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Tax update

Legislative developments

- On 14 November 2012, in *Mills v Commissioner of Taxation* [2012] HCA 51, the High Court of Australia (HCA) upheld the appeal of the taxpayer in a decision involving the Commonwealth Bank of Australia's (CBA) issue of AUD 2 billion of stapled securities to meet regulatory capital requirements. The HCA held that the anti-avoidance provision in relation to franking credits did not apply to the case as follows:
 - The relevant anti-avoidance provision applies where it would be concluded with regard to the relevant circumstances of the scheme that a person entered or carried out the scheme for the purpose (whether or not this is the dominant purpose, but excluding an incidental purpose) of enabling the relevant taxpayer to obtain an imputation benefit.
 - Importantly, the HCA recognised that "a purpose can be incidental even where it is central to the design of the scheme if that design is directed to the achievement of another purpose." On the facts, the HCA concluded that from the perspective of a reasonable person, the fact that the capital raising enabled taxpayers who became holders of the stapled securities to obtain franking credits was incidental to the CBA's purpose of raising Tier 1 capital.

On 21 January 2013, the Australian Taxation Office (ATO) issued a decision impact statement (DIS) in response to the decision. The ATO's view represented in the DIS is that:

- If the same facts and circumstances apply in other cases of Tier 1 capital raising, the anti-avoidance provision will not apply.
 - Where a substantial, albeit not dominant purpose of franking is evident, the franking purpose will need to be carefully considered regarding the extent to which the purpose does no more than further or follow on from some other purposes.
 - In light of the HCA's confirmation that the list of relevant circumstances is not exhaustive, particular fact patterns in other cases may reveal that other relevant considerations beyond the mandatory considerations may be relevant in the question of purpose.
- On 11 January 2013, the Treasury released an exposure draft (ED) of amendments to the Taxation of Financial Arrangement rules. The ED is intended to implement a number of changes announced on 29 June 2010 by the then Assistant Treasurer, Nick Sherry.

The ED includes measures allowing foreign bank branches to rely on their audited Australian Prudential Regulation Authority (APRA) financial statements when applying the taxation of financial arrangements (TOFA) elective methods, provided the reports meet specified criteria.
 - On 21 December 2012, the government announced amendments to improve the operation of the Investment Manager Regime (IMR). The amendments will allow tracing through such funds to underlying investors for the purpose of applying the 'widely held' and 'concentration' tests.
 - On 10 December 2012, the *Tax Laws Amendment (Clean Building Managed Investment Trust) Act 2012* received Royal Assent. The act amends the *Income Tax (Managed Investment Trust Withholding Tax) Act 2008*, the *Income Tax Assessment Act 1997* ("ITAA 1997") and the *Taxation Administration Act 1953* to provide a final withholding tax rate of 10% on fund payments from eligible Clean Building Managed Investment Trusts (MITs) made to foreign residents in information exchange countries.
 - On 6 December 2012, Governor-General Quentin Bryce made the *Income Tax Assessment Amendment Regulation 2012 (No. 2)* under the ITAA 1997. The regulation amends the *Income Tax Assessment Regulations 1997* ("ITAR 1997")

to remove uncertainty concerning the tax treatment of specific hybrid capital instruments (both debt and equity characteristics) as a result of Australia's implementation of the Basel III capital reforms and insurance capital reforms.

The purpose of the regulation is to facilitate the debt tax treatment of certain capital instruments issued by entities that are regulated, either directly or as part of a group, for prudential purposes by APRA, and to comply with the new Tier 2 capital requirements, including the non-viability condition. This is achieved by overlooking the contingency that the non-viability condition imposes on the obligation to pay the principal or interest on the capital instrument for the purpose of determining whether the obligation is a non-contingent obligation.

The regulation commenced on 12 December 2012.

- On 15 November 2012, the assistant treasurer released an ED of proposed amendments to the general anti-avoidance provision in Part IVA of the *Income Tax Assessment Act 1936*. This follows the press release on 1 March 2012 in which the former assistant treasurer announced changes to the anti-avoidance rule based on perceived deficiencies highlighted by a number of decisions from the Full Federal Court of Australia.

The ED notes that a more holistic approach to Part IVA is required and seeks to create a number of new assumptions which are to be made in formulating an 'alternative postulate'.

Subject to the passage of legislation, the proposed amendments will apply to arrangements that have been entered into or started being carried out from 16 November 2012.

- On 25 October 2012, the government released the ED legislation *Tax Laws Amendment (2012 Measures No 6) Bill 2012* proposing to amend the limited recourse debt provisions in Division 243 of ITAA 1997. The draft legislation seeks to clarify the definition of 'limited recourse debt' to include an arrangement where it is reasonable to conclude that the debtor has not been fully at risk because the creditor's recourse is effectively limited to the financed asset or secured property.

If enacted, the amendments will apply to debt arrangements terminated at or after 7.30pm (Australian Eastern Standard Time) on 8 May 2012.

Taxation rulings and determinations

- On 23 January 2013, the ATO released Tax Determination (TD) 2013/1 'Income tax: will interest on a full recourse loan be denied deductibility as a consequence of Division 247 of the *Income Tax Assessment Act 1997* where that loan is used to prepay interest on another loan which is a capital protected borrowing?' ("TD 2013/1").

The purpose of Division 247 is to separately identify any payment for capital protection embedded within the interest payments with respect to some borrowings for the acquisition of certain classes of securities. Under Australian taxation law, interest payments are generally deductible; however, capital protection amounts are generally of a capital nature and are not generally immediately deductible in full. Division 247 therefore seeks to deny the deductibility of the amount which can be identified as the capital protection amount.

TD 2013/1 confirms that where a taxpayer enters into a limited recourse loan under a capital protected borrowing for the purposes of Division 247 and a full recourse loan is entered into solely to fund an amount of prepaid interest on the limited recourse loan, the interest on the full recourse loan will not be denied under Division 247.

- On 19 December 2012, the ATO issued draft TD 2012/D11 'Income tax: does subsection 820-39(3) of the *Income Tax Assessment Act 1997* only apply to special purpose entities that have been established for the purpose of carrying on securitisation activity?'

The Australian thin capitalisation rules provide a statutory debt/equity limit to stop taxpayers using excessive debt to fund operations. Interest deductions may be denied where the prescribed debt/equity ratios are exceeded (subject to certain exemptions and safe harbours).

The draft determination deals with the scope of the exemption from thin capitalisation in section 820-39(3) of ITAA 1997 and provides three conditions. These three conditions are broadly that the entity is established for the purpose of managing some or all of the economic risk associated with assets, liabilities or investments; the total value of debt instruments is at least 50% of total assets; and the entity is insolvency remote according to the criteria of an internationally recognised rated agency.

In particular, TD 2012/D11 focuses on the insolvency remote condition in section 820-39(3)(c). The ATO considers the insolvency remote criteria to be critical to the interpretation of the exemption provision from thin capitalisation and gives specific effect to the policy intention that only special purpose entities that have been established for the purpose of carrying out securitisation activity will satisfy the thin capitalisation exemption.

