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General tax update for financial institutions in Asia Pacific

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Legislative developments

- On 24 May 2012, the assistant treasurer introduced Tax Laws Amendment (2012 Measures No. 2) Bill 2012 ("TLAB2") into the House of Representatives. TLAB2 includes the Australian Government's proposed changes to the operation of the rights to future income (RTFI) rules, consolidation tax cost setting rules and interaction with the operation of the taxation of financial arrangements (TOFA) rules for consolidated groups.

  The tax cost setting rules broadly reset the tax cost of the joining entity's assets, based on prescribed rules in the tax consolidation regime. The tax cost setting rules for RTFI assets were originally enacted on 3 June 2010. They introduced retrospective provisions to clarify that a revenue deduction for tax cost setting amounts allocated to RTFI assets would be available.

  TLAB2 proposes making consolidation amendments to modify the RTFI and tax cost setting rules to make the tax outcomes for consolidated groups more consistent with the tax outcomes that arise when assets are acquired outside the consolidation regime.

  These changes could have significant impacts for financial institutions. We encourage any taxpayer that is part of an Australian tax consolidated group to seek advice about how TLAB2 might affect their business.

- On 21 June 2012, the assistant treasurer introduced the Tax Laws Amendment (Managed Investment Trust Withholding Tax) Bill 2012 (MIT WHT Bill) into the House of Representatives. The MIT WHT Bill seeks to increase the Managed Investment Trust (MIT) final withholding tax from 7.5 percent to 15 percent on income distributed by MITs to non-residents in countries which have exchange of information agreements with Australia. The increased rate applies to income years that commence on or after 1 July 2012. It has been announced that a concessionary 10 percent rate will apply to MITs that invest only in energy efficient buildings where construction commenced after 1 July 2012. However, draft legislation for this concession has yet to be released.

  We noted that the MIT WHT Bill was in accordance with the Federal Budget 2012-13 announcement on 8 May 2012 and is a key measure targeting infrastructure financing in Australia by non-residents. The amendments are proposed to apply from 1 July 2012 and will significantly affect returns for non-resident investors who derive fund payments (which broadly exclude dividends, interest or royalties) from investments in widely held trusts. This measure will increase the required pre-tax return on capital required by foreign investors to address the higher tax rate and will also raise concerns about the long-term stability of project cash flows.

- On 24 May 2012, the assistant treasurer introduced Tax Laws Amendment (Cross-Border Transfer Pricing) Bill (No. 1) 2012 (TLA–TP Bill) into the House of Representatives.

  The TLA–TP Bill inserts a new subdivision into the Australian tax act to confirm that the internationally consistent transfer pricing rules contained in Australia's tax treaties and incorporated into Australia's domestic law provide assessment authority to address treaty-related transfer pricing. The purpose of these rules is to limit taxable profits being shifted or misallocated offshore.

  The amendments also provide direct access to Organisation for Economic Co-operation and Development (OECD) guidance material in interpreting the rules, and clarify how the proposed subdivision will interact with the thin capitalisation rules in the Australian tax law.

This measure is proposed to apply to income years commencing on or after 1 July 2004.

The TLA–TP Bill was subsequently passed by the House of Representatives without amendment on 19 June 2012 and will now move to the Senate for consideration.

- On 21 June 2012, the Tax Laws Amendment (Investment Manager Regime) Bill 2012 was introduced into the House of Representatives. The Bill proposes amending the Australian tax legislation to prescribe:
  - the treatment of returns, gains, losses and deductions on certain investments of widely held foreign funds
  - the taxation treatment of certain returns, gains, losses and deductions for 2010/11 and the earlier income years of widely held foreign funds which have not lodged a tax return and have not had their income tax liability assessed.

  The bill, if enacted, has varying commencement dates.

Taxation rulings and determinations

- Goods and Services Tax Determination (GSTD) 2012/5 and Goods and Services Tax Ruling (GSTR) 2002/2A6 were issued on 6 June 2012 and 16 May 2012 respectively by the Australian Taxation Office (ATO) following the High Court's decision in Travelex Ltd v Commissioner of Taxation [2010] HCA 33 ("Travelex").

  In this case, the High Court held that the supply of foreign bank notes by the taxpayer to a customer on the departures side of the customs barrier at Sydney Airport was made in relation to rights for use outside Australia and therefore was a GST-free supply for Goods and Services Tax (GST) purposes (i.e. the supply was not exempt from GST or subject to GST).

- GSTD 2012/5 Goods and Services Tax refers to acquisitions related to an entity's foreign currency exchange transactions with customers in Australia made solely for a creditable purpose under sections 11–15 of A New Tax System (Goods and Services Tax) Act 1999 ("GST Act").

  The view expressed in the determination is broadly that:
  - to the extent that acquisitions made by the entity relate to supplies of foreign currency to customers intending to use the currency outside of Australia, they relate solely to the GST-free supply of the currency. Consequently, these acquisitions are **made solely for a creditable purpose.**
  - to the extent that acquisitions made by the entity relate to the supply of Australian currency banknotes (AUD) to Australian customers, they relate solely to the input taxed supply of the AUD. Consequently these acquisitions are **not made for a creditable purpose**.

- GSTR 2002/2A6 – Addendum to GSTR 2002/2 Goods and Services Tax refers to the GST treatment of financial supplies and related supplies and acquisitions.

  The ATO released an addendum to amend GSTR 2002/2. It reflects the High Court's decision in Travelex and also updates the ATO view of certain transactions in light of the Travelex decision.

  A financial supply will not be input taxed to the extent that it is GST-free. Subsection 38-190(1) of the GST Act provides that a supply of things, other than goods or real property, for consumption outside Australia, is GST-free.

  GSTR 2002/2 provides guidance on the application of subsection 38-190(1) to financial supplies. Schedule 2 of GSTR 2002/2 sets out the GST treatment of supplies and fees commonly provided by financial supply providers.

  Addendum GSTR 2002/2A6 amends schedule 2 of GSTR 2002/2 to treat the following as a supply made in relation to rights that are used outside Australia, and which is therefore GST-free under subsection 38-190(1) Item 4:
  - The supply of foreign currency notes where the recipient intends to use the notes outside Australia will be GST-free. If the recipient of the notes intends to use the notes in Australia, the supply of notes will not be GST-free and will be input taxed.
  - Consideration for the supply of prepaid travel cards or similar cards loaded with foreign currency will be GST-free. The supply will only be GST-free to the extent that the card is intended to be used when the cardholder is outside Australia.

  The addendum further amends schedule 2 of GSTR 2002/2 to treat fees for effecting an ATM transaction as input taxed, but notes that fees for overseas ATM transactions may be consideration for a GST-free supply.

  The addendum applies both before and after its date of issue.

- On 13 June 2012, the ATO released an update to Issue 43, Taxation Ruling (TR) 2012/3 (previously issued as draft TR 2011/D7) regarding the application of the TOFA regime to gains and losses relating to exempt income or non-assessable, non-exempt income.

