated anti-avoidance provision.

Special tax regime for Production Sharing Contracts (PSCs) within the Boundary Treaty

On 6 March 2018, Timor-Leste and Australia signed the Boundary Treaty (though not yet ratified) effectively replacing the agreements that resulted in the Joint Petroleum Development Area (JPDA). This has resulted in Timor-Leste holding full taxing rights to revenues arising from the (former) JPDA, which was of 90:10 (in favour of Timor-Leste), and a number of other fields not within the JPDA. The fiscal arrangements for the undeveloped Greater Sunrise field are to be split 70:30 or 80:20 (in favour of Timor-Leste) according to where the gas processing occurs.

The income tax rates should now be 30% for all upstream participants. A 20% WHT should apply to most payments for services or passive income paid to non-residents (according to the PSC).

The tax regime *as outlined under 'Taxation of petroleum operations' above* also applies in the JPDA (except for former 'Annex F' PSCs). This is, however, with a number of important modifications, including the exclusion of the service tax, excise tax, sales tax, import duty, and WIT.

Vietnam

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Significant developments

In 2017, the most significant developments related to transfer pricing. Following the establishment of a transfer pricing audit department in the General Department of Taxes (GDT) and some key provinces such as Hanoi, Binh Duong, Dong Nai, and Ho Chi Minh City, in July 2016, the GDT announced the establishment of a Base Erosion and Profit Shifting (BEPS) Working Group, which is responsible for preparing action plans to implement the Organisation for Economic Co-operation and Development (OECD) BEPS Initiatives and overseeing the implementation process.

More recently, the Vietnamese government released Transfer Pricing Decree No. 20/2017/ND-CP guiding the implementation of transfer pricing (Decree 20) and guiding circular 41/2017/TT-BTC (circular 41), which entered into effect from 1 May 2017.

The Ministry of Finance recently released a draft tax law amending the current laws on value-added tax (VAT), special sales tax (SST), corporate income tax (CIT), personal income tax (PIT), natural resources tax (NRT), and customs duty.

There are various changes proposed, notably as follows:

- Transfer of capital outside Vietnam will be subject to capital assignment profit tax at 2% on net gain.
- Preferential CIT rates (from 15% to 17%) will be granted to small and medium enterprises (SMEs).
- New CIT incentives have been introduced:
  - Preferential 10% CIT for 15 years plus 4 years of exemption and subsequent 9 years of 50% reduction for investments in encouraged locations or sectors with especially difficult conditions.
  - Preferential 17% CIT for 10 years plus 2 years of exemption and subsequent 4 years of 50% reduction for investments in encouraged locations or sectors with difficult conditions.
- Proposed to increase VAT rates to 11% from 1 January 2020 and 12% from 1 January 2022. Whereas the 5% VAT rate shall be increased to 6% from 1 January 2022.

It is planned that the draft law will be presented to the government for presentation to the National Assembly in October 2018, and will take effect 1 January 2019.

Taxes on corporate income

Standard rates

All taxes are imposed at the national level. The standard CIT rate is 20%. Enterprises operating in the oil and gas industry are subject to CIT rates ranging from 32% to 50%, depending on the location and specific project conditions. Enterprises engaging in prospecting, exploration, and exploitation of mineral resources (e.g. silver, gold, gemstones) are subject to CIT rates of 40% or 50%, depending on the project's location.

There is no concept of tax residency for CIT. Business organisations established under the laws of Vietnam are subject to CIT and taxed on worldwide income. 20% CIT shall be applicable to foreign income. There are no provisions for tax incentives for such income.

Foreign organisations carrying out business in Vietnam without setting up a legal entity in Vietnam and/or having Vietnam-sourced income are considered foreign contractors, irrespective of whether the services are performed inside or outside Vietnam. Payments to foreign contractors are subject to Foreign Contractor Tax (FCT), which consists of VAT and CIT elements. *See the Withholding taxes section for more information.*

Preferential rates

Preferential CIT rates of 10%, 15%, and 17% are available where certain criteria are met. *See the Tax credits and incentives section for more information.*

Calculation of taxable profit

Taxable profit is the difference between total revenue, whether domestic or foreign sourced, and deductible expenses (*see the Deductions section*), plus other assessable income.

Taxpayers are required to prepare an annual CIT return, which includes a section for making adjustments to accounting profit to arrive at taxable profit.

Local income taxes

There are no local, state, or provincial income taxes in Vietnam.

Corporate residence

There is no concept of tax residency for CIT. Enterprises established under the law of Vietnam are subject to CIT in Vietnam. In addition, Vietnam has a broadly worded 'permanent establishment' definition.

Permanent establishment (PE)

In Vietnam, a PE is defined as "a fixed place of business through which a foreign enterprise carries out part or the whole of its business or production activities in Vietnam". The PE of a foreign enterprise shall include:

- A branch, an operating office, a factory, a workshop, means of transportation, a mine, an oil and gas field, or any place relating to the exploitation of natural resources in Vietnam.
- A building site; a construction, installation, or assembly project.

- An establishment providing services, including consultancy services, through its employees or other persons.
- An agent for a foreign enterprise.
- A representative in Vietnam where one has authority to sign contracts under the name of the foreign enterprise, or where one does not have authority to sign contracts under the name of the foreign enterprise but regularly delivers goods or provides services in Vietnam.

Foreign enterprises with their PEs in Vietnam shall pay tax on the taxable income earned in Vietnam (irrespective of whether it relates to the PE) and on the taxable income generated out of Vietnam and related to operations of the PEs.

