



Tax Update

February 2018 Tax Update highlights the following key points:

- ▶ **Some rulings have been released that provide guidance on the application of the interest deductibility limitation (20% of the total net profit generated from business activities plus loan interest expenses and amortization costs arising in the period (EBITDA)) that was contained in Decree 20/2017/ND-CP (Decree 20).**
- ▶ **Corporate income tax (CIT) and value added tax (VAT) treatments in cases where invoicing taken place some considerable time after the completion of the service to which the invoice relates.**
- ▶ **Foreign contractor tax (FCT) rate applicable to payments of purchasing software from overseas that are consumed outside Vietnam.**

The rules regarding the limitation of deductible interest expense contained in Decree 20 have raised various concerns to enterprises. Recently, local tax authorities have released a number of rulings to clarify some of the concerns. In particular:

One issue is whether the interest limitation rule in Decree 20 applies only to companies which have related party debt, or should be interpreted more broadly and apply to all companies with related party transactions, even where the only debt is from independent third parties. Two rulings have been released with two different points of view:

- ▶ Per Binh Duong Tax Department's ruling, the threshold of 20% EBITDA should only apply to enterprises with loan transactions with related parties.
(Official letter 21065/CT-TT&HT (OL 21065) dated 12 December 2017)
- ▶ Per Hanoi Tax Department's rulings, the 20% EBITDA limit applies to all interest expenses, regardless of whether the interest expense is in relation to loans from related parties or independent parties.
(OL 208/CT-TT&HT (OL 208) dated 3 January 2018;
OL 1990/CT-TTHT (OL 1990) dated 15 January 2018;
OL 3966/CT-TTHT (OL 3966) dated 24 January 2018)

As local tax authorities interpret this matter differently, we recommend enterprises having transactions with related parties and significant interest expense amount should consult with their tax authorities to ensure that their CIT finalization are compliant.

Additional other guidance on the limitation of deductible interest expense have been provided by the Hanoi Tax Department:

- ▶ The 20% EBITDA threshold applies to the total interest expense during the tax period in fiscal year 2017 (OL 208).
- ▶ When enterprises have negative EBITDA and transactions with related parties, the total interest expense incurred during the year will be non-deductible. However, it is unclear that whether the excluded interest expense will be allowed as a CIT deductible expense in the future when there is positive EBITDA (OL 1990).
- ▶ Any capitalized interest of a project is excluded from the total interest expense when determining the threshold of 20% EBITDA for CIT calculation (OL 3966).
- ▶ It is not possible to offset interest income on deposit or loan against interest expense when applying the threshold of 20% EBITDA to calculate deductible interest expenses for enterprise having related transactions (OL 3966).

We note that other tax authorities will not necessarily follow the same interpretation as the Hanoi Tax Department.

Official letter 11014/CT-TTHT (OL 11014) dated 9 November 2017 on the CIT and VAT treatment of expense for services where the invoicing occurs considerably later than the completion of the service.

When services have been completed but the invoicing occurs at a considerably later time (future years), an enterprise is unable to claim CIT deductible expense and VAT credit in the year when the services were completed due to the lack of supporting documents nor in the year when the invoices are issued as the invoiced amount do not correspond with revenue generated in the current year.

However, if an enterprise can locate invoices showing the actual time of services, proof of penalty payments from the suppliers for late issuing invoices and other supporting documents (if any), the invoiced amount can qualify as a CIT deductible expense in the year of the completed services. The enterprise can revise its CIT return accordingly.

Official letter 5763/TCT-CS (OL 5763) dated 15 December 2017 regarding the FCT rate applicable to payments of purchasing software from overseas that are consumed outside Vietnam.

The General Department of Taxation issued OL 5763 specifying that FCT applies to the payments for purchasing software from overseas then being sold and consumed outside Vietnam.

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