  Generally, under the TOFA regime, a gain made from a financial arrangement is included in an entity's assessable income and a loss made from a financial arrangement is deductible to the extent that the loss is made in gaining or producing an entity's assessable income, or necessarily incurred in carrying out business for the purpose of gaining or producing assessable income.

  However, the tax treatment of gains and losses related to exempt income or non-assessable income are exceptions to this general approach. TR 2012/3 is quite comprehensive and should be considered by financial institutions that are bound by TOFA rules.

ATO interpretive decisions

ATO ID 2012/1 GST and brokerage services for foreign shares listed overseas

On 8 December 2011, the ATO released ATO Interpretive Decision ATO ID 2012/1 which provides that the supply of brokerage services to facilitate the sale or purchase of shares in companies incorporated overseas and listed on an overseas exchange relates to rights for use outside Australia and is therefore GST-free under item 4 of section 38-190(1) of the GST Act.

The commissioner accepts that the value of shares is the rights that are attached to it, and while these rights may vary, they broadly consist of:

- a right to participate in dividends and equity distributions whilst the company is a going concern
- a right to participate in the distribution of assets on winding up
- a right to vote.

The interpretive decision states that brokerage services are considered to have a direct connection with rights, as through the acquisition or sale of shares, the recipient of the brokerage services acquires or sells the rights attached to the shares.

The commissioner agrees with the High Court's analysis in Travelex, in that if it is evident that the shares will be used overseas (intended use is also sufficient), then the rights that are attached to the shares will also be used outside Australia.

Where the holder of shares is in Australia and where the company in which the shares are held was incorporated in an overseas location, and the shares are listed on an exchange in that overseas location, the commissioner considers that the rights attached to those shares will be for use overseas.

Other developments

- On 8 May 2012, the treasurer delivered the Federal Budget 2012-13. Some of the significant announcements not mentioned above are summarised below:

  Basel III and Upper Tier 2 instruments

  Under the current rules, Upper Tier 2 instruments are typically debts for tax purposes. Changes to these instruments to retain Tier 2 status triggered by Basel III (particularly the requirement to be written off or to convert to ordinary shares) could have resulted in these instruments being equity for tax purposes. The budget includes measures which are intended to affirm the ongoing debt characterisation of these instruments.

  Bad debt deductions on loans to related parties

  New measures are proposed to deny a deduction for bad debt write-offs after 7:30pm on 8 May 2012 where the creditor and debtor are related parties, with the 'gain' of the debtor not being taxed. Without further details being available, potential areas of concern include securitisation vehicles, infrastructure financing and other forms of structured and cross-border finance of group entities. In this regard, the definition of 'related party' will be the key.

  Extension of limited recourse debt provisions to 'effectively' limited recourse debt

  Where a project is funded via limited recourse debt and that debt cannot subsequently be repaid, there is a broad denial of depreciation and other deductions funded from that debt. It has been proposed to extend these provisions to 'effectively' limited recourse debt, presumably to address the funding of special purpose entities.

- On 24 May 2012, the assistant treasurer announced that the government had commissioned the Board of Taxation to investigate the impacts of Australia's adopting the authorised approach of the OECD regarding the attribution of profits to permanent establishments.

  The Board of Taxation has also been asked to review the current special rule that limits the deemed interest deduction on internal funds used by foreign banks in their Australian branches to the London Interbank Offer Rate (LIBOR).

  The Board of Taxation will deliver a report to the government on these issues by 30 April 2013.

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Official launch of the RMB Qualified Foreign Institutional Investor (RQFII) pilot programme

The China Securities Regulatory Commission (CSRC), the People's Bank of China (PBOC) and the State Administration of Foreign Exchange (SAFE) jointly issued the Measures on the Pilot Programme for Securities Investment in China by RMB Qualified Foreign Institutional Investors of Fund Management Companies and Securities Companies (RQFII Measures) on 16 December 2011, formalising the framework of the official launch of the eagerly-awaited RQFII Pilot Programme. Subsequently, on 20 December 2011, SAFE issued the Notice of SAFE on the Relevant Issues concerning the RQFII Pilot Programme via a notice, Huifa [2011] No.50 ("Notice 50"), to provide further guidance on the RQFII quota and the capital inflows and outflows. This was followed by the Notice of PBOC on the Relevant Issues concerning the RQFII Pilot Programme via a notice, Yingfa [2011] No.321 ("Notice 321"), issued by the PBOC on 4 January 2012 to provide further guidance on matters relating to custodian banks and RMB accounts of the RQFII.

The RQFII programme introduces a new investment channel for RMB in Hong Kong and should be well received by Hong Kong investors seeking alternative ways of investing in the PRC securities market. The move is also a key step towards further liberalising the PRC capital market and internationalising the RMB in the long run. The introduction of the RQFII Pilot Programme in Hong Kong should also strengthen Hong Kong's status as a primary offshore RMB centre. Unfortunately, many aspects of PRC taxation in relation to RQFII, including similar tax issues and uncertainties currently encountered by Qualified Foreign Institutional Investor (QFII) participants, have yet to be clearly guided by the State Administration of Taxation (SAT) to date. Notice 47 is silent on the capital gains tax treatment, and the specific tax regulations governing the taxation of capital gains derived by QFIIs and RQFIIs have not been formally announced by the SAT. For PRC business tax, a tax notice issued by the SAT in 2005 (Caishui [2005] No.155) stipulated that any gains derived by a QFII from the trading of securities are specifically exempt from business tax. It is presently unclear whether the same business tax exemption will be extended to RQFIIs, although the principles in that circular should apply to RQFIIs. Further, the business tax implications on interest derived by a QFII/RQFII from PRC fixed income securities remain unclear and require further guidance from the SAT. In view of some of the uncertainties surrounding the PRC tax position of QFIIs/RQFIIs, we are aware that the SAT has made extensive efforts to confirm the PRC taxation of QFIIs/RQFIIs and a formal announcement may be imminent. Market participants hope that many uncertainties surrounding the taxation of the QFIIs/RQFIIs will be addressed by the SAT soon.

For further information on 'RQFII Measures', Notice 50 and Notice 321, please refer to Issue 1 of *China Alert: Financial Service Focus*. A link to this publication is provided below:

http://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Newsletters/China-alert-Financial-Service-Focus/Pages/china-alert-FS-1202-01-RQFII.aspx

MOF and SAT clarify corporate income tax deduction of loan loss provision for financial institutions

The Ministry of Finance (MOF) and the SAT recently jointly issued Caishui [2012] No.5 ("Circular 5") subsequent to circular Caishui [2009] No.64 ("Circular 64"), Notice on Questions Concerning Corporate Income Tax (CIT) Deductions of Loan Loss Provisions for Financial Enterprises. Circular 5 clarifies the detailed rules on the CIT deduction of loan loss provisions for financial institutions. Circular 5 is in effect from 1 January 2011 to 31 December 2013.

