Media title: CAPT taxation changes afoot
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CAPT taxation changes afoot

By Nam Phuong

Industry experts voiced their opinions on Vietnam's proposal to revise its capital assignment profits tax, which is expected to affect cross-border mergers and acquisitions.

Aiming at transparency

In mid-August, the Ministry of Finance (MoF) proposed a string of changes to Vietnam's taxation system, including the capital assignment profits tax (CAPT). CAPT, which forms part of the corporate income tax, is imposed on foreign investors who sell its interest in a Vietnamese company. Gains from these sales, which are determined as the excess of the proceeds minus cost and transfer expenses, are currently subject to a 20 per cent CAPT.

In its proposal, MoF intends to replace this method with the new 1 per cent CAPT, which is calculated according to gross sales proceeds instead of capital gains. If passed, the bill will take effect on January 1, 2019, together with other overhauls on personal income tax, special consumption tax, and value-added tax.

According to industry experts, the revised CAPT will simplify the process of collecting and managing taxes that are derived from cross-border mergers and acquisitions (M&As). In these cases, determining the taxable amount of capital gains is difficult due to various reasons, including fluctuations in market pricing and transparency.

"When it comes to filing and inspecting taxes, this revised CAPT would reduce the complication of any calculation and administration [issues] relating to the justification of market price. This would improve the transparency in tax inspection," Ta Hong Thai, tax partner at KPMG Vietnam, told *VIR*.

Similarly, Oliver Massmann, general director of Duane Morris LLP, praised the new scheme as a great effort by the government to unify different CAPTs being applied between foreign entities and foreign individuals.

Looking at nearby countries, it is easy to see that there is no hard-and-fast rule to CAPT. Nghiem Hoang Lan, director of tax services at PwC Vietnam, pointed out that some countries like Malaysia, Hong Kong, and Singapore have 0 per cent CAPTs in order to boost their own financial markets, while Thailand only collects capital gain tax if the buyer is a Thai resident. These regulations are tailored to fit with each nation's strategy and policy.

"It's also noteworthy that most of those countries have a wide double tax treaty network, thus the taxing right under the relevant treaty relating to capital gains tax will override the domestic law. Foreign investors may be exempt from tax on capital gains under these treaties, and the same applies to Vietnam," Lan explained.

Photo: Le Toan

Businesses are struggling to make sense of the proposed changes to the capital assignment profits tax

Implications

The downside of this altered CAPT becomes evident when the transaction is at a loss, which means the interest in the Vietnamese company is sold at a lower price than its cost to set up or to buy. According to Lan, by introducing the 1 per cent CAPT, MoF is assuming that all sales will make a profit of 5 per cent; but in reality, sometimes a positive deal cannot be made and losses are incurred.

"This can be seen as not being in line with the taxing principle that companies should only pay corporate income taxes if they generate profit," she told *VIR*.

> **"The downside of the altered CAPT becomes evident when the transaction is at a loss, and the asset is sold at a lower price than it was previously worth.**

Nguyen Hoang Hai, deputy head of the Vietnamese Association of Financial Investors, believes that the 1 per cent threshold is too high for a loss-making transaction. "For example, investors may need to shell out $10,000 for a $1 million deal, even if the sale comes at a great loss to them," he said.

Some experts suggested that if the transactions are made at a loss, firms should be allowed to choose between the current CAPT based on net capital gain and the proposed new CAPT.

There are also worries about whether the revised CAPT will slow down Vietnam's M&A wave. Statistics from the Vietnam M&A Forum 2017 show that the amount of deals in 2016 reached $5.8 billion and foreign investors played a significant role in major transactions.

However, industry experts said that there is little cause for concern. According to Ta Hong Thai from KPMG, M&A activities depend more on long-term business opportunities and strategic plans than tax schemes. Moreover, investors are already aware of CAPT in Vietnam, and the tax itself has not been a driver in either direction for cross-border M&A deals.

The last concern is related to differences between the revised CAPT, which is 1 per cent, and Vietnam's taxes on securities transfers, which is much lower at 0.1 per cent. Will foreign companies try to disguise their transactions as "securities transfers" instead of "capital transfers", in order to be eligible for the 0.1 per cent tax and avoid the higher CAPT?

"Transforming the target company from a limited liability company into a joint stock company for M&A purposes has been a popular method to reduce the tax obligation of local sellers," said Duane Morris' Massmann.

However, he emphasised that this approach is not optimal, as the low tax enjoyed by the seller comes at the expense of transforming the target company, a tactic which potential buyers do not normally accept.■