The determination is proposed to have retrospective and prospective effect.

- On 2 November 2012, the ATO issued Interpretative Decision (ATO ID) 2012/90 'Income Tax Deductions: Internal

estimates of notional funding cost'. The issue to be determined was "In determining the profits attributable to a foreign bank's Australian permanent establishment under the business profits article of a relevant tax treaty, can the bank deduct an amount it estimates would be the funding cost if assets employed in its Australian branch operations had been funded under certain terms and conditions?"

This issue was answered in the negative. This was on the basis that internal charges, such as the amounts charged to a company's particular business operations in its management accounts for transactions with other sections of the taxpayer's business operations are not a loss or outgoing under the general deduction provisions.

- On 2 November 2012, the ATO issued ATO ID 2012/91 'Income Tax Deductibility of net amounts on borrowings'. The issue to be determined was "Can a net amount be a loss or outgoing incurred by a taxpayer within the meaning of section 8-1 of ITAA 1997 where the net amount is the excess of interest expense incurred by the taxpayer on borrowings to fund a particular asset over the income derived by the taxpayer from the asset?"

The issue was answered in the negative on the basis that a net amount cannot be a loss or outgoing under section 8-1 of the ITAA 1997; rather the taxpayer is required to separately record the income derived expenses incurred.

- On 2 November 2012, the ATO issued ATO ID 2012/92 'Income Tax Deduction: Interest expense to fund general reserve liquid assets'. The relevant issue was whether "In determining the profits attributable to a foreign bank's Australian permanent establishment under the business profits article of a tax treaty, is interest expense incurred by the foreign bank on its borrowings that fund the bank's general reserve liquid assets, managed and controlled for use outside Australia, deductible by the bank under section 8-1 of ITTA 1997?"

The issue was answered in the negative. This is on the basis that the interest expenses incurred by the foreign bank on its borrowings that fund the liquid reserve assets do not satisfy the requirements of section 8-1 of ITAA 1997. The purpose of the borrowing and use of borrowed funds for which the foreign bank incurred the interest expense was to fund the liquid reserve assets which are not managed or controlled for use in the course of the business operations carried out by the foreign bank through its Australian permanent establishment.

Other developments

- On 12 December 2012, the Treasury released a proposals paper on 'Implementation of Australia's G-20 over-the-counter derivatives commitments'. These commitments arose from a G-20 summit in Pittsburgh in 2009 following the global financial crisis, and include the reporting of over-the-counter (OTC) derivatives to trade repositories, standardised clearing through central counterparties and the execution of standardised OTC derivatives on electronic trading platforms.
- On 24 October 2012, the Treasury released a policy options paper 'Taxing trust income – options for reform'. This paper follows an initial consultation paper released on 21 November 2011, which outlined three possible models for taxing trust income.

The two models articulated in this policy options paper are the:

- Economic benefits model (EBM) – formerly the 'trustee assessment and deduction' model
- Proportionate assessment model (PAM) – formerly the 'proportionate within class' model

The paper also canvasses two issues that will affect the scope of new arrangements for taxing trust income – the treatment of tax preferred amounts and the possible exclusion of bare trusts from the new arrangements.

Updates on indirect taxes

Commissioner of Taxation v Qantas Airways Ltd [2012] HCA 41 ("Qantas case")

On 2 October 2012, the HCA handed down its decision in the Qantas case, allowing the commissioner's appeal from the previous decision of the Full Federal Court of Australia.

In this case, the court held that Qantas made a taxable supply for non-refundable fares where the passengers did not travel on flights that were booked, as there was a supply of at least a promise to carry the passenger. Further, the court rejected the reasoning of the Federal Court that what is necessary for characterising a supply is identifying the "essence" or "sole purpose" of a transaction.

This decision is relevant to all taxpayers as it considers the fundamental concepts of characterising a supply for GST purposes.

This is an important decision as it provides guidance from the HCA on characterising supplies. The HCA focused on the supply made at the time when consideration was provided, which leads to the outcome, that is, a supply of services/goods may ultimately comprise two separate supplies – the supply of the promise to provide services/goods and then the ultimate supply, for which one lot of consideration is paid.

Following the Qantas decision, a liability for GST may arise at the time the promise is made to provide the relevant goods/

services, even if the underlying supply never eventuates (assuming consideration is received and not refunded).

The ATO has released a DIS on the Qantas case as follows:

- Where a supply of a right to a customer is provided (for example a promise to provide a supply/good in the future) that is GST-free, input-taxed and taxable, the further supply will be given consistent GST treatment.
- GST will only be payable once where the consideration relates to the supply of an entry into an obligation and a further supply.
- There is nothing in the HCA decision that is inconsistent in a material way with existing ATO views.

We note that the commissioner will review and update a number of GST rulings following this decision.

Tax Laws Amendment (2012 Measures No. 4) Act 2012

The amendments are intended to reduce compliance costs for representatives of incapacitated entities such that a mortgagee in possession of an incapacitated entity's property does not have to register separately for GST (as a representative of the incapacitated entity) if it will supply that property to satisfy a debt it is owed by that entity.

ATO Practice Statement Law Administration PS LA 2012/6

On 1 November 2012, the ATO released PS LA 2012/6 which provides guidance to ATO officers on when the ATO may exercise its discretion to retain amounts under the *Taxation Administration Act 1953* for verification purposes.

It will be important to manage large refunds with the ATO so that information to verify the refunds is provided quickly to prevent refunds being withheld for substantial periods of time to verify information.

ATO pilot on indirect taxes

The ATO has announced that it will be conducting an alternative dispute resolution (ADR) pilot using in-house facilitation to resolve indirect tax objections, including substantiation and penalties. The ADR pilot will be an informal process to help taxpayers resolve issues with the assistance of an independent in-house facilitator bound by a code of conduct.

The pilot will run in two stages between November 2012 and April 2013. Stage 1, which commenced in November 2012, is by ATO invitation only and is limited to approximately 10 indirect tax objection cases involving GST, excise, fuel tax credits, luxury car tax and wine equalisation tax (WET) issues. The ATO advises that taxpayers may be invited to participate in stage 1 if the objection has one or more of the following features:

- factual disputes (excluding issues on legal interpretation)
- valuation issues (margin schemes or sales to associates)
- apportionment issues
- penalty issues.

The ATO has advised that participation in the pilot is voluntary, and has provided information on the ADR facilitation process. Taxpayers' rights of review and appeal will not be affected by participating in the pilot.

Restrictions on GST refunds

Following our comments in the previous issue of *General tax update for financial institutions in Asia Pacific* relating to the ED on restrictions to GST refunds, the ATO released advice on the concept of "passing on" in the context of the proposed Division 36. The advice includes examples illustrating the ATO's approach and states the actual conduct of the seller in setting prices.

Our previous comments can be accessed through the following link:

<http://kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Newsletters/General-Tax-Update/Documents/General-tax-update-1212-45.pdf>

Draft determination for correcting GST errors

On 17 December 2012, the ATO released for consultation a draft determination 'Goods and Services Tax: Correcting GST Errors Determination under subsection 17-20(1) of the A New Tax System (Goods and Services Tax) Act 1999'.

