

The background of the top section is a close-up, slightly blurred image of a calculator. The numbers '453', '20', '1', and '474' are visible on the display, with a horizontal line indicating a calculation result.

General tax update for financial institutions in Asia Pacific

Regional co-ordinator and editor –
Charles Kinsley, KPMG in Hong Kong

TAX

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Australia



Tax update

Changes in legislation

- On 1 April 2005, the Tax Laws Amendment (2004 Measures No. 7) Act 2005, No. 41 of 2005 received Royal Assent. The act contains a number of consolidation-related amendments, particularly with respect to the treatment of liabilities for the purposes of calculating allocable cost amounts upon consolidation.
- On 22 April 2005, the Governor-General of the Commonwealth of Australia, Mr Philip Jeffery, made the Income Tax Assessment Amendment Regulations 2005 (No. 2) under the Income Tax Assessment Act 1997. The Regulations were registered on 27 April 2005. The Regulations aim to ease the costs for taxpayers to comply with the existing foreign currency rules by allowing foreign currency amounts to be translated into Australian currency or a functional currency using exchange rates other than the exchange rates prescribed in the current tax law.
- On 10 May 2005, in the Federal Budget, the Treasurer announced changes to the Income Tax Assessment Act 1997 that will provide tax treatment for certain legitimate business expenses, known as 'blackhole' expenditures, which are not currently addressed by the income tax law.
- On 25 May 2005, the Governor-General of the Commonwealth of Australia, Mr Philip Jeffery, made the Income Tax Assessment Amendment Regulations 2005 (No. 3), Select Legislative Instrument 2005 No. 102 under the Income Tax Assessment Act 1997. The Regulations were registered on 26 May 2005. The Regulations amend the Income Tax Assessment Regulations 1997 to clarify that an obligation to redeem or buy back a preference share is not a contingent obligation (for the purposes of classification as debt or equity) merely because it is subject to certain legislative conditions aimed at protecting creditors' interests.
- On 31 May 2005, the Tax Laws Amendment (2005 Measures No. 3) Bill 2005 was passed by the House of Representatives without amendment and will now move to the Senate for consideration. The Bill amends various taxation laws to implement a range of changes and improvements to Australia's taxation system, and includes provisions to encourage charitable giving in Australia, provisions to correct an unintended outcome of the foreign branch profits exemption in relation to international shipping and airline profits, and secrecy provisions to allow the disclosure of relevant information to the Corruption and Crime Commission of Western Australia.

Court cases

- On 26 April 2005, the High Court, in *Commissioner of Taxation v Linter Textiles Australia Ltd (In Liquidation) [2005] HCA 20*, held that, where a winding up order is made in respect of a loss company seeking to transfer losses to a parent company, the parent company's shareholding in the loss company continues to carry the necessary rights to satisfy the loss transfer provisions, despite the loss company being in liquidation.

A second issue in the case was the effect of a winding up order in respect of the parent company (rather than the loss company). The High Court rejected the Commissioner's argument that the beneficial ownership of the parent company's shares in the loss company was affected by the winding up order. However, the High Court accepted the submission that control of the voting

shares in the loss company was no longer held by the ultimate shareholders of the group as a result of the winding up of the parent. As a result, the taxpayer was unable to utilise the prior year losses.

Hong Kong



Abolition of Estate Duty Bill gazetted

The Revenue (Abolition of Estate Duty) Bill 2005, which seeks to implement the proposal to abolish estate duty announced in the 2005 Budget, was gazetted on 6 May 2005. Under the proposal, estates of persons who pass away after the commencement of the Revenue (Abolition of Estate Duty) Ordinance 2005 will not be subject to estate duty. The Bill has been introduced into the Legislative Council.

The abolition of Estate Duty is designed to enhance Hong Kong's asset management industry and further promote Hong Kong as a leading international financial centre.

