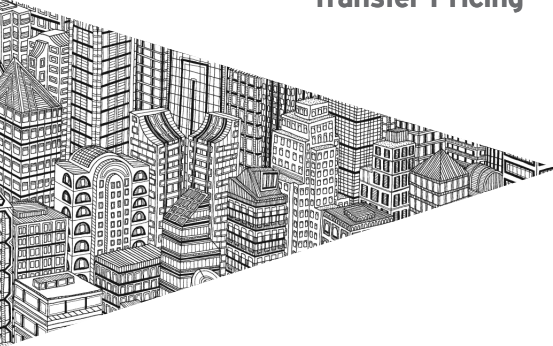


International Tax Alert

News and views from
Transfer Pricing



Vietnam proposes amendments to transfer pricing regulations, other tax changes

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Introduction

Pursuant to the recently approved Tax Reform Strategy for 2011 to 2020, Vietnam's Ministry of Finance (MOF) released a draft amending the Law on Tax Administration. The draft covers new and important matters such as Advance Pricing Agreements, "deemed tax" based on revenue, periodic tax audits and revocation of business licenses of companies with consecutive losses, tax authorities' power to initiate tax criminal investigation and expanding the tax authorities' sources of taxpayer information.

This Alert summarizes and provides comments on the impact of the above proposed key legislative measures with respect to transfer pricing and other related issues.

Key proposed legislation on transfer pricing and other related issues

Advance Pricing Arrangement (APA)

Currently, there is no provision for APAs in Vietnam's tax legislation. The Draft amending the Law on Tax Administration is expected to include provisions that will serve as a legal basis for the application of APAs in Vietnam. An APA is an agreement covering a period of no longer than five years, that determines the basis of tax calculations and pricing methods of related party transactions set by the tax authority prior to the submission of Corporate Income Tax (CIT) and customs declarations, where appropriate.

As APAs are new in Vietnam, the MOF is launching a pilot APA program by entering into APAs first with a few large companies operating in Vietnam in order for the MOF to gain experience and form a basis in choosing the appropriate approach, before promulgating the formal APA implementing regulations.

Deeming income tax based on revenue

If the taxpayer fails to comply with the tax regulations (including transfer pricing regulations), the Draft amending the Law on Tax Administration, allows the Vietnam tax authorities to impose a “deemed income tax” based on revenue using a value added ratio or profit margin method that will be specific for each industry and business activity for certain periods under rules that will be promulgated by the MOF.

Key proposed legislation on tax administration

Periodic tax audit and business license revocation of loss-making enterprises

The draft amending the Law on Tax Administration, stipulates that the company incurring losses equivalent to 50% or more of, but not exceeding the owner’s equity will be subject to periodic tax audits, revocation of business license, suspension of business activities and invalidation of tax codes by competent authorities.

Expansion of sources of taxpayers’ information to overseas counterparts

To facilitate tax and transfer pricing administration, the draft amending the Law on Tax Administration

authorizes the tax authority to collect and process information on taxpayers, including the collection and use of taxpayers’ information from tax authorities of countries having double taxation agreements with Vietnam.

Assignment of criminal investigation function to tax authority

The draft amending the Law on Tax Administration allows the tax authority to initiate criminal investigation of tax-related offenses. Under Vietnamese criminal law, if the evaded (underpaid) tax amount is VND100 million (approximately USD \$4,900) or more, the taxpayer may be subject to tax penalties under criminal proceedings.

Comments

The proposed changes and recent enforcement activities by Vietnam tax and other authorities at both the local and central levels strongly indicate that:

- ▶ Vietnam is strengthening its existing transfer pricing legal framework and enforcement capability, as well as improving the transparency and effectiveness of tax administration on transfer pricing. The proposed introduction of the APA is a strong example of this as the APA is expected to create more transparency in the tax administration process, by involving both the tax authorities and the taxpayers in an agreement, and enabling both parties to control and monitor transfer pricing issues.