The final determination will allow taxpayers to correct those GST errors made in an earlier tax period in a later tax period under specified circumstances.

This determination will give legislative effect to the ATO's current practice.

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Tax update

Relaxed restrictions on foreign investment in the securities industry

The China Securities Regulatory Commission (CSRC) announced a new circular, CSRC No. 86 ("Announcement 86") effective from 11 October 2012.

Announcement 86 introduces relaxed control on foreign investors' participation in Chinese securities companies. The maximum foreign equity shareholding allowed (direct and indirect) was increased from 33.3% to 49%.

New PRC individual income tax (IIT) withholding requirements on dividends put more onus on domestically listed companies and securities companies

The Ministry of Finance (MOF), the State Administration of Taxation (SAT) and the CSRC jointly issued Cai Shui [2012] No. 85 ("Circular 85") on 16 November 2012 to differentiate the IIT rates for dividend income based on the holding period.

From 1 January 2013, individuals who receive dividends from domestically listed companies will be subject to a flat rate of 20%, and an IIT exemption will be available to those who hold the shares for:

1. More than one month, but less than one year: 50% of the dividend income will be exempted from IIT; or
2. More than one year: 75% of the dividend income will be exempted from IIT.

The differentiation of IIT rates based on the holding period poses significant technical challenges for the capabilities of the existing withholding systems of securities companies. Domestically listed companies and securities companies should carry out a detailed review of their IT systems to ensure that the securities companies' systems can support the domestically listed companies to fully comply with the withholding requirements set out in Circular 85.

For details on Circular 85, please refer to our *2012 China Alert Issue 24*:

<http://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Newsletters/ChinaAlerts/Documents/china-alert-1211-24-PRC-Individual-Income-Tax-on-dividends.pdf>

Update on the administration of foreign exchange for direct investment

On 19 November 2012, the State Administration of Foreign Exchange (SAFE) announced a new circular, Huifa [2012] No. 59 ("Circular 59") to simplify the administrative procedures for foreign exchange for direct investment and to improve the domestic investment environment.

We summarise the major changes below:

- Circular 59 shifts foreign exchange control for most businesses from an approval system to a registration system.
- Circular 59 removes the approval requirement on reinvestment by foreign investors with income obtained by legal means in China. It also removes the capital verification confirmation and registration requirements when a Chinese holding company (CHC) reinvests in China.
- Circular 59 allows a foreign invested enterprise (FIE) to provide loans to its overseas parent company. Meanwhile, capital sources for overseas lending have been expanded, and overseas lending sourced from a domestic foreign exchange loan by PRC banks is allowed.

With Circular 59, banks will undertake more responsibilities for documentation review, business data and information reporting.

For details of Circular 59, please refer to our *2012 China Alert Issue 25*:

<http://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Newsletters/ChinaAlerts/Documents/china-alert-1212-25-Foreign-Exchange-for-direct-investment.pdf>

Deed tax clarified for sale and leaseback business

The MOF and SAT jointly issued a circular, Cai Shui [2012] No. 82 ("Circular 82") to clarify the deed tax policies for finance lease companies.

According to Circular 82, finance lease companies which take over ownership of the house and/or the land of a lessee as part of a sale and leaseback business, should be liable for deed tax. The deed tax can be exempted when the lessees buy back ownership of their original houses and/or land after the expiration of the sale and leaseback contracts.

Update on corporate income tax (CIT) consolidated filing by cross-regional enterprises

The SAT recently announced a new administrative rule, SAT Announcement 2012 No. 57 ("Announcement 57") to update the CIT consolidated filing mechanism for cross-regional enterprises. Announcement 57 took effect on 1 January 2013.

According to Announcement 57, a cross-regional enterprise should allocate the CIT payable to its branches for them to file the same with their in-charge tax bureau for both CIT quarterly filings and the annual filing. Previously, the CIT annual filing was only conducted with the head office without any further allocation to branches. This rule created an additional administrative burden for financial institutions which could potentially prolong the annual filing process. In addition, this rule could also create uncertainties for financial institutions, as the tax bureau at the branch level may have adopted a different tax position or interpretation than the tax bureau at head office level.

Hong Kong

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Tax update

Stamp Duty (Amendment) Bill 2012 introduced to give effect to Buyers Stamp Duty (BSD) for residential properties and to update the Special Stamp Duty (SSD)

The Government of Hong Kong Special Administrative Region (HKSAR) gazetted the *Stamp Duty (Amendment) Bill 2012* on 28 December 2012. The bill seeks to:

- introduce BSD for residential properties acquired by any person (including companies) except a Hong Kong permanent resident (HKPR)
- enhance the SSD by extending its coverage period and adjusting the SSD rates.

Subject to enactment of the bill, the enhanced SSD and BSD will be applicable to all residential properties acquired on or after 27 October 2012.

The adjusted SSD will have three levels of regressive rates for different holding periods:

Holding period	Regressive rate (% of the amount/value of the consideration of the residential property)
Less than 6 months	20%
6 to 12 months	15%
12 to 36 months	10%

The BSD will be charged at a flat rate of 15% for all residential properties acquired by any person or entity, except an HKPR, on top of the existing stamp duty and the SSD, if applicable.

The HKSAR Government has put in place a refund mechanism for redevelopment projects in the bill. The bill was introduced into the Legislative Council in January 2013.

For further details, please refer to Issue 1 of *Hong Kong Tax Alert* at the link below:

<http://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Newsletters/Tax-alert/Documents/tax-alert-1301-01-stamp-duty-bill-2012.pdf>

New double taxation agreement with Canada

Hong Kong signed a double taxation agreement (DTA) with Canada on 11 November 2012. This is the 26th comprehensive DTA concluded by Hong Kong.

The new DTA provides the following maximum rates of withholding taxes:

	Non-treaty rate	Treaty rate
Dividends	25%	5% / 15% (1)
Interest	25%	0% / 10% (2)
Royalties	25%	5%

(1) Withholding tax on dividends is reduced to 5% if the beneficial owner is a company (other than a partnership) that directly or indirectly controls at least 10% of the voting power in the company paying the dividends.

(2) Withholding tax on interest is reduced to nil where the recipient is the HKSAR Government; the Hong Kong Monetary Authority; any wholly-owned agency or instrumentality of the HKSAR, a political subdivision or local authority or a statutory body, or financial

establishment appointed by the HKSAR Government and mutually agreed upon by the competent authorities of the two contracting parties; or a resident of Hong Kong who is the beneficial owner of the interest dealing at arm's length with the Canadian payer of the interest.

The DTA will be effective once ratification procedures have been completed by both jurisdictions.