Where a treaty on avoidance of double taxation to which Vietnam is a signatory contains different provisions relating to PE, such treaty shall apply (*see the Withholding taxes section for a list of countries with which such treaties exist*).

Other taxes

Value-added tax (VAT)

VAT applies to goods and services used for production, trading, and consumption in Vietnam (including goods and services purchased from non-residents), with certain exemptions. Depending on the category of goods or services, the VAT rates are as follows:

- A 0% rate applies to exported goods/services, including goods/services sold to overseas/non-tariff areas and consumed outside Vietnam/in the non-tariff areas, goods processed for export or in-country export (subject to conditions), goods sold to duty free shops, certain exported services, construction and installation carried out for export processing enterprises, and aviation, marine, and international transportation services.
- A 5% rate applies generally to areas of the economy concerned with the provision of essential goods and services. These include: clean water, teaching aids, books, unprocessed foodstuffs, medicine and medical equipment, husbandry feed, various agricultural products and services, technical/scientific services, rubber latex, sugar and its by-products, social housing, and certain cultural, artistic, and sport services/products.
- The 10% 'standard' rate applies to activities not specified as not subject to VAT, exempt, or subject to the 0% or 5% rate.

There is a draft law proposed to increase the VAT rates.

Goods or services where VAT declaration and payment are not required

A separate category includes supplies not subject to output VAT, but where related input VAT can, nevertheless, be credited. This category includes the following:

- Compensation, bonus, subsidies, except those provided in exchange for certain services.
- Transfers of emission rights and various financial revenues.
- Certain services rendered by a foreign organisation, which does not have a PE in Vietnam where the services are rendered outside of Vietnam, including repairs to means of transport, machinery, or equipment, advertising, marketing, promotion

of overseas investment and trade, brokerage activities for the sale of overseas goods and services, training, and certain international telecommunication services.
- Sales of assets by non-business organisations or individuals not registered for VAT.
- Transfer of investment projects.
- Sale of agricultural products that have not been processed into other products or have only been through preliminary processing.
- Capital contributions in kind.
- Certain asset transfers between a parent company and its subsidiaries or between subsidiaries of the same parent company.
- Collections of compensation/indemnities by insurance companies from third parties.
- Collections on behalf of other parties that are not related to the provision of goods/services (e.g. if company A purchases goods/services from company B but pays to company C, and, subsequently, company C pays to company B, then the payment from company C to company B is not subject to VAT).
- Commissions earned by (i) agents selling services, including postal, telecommunications, lottery, airlines/bus/ship/train tickets, at prices determined by principals; and (ii) agents for international transportation, airlines, and shipping services entitled to 0% VAT; or (iii) insurance agents.
- Commissions from the selling of exempt goods/services.
- Lending or return of machinery, equipment, goods.
- Goods exported and then re-imported back to Vietnam due to sales returns by overseas customers.

Exempt goods and services

There are stipulated categories of VAT exemptions, including certain agricultural products; goods/services provided by individuals having annual revenue of 100 million Vietnamese dong (VND) or below; imported or leased drilling rigs, aeroplanes, and ships of a type that cannot be produced in Vietnam; transfer of land use rights (subject to limitations); various financial services; various securities activities including fund management; capital assignments; foreign currency trading; debt factoring; certain types of insurance, medical services, education, printing/publishing, public transportation, export of unprocessed natural resources, etc.

When a supply cannot be readily classified based on the tax tariff, VAT must be calculated based on the highest rate applicable for the particular range of goods that the business supplies.

Taxpayers must file VAT returns on a monthly basis by the 20th day of the subsequent month or on a quarterly basis by the 30th day of the subsequent quarter (for companies with prior year annual revenue of VND 50 billion or less).

Customs duties

Import duty rates are classified into three categories: ordinary rates, preferential rates, and special preferential rates.

Preferential rates are applicable to imported goods from countries that have most-favoured-nation (MFN, also known as normal trade relations) status with Vietnam. The MFN rates are in accordance with Vietnam's World Trade Organization (WTO) commitments and are applicable to goods imported from other member countries of the WTO.

Special preferential rates are applicable to imported goods from countries that have a special preferential trade agreement with Vietnam. Currently effective free trade agreements (FTAs) to which Vietnam is a party include FTAs between ASEAN member states, between ASEAN members and Japan, ASEAN and China, ASEAN and India, ASEAN and Korea, ASEAN and Chile, ASEAN and Australia, ASEAN and New Zealand, Vietnam and Japan, Vietnam and Chile, Vietnam and Korea, Vietnam and the Eurasian Economic Union (Vietnam and the Customs Union of Russia, Belarus, Kazakhstan).

Vietnam has concluded two important agreements, the European Union FTA (EFTA) and Trans-Pacific Partnership (TPP, although its future is uncertain given the United States [US] withdrawal). In addition, Vietnam is negotiating other agreements, including the Regional Comprehensive Economic Partnership (RCEP) and FTAs between ASEAN and Hong Kong, and with Israel.

Import duty exemptions are provided for encouraged projects and goods imported in certain circumstances.

Export duties are charged only on a few items, basically certain natural resources. Rates range from 0% to 40%.

Special sales tax (SST)

SST is a form of excise tax that applies to selected goods and services (*see below*). For goods, SST is charged at the production or importation stage. Imported goods (except for various types of petrol) are subject to SST at both the import and selling stages. The SST paid at importation will be creditable against SST paid at the selling stage.