Furthermore, not only will the APA help enhance the enterprises’ tax and transfer pricing compliance level but also increase their certainty and confidence level that a transfer pricing audit is mitigated or avoided for the duration of the APA. It can also prevent double taxation.

- ▶ The Vietnam tax authority is slowly becoming sophisticated and increasingly focused on administering foreign investment enterprises, especially when it comes to transfer pricing.
- ▶ The Vietnam tax authority has shown a particular and growing interest in the transfer prices of services, intangible assets and loan interests.
- ▶ The proposed provisions requiring periodic tax audits, deemed income tax based on revenue and revocation of business license of loss-making enterprises all point to the Vietnam tax authority’s continued focus on the tax/transfer pricing audits of said entities.

Transfer pricing risk management

The current Vietnam transfer pricing regulation (Circular 66) requires that taxpayers: (1) annually disclose related-party transactions in a required form and submit this form along with the annual CIT return; and (2) prepare and maintain contemporaneous transfer pricing documentation, which is to be submitted to the tax authority within 30 days from

written request by the tax authority. Similar requirements existed from 2006 to 2009 under Circular 117.

Given the recent regulatory enforcement, audit activities and future focus on transfer pricing, it is important for enterprises operating in Vietnam to review

their transfer pricing compliance status, especially if they have persistent loss-making years and have significant related-party transactions. The periodic review and compliance with Vietnam transfer pricing regulations with respect to annual related-party transaction disclosure and

contemporaneous transfer pricing documentation has become much more important than at the early stage of application of the regulations in Vietnam and can help mitigate transfer pricing audit and associated risks, including strict penalties.

For additional information with respect to this Alert, please contact the following:

Ernst & Young Vietnam Limited, Ho Chi Minh City

- | | | |
|----------------------|----------------|------------------------------|
| ▶ Nitin Jain | +84 8 38245252 | nitin.jain@vn.ey.com |
| ▶ Christopher Butler | +84 8 38245252 | christopher.butler@vn.ey.com |
| ▶ Phat Tan Nguyen | +84 8 38245252 | phat.tan.nguyen@vn.ey.com |
| ▶ Lea Gracia Molina | +84 8 38245252 | lea.gracia.molina@vn.ey.com |
| ▶ Takahisa Onose | +84 8 38245252 | takahisa.onose@vn.ey.com |

Ernst & Young Vietnam Limited, Hanoi

- | | | |
|------------------|----------------|--------------------------|
| ▶ Huong Vu | +84 4 38315100 | huong.vu@vn.ey.com |
| ▶ Long Ngoc Pham | +84 4 38315100 | long.ngoc.pham@vn.ey.com |
| ▶ Fuyuzi Anzai | +84 4 38315100 | fuyuki.anzai@vn.ey.com |

Ernst & Young Transfer Pricing

- ▶ **Global Transfer Pricing**, Germany
Thomas Borstell, +49 211 9352 10601
- ▶ **Americas**, United States
Bob Ackerman, +1 202 327 5944
Purvez Captain, +1 713 750 8341
- ▶ **EMEA**, Germany
Oliver Wehnert, +49 211 9352 10627
- ▶ **Asia Pacific**, Singapore
Luis Coronado, +65 6309 8826
- ▶ **Japan**, Tokyo
Kai Hielscher, +49 89 14331 16711
- ▶ **Global Markets**, United Kingdom
John Hobster, +44 207 951 6438
- ▶ **TESCM**, Amsterdam
Victor Bartels, +31 88 4071378
- ▶ **Global Financial Services TP**, London
Stephen Labrum, +44 20 7951 5603

