

PROPOSAL TO GOVERNMENT ON TAX ISSUES

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1. Tax treatment on unused balance from the Fund for provision for retrenchment allowance

Issue:

Pursuant to Circular 180/2012/TT-BTC on provision for retrenchment allowance (applicable for taxable year 2012), in case there is unused balance from the Fund for provision for retrenchment allowance (after being utilized for actual payment of retrenchment allowance in 2012), companies shall record this balance as "Other income" in 2012 and are not allowed to carry forward the balance to subsequent years.

Please note that the current standard CIT rate for "Other income" is 25% and therefore, the unused fund shall be subject to CIT of 25% accordingly. However, to some extent, the above treatment may have certain limitations and unreasonableness, in particularly for those enterprises are entitled to preferential CIT rate.

Specifically, the reversal of unused fund as "Other income" is not reasonable. Example below may depict the point:

- A company is entitled to preferential CIT scheme at the rate of 10%. For the period from 2007 to 2011, it has made provision for severance allowance of VND 2.5bil each year (assuming that this amount was within the cap of 1-3% of basic fund for social insurance contribution purpose), or VND12.5bil in total. For the period up to the end of 2012, the company has actually paid retrenchment/severance allowance with an amount of VND 2.5bil, leaving the unused Fund of VND10bil. The amount shall be treated as "Other income" and triggers CIT liability of $VND10bil * 25\% = VND2.5bil$.
- However, such provisions had been recorded as administrative expenses for the period from 2007 to 2011 and thus were subject to deductibility at the rate of 10% only.
- In summary, upon the recording of provision as administrative expenses, the provisions were subject to the deductibility at the rate of 10% but subsequently in 2012, it is recorded as "Other income" and subject to tax rate of 25%. As a result, the company will inherently suffer to a loss of $(25\% - 10\%) * VND10bil = VND1.5bil$.

In principle, a reversal of a provision (e.g. provision for stock devaluation, provision for bad debts as per Circular 228/2009/TT-BTC) shall be recorded by the way of decrease of the corresponding expenses previously booked by a company at the time of making such provisions (i.e. cost of goods sold for provision for stock devaluation and administrative expenses in case of provisions for bad debt). On this basis, reversal of provision for retrenchment/severance allowance (already booked as administrative expenses) into "Other income" appears as not reasonable under the tax principle and regulations, and this may cause significant loss to companies, especially for those during tax incentive period

and having significant balance of unused provision for retrenchment allowance by the end of 2012.

Proposal:

We therefore recommend the Government to consider and take into account of this reversal of a provision severance allowance as other, especially for those being in the period of tax incentives since this is really significant and has material impact to their tax position during their tax holidays. This treatment is so sensible in view that the unused fund should not be reverted as other income to apply CIT rate of 25% as the above mention but allowed to carry forward the balance to subsequent years.

2. Investment Protection

Issue:

All FDI companies shall be granted with the Investment Certificate/ Investment License by the licensing authorities (the local People's Committee, the local Industry Zones Authorities or the Ministry of Planning and Investment previously). Some of those companies have received a written confirmation on specific tax incentives which are mentioned in their Investment Certificate before they disburse their capital in the projects in Vietnam. The rate of tax incentives stated in their Investment Certificate is a very important factor for all the investors to parameter the financial benefits and make a decision on investment in Vietnam or other countries.

During the company's operation, however, the tax incentives under its Investment Certificate have been challenged and reduced by the local tax authorities although the conditions for those tax incentives are satisfied. Many foreign investors claimed that the investment protection commitment would not be secured because there appears different opinions from the competent State authorities on the same issue after granting the Investment Certificate to them. A decision from the tax office on tax incentive rate cannot replace a decision which was made previously by the licensing authority because, in nature, both a tax office and a licensing authority are the State management agencies of Vietnam and that's not a fault from the company and its owners.

Proposal:

We propose the Government to consider and provide a legislative principle that any tax incentive which is already stated under the company's Investment Certificate shall not be changed by any State authority if the conditions for that tax incentive is satisfied.

3. VAT issue for coffee companies

Issue:

- Currently, enterprises are allowed to delay payment of 5% VAT for a three, six, nine month period in order for them to solve some cash flow problems. However, they kept the VAT amount due to pay and disappeared without payment of this VAT amount to the tax office. Then, they used this amount to buy coffee at higher prices for the coffee, compared with that paid by other buyers that were paying VAT. This is such unfair competition in the current coffee market.
- To control the above mentioned issue, in June 2013, the MoF granted an official letter No. 7527 to instruct and request all provincial tax offices to control VAT refund, saying that refunds are held until the inspection is completed. In fact, the inspection is

conducted without a clear deadline for release of the VAT refund and in absence of a commitment to pay back the interest accumulated while keeping the refund.

- Tax offices in various provinces apply the rules differently, which make enterprises not feel safe to do business in Vietnam.

Proposal:

The MoF should promulgate specific and clear instructions and guidance towards the VAT refund targeted to coffee companies (i.e. setting out clear procedures and conditions for eligibility for VAT refund, deadline for refund, etc.). Also, to promulgate restrictions and penalty towards the VAT players, VAT dodge with an aim to evade taxes.

4. Unrealized FX issue:

Issue:

- According to prevailing regulation on corporate income tax (CIT), during tax year for CIT, if the enterprise has FX difference incurred related directly to revenue, expenses of the primary business and production activities shall be accounted to expense or revenue of the enterprise's primary business and production activities. However, towards FX rate differences due to revaluation of payables in foreign currency at the financial year-end, after making off-set, there is positive balance from the difference of FX rates, it shall be accounted to other income; in case there is a loss from the difference of FX rates, it shall be accounted to expenditure for primary business and production activities when determining CIT-able income.
- During our business and production period, a company can frequently incur payables. Upon actual payment, if there is any difference from the FX rates, the company accounts to realized FX gain/loss. At the end of accounting period, balance of these payable shall be revaluated in accordance with current regulations and accounted to unrealized FX gain/loss.
- So, for the same payable related directly to expense/revenue of the primary business and production activities of the enterprise, if it is realized, it shall be considered as related directly to the enterprise's primary business and production activities and entitled to tax incentive and otherwise it is not yet happening and is just revaluated for the compliance with accounting standards, it shall be considered as unrealized and accounted to other income which is subject to a standard tax rate (e.g 25%). For the nature of a company's business activities in Vietnam, this such difference is significant amount and affects enormously our tax declaration results.

Proposal:

We recommend that for the difference from FX rates due to revaluation of payables in foreign currency at the end of the financial year related directly to revenue, expense during the year, if for the CIT purpose or has to be accounted to the expense right at that financial year, it should be accounted to revenue/expense of the primary business and production activities and entitled to tax incentives (if any) in accordance with regulations.