For further details, please refer to Issue 19 of *Tax Alert* at the link below:

<http://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Newsletters/Tax-alert/Documents/tax-alert-1211-19.pdf>

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Tax update

Provisions of unexplained investment in the Income-tax Act, 1961 do not apply once it is established that the transactions are sale transactions and not purchase transactions

In the case of *Threadneedle Investment Funds ICVC Asia Fund* ("the Taxpayer") reported in [2012] 27 taxmann.com 321 (Mumbai – Trib.), the Mumbai Bench of Income Tax Appellate Tribunal ("the Tribunal") held that provisions of section 69 of the *Income-tax Act, 1961* ("the Act") do not apply once it is established that the transactions are sale transactions and not purchase transactions. The Tribunal observed that the provisions can only be invoked for unexplained investments.

The Taxpayer is a non-resident corporate entity registered with the Securities and Exchange Board of India (SEBI) as a sub-account of a foreign institutional investor (FII) for investment in the Indian capital market. During the assessment proceedings, the assessing officer (AO) asked the Taxpayer to reconcile the annual information report (AIR) data provided by the Bombay Stock Exchange (BSE) of various transactions reflected under the Taxpayer's name.

The Taxpayer contended that the transaction reported in the AIR did not pertain to the Taxpayer and the AIR did not provide specific information such as the contact number, script name, quantity, etc. Therefore, in the absence of complete details, the Taxpayer was unable to reconcile the transactions one by one.

The AO, however, without referring to the explanations of the Taxpayer, concluded that the Taxpayer made an investment in one script, and as this transaction was not reconciled or explained, the amount was treated as an unexplained investment under section 69 of the Act and taxed at the rate of 40%.

Based on these facts, the Tribunal observed that the onus of proof does not shift completely to the Taxpayer merely because the Taxpayer's Permanent Account Number (PAN) appears in the AIR. It is the AO's responsibility to examine complete details before requesting a reconciliation and questioning whether the transactions were undertaken.

The Tribunal further observed that based on the findings on record, it is unclear whether the transactions concerned were purchase or sale transactions. Without even examining the nature of the transactions, the AO drew a conclusion that the transaction was an investment from the Taxpayer which was unexplained. However, further information available on record indicated that these are not purchase transactions, but sale transactions executed on behalf of various other funds being managed by Threadneedle Asset Management Ltd. Once it has been established that these are sale transactions, provisions of section 69 for unexplained investment do not apply.

In view of the above, the Tribunal reverted the case to the AO for fresh examination. Conclusions would be drawn based on the facts available. Due and proper opportunity should also be given to the Taxpayer to provide explanations.

The Tribunal has once again upheld that income derived by an FII from derivative transactions can only be considered as capital gains and not as business income

In the case of *Platinum Investment Management Limited*¹ ("the taxpayer"), the Tribunal recently upheld that a gain/loss from derivative transactions is to be treated as a capital gain/loss and not as a business profit/loss by following the decision of its coordinate bench in the case of *LG Asian Plus Limited*².

Facts of the case

The taxpayer is a sub-account of an FII registered under the Securities and Exchange Board of India (FII) Regulations, 1995 (SEBI (FII) Regulations, 1995). The taxpayer was engaged in the purchase and sale of securities in India and in trading derivatives.

¹ ITA No.3598/Mum/2010

² LG Asian Plus Ltd. Vs ADIT(International Transaction)-3(2), reported in (2011) 46 SOT 159

The taxpayer filed its return of income for the assessment year by treating income arising from the sale of shares and derivative transactions as 'capital gains'.

View of the AO

The AO treated the gain on the sale of shares and from derivative transactions as capital gains, whilst the loss on derivatives transactions was treated as a business loss.

Further, by applying the provisions of the tax treaty between India and Australia, the AO held that since the taxpayer had no permanent establishment (PE) in India, the business loss was not taken into consideration to determine the taxpayer's total income.

View of the Commissioner of Income-tax (Appeals)

The Commissioner of Income-tax (Appeals) (CIT(A)) held that both profit and loss arising from derivative transactions should be treated as a business profit and loss, and the loss from derivative transactions should be set off against business income from derivative transactions.

The CIT(A) concurred with the AO's view with respect to the application of the provisions of the tax treaty to ignore the loss arising from derivative transactions.

Taxpayer's contentions

The taxpayer, being an FII, is only permitted to invest in 'securities' as per the SEBI (FII) Regulations, 1995, and therefore the loss arising from derivative transactions cannot be treated as a business loss.

The issue of treating the derivative transaction as business is covered by the decision of the coordinate bench of the Tribunal in the case of *LG Asian Plus Ltd.*

As the taxpayer did not claim any tax treaty benefits, the revenue authorities cannot thrust the provisions of the treaty on the taxpayer, putting it into a disadvantageous position compared to the provisions of the Act, which violates the provisions of Section 90(2) of the Act.

Even if the loss arising from derivative transactions is treated as a business loss, the same can be set off against the business income from derivative transactions and against the short-term capital gain arising from the sale of shares under the provisions of Section 71 of the Act.

The ruling of the Authority for Advance Rulings (AAR) in the *Royal Bank of Canada* case does not apply to the taxpayer being an FII, as the said ruling was pronounced in the case of a bank.

Tribunal's ruling

The Tribunal relied on the decision of its coordinate bench in the case of *LG Asian Plus Ltd* on a similar issue.

Income derived by an FII from the transfer of 'securities' as specified in Explanation (b) to section 115AD of the Act can only be considered as capital gains and not as business income. As the 'derivatives' have been included in the definition of 'securities' for the purposes of this section, the income from derivatives shall also be considered as capital gains.

It is clear that FIIs have been considered as 'investors' (and not traders). Secondly, income from the transfer of securities has been viewed as chargeable to tax under the head 'capital gains'.

Section 43(5) of the Act defining speculative transactions is only relevant in the context of income under the head 'profits and gains of business or profession'. It rules out its application to income under any other head. If that is the position, the picture is clear that section 43(5) has no application to FIIs in respect of securities defined in the explanation to section 115AD, and the income from its transfer is considered as capital gains.

Accordingly, it was held that the income arising from the derivative transactions by the taxpayer, as an FII, cannot be treated as a business profit or loss but has to be a capital gain or loss.

The Tribunal did not go into the taxpayer's alternative plea regarding the provisions of the tax treaty and putting the taxpayer in a disadvantageous position as the issue of the nature of the transaction and the treatment of the same as capital gain or loss has already been decided in favour of the taxpayer.

No capital gains on the transfer of Indian shares if foreign companies are merged without consideration

In the case of *Credit Suisse (International) Holding AG*³ ("the Applicant"), a company incorporated in Switzerland was a wholly owned subsidiary of another company incorporated in Switzerland ("Company C"). Pursuant to the proposed merger of the Applicant with Company C, all the Applicant's assets and liabilities would be assumed by Company C, including its holding in a subsidiary in India ("Indian company"). On merging, no consideration would pass to the Applicant.

The question for consideration before the AAR, inter alia, was whether any capital gains under Section 45 of the Act would be derived by the Applicant on their merging and whether such capital gains would be exempt under Section 47(via) of the Act.