Court case

Baring Securities (Hong Kong) Limited v Commissioner of Inland Revenue

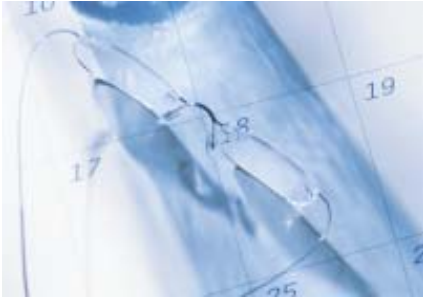
On 1 June 2005, the Court of First Instance allowed an appeal by ING Baring Securities (Hong Kong) Limited ("BSHK") against the decision of the Inland Revenue Board of Review ("Board") in the case of *Baring Securities (Hong Kong) Limited, presently known as ING Baring Securities (Hong Kong) Limited v The Commissioner of Inland Revenue (HCIA 1/2003)*. The Court ruled that the commission, marketing and placement income earned from BSHK's securities brokerage activities were sourced offshore.

The case was first heard in October 2003 and judgment delivered in June 2005. In delivering the judgment, the Court stated that the Barings sub-group's business was that of "agency brokerage" consisting of the execution of client's trades in securities listed on major global stock exchanges. The business could be functionally divided into three main divisions being Research and Sales, Execution and Settlement. In determining the source of profits, the Court ruled that in BSHK's case, it was the execution of the trades that gave rise to the commission income and as this was undertaken by BSHK's agents outside Hong Kong, the profits were sourced offshore. The Court rejected the position that the profits were derived from sales and research activities stating that such activities brought in the clients but did not throw up the income. It went on to elaborate why this position was different from the situation in the case of the *Commissioner of Inland Revenue v Wardley Investment Services (Hong Kong) Ltd*. The Court had in that case ruled that profits were generated from investment advice.

In the same way, the Court ruled that placement income was offshore as it was derived as a result of the execution of orders outside Hong Kong. Finally, marketing income was also determined to be derived offshore as it related to the introduction of customers to execution offices outside Hong Kong.

It may also be significant to note that the conclusions arrived at in the *Barings case* on the source of brokerage commission differ from the Board's in the case of *The Commissioner of Inland Revenue v Indosuez W I Carr Securities Ltd (HCIA 4/2001)*. The High Court had in its judgment delivered in 2002 remitted the *W I Carr case* to the Board to reconsider its conclusions. Currently, there has been no public announcements as to whether the IRD would lodge an appeal against the decision of the Court in Barings case or whether it would now conclude differently in the *W I Carr case*.

India



Advance ruling cases

Briggs of Burton (India) Pvt Ltd., In re - A. A. R. No 654 of 2004 (4 April 2005) (Unreported),

The Authority for Advance Ruling (“ARR”) ruled that bonus redeemable preference shares allotted by the applicant, an Indian company, to its shareholders should not be treated as a “deemed dividend”. As such, the applicant company was not required to withhold tax on the bonus preference share allotment.

Under Indian domestic tax law, any distribution by a company to its shareholders should be considered a dividend if such distribution entails the release of all or any part of the assets of the company to its shareholders.

Despite the domestic tax law, the AAR ruled that the distribution by the applicant company to its existing shareholders through the allotment of bonus redeemable preference shares although representing a distribution of accumulated profits, does not entail the release of assets by the applicant company. As such, the distribution was not considered a dividend for tax purposes.

Indonesia



Indonesia-Netherlands tax treaty

As previously mentioned, the double tax treaty between Indonesia and the Netherlands (“the Treaty”) took effect from January 2004. The Treaty provides a withholding tax exemption on two types of interest paid to Dutch companies: (i) interest on loans with a maturity period greater than two years; and (ii) interest on loans borrowed for the acquisition of certain capital equipment. As many Indonesian companies bear the cost of withholding tax on interest, those companies considering overseas borrowings may have a preference for borrowings from Netherlands companies.

Several months ago, the Indonesian Directorate General of Tax (DGT) issued a ruling letter which created confusion as to the practical application of the Interest article in the Treaty. It was stated in the letter that the tax office will not permit companies to take advantage of the interest withholding tax reduction (to 10%) or exemption under the Treaty as both the Indonesian and Dutch government have not reached an agreement on the “mode of application” of the said interest articles.