Circular 5 specifically extends the scope of financial institutions to cover finance lease companies, and explicitly points out

that accounts receivable under finance leases are within the scope of assets for claim of loan loss provisions. Circular 5 has accordingly removed the administrative approval requirements in Circular 64. Circular 5 reinstates the principles of Circular 64, yet it is only effective until 31 December 2013.

For further information on Circular 5, please refer to Issue 2 of *China Alert: Financial Service Focus*. A link to this publication is provided below:

http://www.kpmg.com/cn/en/IssuesAndInsights/ArticlesPublications/Newsletters/China-alert-Financial-Service-Focus/Documents/china-alert-FS-1202-02.pdf

MOF and SAT clarify corporate income tax deduction of reserves for the securities industry

The MOF and SAT jointly issued Caishui [2012] No.11 ("Circular 11") subsequent to the previous circular bearing the same title, Caishui [2009] No.33 ("Circular 33"), Notice Concerning Policies on CIT Deduction of Reserves for the Securities Industry. Circular 11 clarifies the detailed rules on the CIT deduction of various types of provision funds and reserves for the securities industry. Circular 11 is in effect from 1 January 2011 to 31 December 2015.

Circular 11 sets out in great detail the deduction policies concerning the various types of provision funds and reserves for the securities industry. The policies remain unchanged when compared to Circular 33. Circular 11 continues to allow taxpayers in the securities industry to deduct, on an actual basis, the relevant funds and reserves contributed or set aside in accordance with state regulations. Tax deferral is achieved by (retrospective) taxation only at the time of the liquidation or refunds.

For further information on Circular 11, please refer to Issue 3 of *China Alert: Financial Service Focus*. A link to this publication is provided below:

http://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Newsletters/China-alert-Financial-Service-Focus/Documents/china-alert-FS-1203-03.pdf

MOF and SAT clarify corporate income tax deduction rules for insurance reserves

The MOF and SAT recently jointly issued Caishui [2012] No.45 ("Circular 45") subsequent to circular Caishui [2009] No.48 ("Circular 48"), Notice on CIT Deduction of Reserves for Insurance Companies. Circular 45 clarifies the detailed CIT deduction rules for various reserves for insurance companies. Circular 45 is in effect from 1 January 2011 to 31 December 2015.

Circular 45 further emphasises that the deduction of the unearned premium reserves, life insurance reserves and long-term health insurance reserves of the insurance company for CIT purposes shall be supported by an actuary registered with the China Insurance Regulatory Commission (CIRC) or by professional agencies that are qualified to issue special purpose audit reports in this respect. In respect of the subcategories of outstanding loss reserves, Circular 45 has clearly spelt out that incurred and reported outstanding loss reserves, and incurred but not reported outstanding loss reserves, are deductible. This implies that claim expense reserves are therefore not deductible for CIT purposes when the expense reserve is created.

For further information on Circular 45, please refer to Issue 4 of *China Alert: Financial Service Focus*. A link to this publication is provided below:

http://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Newsletters/China-alert-Financial-Service-Focus/Documents/china-alert-FS-1206-04.pdf

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Budget 2012-2013

The Inland Revenue (Amendment) Ordinance 2012 was enacted on 20 July 2012 and implemented the tax concessions announced in the 2012-2013 budget.

For further details of the 2012-13 budget, please refer to the link below:

http://www.kpmg.com/cn/en/IssuesAndInsights/ArticlesPublications/Documents/Hong-Kong-budget-summary-201202-2.pdf

Islamic finance

In March 2012, the Hong Kong Government launched a two-month consultation on proposed amendments to the Inland Revenue Ordinance (IRO) and Stamp Duty Ordinance to promote the development of an Islamic bond market in Hong Kong. This policy initiative was first articulated by the then Chief Executive Donald Tsang in his policy address in 2007 and most recently by the Financial Secretary John Tsang Chun-wah in the Hong Kong budget for 2012-13.

The consultation demonstrates Hong Kong's commitment to ensuring that it has the legal and tax framework required to support the development of Islamic financing in the region. Against a background of an ever-increasing demand for Islamic financing products from both investors and borrowers, it is essential that Hong Kong provides an efficient platform to promote the sector in the region. To do this, Islamic financing products have to be treated the same as more conventional forms of financing. Introducing such rules will reinforce Hong Kong's position as an international finance centre.

Advance pricing arrangement (APA) programme

In March 2012, the Hong Kong Inland Revenue Department (IRD) issued Departmental Interpretation & Practice Note (DIPN) No. 48 which sets out the procedures for enterprises wishing to enter into an APA with the IRD. The adoption of a formal APA programme is a clear positive step forward by the IRD in implementing transfer pricing guidelines. The programme will enable multinational enterprises to obtain certainty in their transfer pricing position both in Hong Kong and in the relevant counterparty jurisdiction of their group entities.

DIPN 48 builds on the IRD's transfer pricing guidelines, namely DIPN 46, Transfer Pricing Guidelines – Methodologies and Related Issues, released in December 2009. The DIPN provides enterprises with the opportunity to attain certainty regarding the acceptability of their transfer pricing methodology with the IRD and one or more other tax authority.

The initial focus of the programme is on bilateral and multilateral APAs, although unilateral APAs will be considered in certain specified circumstances. The programme represents a significant step forward for transfer pricing in Hong Kong.

Treaty update

The double taxation agreements (DTAs) with Malta, Portugal, Spain and Switzerland have completed their formal ratification procedures. The DTAs will be effective for any year of assessment beginning on or after 1 April 2013 in Hong Kong.

DTAs were signed with Malaysia and Mexico in April and June 2012 respectively. The DTAs provide for the following rates of withholding tax:

	Dividends	**Interest**	**Royalties**
Malaysia	5 / 10 (1)	0 / 10 (2)	8
Mexico	0	0 / 4.9 / 10 (3)	10

1. 5 percent applies where the beneficial owner is a company (other than a partnership) which directly or indirectly holds at least 10 percent of the capital of the company paying the dividends.
2. No withholding tax is payable on interest paid or credited to (i) the Government of the Hong Kong Special Administrative Region (HKSAR); (ii) the Hong Kong Monetary Authority (HKMA); and (iii) such other institutions established by the HKSAR Government for carrying out public functions normally carried out by a government, as may be agreed upon from time to time between the competent authorities of the two contracting parties.
3. No withholding tax is payable on interest paid or credited if (i) the beneficial owner of the interest is in the HKSAR Government, the HKMA or a financial establishment appointed by the HKSAR Government and mutually agreed upon by the competent authorities of the contracting parties; (ii) the interest is paid by any of the entities mentioned in item (i); or (iii) the interest arises in Mexico and is paid in respect of a loan for a period of not less than three years granted by any institution as may be agreed from time to time between the competent authorities of the contracting parties. Withholding tax of 4.9 percent applies where the beneficial owner of the interest is a bank.

In May 2012, the HKSAR Government launched a consultation on whether the IRO should be amended to provide the legal framework for Hong Kong to enter into Tax Information Exchange Agreements (TIEAs). The deadline for submissions was 29 June 2012.