³ AAR No.956 of 2010

Based on the facts and arguments of the case, the AAR observed and held as follows:

- The change of ownership of the shares of the Indian company from the Applicant to Company C would involve the transfer of shares and be within the definition of 'transfer' under Section 2(47) of the Act.
- The transaction does not fulfil the condition specified under section 47(via) of the Act, i.e. at least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company. This is because the shareholders of the Applicant merging with Company C will not or cannot become shareholders of Company C, as Company C is the Applicant's only shareholder..

As the gain in the case, if any, is not determinable within the scope of Sections 45 and 48 of the Act, no capital gains arise to the Applicant as a result of the merger.

Legal fee received by Swiss law firm for adjudication proceedings outside India is taxable in India

In the case of *Schellenberg Wittmer along with its partners*⁴ ("the applicant"), the applicant was a Swiss-based partnership firm ("the Firm") and its partners were tax residents of Switzerland. The Firm practised law in Switzerland and did not carry out its activities in any other country. The applicant was appointed by an Indian company for representation in an adjudication proceeding in Switzerland.

The question posed for consideration before the AAR was whether the applicant could be treated as a resident of Switzerland under the India-Switzerland tax treaty and whether the legal fee received by the applicant from the Indian company would be taxable in India.

Based on the facts and arguments of the case, the AAR observed and held as follows:

- The definition of the term 'person' provided in the tax treaty includes, inter alia, a company, body of persons, or any other entity which is taxable under the laws in force in either contracting state. The firm is not a 'person' under the tax treaty for the following reasons:
 - There is no definition of the term 'person' in Swiss law corresponding to section 2(31) of the Act which confers the status of a 'person' on a partnership firm.
 - The applicant is not a taxable entity in Switzerland.
- Although the Firm's partners are residents of Switzerland, they cannot invoke the tax treaty to determine the taxability of the legal fees received by the Firm since they have not received the legal fees from the Indian company.
- The source of income for rendering professional services to the Indian company is in India. The fact that the major part of the services was rendered outside India, a dispute arising in India cannot alter the source of income.

Accordingly, the applicant would not be treated as a resident of Switzerland under the tax treaty and will not be entitled to treaty benefits. Therefore, the legal fees received by the applicant should be taxable in India.

⁴ AAR No. 1029 of 2010 dated 27 August 2012

Korea

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Tax update

Interest expense appropriated as dividend under the thin capitalisation rule not eligible for tax relief

Under the thin capitalisation rule of Korea, if the total loans from a foreign parent company and loans from a third party guaranteed by the foreign parent company exceed three times the capital injected by the foreign parent company (six times for the financial service industry), the interest expense related to the 'exceeding portion' of the loan is treated as a dividend payment. Such dividend may not be eligible for a tax exemption/reduction available to foreign investors, according to Article 121-2 of the *Special Tax Treatment Control Law* (STTCL) (Jaekukjo-505, 2012.10.22).

According to the STTCL, dividends eligible for tax relief should be derived by investment foreign investors from entities engaging in businesses specified under Article 121-2 of the STTCL. The specified business includes the following:

- Business in industrial support service that is vital to the strengthening of the international competitiveness of domestic industries
- High-technology business
- Business that is conducted by foreign investment enterprises in the foreign investment zone under the *Foreign Investment Promotion Act*
- Business to which a tax reduction or exemption is allowed in order to attract foreign investment and which is prescribed by Presidential Decree

Provision for bad debts allowed for tax purposes

Regardless of provisions for bad debts recorded for accounting purposes, a financial service institution may calculate provisions of allowance for bad debts based on the methods described under Article 62 of the *Enforcement Decree of Corporation Tax Act* and select the most beneficial provision calculation for tax purposes. Accordingly, even if a financial service institution does not record any provision for bad debts in accordance with the Regulation on Supervision of Banking Business, the financial service institution may still calculate and deduct a provision for bad debts within the limit allowed for tax purposes (Deabupwon 2012.8.17 sungo 2009 du 14965 pangyul).

Malaysia

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Tax update

2013 Budget highlights

The Malaysian Prime Minister and Minister of Finance YAB Dato' Sri Mohd. Najib Tun Abdul Razak presented the 2013 Budget on 28 September 2012. Some of the key changes and proposals are as follows:

Non-business income

It is proposed that interest income will no longer be considered as business income unless:

- i. the interest income is derived from a source that forms part of the trading stock of a business of that person; or
- ii. the interest is received from a money lending business and that business is licensed under any written law.

Except for the above proposal, where a person has treated his/her interest income as a business income, any unabsorbed business losses and unutilised capital allowances from that source up to year of assessment (YA) 2012 can be utilised against the aggregate statutory income of that person from other business sources in YA 2013.

In cases where that person has no other business income for YA 2013, the unabsorbed business losses and unutilised capital allowances will be deducted against any other sources of that person's income until the amounts are fully utilised.

The proposal is effective from YA 2013.

Business trust

It is proposed that a business trust, which is a unit trust scheme established under the *Capital Markets and Services Act 2007*, be treated in the same manner as a company in terms of income tax, stamp duty and real property gains tax purposes. This proposal is effective from YA 2013.

At the initial stage of the establishment, it is also proposed that:

- i. the business trust be given a one-off stamp duty exemption on the instrument of transfer of businesses, assets or real properties
- ii. the person disposing of real properties or shares in a real property company to a business trust be given real property gains tax exemption on any disposal gains derived.

Proposal (i) is effective for instruments executed from 1 January 2013, while proposal (ii) is effective for disposals made from 1 January 2013.

Takaful operators – losses

It is proposed that the adjusted loss arising from the business of a family fund of a Takaful operator for a YA is not deductible against its aggregate statutory income from sources other than the family fund for the relevant YA. Similarly, any unabsorbed business losses from sources other than the family fund for the relevant YA are not allowed to be deducted against the statutory income of the family fund of that Takaful operator.

The proposal is effective from YA 2012.

Special deduction for expenditure on treasury shares

The following has been proposed in relation to expenses incurred in acquiring treasury shares:

- i. Where a company offers treasury shares to its employees, a deduction on the net expenditure (the cost of acquiring the treasury shares less the amount payable by the employee) shall be given to the company in the basis period in which the employee exercises his/her rights to acquire the shares.
- ii. Where a holding company transfers treasury shares to an employee of its subsidiary company having the right to

acquire such shares, a deduction shall be given to the subsidiary company instead of the holding company on the later of either the date of transfer of the treasury shares or the date of payment to the holding company for the treasury shares. The deduction for the subsidiary company would be the lower of either the amount paid to the holding company or the net amount (the cost of acquiring the treasury shares less the amount payable by the employee) incurred by the holding company in acquiring the treasury shares.

- iii. The cost of acquiring these treasury shares which are transferred shall be determined on a first-in, first-out basis.

The proposals are effective from YA 2013.

Withdrawal of contribution to a private retirement scheme

It is proposed that the withdrawal of contributions made to an approved private retirement scheme (PRS) by an individual before reaching the age of 55 (other than on their death or permanent departure from Malaysia) will be subject to a final withholding tax of 8%.

It is the PRS's responsibility to remit the withheld tax to the Inland Revenue Board of Malaysia (IRBM) within one month of making payment to the individual. Failure to do so will result in the imposition of a 10% penalty on the tax which should have been withheld.