The SST rates are as follows:

Products/services	**SST rate (%)**
Cigar/cigarette:	
From 1 January 2016 to 31 December 2018	70
From 1 January 2019	75
Spirit/wine:	
With ABV ≥ 20°:	
From 1 January 2018	65
With ABV < 20°:	
From 1 January 2018	35
Beer:	
From 1 January 2018	65
Automobiles having less than 24 seats:	
From 1 January 2018	10 to 150
Motorcycle with cylinder capacity above 125cm^3	20
Airplanes	30
Boats	30
Petrol	7 to 10
Air-conditioners (not more than 90,000 BTU)	10
Playing cards	40
Votive paper	70
Discotheques	40
Massage, karaoke	30
Casinos, jackpot games	35
Entertainment with betting	30

Products/services	SST rate (%)
Golf	20
Lottery	15

Property taxes

Foreign investors generally pay rental fees for land use rights. The range of rates is wide depending upon the location, infrastructure, and the industrial sector in which the business is operating.

In addition, owners of houses and apartments have to pay land tax under the law on non-agricultural land use. The tax is charged on the specific land area used based on the prescribed price per square metre at progressive tax rates ranging from 0.03% to 0.15%.

Stamp taxes

Certain assets, including houses, land, automobiles and motorcycles, etc., that are subject to registration of ownership are subject to stamp duty. The stamp duty rates vary depending on the asset transferred.

Payroll taxes

Social insurance (SI) and Unemployment insurance (UI) contributions are applicable to Vietnamese individuals only. Health insurance (HI) contributions are required for Vietnamese and foreign individuals that are employed under Vietnam labour contracts. Effective from 1 January 2018, SI contribution is also applicable to foreign individuals working in Vietnam under a work permit or practicing certificate or licence.

Accordingly, from 1 January 2018, the salary subject to SI/HI/UI contributions is the salary, certain allowances, and other regular payments according to labour law, but this is capped at 20 times the minimum salary for SI/HI contributions and 20 times the minimum regional salary for UI contributions. Effective from 1 July 2018, the minimum salary is increased from VND 1,300,000 per month to VND 1,390,000 per month. Effective from 1 January 2018, the minimum regional salary varies from VND 2,760,000 per month to VND 3,980,000 per month. These minimum salaries are subject to change each year.

Social insurance (SI) contributions

The level of compulsory SI contribution is 25.5% of total salary, of which 17.5% is the employers' obligation and the remaining 8% is the employees' obligation.

Health insurance (HI) contributions

HI contribution rates are 4.5% of total salary, with two-thirds contributed by the employer and one-third by the employee.

Unemployment insurance (UI) contributions

The employer and employee UI contributions are 1% on gross salary each.

Natural resources tax (NRT)

NRT is payable by industries exploiting Vietnam's natural resources, including petroleum, minerals, natural gas, forest products, natural seafood, natural bird's nests, and natural water. Natural water used for agriculture, forestry, fisheries, salt industries, and sea water for cooling purposes may be exempt from NRT, provided that certain conditions are satisfied. The tax rates vary depending on the natural resource being exploited, ranging from 1% to 40%, and are applied to the production output at a specified taxable value per unit. Various methods are available for the calculation of the taxable value of the resources, including cases where the commercial value of the resources cannot be determined. Crude oil, natural gas, and coal gas are taxed at progressive tax rates depending on the daily average production output.

Environment protection tax (EPT)

EPT is an indirect tax that is applicable to the production and importation of certain goods deemed detrimental to the environment, the most significant of which are petroleum and coal. The tax is calculated as an absolute amount on the quantity of the goods.

The tax rates are as follows:

Goods	Unit	Tax range (VND)
Petrol, diesel, grease, etc.	litre/kg	300 to 3,000
Coal	ton	10,000 to 20,000
HCFCs	kg	4,000
Plastic bags *	kg	40,000
Restricted use chemicals	kg	500 to 1,000

* Excludes plastic bags used for packaging or that are 'environmentally friendly'.

Branch income

Branches of foreign entities are subject to the same CIT regime as entities incorporated in Vietnam.

Income determination

Inventory valuation

At present, there are no provisions for valuing inventories or determining inventory flows. The tax treatment follows the accounting treatment.

Asset revaluation

Gains from the revaluation of assets for the purposes of capital contribution or transfer upon division, demerger, consolidation, merger, or conversion of business are subject to the standard CIT rate.

Capital gains

Gains made by a foreign investor on the transfer of an interest (as opposed to shares) in a limited liability company are subject to the standard CIT rate. The assignee is required to withhold the tax due from the payment to the assignor and account for this to the tax authorities. Where both the assignor and the assignee are foreign entities, the Vietnamese company in which the capital interest is transferred is responsible for the above administration.

Gains earned by a foreign investor from selling securities (i.e. bonds, shares of public joint-stock companies, irrespective of whether they are listed or non-listed) are subject to CIT at a deemed rate of 0.1% of the sales proceeds. The standard CIT rate will apply to any gains earned by a foreign company (not incorporated in Vietnam) upon a sale of shares in a non-public, joint-stock company.

There is a draft law proposed to tax transfer of capital outside Vietnam where the transferred capital includes capital from investment in Vietnam at 2% on sales proceeds effective from 1 January 2019. The draft law is still under discussion and revision.

Dividend income

Dividends received from investments in other companies in Vietnam are from after tax profits and are not subject to CIT.