The IRO was previously amended in 2010 to remove the domestic tax interest requirement for exchanging tax information under DTAs. This allowed Hong Kong to adopt the latest international standard on exchange of information (EoI) and to further expand its network of DTAs from five to the current 25. The amendment in 2010 only allows Hong Kong to enter into an EoI as part of a CDTA and not as a standalone TIEA.

The consultation follows the October 2011 Phase 1 peer review report on Hong Kong by the Global Forum on Transparency and Exchange of Information for Tax Purposes ("the Global Forum"). The report recommended that Hong Kong put in place the legal framework for entering into TIEAs.

Hong Kong runs the risk of being labelled as an uncooperative jurisdiction if it does not amend its legal framework to allow it to enter into TIEAs. On the other hand, if Hong Kong amends its legal framework to comply with the Global Forum's recommendation, the concern is that there may be little incentive for jurisdictions to enter into a Comprehensive DTA (CDITA) with Hong Kong when a TIEA is already in force. This could place Hong Kong at a disadvantage in its future C DTA negotiations with a jurisdiction that has already signed a TIEA with Hong Kong. While Hong Kong wants to ensure it remains a cooperative jurisdiction in the eyes of the international community, it needs to weigh the above concerns against its overriding objective of continuing to expand its CDTA network with its major trading partners.

Latest development of the Nice Cheer Case on unrealised gains

In a clear and well-reasoned decision, the Court of Appeal in Nice Cheer Investment Limited v Commissioner of Inland Revenue (CACV 135-2011) upheld the decision of the Court of First Instance that unrealised gains from trading investments held at the year end are not taxable, as they are not realised profits taxable under the IRO. Whilst accounting treatment may play a role in determining when profits may be taxable, their importance should not be over-emphasised. The assessable profits recognised in the financial statements must be calculated in accordance with the statutory provisions of the IRO.

Nice Cheer recorded net unrealised gains in its profit and loss account in respect of trading securities held at the year end. The unrealised gains were based on the changes in the fair value (i.e. quoted market price) of the trading securities held at the year end. In computing the company's assessable profits, the unrealised gains were treated as non-taxable, while the unrealised losses were claimed for deduction. The IRD argued that the unrealised gains were taxable in the year they were recognised in the profit and loss account.

The court's decision is clear and unambiguous – unrealised gains from trading investments held at the year end are not taxable as they are not realised profits taxable under the IRO.

Although accounting treatment may play a role in determining when profits may be taxable, their importance should not be over-emphasised. The assessability of profits recognised in the financial statements must be calculated in accordance with

the statutory provisions of the IRO. CIR v Secan Ltd, which was central to the Commissioner's appeal regarding when a profit is taxable under the IRO, was not authority for the proposition that a profit is taxable simply because it is recorded in the accounts.

It is perhaps time for the IRD to critically examine its approach to the treatment of unrealised gains, and more generally re-examine the interaction between accounting and tax profits.

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Tax update

New reporting requirement for foreign stock-based compensation

A new reporting requirement for foreign stock-based compensation was introduced under the 2012 tax reform and will apply for stock-based compensation earned from 2012 onwards.

New reporting requirement

When a director/employee of a Japanese subsidiary of a foreign company (where 50 percent or more of the outstanding shares in the Japanese subsidiary are directly or indirectly held by the foreign company) or a Japan branch of a foreign company earns stock-based compensation of the nature listed below, the subsidiary/branch is required to prepare and submit a Statement to Report Foreign Stock-based Compensation (Form 9(3)) to the competent tax office by 31 March of the following year.

Stock-based compensation to be reported
Stock, money or any other benefits received from the foreign company based on the following rights granted under a contract between the director/employee and the foreign company: • Rights to receive stock without consideration or at a preferable price • Rights to receive money or any other benefits equivalent to the stock price or the dividends derived from the stock • Rights to receive stock, money or any other benefits where the stock price, the performance of the foreign company or any other indicator achieves a predetermined target

Note that in the above, 'stock' includes stock issued by another foreign company that has a capital relationship of at least 50 percent, with the foreign company having a contract with the director/employee.

This new requirement will be implemented for the Statement to Report Foreign Stock-based Compensation to be submitted on or after 1 January 2013. Thus, the first submission should include stock-based compensation earned in 2012.

Items to be reported

Items to be reported in a Statement to Report Foreign Stock-based Compensation 2012.t9(3)) are as follows:

Items to be reported		**Note**
Information on directors/employees who earn stock-based compensation	• name • address (*)	(*) as at the date they receive the stock-based compensation
Information on the stock-based compensation	• date of receipt of the stock-based compensation • details of the stock-based compensation(*)	(*) Examples: distribution of stock (with/without cash payments) or cash payments (equivalent to stock price/equivalent to dividends)

	• total value of the stock-based compensation and its currency • number of units for the stock-based compensation (e.g. amount of stock) • value of the stock-based compensation per unit (e.g. the stock price on the exercise date) and its currency	
Information on the rights on which the stock-based compensation is based	• date that the contract for the rights was concluded (grant date of the rights) • type of rights(*) • total number of shares/units or total value of cash/any other benefits to be received based on the granted rights	(*) Examples: stock options, restricted stock, restricted stock units, employee stock purchase plans (ESPPs), stock appreciation rights (SARs), performance-based shares, performance-based units or phantom stock
Information on the foreign company	• name • name of the state where the headquarters of the foreign company is located	
Other related information		Example: when stock options are exercised with cash, the exercise price should be reported

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Tax update

Guidelines for application for reduced treaty rate ("the Guidelines")

One of the revisions of the Korean tax law is that non-residents (the "beneficial owner" herein) deriving Korean sourced income and seeking to obtain reduced treaty rates are required to submit an application form for the reduced tax treaty rate to their withholding agents before receiving the income in question.

The Guidelines specify the application form filing procedures and requirements that need to be followed by different categories of the beneficial owners. The Guidelines are summarised below:

Procedures for direct investment

Beneficial owners who are not investing through an Overseas Investment Vehicle (OIV) in Korea, e.g. foreign corporations, will be required to submit an Application for Reduced Tax Rate to their tax withholding agents. The withholding agents will apply the reduced tax rate based on the resident country information in the Application for Reduced Tax Rate submitted.

Procedures for indirect investment

For beneficial owners who invest in Korea through OIVs and who have derived Korean-sourced income through the OIVs, the OIVs are required to collect and retain the Application for Reduced Treaty Rate on Korean-sourced Income from the beneficial owners. The OIV should prepare a Report of OIV based on the collected information and submit it to the withholding agents.

Among OIVs, there is an investment vehicle defined as an Overseas Public Collective Investment Vehicle (OPCIV). The distinction between OPCIVs and OIVs are as follows:

- The OPCIV is an overseas investment vehicle similar to a collective investment vehicle under the Financial Investment Services and Capital Markets Act and registered or approved in a tax treaty country of Korea.
- The securities of OPCIV are not issued by private placement and the OPCIV has 100 or more investors (an overseas investment vehicle shall be counted as one investor for this purpose) as at the end of the preceding fiscal year (or as at the date of submission of this report if the OPCIV is newly established).
- The OPCIV is not an overseas investment vehicle subject to any tax treaty provisions that deny tax treaty benefits.