On 1 June 2005, the DGT issued a clarifying regulation (DGT Circular SE-17/PJ/2005) which allows the reduced withholding tax rate of 10% but does not allow the exemption. There is no explanation as to why a special “mode of application” is required to obtain the withholding tax exemption for interest paid to Netherlands tax residents when there is already a tax regulation in place explaining the mode of application of the aforesaid Treaty relief. The existing tax regulation provides that a “Certificate of Tax Domicile” to substantiate the Dutch lenders’ residency status is required from the Netherlands government before the Treaty relief would be granted.

Until the regulation on the “mode of application” is finalised, the DGT has taken the position that no withholding tax exemptions would be granted to interest paid to Netherlands tax residents. However, the reduced rate of 10% is available on such interest.

The Dutch tax authorities have been informed of the DGT's letter and it is hoped that an agreement may be reached shortly to reconfirm the interest withholding tax exemption under the Treaty.

Japan



Japan Tax reform 2005

The 2005 Tax Reform Bill mentioned in Issue 14 has been passed on 30 March 2005 and the Cabinet orders and Ministerial orders have subsequently been made public. The salient features are summarised as follows:

Withholding tax on profit allocation from partnerships

Under the 2005 Tax Reform Bill, profit allocations to foreign partners derived from businesses carried on in Japan using a Nini-Kumiai (NK) type partnership will be subject to withholding tax at 20%.

Capital gains on disposal of shares in a Japanese company by substantial foreign shareholders

A foreign investor (either a non-resident individual or a foreign company, including investors that do not have a permanent establishment in Japan) is taxed on capital gains on the disposal of shares in a Japanese company if both of the following conditions are satisfied:

- the aggregate shareholding in the Japanese company of the foreign investor and related persons of the foreign investor at any time during the preceding three fiscal years (including the fiscal year of disposal of the shares) was 25% or more of the total issued shares of the Japanese company, and
- the foreign investor and related persons disposed of 5% or more of the total issued shares of the Japanese company during the fiscal year of disposal of the shares.

Before the 2005 tax reform, "related persons" of a shareholder were defined as individuals or companies having a special relationship with the shareholder. However, by virtue of the 2005 tax reform, where a foreign investor holds shares in a Japanese company through an NK-type partnership, "related persons" will include any other partners of the partnership.

If a foreign shareholder owns shares in a Japanese company through two or more partnerships, all partners of those partnerships will be treated as "related persons" for the foreign shareholder. Note that the aggregate shareholding in a domestic company does not include shares that these partners hold not through those partnerships.

Limitation on utilisation of losses derived from partnerships

A new rule similar to the "Passive Activity Loss Rule" in the U.S. will be introduced for individual partners in certain partnerships. Where a specified individual partner of a partnership that is involved in the rental of real property incurs losses from the rental activity, such losses will be disregarded for income tax purposes and cannot be carried over to the following years.

A new rule similar to the "At-Risk Rule" in the U.S. will be introduced for corporate partners. When a specified corporate partner in a partnership incurs losses from the partnership business during an accounting year, the losses exceeding the capital contribution made by the partners are not deductible for tax purposes.

Introduction of taxation on capital gains from disposition of specified Japanese real estate interests

By virtue of the 2005 tax reform, capital gains from a disposition of shares in real estate holding companies or beneficial interests in certain real estate trusts by a foreign investor (both individuals and companies) will be taxed in Japan. The foreign investor is required to file a tax return to declare such income.

For a more detailed analysis of the 2005 tax reform, please visit the following Web site: http://www.kpmg.or.jp/resources/newsletter/tax/taxnl200505_e.pdf

Korea



Recent ruling cases

In the application of the Thin Cap ratio, head office remittance payables shall not be included as liabilities when calculating net capital.

Article 14 of the Law for the Coordination of International Tax Affairs (LCITA) directs that for application of the thin capitalisation ("thin cap") rule, the branch should calculate its net capital by subtracting total liabilities from total assets.

A domestic branch of a foreign bank reported "head office remittance payables" (which had previously been reported as capital reserve) as liabilities in its balance sheet in accordance with the Financial Supervisory Service Regulations. A request for ruling was then submitted to the Ministry of Finance and Economy (MOFE) as to whether the "head office remittance payables" that are stated as liabilities in the balance sheet for financial reporting purposes should be counted as liabilities in calculating the branch's net capital for determining the thin cap ratio.