Interest income

Certain types of interest income are entitled to tax incentives granted to the investment project, depending on the conditions on which tax incentives are granted.

Royalty income

Currently, royalty income is subject to tax at the standard CIT rate.

Other significant items

Tax incentives that are available for investment in encouraged sectors do not apply to other income (except for income that directly relates to the incentivised activities, such as disposal of scrap), which is broadly defined.

The following income items are subject to the standard CIT rate and are not entitled to tax incentives (including preferential tax rate and exemption/reduction):

- Income from transfer of the right to make capital contribution; income from transfer of immovable property (except for income from investment in social houses); income from transfer of investment projects, transfer of the right to take part in investment projects, and transfer of the right to exploration and exploitation of minerals.
- Income from activities of prospecting for, exploration of, and exploitation of oil, gas, and other rare and precious resources; income from activities of exploiting minerals.
- Income from providing services subject to SST in accordance with the provisions of the law on SST.

Foreign income

Foreign income, under the domestic tax law, is subject to the standard CIT rate with tax credits available (*see Foreign tax credit in the Tax credits and incentives section*).

Foreign income shall be taxed when earned. There are no provisions for tax deferral or preferential tax rates for foreign income.

Deductions

Depreciation and amortisation

Tax depreciation may differ from accounting depreciation. Depreciation in excess of the rates specified in the regulations on tax depreciation is not deductible. These regulations specify maximum and minimum permissible effective lives for various classes of assets, including intangibles. Current straight-line tax depreciation rates are as follows:

Assets	Rate (%)
Buildings	2 to 16.67
Office equipment	10 to 20
Automobiles	3.33 to 16.66
Machinery and equipment	5 to 33.33
Intangible assets	Not more than 5
Goodwill	33.33

The depreciation period of assets of the Build Operate Transfer (BOT) and Business Cooperation Contract (BCC) projects is the period the investors use them to recover their investment capital.

Start-up expenses

Pre-establishment expenses (i.e. expenses for setting up a company) and certain expenses (i.e. training, advertising before establishment, costs for the research stage, relocation cost) can be amortised over a period of up to three years from the commencement of operations. In order for pre-establishment and pre-operating expenses to be deductible for CIT purposes, supporting documents to substantiate the fact that these pre-operating expenses were necessarily and legitimately incurred for the establishment of the company should be available.

Interest expenses

Interest on loans corresponding to the portion of charter capital not yet contributed as scheduled is not deductible.

Interest on loans from non-economic and non-credit organisations exceeding 1.5 times the interest rate set by the State Bank of Vietnam is not deductible.

Interest on loans that has been capitalised is not deductible.

Tax deductibility of interest on loans is to be capped at 20% of earnings before interest, taxes, depreciation, and amortisation (EBITDA) (*see Transfer pricing in the Group taxation section*).

Bad debt

Provisions for bad debts are deductible if the provision is made in accordance with the guidance by the Ministry of Finance (MoF). Certain conditions must be satisfied in order to set up a provision for bad debts (e.g. the debts must be supported by original documentation, there must be confirmation from clients of the overdue amounts, the debts must be overdue under the terms of an economic contract). In the absence of satisfying the necessary conditions, the provision for bad debts will generally not be deductible until incurred and supported by invoices.

Charitable contributions

Donations are generally non-deductible, except certain donations for education, health care, natural disasters, building charitable homes for the poor, or scientific research.

Fines and penalties

Administrative penalties and fines are specifically considered non-deductible.

Taxes

Creditable input VAT, CIT, and other fees/charges are not deductible for CIT purposes.

Other significant items

The following other expenditures are specifically stated to be non-deductible:

- Employee remuneration expenses that are not actually paid or are not stated in a labour contract, collective labour agreement, or the financial regulations of the company.
- Staff welfare (including certain benefits provided to family member of staff) exceeding a cap of one month's average salary.
- Provisions for severance allowance (except for companies not subject to mandatory unemployment insurance contributions) and payments of severance allowance in excess of the prescribed amount per the Labour Code.
- Contributions to voluntary pension funds and the purchase of voluntary pension for employees exceeding VND 3 million per month per person.
- Reserves for research and development (R&D) that are not in accordance with the prevailing regulations.
- Provisions for stock devaluation, bad debts, financial investment losses, product warranties, or construction work that are not in accordance with the prevailing regulations.
- Unrealised foreign exchange gain/losses due to the revaluation of foreign currency items other than account payables at the end of a financial year.
- Management expenses allocated to PEs in Vietnam by the foreign company's head office that are not in accordance with the regulations.
- Certain expenses directly related to the issuance, purchase, or sale of shares.
- Services fees paid to related parties that do not meet certain conditions.

For certain businesses (e.g. insurance companies, securities trading, lotteries), the MoF provides specific guidance on deductible expenses for CIT purposes.

Net operating losses

Losses may be carried forward fully and consecutively for a maximum of five years. Carryback of losses is not permitted.

Payments to foreign affiliates

There are no special restrictions on the deductibility of royalties, loan interest, and service fees paid to foreign affiliates (except for those paid by branches). However, the payment must be defendable on an arm's-length basis as required by transfer pricing regulations (*see Transfer pricing in the Group taxation section*). Certain contracts for the transfer of technology and foreign loans must be registered with the competent authorities.

Group taxation

There is no provision for any form of consolidated filing or group loss relief in Vietnam.