The proposal is effective from 1 January 2013.

Tax incentives for the issuance of retail sukuk (Islamic bonds) and retail bonds

To reduce the cost of issuing retail sukuk and retail bonds, and to encourage individual investors to participate in the capital market, it is proposed that the following are given:

- i. double deduction on additional expenses for the issuance of retail sukuk and retail bonds
- ii. stamp duty exemption on instruments relating to the subscription for retail sukuk and retail bonds executed by individual investors.

Proposal (i) is effective from YA 2012 to YA 2015.

Proposal (ii) is effective for instruments executed from 1 October 2012 to 31 December 2015.

Review of real property gains tax (RPGT)

To curb speculative activities in the real property market, it is proposed that the RPGT rates on gains arising from the disposal of residential and commercial properties be reviewed as follows:

- i. Increase from 10% to 15% where the property has been held for up to two years
- ii. Increase from 5% to 10% where the property has been held for more than two years and up to five years
- iii. 0% tax where the property has been held for more than five years.

The proposal is effective for disposals from 1 January 2013 onwards and when the *Real Property Gains Tax (Exemption) Order 2012* to effect the changes has been gazetted.

Reviving abandoned housing projects

To encourage the involvement of the private sector in reviving abandoned housing projects, it is proposed that tax exemption be given on interest income received by banking and financial institutions from the rescuing contractor.

Abandoned housing projects eligible for the above tax incentives must be certified by the Ministry of Housing and local government.

The above proposal is effective for loans approved between 1 January 2013 to 31 December 2015 and the tax exemption will be applicable for three consecutive YAs from the year the loans are approved.

Tax exemption on income of the annuity fund

To encourage individuals to invest in annuity schemes to provide savings for retirement, it is proposed that the tax treatment on annuity scheme funds be streamlined with other retirement scheme funds, whereby tax exemption is given on income received by approved annuity funds.

The proposal is effective from YA 2012.

Reduction in tax rates

It is proposed that the tax rate for resident individuals be reduced by 1% for chargeable income bands from MYR 2,501 to MYR 50,000.

The proposal is effective from YA 2013.

Time bar for tax assessments

It is proposed that the time bar for raising tax assessments or additional assessments be reduced from six years to five years (except for cases related to investigation, fraud, wilful default and negligence). The existing requirement to maintain records for seven years remains unchanged.

The proposal is effective from 1 January 2014.

Stamp duty on loans

At present, instruments of transfer and loan agreements executed by Malaysians for purchasing their first residential property not exceeding MYR 350,000 are given a 50% stamp duty exemption. The exemption can only be claimed once.

To reduce the cost of owning the first residential property and taking into consideration the increased price of residential property, it is proposed that the existing 50% stamp duty exemption be extended to 31 December 2014. In addition, the ceiling price of the property is increased to MYR 400,000.

The proposal is effective for sale and purchase agreements executed between 1 January 2013 and 31 December 2014. The remission orders to effect the above proposal have been gazetted.

Recent income tax rules gazetted

Income Tax (Deduction for Contribution by Licensed Insurers to the Malaysian Motor Insurance Pool) Rules 2012

These rules allow a licensed insurer to claim a double tax deduction on contributions made to the Malaysian Motor Insurance Pool to ascertain the adjusted income of its general insurance business. The rules are effective from YA 2011 to YA 2015.

Public Rulings

The IRBM has recently issued, amongst others, the following Public Rulings:

Public Ruling No. 7/2012: Taxation of Unit Holders of Real Estate Investment Trusts/Property Trust Funds

This ruling explains the tax treatment of the distribution of income from real estate investment trusts/property trust funds in Malaysia to unit holders.

Public Ruling No. 8/2012: Real Estate Investment Trusts/Property Trust Funds – An Overview

This ruling explains the taxation of real estate investment trusts/property trust funds and Islamic real estate investment trusts in Malaysia.

The full text of the Public Rulings is available at:

<http://www.hasil.gov.my/index.php>

Double taxation agreements

Malaysia–India

The new DTA between Malaysia and India has been gazetted. The maximum withholding tax rates under the DTA are as follows:

Types of payment	Rate
Interest	10 %
Royalties	10 %
Technical fees	10 %

Labuan is, however, excluded from the new DTA unless the Labuan entity has made an irrevocable election to be charged under the *Income Tax Act, 1967*. The DTA has not yet come into force.

Malaysia–Hong Kong Special Administrative Region

The DTA between Malaysia and the HKSAR has been gazetted. The maximum withholding tax rates under the DTA are as follows:

Types of payment	Rate
Interest	10 %
Royalties	8 %
Technical fees	5 %

The DTA has not yet come into force.

New Zealand

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Tax update

Employee taxation issues

The New Zealand Government and New Zealand Inland Revenue (“NIRD”) is increasingly focusing on benefits received by employees, in particular non-taxable benefits:

- **Draft legislation taxing car parking spaces (and other employee) benefits** – Draft legislation has been introduced to tax employer-provided car parking spaces in a range of circumstances, under New Zealand’s fringe benefit tax (FBT) regime. This will mainly involve car parks located in the Auckland and Wellington central business districts. Vouchers for goods and services provided to employees of charitable organisations will also be subject to FBT. The value of employer-provided car parking spaces, cars and vouchers will be considered ‘income’ for calculating individuals’ social welfare if explicitly provided as part of an employee’s remuneration package. The changes will apply from 1 April 2014.
- **Taxing employee accommodation and meal benefits** – The NIRD has released a consultation paper proposing taxing employee allowances/reimbursements (e.g. for accommodation, meal and communication costs) in a range of circumstances. The concern is that such employee benefit payments (which are currently generally non-taxable) may be a way for employers to provide employees with benefits in kind, without the requisite tax expense. Among the proposals are limiting the payment of non-taxable accommodation to a maximum period of 12 months and work-related meal payments to three months, as well as taxing all internet/phone costs if there is any private use.
- **IRD statement on employee benefits** – Related to the above, the NIRD has also released a statement on its view of the current law. The statement reverses the department’s long-held position that some accommodation benefits are non-taxable. This has wide-ranging implications for taxpayers, including potential retrospective tax liabilities.
- **IRD draft statement on tax residence** – The NIRD has released for consultation its updated view of tax residence (the current guidance was published in 1988). The NIRD has changed its approach to individuals’ tax residence, placing more emphasis on the availability of a dwelling when considering whether tax residence is retained. One of the main changes is the reversal of the previous position that a person seconded overseas with their family for three years would cease to be a resident, even if they keep their home in New Zealand and rent it out and retain other ties.

Draft legislation taxing lease incentives introduced

The New Zealand Government has introduced draft legislation to tax lease incentive payments made by landlords to tenants, outlined in Issue 45:

<http://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Newsletters/General-Tax-Update/Documents/General-tax-update-1212-45.pdf>

However, in response to public concerns about key features of the original proposals, the government has decided to shift the application date to 1 April 2013 (previously 26 July 2012), confirm a deduction for the payer of a lease incentive (a deduction is not currently guaranteed), and extend deductibility to payments made to surrender a lease (currently, the receipt is taxable, with no offsetting deductions).