The MOFE responded that head office remittance payables are created as a result of internal transactions between a foreign controlling office and its branch, and as such, are part of the head office accounts from the perspective of the branch. The LCITA Basic Regulations 92-0-1 state that "in the calculation of the appropriate net capital of a domestic branch of a foreign corporation, the head office account balance is not to be regarded as liabilities of the branch". Accordingly, the MOFE ruled that the "head office remittance payables" should not be treated as the liabilities of the branch when calculating the branch's net capital for the purpose of application of the thin cap rule, despite the fact that the "head office remittance payables" had been recorded as liabilities for financial reporting purposes.

Timing of capital gain (loss) recognition for shares transferred under a put option

Company A transferred shares of its subsidiary, Company B, to Company C. The shares were transferred subject to a put option, whereby the option is exercisable if dividends distributed by Company B fall below a certain level. Subsequently, Company C exercised the put option and Company A repurchased the shares.

A request for ruling was submitted to the National Tax Service (NTS) to determine the effective date of recognition of gains or losses where shares are sold and then repurchased in accordance with contractual obligations of a put-option.

The NTS responded that the timing of the recognition of gains (losses) from the transfer of shares shall be the date when (i) the purchase price for the shares is paid, or (ii) the shares are delivered, or (iii) the recorded owner of the shares is changed, whichever is the earliest. This is the case regardless of the fact that shares are repurchased under a put option. Moreover, where Company C in fact exercises the put option and Company A repurchases the shares, the initial sale and the subsequent repurchase are treated as separate and independent transactions, and thus the exercise price of the put option is deemed to be the acquisition cost of the repurchased shares in the hands of Company A. The NTS expressed that irrespective of the conditions attached to the initial sale (such as a put option or call option), the original transaction will be deemed to be a complete transaction as long as conditions in respect of the transfer of shares such as delivery of shares, change of record owner, or registration of the shares are met.

Interest expenses on corporate bonds that are issued by a foreign corporation as a capital contribution into its Korean branch will be deductible for tax purposes. (Seomyon 2 Team-363,2005.03.02)

Under the Korean law, a branch of a foreign company is not allowed to issue corporate bonds. However, the NTS opined that where the foreign corporation is allowed to issue the corporate bonds under its own name with the domestic branch's assets as security and the purpose of the issuance is clearly to inject capital into the Korean branch and such capital is to be used by the branch for business purposes, the relevant interest expenses paid by the Korean branch should be tax deductible.

An overseas stock broker that carries out brokerage activities for its client through a domestic broker on a continuous and repetitive basis will be deemed to have a permanent establishment (PE) in Korea (Seomyon 2 Team -274, 2005.2.11)

The NTS deems an overseas stock broker as having a PE in Korea in the case where the stock broker is engaged in investment in Korean stocks and undertakes the following activities on a repetitive basis:

- Opens an account with a domestic securities company under the name of a stock broker's non-resident investor;
- Performs client management, company analyses, and market status analyses;
- Executes orders and performs settlement on behalf of the non-resident investors.

Changes in legislation

Classification of income from a securities lending transaction (SLT)

Effective from 1 January 2005, income arising from a SLT between two non-residents where both parties have no PE in Korea, will not be treated as Korean sourced income.

Prior to 1 January 2005, the substitute payment made by the borrower to the lender was treated as dividend income in cases where the borrower took a long position (i.e. held the securities rather than selling short). This treatment has resulted in double taxation being imposed on the same dividend income.

Private Equity Funds Exempt from Securities Transaction Tax

Effective from 1 January 2005, shares transferred by Private Equity Funds (PEF) and Special Purpose Companies (SPC) through the Korean Stock Exchange, KOSDAQ, or the electronic over-the-counter market, will be exempt from securities transaction tax (STT).

The government's intention is to allow investment vehicles which perform similar functions to mutual funds and Corporate Restructuring Companies (CRCs) (i.e. act as nominal indirect investors and indirectly manage the securities) to enjoy the same tax concession (i.e. exemption from STT) that is currently available to mutual funds and CRCs.