Transfer pricing

Decree 20/2017/ND-CP was enacted on 24 February 2017 and shall be effective from 1 May 2017. The guiding Circular 41/2017/TT-BTC was enacted on 28 April 2017 and is effective from 1 May 2017.

Decree 20 is based closely on the existing Circular 66/2010/TT-BTC, and extends the interpretation of existing provisions and introduces additional concepts and principles from the Transfer Pricing Guidelines of the OECD and BEPS Action Plan.

Related party definition

The ownership threshold required to be a 'related party' under Decree 20 is 25%, higher than the prior 20% under Circular 66. In addition, Decree 20 removes from the related party definition of Circular 66 two entities having transactions between them accounting for more than 50% of their sales or purchases. Vietnam's transfer pricing rules also apply to domestic related-party transactions.

Transfer pricing methodologies

The acceptable methodologies for determining arm's-length pricing are analogous to those espoused by the OECD in the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (i.e. comparable uncontrolled price, resale price, cost plus, profit split, and comparable profits methods).

Transfer pricing documentation

Compliance requirements include an annual declaration of related-party transactions and transfer pricing methodologies used, and a taxpayer confirmation of the arm's-length value of their transactions (or otherwise the making of voluntary adjustments), which is required to be filed together with the annual CIT return. Decree 20 requires that the transfer pricing method applied must ensure that there is no loss of tax revenue to the state budget, which could imply that no downward adjustments are allowed. Decree 20 also introduces a new transfer pricing declaration form that requires disclosure of more detailed information, including segmentation of profit and loss by related-party and third-party transactions.

Decree 20 gives the tax authorities the power to use internal databases for transfer pricing assessment purposes in cases where a taxpayer is deemed noncompliant with the requirements of the Decree.

Taxpayers engaged in related-party transactions solely with domestic related parties could be exempt from the requirement to disclose information on such transactions in the new transfer pricing declaration form, where both parties have the same tax rate and neither party enjoys tax incentives.

Companies that have related-party transactions must also prepare and maintain contemporaneous transfer pricing documentation. Decree 20 introduces a three-tiered transfer pricing documentation approach to collect more tax-related information on multinational companies' business operations, specifically a master file, a local file, and country-by-country (CbC) reporting. The three-tiered transfer pricing documentation has to be prepared before the submission date of the annual tax return, which gives taxpayers just 90 days (from the fiscal year-end date) to complete the year's transfer pricing documentation.

A taxpayer is exempt from preparing transfer pricing documentation (but not all other aspects of the Decree) if one of the following conditions is met:

- has revenue below VND 50 billion and total value of related-party transactions below VND 30 billion in a tax period
- concludes an Advance Pricing Agreement (APA) and submits annual APA report(s), or
- has revenue below VND 200 billion, performs simple functions, and achieves at least the following ratios of earnings before interest and tax to revenue on the following business: distribution (5%), manufacturing (10%), processing (15%).

As of early 2018, the GDT is in negotiations with the competent authorities of various overseas tax jurisdictions to conclude the first bilateral APAs for several taxpayers.

Substance-over-form principle

Decree 20 emphasises the need for closer scrutiny of all related-party transactions to ensure that value creation is actually generated from intra-group transactions. The substance-over-form principle is especially relevant to CIT deductions, and transfer pricing documentation will need to provide support for such related-party transactions.

20% EBITDA cap on total interest expense

Decree 20 provided a 20% EBITDA cap on total interest expense. While Decree 20 is the guiding tax administration applicable to associated enterprises, it seems that the 20% EBITDA cap is applied to both related-party and third-party loans.

Thin capitalisation

There are no thin capitalisation requirements in the tax legislation. However, the level of permitted debt funding will be limited by virtue of licensing requirements. The maximum amount of debt funding is the difference between the licensed investment capital and charter capital.

Decree 20, however, provides that deductible interest on loans shall be subject to the cap of 20% of EBITDA (*as above*).

Controlled foreign companies (CFCs)

Vietnam does not have any CFC legislation.

Tax credits and incentives

Foreign tax credit

In respect of Vietnamese enterprises earning income from overseas investment, CIT (or a kind of tax with a nature similar to CIT) paid in a foreign country or paid on behalf by its partner in the country receiving the investment (including tax levied on the dividend) is allowed to be creditable. The credit shall not exceed the CIT amount payable in Vietnam.

The foreign income tax that is entitled to exemption or reduction in accordance with the foreign law shall also be credited.

Inbound investment incentives

Tax incentives are granted based on regulated encouraged sectors, encouraged locations, and size of the projects.

The sectors that are encouraged by the Vietnamese government include education, health care, sport/culture, high technology, environmental protection, scientific research and technology development, infrastructural development, processing of agricultural and aquatic products, software production, and renewable energy.

The encouraged locations include qualifying economic and high-tech zones, certain industrial zones, and difficult socio-economic areas. Large manufacturing projects with investment capital of more than VND 6 trillion disbursed within three years of being licensed can also qualify for CIT incentives if:

- the minimum revenue is VND 10 trillion *per annum* by the fourth year of operations at the latest, and
- the minimum headcount is 3,000 by the fourth year of operations at the latest.

The preferential incentive rate applied for large manufacturing projects can be extended for a maximum additional 15 years if the project manufactures goods having 'international competitiveness' whose revenue exceeds VND 20 trillion *per annum* within five years from the first year of revenue generation, or whose average head count is over 6,000.

