



Tax

I. Introduction

Over the last years, Vietnam's continuing efforts have improved its overall tax regime significantly and EuroCham acknowledges the positive steps the government has taken to date. In particular, we would like to thank the government for addressing our concerns raised in the 2008 White Book and re-instating the favorable tax treatment of certain benefits in kind provided to expatriates such as housing, schooling and relocation. We believe that this is beneficial in making Vietnam competitive in terms of attracting international talent which will be favorable to new foreign investment as well as the ongoing transfer of knowledge and skills to Vietnamese.

We would also like to congratulate the government in taking swift action to lessen the potential impact of the global financial crisis: Postponing and then eliminating Personal Income Tax (PIT) clearly had a positive impact on the Vietnamese economy for the first half of 2009 and helped avoid the down turns suffered by many neighboring countries in South East Asia. Eurocham members have also benefited directly from other elements of the stimulus package for example in the tourism sector through the reduction in VAT rates and by corporate tax reductions for those which qualify as small and medium sized enterprises. They have also benefitted indirectly from the increase in consumption resulting from the additional money that has been put in people's pockets.

Vietnam's tax system has evolved remarkably over the past decade and this year has had some major revisions as part of the third stage of tax reform with many welcome changes including the reduction in the corporate income tax rate to 25%. The international trend is for tax rates to reduce still further as countries compete for capital and expertise and we hope this will also be the case in Vietnam. Overall foreign investors are attracted by a tax system that is certain and transparent and the administrative burden in paying or seeking relief from tax is minimized. Accordingly, EuroCham's primary objective is to promote clarity and simplicity in the tax system and reduce the administrative burden on taxpayers. We have focused our comments on a few representative tax issues which are currently being experienced by EuroCham members but which are also we believe relevant to the wider business community both foreign and Vietnamese. In particular:

II. Deductibility of Advertising & Promotional Expenditures

Advertising and promotion is another means by which domestic consumption can be stimulated and we are of the view should be encouraged at this time: Notwithstanding the reduction in the Corporate Income Tax (CIT) Rate to 25%, many EuroCham members continue to suffer effective tax rates of up 50% due to the limited deductibility of advertising and promotional expenditures: The latest Corporate Income Tax Law put into practice 1st January 2009 has increased the cap from 10%



to 15%, however only for companies during the first 3 years of operations. The cap on advertising and promotional expenditure is also beginning to have an increasing effect on locally owned Vietnamese companies as they are growing very successfully due in part to their close knowledge of the local market.

Recommendation: EuroCham strongly believes that allowing full deductibility of advertising and promotional expenditure will have a major positive effect on future economic development in Vietnam, increase the attractiveness of Vietnam for long term investment, increase GDP per capita, provide Vietnamese consumers a larger choice at lower prices, and encourage Vietnamese businesses to start to build their brands. We believe that now is the right time for Vietnam to fully remove the restriction. We therefore recommend that advertising and promotional expenditure is recognized as a normal business expense and is eliminated from expenses with restricted deductibility. If it cannot be removed, EuroCham believes that only the publication of a committed roadmap towards the full removal of the A&P tax cap in the CIT law by 2012 or earlier will create confidence within the European business community. Any such implementation guidelines should again widen the scope of eligible items for tax deduction thus reducing the negative tax impact under the new CIT law.

III. VAT on International Transportation

EuroCham members include many companies in the international transportation and related industries in Vietnam. Accordingly, tax issues relating to international transportation have been high on EuroCham's agenda. We are appreciative of the change, effective January 2009 replacing the previous VAT exemption for international transportation with VAT zero rating which is positive in allowing the recovery of input VAT. However, EuroCham notes that some changes with respect to VAT have unfortunately caused some difficulties. There have also been difficulties in claiming tax treaty relief for corporate tax (see below).

There are also a number of related services that are an essential part of the international transportation of goods which we submit should also be zero rated as is generally the case in other countries. In addition the zero rating of the international delivery of documents and parcels rather than being subject to 10% VAT would be more consistent with international practice. To apply zero rating to these services will keep the cost of freight from and to Vietnam competitive with other countries which will have a positive impact for Vietnamese exporters. It would also resolve the practical issues which are causing great difficulties in implementing separate treatment for international transportation and the arranging of that transportation as well as other related services subject to different VAT rates.

To summarize some of the issues: While the services of airlines and shipping lines are considered to be international transportation subject to 0% VAT freight forwarding is subject to VAT at 10%. For freight forwarders the transportation cost is zero rated for VAT purposes but the profit element is subject to 10% VAT. This is a significant



issue for accounting and reporting purposes. Further clarity has been requested on whether invoices should be divided into both zero rated invoices and 10% VAT invoices. This means disclosing the margin (taxed at 10%) to customers which is not a reasonable outcome for any business.