If an OIV is qualified as an OPCIV, the OPCIV is required to submit to the withholding agent (or another OIV) documentation supporting its OPCIV status and a schedule listing out the total investment amount and number of beneficial owners by country (the Report of Overseas Investment Vehicles).

The benefits of the simplified procedure for OPCIV are as follows:

- The applicant does not have to collect Application for Entitlement to Reduced Tax Rate forms from the ultimate investors.
- The applicant does not have to attach a Schedule of Beneficial Owners with the application.

Exception from application of reduced tax rates

If the withholding agent is not provided with the application form or is not able to clearly determine the substantive earner of the income, the withholding agent is required to withhold tax, applying the withholding tax rates stipulated in the Korean tax laws.

Holding period of the documents

Once the application form has been submitted to the withholding agent and there is no subsequent change to the form, the submitted application form is valid for three years from the submission date. The withholding agents are required to maintain information related to the applicable reduced tax rate for five years from the next day of the withholding payment due date.

This new provision is applicable to income subject to withholding tax on or after 1 July 2012.

For more details, please refer to the guidelines published by the Korean tax authorities:

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Tax update

Statement of monetary and non-monetary incentive payment to agents, dealers or distributors ("Form CP58")

Further to the issuance of Form CP58 by the Malaysian Inland Revenue Board (MIRB) to report monetary and non-monetary incentive payment to agents, dealers or distributors, the MIRB has provided further clarification. This includes the following:

- The Form CP58 reporting requirement will not apply to payments made from 1 January 2011 to 31 December 2011 if the payer companies have issued to their agents, dealers or distributors an annual statement recording the monetary and non-monetary incentive payments made to them. With regard to companies which did not issue annual statements to the agents, dealers or distributors, the MIRB agrees to extend the concession to file Form CP58 by one month from the date the minutes of Joint Memorandum on Issues for Post 2012 Budget Dialogue was published, that being 14 June 2012.
- For payments made from 1 January 2012 onwards, as an administrative concession, the CP58 reporting requirement is only required for monetary and non-monetary incentive payments which exceed RM 5,000 per annum.
- For non-monetary incentives, the amount to be disclosed should be based on the actual cost incurred by the payer companies.

Recent income tax rules gazetted

Income Tax (Transfer Pricing) Rules 2012 and Income Tax (Advance Pricing Arrangement) Rules 2012

The Income Tax (Transfer Pricing) Rules ("the Rules") require taxpayers engaging in related party transactions to prepare contemporaneous transfer pricing documentation. The Rules also prescribe the method to be applied to determine the arm's length price. They are applicable to both cross-border and domestic transactions involving related parties, and specifically address the treatment of the following related party transactions:

- intra-group services
- cost contribution arrangements
- intangible properties
- interest on financial assistance

The Income Tax (Advance Pricing Arrangement) Rules, which only apply to cross-border transactions, set out the process and expected timeline for the application and negotiation of unilateral, bilateral or multilateral advance pricing arrangements.

The above rules are retrospective in their application from 1 January 2009.

Recent exemption orders gazetted

Income Tax (Exemption) (No. 3) Order 2012

Expatriates working in an approved treasury management centre in Malaysia are only taxed on that portion of their chargeable income attributable to the number of days that they are in Malaysia. The order is effective from the year of assessment 2012.

Stamp Duty (Exemption) (No. 2) Order 2012

All instruments of loan agreements and service agreements executed on or after 8 October 2011 and not later than 31 December 2016 by an approved treasury management centre are exempt from stamp duty which would otherwise be chargeable under the Stamp Act 1949.

Public rulings

The MIRB has recently issued the following public rulings, amongst others:

- **Public Ruling No. 2/2012: Foreign Nationals Working in Malaysia – Tax Treaty Relief**

  This public ruling explains the application of tax treaty relief to foreign nationals from treaty countries seconded to Malaysia by their employers.

- **Public Ruling No. 3/2012: Appeal against an Assessment**

  This public ruling explains the new procedure on lodging an appeal against an assessment. It now requires an appeal to be lodged using the prescribed form (Form Q). This is different from the past practice where an appeal lodged by way of letter was acceptable and the taxpayer would subsequently be requested to complete and file Form Q if it became necessary to forward the appeal case to the Special Commissioner of Income Tax for handling.

- **Public Ruling No. 4/2012: Deduction for Loss of Cash and Treatment of Recoveries**

  This public ruling explains the deductibility of loss of cash in the course of business caused by theft, defalcation or embezzlement, and the income tax treatment of subsequent recoveries of the loss of cash in which a tax deduction was claimed in previous years.

  It replaces Public Ruling No. 5/2005 issued on 14 November 2005.

The full public rulings are available at *http://www.hasil.gov.my.*

Mauritius

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Tax update

Updates on Mauritius treaties

- The following exchange of information agreements have come into force:
  - Denmark (effective from 1 June 2012 for criminal matters and 1 January 2013 for other matters)
  - Norway (effective from 18 May 2012 for criminal matters and 1 January 2013 for other matters)
- Finland ratified its exchange of information agreement with Mauritius in May 2012.
- Kenya and Mauritius signed an income tax treaty and an investment promotion and protection agreement in May 2012.
- Luxembourg and Mauritius initialled a protocol to the current treaty in April 2012.
- France ratified the amending protocol, signed in June 2011, to its double taxation agreement with Mauritius in March 2012.

Income tax ruling

Is *société* considered a resident of Mauritius and is it subject to income tax?

A Fund, ("the Fund") together with its non-resident partners ("the Partners") set up a special purpose vehicle (Mauritius SPV) in the form of a partnership under the laws of Mauritius. The Fund and its Partners are non-Mauritius tax residents. The Mauritius SPV acquired a 15 to 17.5 percent equity interest in S Ltd, a partnership organised under the laws of Norway. S Ltd holds varying equity interest in companies located in Benin, Gabon, Ghana, Gibraltar, Liberia, Sierra Leone, Tanzania and Togo.

The Fund proposed setting up a holding company, H Ltd, a company resident in Mauritius with a Category 1 Global Business Licence (GBC1) to own its shareholding in the Mauritius SPV.

It was held that:

1. The Mauritius SPV is considered to be a resident *société* for tax purposes in Mauritius in accordance with its definition in Section 73 of the Income Tax Act.
2. Since the Mauritius SPV is considered a resident *société* and derives income solely from sources outside Mauritius, the share of income of its associate H Ltd is deemed to be foreign sourced income. Accordingly, H Ltd is entitled to claim credit for foreign tax suffered in the African countries or the presumed 80 percent tax credit.
3. If the Mauritius SPV holds a GBC1 and opts to be liable for tax under Section 47(6) of the act, it will benefit from the 80 percent presumed tax credit or the actual tax suffered to set off against the Mauritian tax payable in accordance with the provisions of regulations 3 and 8 of the Income Tax (Foreign Tax Credit) Regulations 1996.
4. If the Mauritius SPV opts to be liable to tax at 15 percent, its distribution of income will be treated as dividends in the hands of the recipients, which are exempt from Mauritian tax.