Large manufacturing projects include projects with investment capital of VND 12 trillion or more, disbursed within five years of being licensed (excluding those related to the manufacture of products subject to SST or those exploiting mineral resources) and using technologies appraised in accordance with relevant laws.

Further, new investment projects engaging in manufacturing industrial products prioritised for development will be entitled to CIT incentives if the products support:

- the high technology sector, or
- the garment, textile, and footwear; information technology (IT); automobiles assembly; or mechanics sector and were not produced domestically as of 1 January 2015, or, if produced domestically, they meet the quality standards of the European Union (EU) or equivalent.

The two preferential rates of 10% and 20% for 15 years and 10 years, respectively, are available starting from the commencement of generating revenue from the incentivised activities. From 1 January 2016, enterprises entitled to the pre-2016 preferential CIT rate of 20% will enjoy the rate of 17% instead. When the preferential rate expires, the CIT rate reverts to the standard rate. The preferential rate of 15% will apply for the entire project life in certain cases. Certain socialised sectors (e.g. education, health) enjoy the 10% rate for the entire life of the project.

Business expansion projects are now entitled to CIT incentives if any of the following criteria are met:

- Additional fixed assets costing at least VND 20 billion (or VND 10 billion if the projects are in certain specified regions with difficult socio-economic conditions) are invested.

- There is at least a 20% increase in the value of fixed assets compared with the period before expansion.
- There is at least a 20% increase in the designed capacity compared with the period before expansion.

Investment projects are allowed to access more favourable tax incentives available under an amended or new law on CIT for the remaining project period, from tax year 2015. This entitlement is specifically applicable to the following cases:

- Expansion projects licensed or implemented during the period from 2009 to 2013 that were not previously entitled to any CIT incentives.
- Investment projects commencing operations in industrial zones during the period from 2009 to 2013 that were not previously entitled to any CIT incentives.
- Investment projects located in areas that were not previously designated as encouraged.

Tax holidays

Investors may be considered for tax holidays and reductions. The holidays take the form of a complete exemption from CIT for a certain period beginning immediately after the enterprise first makes profits, followed by a further period where tax is charged at 50% of the applicable rate. However, where the enterprise has not derived profits within three years of the commencement of operations, the tax holidays/tax reduction will start from the fourth year of operation. Criteria for eligibility to these holidays and reductions are set out in the CIT regulations as follows:

- Four years of tax exemption and nine subsequent years of 50% reduction shall be applied to:
  - Income earned by enterprises carrying out new investment projects entitled to 10% CIT.
  - Income earned by enterprises carrying out new investment projects in the socialised sectors and difficult socio-economic areas.
- Four years of tax exemption and 50% tax reduction for five subsequent years shall be given to income earned by enterprises carrying out new investment projects in the socialised sectors and in regions not included in the list of difficult socio-economic areas.
- Two years of tax exemption and four subsequent years of 50% reduction shall be applied to:
  - Income earned by enterprises from carrying out new investment projects in regions with difficult socio-economic conditions.
  - Income earned by enterprises from carrying out new investment projects, including production of high-grade steel, production of energy saving products, production of machinery or equipment used to serve agricultural, forestry, fishery, or salt production, production of irrigational equipment, production and refinement of foodstuff for cattle, poultry, or aquatic products, and development of traditional trades.
  - Income earned by enterprises that carry out new investment projects in industrial zones (except for industrial zones located in regions with favourable socio-economic conditions).

From 1 January 2018, certain incentives, including a lower CIT rate, will be granted to small and medium enterprises (SMEs) (various criteria applied to be considered as SMEs).

Employment incentives

Additional tax reductions may be available for engaging in manufacturing, construction, and transportation activities that employ several female staff and/or ethnic minorities. CIT reduction must correspond with the actual payment for those employees.

Research and Development (R&D) Fund

Business entities in Vietnam are allowed to set up a tax deductible R&D Fund. Enterprises can appropriate up to 10% of annual profits before tax to the fund. Various conditions apply.

Withholding taxes

Foreign Contractor Tax (FCT) is withheld on payments to foreign contractors.

Payments to foreign contractors

FCT on payments to foreign contractors applies where a Vietnamese contracting party (including a foreign-invested enterprise incorporated in Vietnam) contracts with a foreign party that does not have a licensed presence in Vietnam, irrespective of whether the services are provided in Vietnam or overseas.

This FCT generally applies to payments derived from Vietnam, except for the pure supply of goods (i.e. where the responsibility, cost, and risk relating to the goods passes at or before the border gate of Vietnam and there are no associated services performed in Vietnam), services performed and consumed outside Vietnam, and various other services performed wholly outside Vietnam (e.g. certain repairs, training, advertising, promotion).

In addition, certain distribution arrangements where foreign entities are directly or indirectly involved in the distribution of goods or provision of services in Vietnam are subject to FCT (e.g. where the foreign entity retains ownership of the goods; bears distribution, advertising, or marketing costs; is responsible for the quality of goods or services; makes pricing decisions; or authorises/hires other Vietnamese entities to carry out part of the distribution of goods/provision of services in Vietnam).

Foreign contractors can apply to be deduction-method VAT payers if they adopt the Vietnamese accounting system. If accounting records are adequate, the foreign contractor will pay CIT on actual profits, but otherwise on a deemed-profit basis.

For direct (non-deduction-method) foreign contractors, VAT and CIT will be withheld by the contracting party at deemed rates. Various rates are specified according to the nature of the contract performed. For CIT, the FCT rate varies from 0.1% to 10%. For VAT, the FCT rate can also range from 2% to 5%. The VAT withheld by the contracting party is an allowable input credit in its VAT return.