Malaysia



Update on introduction of GST

The preparation for the introduction of GST is progressing. It has been proposed that GST will be implemented in 2007. Various financial institutions have already made their representations to the Tax Review Committee on their proposed treatment of financial assets and revenue under the GST Regime. It is widely anticipated that the draft GST legislation would be made available to the public in the third quarter of 2005 for comments.

Issues with implementation of FRS 39

The implementation of Financial Report Standard (FRS) 39 (the equivalent to IAS 39) may have tax implications as to how trading assets should be valued and thereby the calculation of the amount of any taxable gains. Currently the prescribed valuation method under the Income Tax Act is "lower of cost or net realisable value" for trading assets. As such, the tracking of original cost required under the current income tax legislation would pose a problem for most financial institutions when they adopt FRS 39.

Another area where there is a major divergence is the calculation of recoverable amount/ impairment of loans and receivables. The new valuation method under FRS 39 is to use the present value of expected cash flows discounted at the original effective interest rates, whereas the current method adopted is the realisable value of collateral. The possible impact on the taxability of the "difference" as a result of the change in valuation methodology is not envisaged in the current Income Tax Act.

As a result, until some clarification or guidance is given, financial institutions would need to make a judgement call on the tax treatment to be adopted when filing their tax returns.

Mauritius



Changes in legislation

Further to the adoption of the Finance Act 2005 in late April, the Income Tax Act 1995 has been amended and the following are relevant for financial institutions:

- The Alternative Minimum Tax (AMT) was introduced by the Finance Act 2004 and is payable if the normal tax payable by any company is less than 5% of its accounting profit in an income year. AMT will be charged at a rate of 5% on accounting profit or 10% on any dividends declared for that income year, whichever is the lesser.

Prior to the amendment to the Finance Act 2005, AMT would not be chargeable to a company that did not declare any dividend for that income year. However, the Act has been amended such that AMT will now be applicable to all companies irrespective of whether they have declared dividends or not, so long as the normal tax payable of a company is less than 5% of its accounting profit for the year. A second amendment is that AMT also applies on any amount distributed by way of shares in lieu of dividends.

- It does not, however, apply to companies which are (i) exempt from income tax, or (ii) where the AMT amount equivalent to 10% of the dividends declared for that income year would still not exceed the company's normal tax payable amount.
- The definition of "non-resident" in the case of banks holding a banking licence under the Banking Act 2004 has changed to include:
 - In the case of an individual, a person whose permanent place of abode is outside Mauritius and who is outside Mauritius at the time when the services are performed.
 - In the case of any other person, a person whose centre of economic interest is located outside Mauritius. "Person" includes a company incorporated in Mauritius but with its banking transactions carried out through a permanent establishment outside Mauritius. "Person", however, does not include a company incorporated outside Mauritius but with its banking transactions carried out through a permanent establishment in Mauritius.
- Where there is expenditure/ loss that cannot be directly traced/ attributed to a particular source of income, i.e. the expenditure cannot be directly attributable to the income derived from Mauritius or the income derived outside Mauritius, a bank has to furnish together with its tax return, a certificate from a qualified auditor certifying that this expenditure/ loss has been apportioned in a fair and reasonable manner to the sources of income derived by the bank.

New Zealand



2005 Budget

On 19 May 2005, the Government delivered the 2005 Budget. On the same day, a new Tax Bill was introduced, incorporating changes announced within the Budget or foreshadowed in the days leading up to the official Budget announcement.

The relevant principal changes in the Budget include:

- The tax treatment of managed funds is to be placed on a more equal footing with the tax treatment applying to individuals, i.e. capital gains exempt from tax while the income of the fund is passed through to the individual investors and taxed in their own name.
- The tax treatment of securities lending transactions will be reformed such that “qualifying” share lending transactions would not be treated as a taxable disposal for tax purposes. Share lending transactions are required to meet a number of criteria in order not to be treated as a taxable disposal.
- Taxpayers will now have an ability to defer tax losses arising from research and development deductions which might otherwise be forfeited if there is a shareholding change in the taxpayer company.
- Non-resident investors investing venture capital in companies alongside the New Zealand Venture Investment Fund Limited will be exempt from tax on the sale of shares in those companies. This complements recent amendments provide that where certain non-residents that are exempt from tax in their own country and are resident in a country with which New Zealand has a double tax treaty (except Switzerland), they will be exempt from tax on the sale of shares in unlisted companies.
- Temporary tax exemptions for migrants into New Zealand that have not been tax resident in New Zealand for at least 10 years. These exemptions will mean that many types of overseas income that the migrant derives while resident in New Zealand will be exempt from New Zealand tax. These exemptions will apply for a period of three to five years depending on the migrant’s employment situation.