The non-resident partners of the Mauritius SPV would not be liable to pay income tax in Mauritius in respect of their share of income in the Mauritius SPV, given that the latter will derive income from outside Mauritius.

Income tax treatment of different funding methods

P Ltd and its subsidiaries are engaged in the operation and management of hotels. Both P Ltd and its Mauritian subsidiaries require cash for their current operating activities.

It is proposed that the existing shareholders of P Ltd will obtain the necessary funding through the issue of convertible bonds (CBs), which will be listed on the Stock Exchange of Mauritius and will be convertible after three years. Any CB that has not been converted will be redeemed by P Ltd after seven years. The income from the CBs, referred to as the 'CB interest', will be computed according to the aggregate of the prime lending rate plus 1.5 percent.

The funds raised from the CBs will be applied towards the trading operations of P Ltd and its operating subsidiaries. The operating subsidiaries will be funded in one of the following ways:

- interest bearing loans
- convertible bonds
- redeemable preference shares
- equity
- zero coupon bonds.

It was held that:

Interest bearing loans

Based on the facts given and the understanding that the interest rate is at arm's length, it has been confirmed that where P Ltd funds the Mauritian subsidiaries through the 'interest bearing loans', the interest income will be fully taxable in accordance with the provisions of Section 10(1)(d) of the Income Tax Act 1995. It has also been confirmed that the CB interest will be fully deductible, subject to the provisions of Section 19 of the act.

Convertible bonds

It has been confirmed that in the event that P Ltd itself funds the Mauritian subsidiaries through CBs ("the secondary CB"), on the understanding that the interest rate is at arm's length, the income derived by P Ltd would be fully taxable and the interest incurred fully deductible as ruled above. In the event the secondary CB is converted into equity shares, however, the CB interest would be disallowed for tax purposes.

Redeemable preference shares

It has been confirmed that subject to the conditions for the issue of the redeemable preference shares (RPS), the distribution on the RPS will be considered, in accordance with the Statement of Practice (SP 6/10) issued by the Mauritius Revenue Authority (MRA), as dividend or interest.

Equity

It has been confirmed that in cases where the funding is through equity investments, P Ltd will derive dividend income from subsidiaries, which will be exempt from corporate tax if the distribution satisfies the definition of 'dividends' under Section 2 of Part 1 of the act. In such cases, the CB interest is not deductible, and any expenditure incurred in the production of exempt dividends will be disallowed in accordance with the provisions of Section 26 of the act.

Zero coupon bonds

It has been confirmed that interest receivable by P Ltd on the zero coupon bonds will be subject to tax on an accrual basis in accordance with Section 5 of the act.

Will the appointment of a new beneficiary to a trust affect its income tax status?

'A' is a trust administered by C Ltd ("the Company") in its capacity as a trustee. All of A's beneficiaries appointed to date, as well as the settler, are non-residents of Mauritius, and none of the trust's assets are located in Mauritius. Every year, A has filed a declaration of non-residence with the MRA under Section 46(3) of the Income Tax Act.

'B' is a charitable trust administered by the Company and is registered with the MRA, thus benefiting from income tax exemption. The Company would like to appoint B as a new beneficiary to A, so that B will be entitled to the distributions made by A.

It was held that:

On the basis of the facts, as B is registered with the MRA as a charitable trust, it is therefore a trust which is resident in Mauritius under the Trusts Act 2001. In order for A to benefit from the exemption provided under Section 46(3) of the act, it must satisfy the condition laid down under subsection (2)(b) (i) of the above section, i.e. that "all the beneficiaries of the trust are, throughout an income year, non-residents".

With the appointment of B as a new beneficiary which is resident in Mauritius, not all the trust's beneficiaries will be non-residents. Since A will not qualify under subsection 2 of Section 46, it will therefore not benefit from the exemption under Section 46 (3) of the act.

Do expenses qualify as being tax deductible?

A Ltd is a GBC1 company incorporated in Mauritius and is authorised to operate as a collective investment scheme (CIS) manager by the Financial Services Commission. It is licensed to provide both investment management and advisory services to fund entities and other investment managers. It is the CIS manager for the following funds in addition to B Ltd and C:

1 D (Mauritius-based fund)

2 E (Mauritius-based fund)

3 F (Mauritius-based fund)

4 G (Jersey registered fund)

A Ltd also provides investment advisory services to H, a Singapore-based entity, and J, a Mauritian-based CIS manager.

In accordance with its strategy and plan to continuously look for new business and build up its current business, A Ltd has targeted and acquired the investment management contracts of an existing GBL1 CIS manager, K Ltd, which acted as CIS manager to two Mauritian-based GBL1 funds, namely B Ltd and C.

The transaction was carried out by A Ltd through the acquisition of K Ltd and its holding company, R Ltd, and, after the amalgamation and consequential dissolution of the other two companies, the Company remained as the sole surviving entity.

Following the conclusion of the transaction, A Ltd had successfully expanded its business operations with two additional investment management contracts with B Ltd and C respectively. In turn, this contributed to generating additional income streams for A Ltd. It incurred sizeable professional fees in connection with the crystallisation of the transaction, including costs for legal counsel, tax advisors and various other service providers. It also secured a long-term interest bearing loan to finance the acquisition/amalgamation and transaction costs. An upfront arrangement fee was also payable in respect of the loan agreement.

It was held that:

1. Based on the facts provided, the professional fees in connection with, and the arrangement fee paid to, secure a loan to finance the acquisition/amalgamation of K Ltd and its holding company R Ltd, are expenses that are capital in nature, and do not qualify as deductible expenses for the purpose of computing its chargeable income, in accordance with the provisions of section 26 (1) (a) of the Income Tax Act.

2. Since, however, the purpose of the loan was to finance the acquisition/amalgamation transaction, thereby benefiting the business of A Ltd by generating additional income, the interest incurred thereon constitutes an expenditure on capital employed exclusively in the production of gross income under section 10 (1) (b), and therefore qualifies as a deductible expense in accordance with the provisions of section 19 (1) of the act.

Income tax ruling – will distribution by the trust be deemed as dividends and hence be exempt in the hands of the recipient?

ABC Trust holds a GBC1 licence and is authorised by the Financial Services Commission to operate as a CIS. It is a resident of Mauritius and is liable to tax there, whereas its settlor and beneficiaries are non-residents of Mauritius.

It is considering a restructure whereby a company holding a GBC1 licence will be added as the sole beneficiary of the applicant, instead of the existing non-resident beneficiaries.

After the restructure, the applicant will continue to be a tax resident of Mauritius and will have a single beneficiary, i.e. a holding company, held by the original beneficiaries of the applicant.