New Zealand–Japan double taxation agreement updated

The new DTA reduces withholding tax rates for the following sources of payments:

- Dividends (in some cases to nil)
- Interest (a maximum rate of 10% applies and 0% applies for interest paid on financial institutions' unrelated party lending that is not part of an arrangement involving back-to-back loans)
- Royalties (a maximum rate of 5% applies).

The new DTA also updates the permanent establishment provisions (the updated provisions more closely resemble those in other recent NZ tax treaties) and contains the comprehensive exchange of information provisions.

The new DTA will come into force from 1 January (for the reduced withholding rates) after both countries have put through the necessary legislative amendments to give effect to the new treaty.

Philippines [▲Top](#)



Tax update

Tax treatment of interest income from financial instruments and other related transactions

The Bureau of Internal Revenue (BIR) issued Revenue Regulations (RR) No. 14-2012 dated 7 November 2012, Revenue Memorandum Circular No. 77-2012 dated 22 November 2012 and Revenue Memorandum Circular No. 81-2012 dated 10 December 2012 to govern the proper tax treatment of interest income earnings on financial instruments and other related transactions.

The following are the salient features of the above issuances:

Tax treatment of interest income derived from government debt instruments and securities

Government debt instruments and securities, including Bureau of the Treasury (BTr) issued instruments and securities such as Treasury Bonds (T-bonds), Treasury Bills (T-bills) and Treasury Notes, shall be considered as deposit substitutes, irrespective of the number of lenders at the time of origination. Interest income derived from these is subject to 20% final withholding tax (FWT).

- In the case of zero coupon instruments and securities, the FWT is payable upon their original issuance.
- In the case of interest bearing instruments and securities, the FWT is payable upon payment of the interest.

The original issuance is subject to documentary stamp tax (DST).

Tax treatment of interest income derived from long-term deposits or investment certificates

1. Interest income from long-term deposits or an investment in the form of savings; common or individual trust funds; deposit substitutes; investment management accounts; and other investments evidenced by certificates in such form prescribed by the Bangko Sentral ng Pilipinas (BSP) shall be exempt from income tax, provided that the following characteristics/conditions are satisfied:
 - a) The depositor or investor is an individual citizen, a resident alien or a non-resident alien engaged in trade or business in the Philippines.
 - b) The long-term deposits or investment certificates should be under the name of the individual and not under the name of the corporation or the bank, or the trust department/unit of the bank.
 - c) The long-term deposits or investments must be in the form of savings, common or individual trust funds, deposit substitutes, investment management accounts and other investments evidenced by certificates in such form prescribed by the BSP.
 - d) The long-term deposits or investments must be issued by banks only and not by other financial institutions.
 - e) The long-term deposits or investments must have a maturity period of not less than five years.
 - f) The long-term deposits or investments must be in denominations of PHP 10,000 and other denominations as prescribed by the BSP.
 - g) The long-term deposits or investments should not be terminated by the investor before the fifth year; otherwise they shall be subject to the graduated rates of 5%, 12% or 20% on interest income earnings.

- h) Any other income such as gains from trading, foreign exchange gain shall not be covered by income tax exemption (existing exemptions continue to apply).

For interest income individuals derive from investing in common or individual trust funds or investment management accounts to be exempt from income tax, the following additional characteristics/conditions must be satisfied:

- a) The investment must be held/managed by the bank (duly licensed as such by the BSP) for at least five years.
- b) The underlying investments of the common or individual trust fund or investment must comply with the requirements of Sec. 22(FF) of the *1997 Tax Code*, as amended, as well as the requirements a) to h) above.
- c) The account must hold on to such underlying investment for at least five years.

In the absence of any of the characteristics/conditions stated above, FWT at the rate of 20% shall be imposed.

2. Interest income from long-term deposits or an investment that is terminated by the depositor or investor before the fifth year shall be subject to the following graduated rates of FWT on the entire income and shall be deducted and withheld by the depository bank from the proceeds of the long-term deposit or investment certificate based on the remaining maturity thereof, as follows:

4 years to less than 5 years.....	5%
3 years to less than 4 years.....	12%
Less than 3 years.....	20%

3. Interest income from long-term deposits or an investment shall be subject to FWT of 25% if received by a non-resident alien not engaged in trade or business in the Philippines.
4. Interest income from long-term deposits or an investment shall be subject to FWT of 30% if received by a non-resident foreign corporation.

The above provisions cover interest income from current outstanding investments, securities or accounts from 23 November 2012.

Tax treatment of interest income derived from currency bank deposits and yield, or any other monetary benefit from deposit substitutes, trust funds and similar arrangements

FWT of 20% will apply if the interest income is received by:

- a) Citizens
- b) Resident aliens
- c) Non-resident aliens engaged in trade or business in the Philippines
- d) Domestic corporations
- e) Resident foreign corporations.

FWT of 25% will apply if the interest income is received by non-resident aliens not engaged in trade or business in the Philippines; and FWT of 30% will apply if received by a non-resident foreign corporation, unless the interest income is from foreign loans contracted on or after 1 August 1986, in which case it is subject to FWT of 20%.

Tax treatment of interest income derived from a depository bank under the Expanded Foreign Currency Deposit System (EFCDS)

FWT of 7.5% will apply if the interest income is received by:

- a) Citizens
- b) Resident aliens
- c) Non-resident aliens engaged in trade or business in the Philippines
- d) Domestic corporations
- e) Resident foreign corporations.

Any interest income of non-residents, whether individuals or corporations, shall be exempt from income tax.

For joint bank accounts in the name of a non-resident citizen and a resident citizen (e.g. an overseas contract worker or Filipino seaman and his/her spouse or dependent who is a resident of the Philippines), 50% of the interest income shall be exempt while the other 50% shall be subject to FWT of 7.5%.

Interest income a depository bank derives under the EFCDS from foreign currency transactions with non-residents, offshore banking units in the Philippines, local commercial banks including branches of foreign banks that may be authorised by the BSP to transact business with foreign currency deposit system units, and other depository banks under the EFCDS, shall be exempt from all taxes, except net income from such transactions as may be prescribed by the Secretary of Finance upon recommendation by BSP's Monetary Board to be subject to the regular income tax payable by banks.

Interest income from foreign currency loans granted by such depository banks under the EFCDS to residents other than offshore banking units in the Philippines or other depository banks under the expanded system shall be subject to a final tax rate of 10%.

Tax treatment of interest income derived from offshore banking units (OBU)

Interest income derived from OBUs authorised by the BSP, from foreign currency transactions with non-residents, other OBUs, and local commercial banks including branches of foreign banks that may be authorised by the BSP to transact business with OBUs, shall be exempt from all taxes except interest income from such transactions that may be specified by the Secretary of Finance upon recommendation of BSP's Monetary Board, which shall be subject to the regular income tax payable by banks.