A summary of VAT and CIT FCT rates follow:

Types of payment	Deemed VAT rate (%) (3)	Deemed CIT rate (%)
Supply of goods in Vietnam or associated with services rendered in Vietnam (including in-country import-export and imports, distribution of goods in Vietnam or delivery of goods under Incoterms where the seller bears risk relating to goods in Vietnam)	Exempt (1)	1
Services	5	5
Services together with supply of machinery and equipment (2)	3	2
Restaurant, hotel, and casino management services	5	10
Construction, installation without supply of materials, machinery, or equipment	5	2
Construction, installation with supply of materials, machinery, or equipment	3	2
Leasing of machinery, equipment, and drilling rigs	5	5
Leasing of aircraft and vessels	Exempt (4)	2
Transportation	3 (5)	2
Interest	Exempt	5
Royalties	Exempt/5 (6)	10
Insurance	Exempt/5 (7)	5
Re-insurance, commission for re-insurance	Exempt	0.1
Transfer of securities	Exempt	0.1
Financial derivatives	Exempt	2
Other activities	2	2

Notes

1. VAT will not be payable where goods are exempt from VAT or where import VAT is paid upon importation.
2. Where the contract does not separate the value of goods and services.
3. The supply of goods and/or services to the oil and gas industry is subject to the standard 10% VAT rate. Certain goods or services may be VAT exempt or subject to 5% VAT.
4. Where aircraft and vessels cannot be manufactured in Vietnam.
5. International transportation is subject to 0% VAT.
6. Software licences, transfer of technology, and transfer of intellectual property (IP) rights (including copyrights and industrial properties) are VAT exempt. Other royalties may attract VAT.
7. Certain types of insurance are exempt from VAT (*see Exempt goods and services under VAT in the Other taxes section*).

Interest

The FCT applied to interest payments to an overseas lender is 5%. Interest on pre-1999 loans may be exempt from FCT. Offshore loans provided by certain government or semi-governmental institutions may obtain an exemption from the interest FCT where a relevant double tax agreement (DTA) or inter-government agreement (IGA) applies.

Interest earned from bonds (except for tax-exempt bonds) and certificates of deposit are subject to 5% FCT. The sale of bonds and certificates of deposits are subject to deemed tax of 0.1% of the gross sales proceeds.

Royalties, licence fees, etc.

A 10% royalty FCT applies in the case of payments made to a foreign party for transfers of technology or software licence, unless the transfers are contributed as part of legal capital (akin to equity). Transfers of technology are defined very broadly. Certain contracts for the transfer of technology must be registered with the competent authorities.

Recently, the MoF has consistently sought to impose a 5% VAT on the payments for the right to use a trademark.

Management fees and head office charges

FCT applies on management fees and head office charges at the rates applicable to services (*see above*).

Cross-border leases

A Vietnam-based lessee is required to withhold tax from payments to an offshore lessor. 5% VAT and 5% CIT is applicable to the rental charge if it is an operating lease. If it is a finance lease, the interest portion will be exempt from VAT and subject to 5% CIT.

Tax treaties

The above FCT rates may be affected by a relevant DTA.

	FCT (%)	
Recipient	**Interest**	**Royalties**
Non-treaty	5	10
Treaty:		
Algeria (1, 3)	15	15
Australia	10	10
Austria (2, 3, 4)	10	7.5/10
Azerbaijan (3)	10	10
Bangladesh (2, 3)	15	15
Belarus (2, 3)	10	15
Belgium (2, 3, 4)	10	5/10/15
Brunei Darussalam (3)	10	10
Bulgaria (2, 3)	10	15
Canada (3, 4)	10	7.5/10
China (3)	10	10
Cuba	10	10
Czech Republic (3)	10	10
Denmark (2, 3, 4)	10	5/15
Egypt (1)	15	15
Estonia	0	10
France	0	10
Finland (3)	10	10
Germany (3, 4)	10	7.5/10
Hong Kong (3, 4)	10	7/10
Hungary	10	10
Iceland (3)	10	10
India (3)	10	10
Indonesia (2, 3)	15	15
Iran (3)	10	10
Israel (2, 3, 4)	10	5/7.5/15
Italy (3, 4)	10	7.5/10
Ireland (2, 3, 4)	10	5/10/15
Japan (3)	10	10
Kazakhstan (3)	10	10
Korea (North) (3)	10	10
Korea (South) (2, 3, 4)	10	5/15

Vietnam

	FCT (%)	
Recipient	**Interest**	**Royalties**
Kuwait (1, 3)	15	20
Laos	10	10
Luxembourg	10	10
Macedonia (1)	10	10
Malaysia (3)	10	10
Malta (4)	10	5/10/15
Mongolia (3)	10	10
Morocco (3)	10	10
Mozambique	10	10
Myanmar (3)	10	10
Netherlands (2, 3, 4)	10	5/10/15
New Zealand	10	10
Norway (3)	10	10
Oman (3)	10	10
Pakistan (2)	15	15
Palestine	10	10
Panama	10	10
Philippines (2, 3)	15	15
Poland (2, 4)	10	10/15
Portugal (4)	10	7.5/10
Qatar (3, 4)	10	5/10
Romania (2, 3)	10	15
Russia (2)	10	15
San Marino (4)	10/15	10/15
Saudi Arabia (3, 4)	10	7.5/10
Serbia (3)	10	10
Seychelles (2)	10	10
Singapore (2, 3, 4)	10	5/10
Slovakia (3, 4)	10	5/10/15
Spain (3)	10	10
Sri Lanka (2, 3)	10	15
Sweden (3, 4)	10	5/15
Switzerland	10	10
Taiwan (2)	10	15
Thailand (2, 3)	10/15	15
Tunisia (3)	10	10
Turkey (3)	10	10
Ukraine (3)	10	10
United Arab Emirates (3)	10	10
United Kingdom (3)	10	10
United States (1, 2, 3, 4)	10	5/10
Uruguay	10	10
Uzbekistan (2, 3)	10	15
Venezuela (3)	10	10