We submit that as in most other countries with a VAT system that freight forwarding i.e. arranging the transportation of goods from Vietnam to overseas should also be treated as part of international transportation and zero rated. As a general principle within the VAT Law we believe that the arranging a service that is VAT zero rated should also be zero rated. Even if transportation costs are zero rated for VAT purposes there are still many traditional services that are not included in the zero rated treatment such as, documentation fees, demurrage, detention, container cleaning, terminal handling and a number of other charges to which different VAT rates apply. This leads to difficulties in compliance, inconsistent treatment in the industry and the potential for income shifting and other abuses.

Recommendation: We recommend that for ease of compliance, to encourage the export sector in Vietnam and to be consistent with most other countries that freight forwarding services as well as ancillary services integral to international transportation such as documentation fees, demurrage, detention, container cleaning, terminal handling are treated as zero rated.

IV. Corporate restructurings

Many countries do not address the tax treatment of reorganizations until a later stage in the development of their tax systems. However, in Vietnam, restructuring is becoming common for local and foreign owned groups for many reasons including improving efficiency and to realign corporate strategies. Accordingly, the tax treatment of corporate restructuring is a key area that should be further developed.

Currently, Vietnam's tax laws and regulations do not provide specific provisions on the tax treatment of corporate restructurings other than some limited provisions for restructuring taking a specific regulated form e.g. merger or demerger. EuroCham believes this is an area that merits future attention and resources to help prepare the tax system to keep pace with the level of development expected over the next few years. Currently, there are no clear provisions for defining tax free reorganizations or the conditions that could lead for tax free treatment of certain transactions that are undertaken not as a part of normal business operations. There have been some official letters allowing tax free restructurings involving the transfer of shares but these are taxpayer-specific and do not provide detailed guidance for taxpayers in general.

Recommendations:

- We believe it would be beneficial for the Government to provide guidance on certain special transactions typically carried out as part of the corporate



reorganization process. Once this process is complete, if certain restructurings were to meet the required conditions and qualify for such treatment.

- The authorities should consider introducing an intra-group reorganization exemption that would allow investors to change the ownership of their subsidiaries to better coordinate with regional or global restructuring needs.
- One area where official guidance would be helpful would be in clarifying the approach to and allowing such restructuring transactions to be completed at historical book cost so that no taxable gain would be recognized on these simple changes in form or location of business operations. Allowing such treatment would encourage the free flow of capital into Vietnam and would also allow Vietnamese business operations to capture efficiencies necessary to compete globally. Since we consider that a restructuring is not a transaction that is in the normal course of business it seems that it would be more reasonable to carry over the historic cost basis and in this way the assets would be treated consistently and uniformly with the assets already held by the acquiring entity in the reorganization. This would expand on and reinforce the official letters and unofficial guidance that has been provided to date and provide a unified tax framework to support such transactions.
- We recommend that consideration be given to drafting a comprehensive framework for the taxation of restructuring including both the corporate income tax and VAT consequences.

V. Tax Treaties

Taxpayers operating in and with Vietnam are fortunate in that Vietnam has a wide tax treaty network with treaties with more than 50 countries. However, in the past the process of benefitting from these treaties has not been straightforward. In most countries a taxpayer can self assess their entitlement to relief under a tax treaty. Therefore when Circular 60 in 2007 generally introduced self-assessment for entitlement to relief under tax treaties this was greatly welcomed by international businesses and globally mobile individuals. Although the new guidelines under Circular 60 greatly simplified the previous approach under the Circular 133, some issues remain.

Recently, the Ministry of Finance has been informed by taxpayers of obstacles in implementing the procedures under tax treaties. A recent official letter issued by the MOF, No: 2492 / BTC-TCT stated that income from loan interest would be covered under the procedures of applicable DTA as stipulated in Circular 60/2007/TT-BTC ("Circular 60") but income from capital transfer would be covered under the procedures applicable DTA as stipulated in Circular 133/2004/TT-BTC on December 31, 2004 ("Circular 133").



Recommendation: EuroCham believes that referring back to Circular 133 leads to uncertainty and causes a great deal of confusion for both tax payers and the tax authorities. A much better approach would be for all new rules regarding the implementation of tax treaties to be in one regulation, Circular 60. This approach would lead to consistency, transparency and avoid the potential risks associated with not knowing which provisions of the old Circular 133 are still valid and which ones have been superseded by the new Circular.

We understand the intention of the government has been to implement self assessment however having two sets of rules leads to the potential varying interpretations at the local authority level. There is a risk that from a practical perspective that officials will use familiar procedures and ignore new ones included in Circular 60 due to lack of information or experience in applying such new procedures. We also note that the widen scope of personal income tax will mean that individuals will need to have greater recourse to tax treaties to claim tax relief in this case a simpler process consistent with the principle of self assessment should be possible.

