



MNCs & Tax Policy Trends in Asia Pacific

A process of fiscal consolidation is in store for the Asia-Pacific region. What can multinational corporations expect?

In general, multinational corporations (MNCs) operating in Asia Pacific will have to be prepared for a process of fiscal consolidation as countries seek to increase tax collection and reduce debt accumulated during the global financial crisis. One can foresee the following key trends in the development and direction of tax policies over the next few years in the Asia-Pacific region:

- Lowering of corporate tax rates in some Asian countries.
- Broadening of the tax base so that corporate tax receipts will remain stable.
- Tax incentives for selected activities such as high-tech companies, financial services and 'green' industries.
- Aggressive tax enforcement to maintain revenue by enforcing economic substance rules, imposing stricter transfer pricing regimes, auditing cross-border transactions, cooperating internationally to reduce tax avoidance or evasion, etc.
- Increased taxation of immobile assets such as land and minerals, because those taxes generate predictable revenue with minimal difficulty in administration. For example, China has some new taxes on land and Australia has introduced new mining taxes.
- Shift to indirect taxes will continue although there may be resistance from the public.

Financial services centres and holding company jurisdictions

Competition to become a major financial services hub has heated up in the Asia-Pacific region. Hong Kong has held the paramount position for many years, and tax policy is arguably a major reason as its corporate tax rate is the lowest in the region, but it has continued to reinforce its standing in the financial services industry.

Another important aspect is Asia's leading holding company jurisdictions and there is competition among Hong Kong, Malaysia and Singapore in attracting global business and capital

with regional headquarters/treasury management incentives.

Shanghai has long been a contender in the area of financial services, and now Australia, New Zealand and Malaysia continue to fine-tune their tax policies to attract the financial services industry.

Malaysia enacted additional laws and amended some of the existing laws to re-position Labuan as an international business and financial hub. In particular, Malaysia encourages investment holding companies, trading companies, shipping companies, captive insurance business, investment funds, and special purpose vehicles to consider as a place where raising financing is comparatively easy.

TAX ENFORCEMENT

■ Stricter Tax Audits

Stricter auditing is an almost universal feature of an increasingly aggressive tax administration. China will continue to tighten up the enforcement on non-resident taxpayers and cross-border transactions, intensifying the country's anti-avoidance campaign. Since 2009, China's tax authorities have issued a series of major tax circulars that instruct taxpayers on the procedures to be followed to benefit from tax treaties or to enjoy tax preferences for targeted industries.

One such circular asserts China's authority to ignore any legal entity that is set up, in the opinion of China's tax authorities, for tax-avoidance purposes. This is the 'substance over form' doctrine. Hence, if the sale of an asset in China is made by a legal entity in a low or no-tax jurisdiction, China will look to the residence of the owners when assessing taxes. In the same circular, China imposed a new documentation-filing requirement on gains that non-residents derive from transferring equity interest in Chinese resident companies if the gain is taxed in locations with a corporate income tax lower than 12.5%.

Malaysia, like some other countries, plans more aggressive tax audits and investigations to increase compliance and increase revenue.

Tax avoidance is becoming a bone of contention in Asia. From what was a liberal approach adopted by most Asian tax administrations in the past, we now are seeing a fast-paced aggressive development – countries are either rushing to legislate general anti-avoidance rules (GAAR) or tax administrations are getting aggressive in their approach towards audits. Whereas Australia has been the torchbearer for most of the global tax administration's desire to invoke GAAR, China and India have had the most attention of global tax directors of multinational corporations (MNCs). China issued various administrative circulars in 2009 as mentioned above and one of these was in response to the Indian Vodafone case where the tax authorities decided to tax offshore sale of shares (Note: The decision of the Supreme Court of India in the Vodafone case was issued in January 2012 and it was decided that the tax authorities could not impose a tax on the sale of the shares). India has been invoking GAAR using the judiciary approach and is bracing itself to introduce a legislative GAAR in 2012 via the new Direct Tax Code, labelled by most observers as being the toughest form of anti-avoidance legislation.

■ Taxpayer Information Exchange

Tax administrations in pursuit of information regarding global investors' international activity have found success with tax information exchange agreements. If an agreement is in place, two Governments can request information from each other such as the status of individual or corporate bank accounts suspected of containing undeclared assets.

■ Transfer Pricing

Transfer pricing continues to be perceived as one of the most dominant challenges facing companies and tax administrations alike.

Transfer pricing is assuming centre-stage in most parts of Asia. It is interesting to witness the trends in Asia Pacific as we have countries such as Australia and Japan with advanced regulations and sophisticated tools. On the other hand, we have jurisdictions such as Malaysia, Vietnam, Indonesia and the Philippines settling down with new regulations in the past few years. The aggressive approach by tax administrations in certain jurisdictions such as India and Korea is being keenly watched by regional tax directors of MNCs. We are also witnessing the introduction of the Advance Pricing Agreement (APA) regime in the region to avoid tax disputes with some having a multilateral mechanism and some allowing

unilateral APAs. On the other hand, countries such as India are still thinking about legislating APA as part of their larger tax reform agenda from April 2012.

Malaysia introduced APAs in its legislation in 2009 and has signed at least one unilateral APA to date. In December 2010, China published its first public document on APAs. It describes the regulations and forms associated with China's unilateral, bilateral and multilateral APAs. It plans to revise this document annually, and by doing so, promote systematic administration of transparent APAs.

Indonesia has also published new guidelines both for transfer pricing in general and for filing for APAs. Korea has published rules that enable taxpayers to submit documentation and thereby avoid penalties during transfer pricing adjustments.

INDIRECT TAXES

The trend towards more indirect taxes will continue though it may face a fair bit of resistance among the electorate such as in Japan, Thailand (which extended its rate cut from 10% to 7% for another two years) and in Malaysia which has had to repeatedly postpone its effort to enact a GST. However, there is still some momentum for indirect taxes. In Malaysia, the effort to introduce a GST is still in motion and value-added tax reform is a hot topic in China.

New Zealand has raised its GST rate from 12.5% to 15% while simultaneously cutting personal and corporate income tax rates, which is widely seen as an economically beneficial trade-off and such a policy measure has become conventional wisdom in public finance around the world. This is an important point to note because part of globalisation is a more consistent mindset worldwide about what the right monetary and fiscal policies are.

CONCLUSION

All over the world, tax and regulatory changes have resulted in additional costs. They have impacted business strategies, systems, controls and sometimes even resources. Transfer pricing and income tax disputes have been identified in various surveys as being the most significant. While corporations express their concerns over unexpected and sudden changes in law, most of them also stress their apprehension that the changes may add to the complexity rather than bringing certainty.

With the tax and regulatory landscape changes that may be forthcoming, the time is right for corporations to re-evaluate their level of preparedness in light of these factors. For this, corporations would need to re-familiarise themselves objectively with the internal reporting systems, documentation policies, litigation history and positions adopted before tax authorities. Towards this end, businesses should continuously review their overall tax strategy including placing taxation issues on the agenda of the Board of Directors. 

Dr Veerinderjeet Singh is Chairman of Taxand Malaysia Sdn Bhd, which is part of the Taxand Global organisation, the first global organisation of independent tax advisers with a presence in nearly 50 countries. He is a member of the Global Taxation Board as well as a member of the Commission on Taxation of the International Chamber of Commerce based in Paris. He can be contacted at vs@taxand.com.my. The views expressed here are his own.