Discussion document on taxation of overseas portfolio investment

The Government has also recently issued a discussion document proposing significant changes to the taxation of overseas portfolio investment (being investment where no more than 10% of a company’s capital is owned).

At present, overseas portfolio investment into companies resident in “grey list” countries, such as Australia, the United Kingdom, Japan and the United States, are exempt from New Zealand’s foreign investment fund (“FIF”) regime. As such, only distributions from these companies are taxed.

Briefly, the new proposals would abolish the grey list and would tax all overseas portfolio investments on movements in their market value over the course of a tax year. A deemed rate of return method will apply if there is no readily verifiable market value. An exemption would apply for individuals where their overseas investments total less than \$50,000, and are made into countries with which New Zealand has a double tax treaty.

Thin capitalisation rules for banks

These have been discussed in prior issues. The rules, which require a minimum equity equal to 4% of risk weighted assets, have now been enacted and are effective from 1 July 2005.

Philippines



Changes in Legislation

Republic Act No. 9337 (Value-Added Tax Act of 2005) was enacted on 24 May 2005. This new Act amends the 1997 Philippine Tax Code and the changes shall take effect from 1 July 2005.

The relevant provisions are summarised below:

Corporate income tax rate

For the period from 1 July 2005 to 31 December 2008, the corporate income tax rate for both domestic and foreign corporations will be increased from 32% to 35%. The corporate tax rate will then be reduced to 30% from 1 January 2009 onwards.

Other changes in tax rates

The previous tax credit requirement of 17% for the application of the 15% preferential tax (tax sparing rate) on inter-corporate dividends payable to non-resident foreign corporations (the rate being the difference between the 15% tax and the 32% corporate income tax rate) will be increased to 20% under the 35% corporate income tax regime and reduced to 15% under the 30% corporate income tax regime.

With the enactment of the New Act, as the corporate income tax will be increased from 32% to 35%, consequently, the interest cost arbitrage (i.e. the non-deductible interest expense) has been increased from 38% to 42% of the interest income derived.

Percentage taxes

Under Section 121 of the Tax Code, the gross receipts tax (GRT) imposed on banks and non-bank financial institutions (such as securities companies, deposit taking companies etc) will increase from 5% to 7% on the following transactions:

- royalties, rentals of property, real or personal, profits from exchange and all other items of gross income; and
- net trading gains on foreign currency, debt securities, derivatives, and similar financial instruments.

Please note that the constitutionality of Republic Act No. 9337 has been raised before the Supreme Court. On 1 July 2005, it issued a temporary restraining order enjoining the Executive Secretary, Secretary of Finance and the Commissioner of Internal Revenue, among others, from enforcing and implementing the said new Act, the VAT Regulations and any such other implementing rules and regulations until further order from the Supreme Court. In obedience to the order of the Supreme Court, the Commissioner of Internal Revenue issued Revenue Memorandum Circular No. 30-2005 dated 2 July 2005 deferring the implementation of Republic Act No. 9337 and the VAT Regulations. Accordingly, all taxpayers shall be liable for the taxes and the tax rates they were subject prior to the intended effective date of Republic Act No. 9337 on 1 July 2005.

No-Audit Program

On 26 April 2005, the Philippine Government, through its Executive Department released Executive Order No. 422 and accompanying implementation rules, which simplifies and reduces the required fiscal thresholds/ standards that a taxpayer must satisfy in order to qualify under the "No Audit Program" (NAP).

The NAP Program is a 5-year tax program designed to raise revenue for the government by enticing taxpayers, including financial institutions, to voluntarily pay their taxes from 1 August 2004 in exchange for the privilege of not being audited by the Bureau of Internal Revenue (BIR).