We therefore recommend that Circular 60 is revised so that the Circular can be referred as one single comprehensive code for guidance in relation to all areas in which treaty relief is able to be claimed and that obtaining such relief is simplified consistent with the principle of self assessment. Circular 133 should be specifically repealed.

VI. Statutory Limitation Period

The statutory limitation period is a key area of concern for foreign investors. The statutory limitation period for re-assessment of tax can currently be interpreted as unlimited. This is the cause for much concern among our members. Currently, according to the Law on Tax Administration, the statutory limitation applies only for penalties, not for tax arrears. This means that tax authorities and companies have the right to adjust tax obligations for an unlimited period of time if there are any mistakes or misunderstandings.

As it currently stands, the tax authorities have the right to make tax adjustments arguably for an unlimited years from the tax year in which the transaction occurred. This would be difficult to implement for both tax authorities and taxpayers. Moreover, this is not appropriate as it causes unnecessary delays in business due to such inability to minimize and manage past risks within a reasonable timeframe to be able to focus on the future growth and needs of a business by its management.

It is also unclear from the point of view of strategic investors considering investing into companies in Vietnam how far potential tax liabilities may extend into the past. This is the case where the regulations may not have been as clear in the past. We do not however believe that the tax authorities should not have the power to go back more than five years in all cases. We believe that the tax authorities should be able to reassess back further than five years in cases of tax evasion.



Recommendation: We therefore recommend that the five-year statutory limitation on re-assessment of tax obligations is re-instated.

VII. Loss Offsets

An important issue has been raised by our members regarding and the use of losses for corporate income tax purposes as a part of their diversification and risk management strategies. Many companies diversify as they expand and this clearly creates more jobs, builds expertise and spreads the risk of the company or group of related companies of failing should there be some type of unforeseen events such as a natural disaster or economic crisis in an industry.

It is widely viewed that such risk management techniques as diversification are good for businesses and for society and should be encouraged. One such way that governments can support diversification is by allowing groups of companies that are owned or managed as related parties to offset losses from one company against the gains of another related company. In this way, the government gives added incentives for companies to diversify and generally be in a better position to survive down cycles in their core businesses or to invest in important business ventures that may be less profitable in the short term due to high start up costs or capital requirements.

Recommendation: We request the government considers promoting business through granting the ability to use such related party group losses to offset gains from other members of the same corporate group as many other countries already do.

VIII. Customs valuation of intellectual property

Customs authorities applying imputed values of intellectual property in the form of royalties on imported goods has been a major issue recently. The valuation of intellectual property is often difficult and fraught with numerous potential pitfalls. EuroCham seeks to raise awareness of the need for greater clarity on the challenges of meeting all multi-lateral and bi-lateral treaty obligations for the valuation of goods for customs purposes with a specific focus on intellectual property and royalties. The key issue focuses on the difficulty in the government being able to accurately capture the value of intellectual property on goods when no such agreements are in place. This would seem to be a fairly difficult area for the authorities to confidently determine the value of such royalties. Since by its nature intellectual property is very specialized making any form of benchmarking or comparable analysis difficult and open to potential misinterpretation.

Recommendation: We ask that customs authorities only apply royalties' values to imported goods if such royalties are supported by underlying agreements.

IX. Withholding Taxes



The Tax Sector Committee welcomes the re-introduction through Circular 197 of the “hybrid” method under which foreign contractors are able to recover their input VAT while paying corporate income tax on a deemed basis. This recovery of input VAT affects is generally of most relevance to foreign contractors engaged in large infrastructure projects. This change will therefore be of encouragement to such projects. We note however that major cost of infrastructure projects is the funding cost. In this regard the interest withholding tax is a significant issue and can determine whether a project is viable or not. The non-resident lender will often exploit the inequality of bargaining power so as to force the borrower to bear the cost of the withholding tax thus increasing the cost of borrowing.

Recommendation: We recommend that consideration be given to removing the withholding tax on interest. There could be restrictions to prevent abuse such for the interest to be free of withholding tax it needs to be paid between unrelated parties.

X. Filing Period for tax returns

We believe that Vietnam has one of the shortest periods for filing tax returns globally. The deadline for submission of annual finalization dossiers (applicable to Personal Income Tax and Corporate Income Tax) is the 90th day from the end of the calendar year or fiscal year. This leads to difficulties for example in terms of the ability of companies to prepare audited financial statements and to prepare their returns by the deadline. It also leads to difficulties for individuals and increasingly corporates as they expand offshore being able to obtain the required supporting documentation to claim foreign tax credits within the required timeframe.

Recommendation: We recommend that consideration is given to extending the period for filing of annual tax returns. As in other countries an additional measure may be to allow tax agents extension of time arrangements where taxpayers who file tax returns through tax agents are able to be benefit from extended filing deadlines. This incentive should also improve the quality of tax reporting and well as compliance.