Interest income derived from foreign currency loans granted to residents other than OBUs or local commercial banks, including local branches of foreign banks that may be authorised by the BSP to transact business with OBUs, shall be subject to FWT of 10%.

Any interest income of non-residents, whether individuals or corporations, from transactions with these OBUs shall be exempt from income tax.

Tax treatment of interest income derived from all other instruments

Interest income derived from any other debt instruments not within the coverage of deposit substitutes shall be subject to a creditable withholding tax (CWT) of 20%.

For this purpose, the income payer is required to withhold and remit this tax to the BIR.

The 20% CWT shall apply to each interest payment made beginning on 23 November 2012, irrespective of when the instruments or securities were issued.

The 19-lender rule

For an instrument to qualify as a 'deposit substitute', the borrowing must be made from 20 or more individuals or corporate lenders at any one time. The mere floatation of a debt instrument is not considered to be a 'public' borrowing and is not deemed a 'deposit substitute' if there are only 19 or fewer individuals or corporate lenders at any one time.

However, any person holding any legal or beneficial interest in a debt instrument or holding thereof, either by assignment or participation and with or without recourse, shall be considered a lender and thus be counted for the purpose of the 19-lender rule.

Documentary stamp tax

The original issuance of debt instruments shall be subject to DST at the rate of PHP 1 on each PHP 200, or a fractional part thereof, of the issue price. The assignment or re-assignment of the debt instruments which entails changing the maturity date or remaining period of coverage from that of the original instrument, or carries with it a renewal issuance of new instruments in the name of the transferee to replace the old ones, shall be subject to DST at the same rate imposed on the original instrument.

Singapore ▲Top



Tax update

Consultation on the designation of certain serious tax crimes as money laundering predicate offences

The Monetary Authority of Singapore (MAS) has issued a consultation paper to invite feedback on the designation of certain serious tax crimes as money laundering (ML) predicate offences.

Based on the consultation paper, tax offences under Sections 96 and 96A of the *Income Tax Act* and Sections 62 and 63 of the *Goods and Services Tax Act* are proposed to be designated as ML predicate offences. Such offences include tax evasion or assisting another person to evade tax through:

- omitting any income that should be included in a tax return
- making any false statements or entries in a tax return
- giving any false answers, whether verbally or in writing, to any question or requests for information asked or made in accordance with the provisions of the relevant tax legislations.

To comply with this new requirement, financial institutions would generally need to put in place internal policies and procedures to understand a client's tax risk profile and apply customer due diligence, transactions monitoring and control measures that are commensurate with the assessed risk. The intention is to detect and deter the laundering of proceeds from serious tax offences through the financial system.

Sri Lanka

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Tax update

Budget 2013

On 8 November 2012, the president of Sri Lanka presented the Budget for the fiscal year 2013. Below is a summary of the Budget proposals applicable to banks and financial institutions.

Income tax exemptions

The following are proposed to be exempt from income tax:

- Interest income earned by non-residents on investments in bonds
- Interest income on corporate debt securities which are listed on the stock exchange on or after 1 January 2013
- Interest income on municipal bonds issued with the approval of the General Treasury
- Investment income that DFCC Bank and NDB Bank derive from long-term projects funded by foreign borrowings.

Withholding tax on corporate debt securities

Withholding tax on corporate debt securities that carry a floating interest rate should be withheld at the point at which the interest is paid. In all other instances, withholding would be at the time of issuance.

Exchange control relation

Licensed commercial banks are permitted to borrow up to USD 50 million per annum for three ensuing years without prior permission from the Exchange Control Department.

Investment Fund Account

The list of qualifying sectors for lending through the Investment Fund Account is proposed to be expanded to include:

- Investment in sustainable energy sources
- Investment in women's entrepreneurship venture capital projects where the investment should not exceed LKR 10 million.

Funds lying in the Investment Fund Account that are not invested as per the guidelines set out by the Central Bank of Sri Lanka/Department of Inland Revenue by 30 June 2013 will be transferred to the Government Consolidated Fund.

Introduction of new levy

A special levy of 1% on the profits of banking institutions will be imposed and the levy is to be transferred to the National Insurance Trust Fund to establish an insurance scheme for farmers.

Other proposals

Banks have been asked to defer the recovery of related agricultural loans until after the Maha harvest and to waive the interest charged on such loans.

Unit trusts

The rate of income tax for unit trust management companies is to be reduced to 10% (currently at 28%). The supply of services to a unit trust by a unit trust management company is to be exempted from VAT.

Taiwan [▲Top](#)



Tax update

Proposed controlled foreign company rule

The Executive Yuan recently proposed the inclusion of a 'Controlled Foreign Corporation' rule into the Taiwan *Income Tax Act*. Under the proposed amendment, if a Taiwan company directly/indirectly owns more than 50% of a foreign company's capital or if a Taiwan company has significant influence over the foreign company, the Taiwan company is required to recognise the foreign company's earnings (based on its ownership percentage) as its investment income for Taiwan income tax purposes. When the foreign company distributes its dividend to the Taiwan company, the portion which has been recognised as the Taiwan company's investment income will not be counted as part of its taxable income.

In addition, if a foreign company's effective place of management is Taiwan, it will be deemed as being based in Taiwan for Taiwan income tax purposes and is subject to Taiwan income tax.

The detailed enforcement rules for the proposed Controlled Foreign Company Rule will subsequently be decided by the Ministry of Finance.

The proposed amendment has been submitted to the Legislative Yuan for review before it can be submitted to the president to be signed into law.

Taiwan–German double taxation treaty

The Taiwan-German DTA signed on 19 December 2011 has come into effect. The DTA is applicable to income taxable in Taiwan or Germany, derived on or after 1 January 2013.

Similar to other DTAs entered into by Taiwan, tax residents of Taiwan and Germany will only be subject to tax on income generated from their permanent establishments in either country. The DTA also offers reduced withholding tax rates on dividend, interest and royalty income from the standard withholding tax rate of 20%. The reduced rates are as follows:

- Dividend: 10%
- Interest: 10% or 15% (interest relating to real estate trust)
- Royalty: 10%

Unlike the adoption for income tax exemption treatment, no pre-approval from the tax authority will be required for the application of the reduced withholding rates, pursuant to the DTA.

Thailand

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Tax update

Cabinet approves lower individual income tax rate from 2013

On 17 December 2012, the Thai cabinet agreed to revise the individual income tax schedule. The new tax rates are divided into seven income bands as opposed to the current five income bands, and the highest tax rate will be reduced from 37% to 35%. The new individual income tax rates will take effect from 1 January 2013.

The proposed new individual income tax rates are as follows:

Net taxable income	Rate
THB 0–THB 150,000	Exempt
THB 150,001–THB 300,000	5%
THB 300,001–THB 500,000	10%
THB 500,001–THB 750,000	15%
THB 750,001–THB 1,000,000	20%
THB 1,000,001–THB 2,000,000	25%
THB 2,000,001–THB 4,000,000	30%
THB 4,000,000 and over	35%

The changes to the individual income tax for 2013 will take effect upon the issuance of the Royal Decree which we anticipate to be in 2013.

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