The revised thresholds/ standards are as follows:

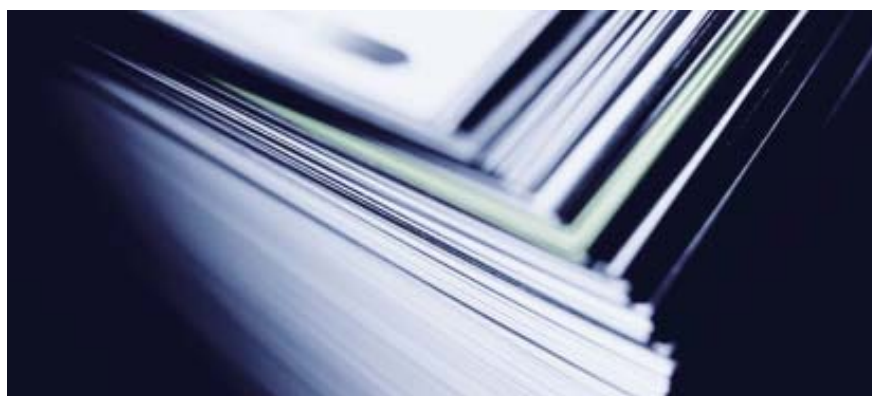
- growth rate of income tax for the current tax year compared with the previous tax year must be at least 20%;
- ratio of income tax payment to gross sales/receipts for the current taxable year must be at least equal to that of the previous taxable year; and
- ratio of net value-added tax or business tax actually paid to gross sales/receipts for the current taxable year must be at least equal to that of the previous taxable year, or the benchmark of the industry, as set by the Commissioner of Internal Revenue, whichever is higher.

People's Republic of China

New rules on swap transactions and overdue interest income

The PRC State Administration of Taxation has issued new rules dealing with withholding tax implications on cross border swap transactions. The new rules state that if the foreign swap dealer is the lender of the relevant loans (or is related to the lender, i.e. the swap dealer has a 80% beneficial ownership interest in the lender or vice versa), the net swap payment received by the foreign swap dealer should be regarded as interest income of the foreign swap dealer and be deemed to be income derived from the PRC and taxed accordingly.

Another new set of rules have also been issued by the PRC State Administration of Taxation clarifying the business tax implications to financial institutions on interest income received from overdue loan interest. It was stated that as soon as the loan interest has been overdue for more than 90 days, the accrued loan interest could be reversed to offset against the loan interest income of the current period. However, the overdue loan interest cannot be used to offset against any other income derived by that financial institution.



Singapore



Further details on 2005 budget

Enhancements to the commodity derivatives trading scheme

In the previous issue, it was mentioned that approved commodity derivatives traders have been granted a concessionary tax rate of 5 percent on qualifying trading and service income derived from commodity derivatives transactions traded over-the-counter. Such concession has been extended to cover qualifying income derived from exchange-traded commodity derivatives with effect from 18 February 2005.

It was announced in May 2005 that :-

- The definition of "commodity derivatives" has been expanded to include forward freight agreements with effect from 18 February 2005;
- Income derived from forward freight agreements transacted with a shipping company (not applicable to commodity derivatives) will also be granted the concessionary rate of 5 percent.

Sri Lanka



Changes in legislation

Tax on the sale of shares

With retrospective effect from 1 January 2005, where a Share Transaction Levy of 0.2% has been paid on the sale of shares, the profit derived from the disposal would not be liable to Income Tax of 15%, irrespective of the period of holding of the disposed shares.

Transfer Tax

On the transfer of real estate to a non-citizen of Sri Lanka, a 100% tax will be imposed on sales proceeds (or market value if higher) on the non-citizen acquirer. This tax was repealed in 2002 but reintroduced again in October 2004. The definition of "non-citizen" has been recently extended to cover companies where more than 25% of its equity is held by non-citizens.

A transfer of property made to a licensed bank or finance leasing institution, will be exempt from Transfer Tax only if the transfer is:

- By an order of the Court in an action for recovery of a debt;
- Upon the discharge of a mortgage of such property; and
- To carry on its normal business activities.