Notes

1. The treaty is not yet in force.
2. In most cases, the limits set by the DTA are higher than the present FCT rates under domestic law; consequently, the domestic rates will apply.

3. Interest derived by certain government bodies is exempt from FCT.
4. Royalty FCT rates vary for certain types of royalties.

Tax administration

Taxable period

The standard tax year is the calendar year. However, different accounting year-ends can be used if approval is obtained from the authorities.

Tax returns

The annual final CIT return and the audited financial statements must be filed no later than 90 days from the end of the financial year.

Payment of tax

Enterprises are required to make quarterly provisional CIT payments (no later than the 30th day of the next quarter) based on estimates. If the provisional quarterly CIT payments account for less than 80% of the final CIT liability, the shortfall in excess of 20% is subject to late payment interest (currently as high as 11% *per annum*), counting from the deadline for payment of the fourth quarter CIT liability.

Final payment of CIT is due with the final CIT return (i.e. the 90th day of the following financial year).

Penalties

There are detailed regulations setting out penalties for various tax offences. These range from relatively minor administrative penalties to tax penalties amounting to various multiples of the additional tax assessed.

In practice, imposition of penalties has been arbitrary and inconsistent. However, in recent periods there has been a much tougher stance adopted by the tax authorities. Hence, where tax is paid late (e.g. as a result of a tax audit investigation), there is a significant likelihood of penalties being imposed.

Tax audit process

Tax audits are carried out regularly and often cover a number of tax years. Prior to an audit, the tax authorities send the taxpayer a written notice specifying the timing and scope of the audit inspection.

Statute of limitations

The general statute of limitations for imposing tax is ten years (effective 1 July 2013) and for penalties is five years. Where the taxpayer does not register for tax or commits evasion liable to criminal prosecution, the tax authorities can collect unpaid tax and penalties at any time.

Topics of focus for tax authorities

Transfer pricing

Transfer pricing is commonly discussed in the press, and the enterprises that are attracting the attention of the tax authority are generally multinational companies that have many inter-company transactions, have reported losses for many years, and/or are expanding businesses.

CIT incentives

The regulations on the conditions to enjoy CIT incentives are complicated. The guidance to classify new investment and investment expansion (these are subject to different incentive regimes) is not entirely clear. In addition, the ability to apply tax incentives is conditional on compliance to the strict accounting system requirements. Taxpayers are required to self-assess their eligibility to the tax incentives. The tax authorities therefore in tax audits focus on reviewing the taxpayers' fulfilment of the conditions.

Documentation of expenses

The tax authorities are strictly reviewing the documentation of expenses, including contracts, invoices, evidence of work done/benefit received, etc. Insufficient documentation is resulting in disallowance of input VAT credit/refund and CIT deductibility.

FCT on supply of goods

The customs authority has been requested to provide the tax authority with information of companies engaged in in-country import/export transactions in an effort to collect under-declared FCT arising from these transactions.

Secondment arrangements

We have seen the tax authority seek to impose FCT on reimbursements of expatriate remuneration costs by Vietnamese entities. Companies need to ensure that supporting documents are available to show amounts have been reimbursed at cost.

Other issues

Foreign investment restrictions

In several fields, foreign investment will not be licensed or will only be licensed under special conditions. The List of Conditional Investment Sectors include, amongst 243 sectors, television, production and publishing cultural products, telecommunication, transportation by all means, cigarette production, exploring and processing natural resources, real-estate business, education, and medical services and distribution.

Exchange controls

All buying, selling, lending, and transfer of foreign currency needs to be made through credit institutions and other financial institutions authorised by the State Bank of Vietnam (SBV).

Outflow of foreign currency by transfer is authorised for certain transactions, such as payments for imports and services abroad, refund of loans contracted abroad and payment of interest accrued thereon, transfer of profits and dividends, and revenues from transfer of technology.

All monetary transactions in Vietnam must be undertaken in Vietnamese dong. Exceptions are applicable to payments for exports made between principals and their agents, and payments for goods and services purchased from institutions authorised to receive foreign currency payments such as for air tickets, shipping and air freight, insurance, and international communications.

Forms of doing business

According to the Law on Enterprises, a foreign-invested enterprise may be established as either a single member limited liability or a limited liability with more than one member, a joint-stock company, or a partnership.

Intellectual property (IP)

IP rights are protected by the Civil Code (1995 and 2005), the Law on Intellectual Property (2005), and a host of subordinate legislation.

Vietnam is signatory to the Paris Convention, the Madrid Agreement on International Trademark Registration, and the Patent Cooperation Treaty, and is a member of the World Intellectual Property Organisation. Vietnam has entered into an agreement on copyrights with the United States (US). According to the Vietnam-US Bilateral Trade Agreement, Vietnam is further under the obligation to adhere to the Berne Convention.

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