Ernst & Young Member Firm Contacts

▶ Argentina	Carlos Casanovas	+54 11 4318 1619
▶ Albania	Alexandros Karakitis	+355 4 24 19 574
▶ Australia	Paul Balkus	+612 9248 4952
▶ Austria	Andreas Stefaner	+43 1 211 70 1041
▶ Belgium	Herwig Joosten	+32 02 774 9349
▶ Brazil	Werner Stuffer	+ 55 11 2573 3902
▶ Bulgaria	Laszlo Szaka	+359 2 8177 141
▶ Canada	Sean Kruger	+1 416 941 1761
▶ Chile	Osiel Gonzales	+56 26 761 141
▶ China	Jessica Tien	+86 21 22282115
▶ Colombia	Gustavo Pardo	+1571 651 2210
▶ Costa Rica	Rafael Sayagues	+1 212 773 4761
▶ Croatia	Denes Szabo	+385 1 2480 540
▶ Czech Republic	Libor Frýzek	+420 225 335 310
▶ Denmark	Thomas Bjerre	+45 3 587 2901
▶ Ecuador	Javier Salazar	+1 593 2 255 5553
▶ Egypt	Seema Sharma	+1 214 969 8077
▶ Estonia	Ranno Tingas	+372 611 4578
▶ Finland	Kennet Pettersson	+358 40 556 1181
▶ France	Franck Berger	+33 4 78 63 17 10
▶ Germany	Oliver Wehnert	+49 211 9352 10627
▶ Greece	Aggelos Benos	+30 210 288 6 024
▶ Hong Kong	Patrick Cheung	+852 2846 9905
▶ Hungary	Zoltan Liptak	+36 1 451 8638
▶ India	Vijay Iyer	+91 98 1049 5203
▶ India (TPC)	Puja Ramasubban	+91 80 6608 6895
▶ Indonesia	Carlo Navarro	+62 21 5289 5000
▶ Ireland	Dan McSwiney	+353 1 221 2094
▶ Israel	Lior Harary-Nitzan	+972 3 623 2749
▶ Italy	Davide Bergami	+39 02 851 4409
▶ Japan	Kai Hielscher	+81 3 3506 1356
▶ Kazakhstan	Roman Yurtayev	+87 727 258 5960
▶ Korea	Rap Choi	+82 2 3770 1001
▶ Latvia	Ilona Butane	+371 704 3836
▶ Lithuania	Leonas Lingis	+370 5 274 2279
▶ Luxembourg	Paul Leyder	+352 42 124 7240
▶ Malaysia	Janice Wong	+6 03 7495 8223
▶ Mexico	Jorge Castellon	+52 81 81521829
▶ Netherlands	Danny Oosterhoff	+31 88 40 71007
▶ New Zealand	Mark Loveday	+64 9 300 7085
▶ Norway	Marius Leivestad	+47 24 00 23 86
▶ Peru	Marcial Garcia	+151 1 411 4424
▶ Philippines	Romulo Danao	+63 2 894 8392
▶ Poland	Aneta Blazejewska-Gaczynska	+48 22 557 8996
▶ Portugal	Paulo Mendonca	+351 21 791 2045
▶ Romania	Alexander Milcev	+402 1402 4000
▶ Russia	Evgenia Veter	+7 495 660 4880
▶ Singapore	Luis Coronado	+65 6309 8826
▶ Slovak Republic	Gunter Oszwald	+421 2 333 39610
▶ Slovenia	Denes Szabo	+36 1 451 8209
▶ South Africa	Karen Miller	+27 21 443 0200
▶ Spain	Ramón Palacín Sotillos	+34 915 727 485
▶ Sweden	Mikael Hall	+46 8 520 592 35
▶ Switzerland	Edvard Rinck	+41 58 286 4250
▶ Taiwan	George Chou	+86 21 2228 8888
▶ Thailand	Anthony Loh	+662 264 0777
▶ Turkey	Alper Yilmaz	+90 212 368 53 60
▶ United Arab Emirates	Seema Sharma	+1 214 969 8077
▶ United Kingdom	Tim Steel	+44 20 7951 1149
▶ United States	Bob Ackerman Purvez Captain	+1 202 327 5944 +1 713 750 8341
▶ Venezuela	Jose A. Velazquez	+58 212 905 66 59
▶ Vietnam	Nitin Jain	+84 8 832 45252

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