Following the restructure, the applicant will be making distributions only to the holding company, instead of to the non-resident beneficiaries.

It was held that dividends or other distributions paid by a company holding a Global Business Licence under the Financial Services Act to another company holding a Global Business Licence under the Financial Services Act will constitute exempt income in accordance with the current provisions of the Income Tax Act.

New Zealand

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Tax update

Use of optional convertible notes (OCNs) in funding arrangement found to be tax avoidance

In December 2011, the New Zealand High Court held that the use of hybrid financing in the form of OCNs (i.e. loan notes convertible to shares in the issuer) as part of a cross-border funding arrangement was tax avoidance, as this was structured to obtain impermissible tax benefits.

Broadly, the arrangement involved a wholly owned New Zealand subsidiary (Alesco NZ) of an Australian listed company (Alesco Corporation) issuing zero coupon rate OCNs to its Australian parent to raise funding for the acquisition of two New Zealand businesses.

For New Zealand purposes, OCNs are treated as having both debt and equity components, with notional (tax deductible) interest arising on the debt component under New Zealand's financial arrangements tax rules (notwithstanding the zero coupon). The notional interest was not taxable to Alesco Corporation in Australia, as OCNs in Australia are treated fully as equity.

New Zealand Inland Revenue challenged the transaction as tax avoidance, arguing that while the 'black letter' of the law was complied with, economically the OCNs were no more than interest-free advances stapled to valueless and purposeless share warrants/options.

The taxpayer argued that there was economic reality in the transactions – the financial arrangements rules reflected this economic reality by treating notional interest on the debt component as an economic cost. Further, the next best alternative to the OCN funding structure (an interest bearing loan) would have resulted in higher New Zealand interest deductions being claimed by Alesco NZ.

When ruling in favour of the New Zealand Inland Revenue, the High Court considered the following:

- No real interest expense was incurred by Alesco NZ and the notional interest claimed was not a real economic cost.
- There was no negotiation between Alesco Corporation and Alesco NZ on the terms of the OCN, which would be expected in an arm's length transaction. Accordingly, the OCNs did not have any inherent economic value to a third party.
- The arrangement was artificial in terms of its design to secure a tax advantage in New Zealand.
- There was no corresponding taxable income returned by Alesco Corporation for the interest deductions claimed by Alesco NZ.
- New Zealand Inland Revenue did not have to rely on evidence that Alesco would have funded the transaction differently (i.e. using an interest bearing loan) in the alternative.

In summary, the High Court concluded that the use of the OCNs, when viewed in a commercially and economically realistic way, did not meet policymakers' intention for use of the tax rules in such a manner. (This is referred to as the 'Parliamentary Contemplation' approach.)

KPMG's view

The ruling has wide ramifications, as a number of similar transactions are also being challenged by New Zealand Inland Revenue. The decision casts serious doubt over the use of (what were considered at the time to be unremarkable) hybrid funding structures for commercial transactions. [*Disclosure: KPMG in New Zealand was the tax advisor to Alesco on its OCN transactions.*]

Draft statement on application of the tax avoidance provisions

New Zealand Inland Revenue's view on tax avoidance was also the subject of a draft interpretation statement released in late December 2011.

The statement confirms that in the Commissioner's view, the Parliamentary Contemplation approach (see above) is the new standard, and the commercial and economic reality of transactions is paramount to the tax avoidance considerations.

KPMG has concerns about a number of the conclusions reached in the draft statement, including New Zealand Inland Revenue's view that certainty is undesirable when applying the anti-avoidance rule, the apparent change in interpretation of the general rule (as the legislative wording is unchanged), and the omission of a requirement for the Commissioner to determine an appropriate and realistic commercial counterfactual to test whether the tax advantage achieved is contemplated.

New Zealand Government's tax priorities for 2012-13

The government released its tax policy work programme in March 2012, outlining its tax focus for the next 12 to 18 months. The focus is on improving the coherence, efficiency, sustainability and fairness of the existing tax system rather than making any radical changes to the tax base and/or tax rates. Tax priorities are aligned to the government's wider economic priorities to manage its finances, build a more competitive and productive economy, deliver better public services and rebuild Christchurch, following the earthquakes in 2011.

The immediate tax focus is primarily tax base protection, with changes signalled to tighten deductibility of expenditure relating to 'mixed-use' assets (i.e. those with dual business and personal uses, such as holiday homes, private yachts and aircraft) and to tax certain exempt employee benefits (see below). A number of these base protection tax changes were formally announced in the government's 2012 budget in May (also discussed below).

The work programme also includes reviews of the dividend rules and New Zealand's imputation system (the latter, around whether credits should be refundable or able to be streamed to certain shareholders). Consideration of an 'active' income exemption for foreign branches of New Zealand entities and active financial institutions is also on the government's agenda, as is a further review of New Zealand's thin capitalisation regime.

Given the importance of revenue collection to achieving the government's economic objectives, legislative changes supporting a number of administrative changes by New Zealand Inland Revenue (such as IT system upgrades and improving information sharing capabilities with other government agencies) have also been prioritised.

New Zealand 2012 budget

On 24 May, the New Zealand Government unveiled its budget, amidst the ongoing economic turbulence in Europe, a fragile domestic economy, and the challenges of rebuilding Christchurch.

Widely publicised as a 'zero' budget, there was little in new government spending other than for health, social welfare and education. The key driver was the government's commitment to returning its books to balance by 2015. Based on the budget forecasts, this is on track – but only just. A key determinant will be the timing and extent of the Christchurch rebuild, given its projected contribution to New Zealand's overall economic growth during the next few years.

Tax has played a background part in this year's budget. The limited tax announcements are designed to support the government's surplus target by plugging a number of tax revenue holes. The key changes include:

- tightening the rules around the deductibility of costs relating to mixed-use assets, such as holiday homes
- making changes to valuation rules to prevent tax benefits from changing valuation methods (aimed at the agricultural

sector)

- removing certain tax rebates for individuals
- providing extra funding for New Zealand Inland Revenue over the next four years for its assurance/audit function (based on the success of past funding, the additional NZD 78 million proposed is expected to generate NZD 350 million in additional tax revenue).

Employee benefit taxation proposals

As part of the government's base protection focus, New Zealand Inland Revenue and Treasury officials released a consultation paper that aims to tax currently tax-exempt benefits provided to employees, where there is an element of salary trade-off (i.e. where cash salary is substituted, either explicitly or implicitly, for non-taxed benefits, such as car parks and childcare provided on the employer's premises). These benefits will also be captured for determining social assistance entitlements and repayments.

The options presented are to either tax such benefits as salary (subject to New Zealand's pay-as-you-earn regime) or under the fringe benefit tax (FBT) rules (by restricting the current FBT exemptions).

KPMG's comment

While the proposals are understandable both from a fiscal and social policy perspective, our key concern is the compliance costs that will be imposed on employers by having to identify, value and attribute benefits to their employees for tax purposes. Another concern is the potential for overreach, particularly if implied salary trade-offs (i.e. where there is no cash alternative offered) are taxed. For example, if an employer provides a car park, it will be of no value to an employee if there is free parking available as an alternative, and should therefore not be taxable as a benefit.