Exemption from the Transfer Tax will also be granted on the transfer of properties in a merger transaction where the transferor company had acquired the same prior to 5 October 2004, and the merger would result in the dissolution of the transferor company.

Taiwan



Ruling on tax treatment of stock options issued by foreign companies

The Ministry of Finance (MOF) issued a tax ruling on 17 May 2005, which sets out the individual income tax treatment for stock options issued by foreign companies as well as the compliance requirements of Taiwan employer companies.

The key aspects of the ruling are highlighted below:

Tax treatment for individuals

The profits derived from the exercise of stock options by (i) employees of a foreign company being seconded to Taiwan to provide services and (ii) employees of a Taiwan subsidiary, branch, or representative office of a foreign company (collectively called "Taiwanese entities") where the stock options were issued by the foreign company, will be subject to Taiwan income tax.

Taxable year

The taxable year is the year when the employees exercise the stock options.

Taiwan sourced income

If the individual provides services in Taiwan between the period from the grant date to the vesting date of the stock options (the vesting period), the amount of income derived from exercising the options is the difference between the fair market value of the shares as of the exercise date and the exercise price paid.

In addition, the amount of income sourced from Taiwan will be further determined by pro-rating the total amount of taxable income by the ratio of the number of days the employees reside in Taiwan during the vesting period over the total number of days of the vesting period.

Gains or losses from selling the shares

Any gains or losses derived from the disposal of foreign stock would be deemed to be foreign sourced and not subject to individual income tax in Taiwan.

Compliance requirements for Taiwanese entities

If employees of Taiwanese entities have obtained and exercised stock options that were issued by foreign companies (e.g. head offices of these Taiwanese entities), these Taiwanese employers must file the non-withholding tax statements along with the relevant information to the tax authorities by the end of January of the following year.

Continuation of Gross Business Receipt Tax ("GBRT") to financial institutions

GBRT was introduced to fund the Financial Restructuring Fund (RTC) which was set up by the Taiwanese government to resolve the bad debts issues encountered by local banks.

GBRT was imposed on financial institutions at a rate of 2% of their core business revenue derived until an exemption clause was introduced to the Value-added and Non-value-added Business Tax Act (the "Act") to specifically exempt financial institutions from GBRT.

On 31 May 2005, the Legislative Yuan (Legislative Court) passed an amendment to the Act to delete the exemption clauses previously inserted in the Act. As such, subsequent to the amendment, financial institutions are now required to pay GBRT at a rate of 2% on their core business revenue derived.

Contact us

Australia

Jenny Clarke
+61 2 9335 7213
jeclarke@kpmg.com.au

Hong Kong

Charles Kinsley
+852 2826 8070
charles.kinsley@kpmg.com.hk

India

Naresh Makhijani
+91 22 2491 3131
nareshmakhijani@kpmg.com

Japan

James Dodds
+ 81 3 6229 8230
james.dodds@jp.kpmg.com

Malaysia

Shalet Marian
+60 3 2095 3388
shaletmarian@kpmg.com.my

Mauritius

Prakash Ramhotar
+230 207 8830
pramhotar@kpmg.intnet.mu

New Zealand

Brahma Sharma
+64 9 367 5816
bdsharma@kpmg.co.nz

Philippines

Francisco Tagao
+63 2 894 1833
fgtagao@kpmg.com.ph

PRC

Lewis Lu
+86 21 6288 1657
lewis.lu@kpmg.com.cn

Singapore

Eng Meng Leong
+65 6213 2417
meng@kpmg.com.sg

South Korea

Lee Jae Won
+82 2 2112 0955
jlee20@kr.kpmg.com

Sri Lanka

Premila Perera
+94 11 2426 501
premilaperera@kpmg.lk

Taiwan

Stephen Hsu
+886 2 2715 1815
stephenhsu@kpmg.com.tw

Thailand

Kullakattimas Benjamas
+66 2 677 2000
benjamas@kpmg.co.th

If you would like to subscribe for this publication, please contact Adam Williams on +852 2143 8792 or adam.williams@kpmg.com.hk of our Hong Kong office.

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