The proposals need to be carefully targeted at situations where there is genuine benefit, and where the adverse impact on employers is minimised.

The charitable sector will also be hit hard, as the proposals will severely restrict charities' tax exemption for benefits provided to employees – thus likely raising costs in a sector where every dollar counts.

Tax bill with new international tax rules passed

In May 2012, the Taxation (International Investment and Remedial Matters) Act 2012 was signed into law. The act introduced new tax rules for non-portfolio (i.e. greater than 10 percent) shareholdings in foreign entities that are not controlled foreign companies (CFCs).

The new rules, which largely mirror the tax rules for offshore CFCs, introduce an exemption from New Zealand tax where the foreign entity is an 'active' business (i.e. less than 5 percent of its income is from passive sources, such as dividends and interest). Distributions are also exempt where the New Zealand shareholder is a company.

The other key change is the allowance of a 0 percent rate under New Zealand's Approved Issuer Levy (AIL) rules for certain widely-held/listed debt issues. (AIL is a replacement for withholding tax on the interest, which is generally levied at 10 or 15 percent.)

The Taxation (Annual Rates, Returns Filing and Remedial Matters) Bill

The Taxation (Annual Rates, Returns Filing and Remedial Matters) Bill, introduced to parliament in September 2011, has finally been reported back from the parliamentary Select Committee. The Select Committee received public submissions on the bill and recommended a number of changes to the draft legislation.

The bill taxes shares issued under certain capital retention schemes by New Zealand companies (called 'profit distribution schemes'), clarifies the availability of a tax deduction for expenditure on unsuccessful software projects, simplifies tax return filing requirements for individuals, and tightens the New Zealand thin capitalisation requirements for banks, in addition to a number of other miscellaneous changes.

The Select Committee's report takes note of concerns about New Zealand Inland Revenue's ageing IT infrastructure, and recommends the deferral of a number of measures to allow the department's systems to cope. We are particularly concerned that this has the potential to constrain future tax policy development and effective delivery of operational changes. This therefore needs to be a priority focus for the government and the department.

Philippines

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Tax update

Revenue Memorandum Circular No. 22-2012 dated 7 May 2012

This circular clarifies the implementation and interpretation of Revenue Regulations No. 5-2012. It provides that all rulings issued by the Bureau of Internal Revenue (BIR) prior to 1 January 1998:

- are not to be used as a precedent by any taxpayer as a basis to secure rulings for themselves on current business transactions or in support of their position against any assessment
- are not to be used by any BIR action lawyer for issuing new requested rulings involving current business transactions
- continue to be valid, but only:
  - to the taxpayer who was issued the ruling
  - in terms of the specific transactions covered, which are subject to the same ruling.
- shall remain valid as mentioned above, unless the authority has expressly provided notification regarding its revocation, or the legal basis in law for such issuance has already been repealed or amended in the Tax Code.

BIR Ruling No. 210-2012 dated 23 March 2012

The BIR held that with the issuance of Revenue Memorandum Circular (RMC) No. 18-2011 dated 12 April 2011, pertaining to the income tax exemption of interest income earned from long-term deposits or investment certificates, the issuance of a BIR ruling is not necessary.

The BIR held that the taxability of interest income from long-term deposits or investment is dependent on the full compliance of the requisites under RMC No. 18-2011. If the requirements are not complied with, a final tax of 20 percent will be imposed.

Singapore

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Tax update

Tax certainty on gains on the disposal of equity investments

The safe harbour rule was announced by the finance minister in the 2012 budget to provide certainty on gains derived from the disposal of shares and was discussed in *General tax update for financial institutions in Asia Pacific* Issue 43:

http://kpmg.com/cn/en/IssuesAndInsights/ArticlesPublications/Newsletters/General-Tax-Update/Documents/General-tax-update-1205-43.pdf

The Inland Revenue Authority of Singapore has released further information on the qualifying criteria:

- The exemption on gains from the disposal of equity investments ("the exemption") will apply regardless of the place of incorporation of the investee company or whether it is listed.
- The exemption is not applicable to:
  - the disposal of shares in an unlisted company that is in the trading business or that holds Singaporean immovable properties
  - a divesting company whose gains from the disposal of shares are included as part of its income as an insurer under Section 26 of the Singapore Income Tax Act.

The exemption is only applicable to the disposal of ordinary shares. It would not be applicable to the disposal of shares of a preferential nature or shares with redeemable or convertible features.

The tax exemption would apply to qualifying disposals made during the five-year period from 1 June 2012 to 31 May 2017.

Taiwan

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Tax update

Amendments to capital gains tax on Taiwan securities trading

Under the current Taiwan income tax law, capital gains derived from trading Taiwan securities are exempt from income tax. Earlier this year, the Ministry of Finance (MOF) of the Executive Yuan initiated discussions on the imposition of tax on capital gains from trading Taiwan securities. The MOF has subsequently proposed a draft amendment to the Legislative Yuan for review.

Based on the draft amendment proposed by the MOF, the capital gains on securities and futures are taxed under the Alternative Minimum Tax (AMT) regime. Under the current AMT regime, if a foreign company maintains a permanent establishment in Taiwan and trades Taiwan securities through its foreign institutional investor (FINI) account registered in Taiwan, the capital gains derived by the foreign investor will be subject to AMT. Based on the MOF's proposal for the capital gains tax regime, the deductible amount for the AMT calculation would be reduced from TWD 2 million to TWD 500,000 and the AMT rate range would be increased from 10-12 percent to 12-15 percent. In addition, for shares which have been held for three years or more, the company is only required to report half of the capital gains from sales for AMT purposes.

The MOF's submission of the proposed capital gains tax amendment to the Legislative Yuan for review and approval sparked heated discussion among legislators, as well as the general public. Currently, in addition to the MOF's version of the draft bill, four other versions have been presented by legislators from different political parties. Most notably, the ruling party presented its own version of the capital gains tax amendment. Under this version, with the exception of treatment of individual investors, the treatment for corporate investors is similar to the version presented by the MOF – that is, the capital gains will be taxed under the AMT regime and with the increased tax rate of 12-15 percent.

The Legislative Yuan has not announced which of the five different versions of the capital gains tax law submitted earlier in June it will adopt for review. The Legislative Yuan will hold an extra legislative session in July to resolve this matter.

Thailand

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Tax update

Tax exemptions on dividends received by a resident of Thailand

Royal Decree No. 538 issued on 11 June 2012 provides a tax exemption to residents of Thailand who receive dividend income from foreign companies listing on the Stock Exchange of Thailand.

Under this royal decree, an individual who is a resident of Thailand, can exclude such dividend income from his/her taxable income in computing personal income tax, provided that:

- the individual has had tax deducted at 10 percent of the dividend received
- the individual has not requested/will not request a refund or tax credit, either for part or for the entire amount, of the tax deducted from the dividend.

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