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November 2021

Hong Kong tax development

1 Hong Kong being put on the European Union's (EU) grey list of non-cooperative jurisdictions for tax purposes

The EU recently completed its review and concluded that the foreign sourced income exemption regime (FSIE) of Hong Kong is harmful insofar as foreign source passive income is concerned. Specifically, the EU is concerned that corporates with no substantial economic activity in Hong Kong are not subject to tax in respect of certain offshore passive income (such as interest and royalties), hence leading to circumstances of double non-taxation. As a result, Hong Kong has been included on the EU's grey list.

In its response to the EU's FSIE assessment on Hong Kong, the HKSAR Government stresses that Hong Kong will continue to adopt the territorial source principle of taxation in respect of both passive and active income. As such, the current thinking is that Hong Kong would not abolish its territorial source regime.

Instead, to avoid being blacklisted which may result in punitive measures being imposed on Hong Kong businesses by EU member states, Hong Kong has committed to amend or impose additional conditions, in line with the guidance on FSIE regimes (the Guidance), by the end of 2022 before the relevant passive income could be claimed as being offshore sourced in Hong Kong.

It appears that the HKSAR Government may wish to implement adequate substance requirements for the entities concerned in line with EU standards as it indicates that the proposed legislative amendments will merely target corporations with no substantial economic activity in Hong Kong, and make use of passive income to evade tax across a border.

The HKSAR Government further states that it will consult the stakeholders on the specific contents of the legislative amendments and strive to minimize the compliance burden of corporates.

Unlike the OECD/G20 Base Erosion and Profit Shifting Project (BEPS) 2.0 which will only affect large in-scope multinational enterprises, the impending changes as a result of the EU's FSIE assessment on Hong Kong will affect all taxpayers in Hong Kong, regardless of their industries and sizes.

While the Guidance has already prescribed the options that Hong Kong could adopt to remedy the features considered harmful by the EU, implementing any of these options with such a tight deadline is a challenge for both the HKSAR Government and taxpayers.

It is to be hoped that the HKSAR Government will set out the pros and cons of the available options and gauge the views of the stakeholders concerned before finalizing its response to the EU's FSIE assessment on Hong Kong.

PE firms that have Hong Kong entities in their structures should closely monitor the development in this regard and assess how the changes would impact their current operations or tax strategies. Professional tax advice should be sought where necessary.

Mainland China tax development

2 Stamp duty regulations evolved into law

As a part of the tax legislation process, the Standing Committee of the National People's Congress (NPC) of China has approved the Stamp Duty Law (the Law) in June 2021. The Law will become effective from 1 July 2022 and the current Stamp Duty Provisional Regulations issued by the State Council in 1988 will be abolished since then.

The Law retains the basic taxation regimes of the Provisional Regulations and makes several amendments, including:

- In order to encourage innovation, the Law lowers the tax rate of transfer agreement of trademark/ copyright/ patent/ special techniques from 0.05% to 0.03%, on an ad valorem basis.
- The Law confirms that the tax basis of stamp duty should exclude Value Added Tax (VAT) amount stated in the agreement. Therefore taxpayers should state VAT amount separately as far as possible to avoid potential tax dispute.
- Confirm the electronic orders between individuals and e-commerce business are exempt from stamp duty. In other words, online business-to-business orders shall be subject to stamp duty.
- Trade of stocks (including stock based depository receipt) is included as taxable by the Law. The tax rate remains unchanged at 0.1% and is levied on the seller only.
- If the taxable agreement doesn't state the amount of transaction, the taxable basis shall be recognized in the following order: 1) the actual executed amount; 2) the fair market value.

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2 Stamp duty regulations evolved into law (cont.)

Upon record filing with the Standing Committee of the NPC, the Law authorizes the State Council to set tax recession or exemption in three fields only: (1) guarantee the people's housing needs, (2) corporate restructuring and bankruptcy, (3) support the development of small and micro businesses. Besides, the State Council will also issue guidance regarding the tax reporting/ withholding for offshore taxpayers.

Generally speaking, the effectiveness of the Law would bring more certainty and transparency to taxpayers. Investors can keep close eyes on the optimization of Mainland China's business environment and emerging opportunities on Mainland China market.

Taiwan tax development

3 Amendment to capital gains tax law for transfers of real property

The Taiwan Legislative Yuan passed an amendment to the current capital gains tax law in respect of the transfer of real property (the New Law). The New Law is effective from 1 July 2021 and specifically applies to the transfer of real property acquired on or after 1 January 2016. The pre-amendment capital gains tax law applies to transfers of real property acquired before 1 January 2016. Under the New Law, the tax rates for capital gains derived from the transfer of real property have been increased and capital gains tax on indirect share transfers (where the transferred shares are "real property rich") has been introduced.

The New Law revised the current capital gains tax law in respect of the transfer of real property by: (1) increasing the progressive tax rates; (2) extending the taxing scope; and (3) reducing deductions when computing capital gains.

1. Increase in progressive tax rates

The capital gains tax on the transfer of real property situated in Taiwan is taxed at higher progressive rates subject to different holding periods under the New Law.

2. Extension of taxing scope

2.1 Transfers of pre-sold condominium/homes

Under the New Law, transfers of pre-sold condominiums/homes (either with or without land) by companies are treated as the transfer of real property and capital gains derived thereon are subject to the progressive rates (prior to the New Law, such transfer was not a taxable event). Relevant costs for acquiring the pre-sold condominium/homes can be deducted from the transaction amount when calculating the capital gains tax amount.

2.2 Indirect share transfers

Prior to the New Law, gains derived from the transfer of a foreign company's shares would be subject to capital gains tax on the transfer of real property if the value of shares being transferred substantially comprised Taiwanese real property (i.e., where more than 50% of the value of the shares or share capital of the company in question comprised Taiwanese real property, the shares were "real property rich"). Such gain derived from the transfer would be reclassified as capital gains from the transfer of real property rather than as a transfer of qualified securities and the progressive tax rates would apply. Based on additional guidance published on 30 June 2021, the value of the shares and share capital is determined based on the net asset value from the financial statements of the company.

Under the New Law, if the shares are "real property rich," regardless of whether the shares are of a foreign company or a Taiwanese company, the gain derived thereon would be reclassified as capital gains on the transfer of real property and the progressive rates under the New Law would apply from 1 July 2021. That is, the New Law also applies to the indirect transfer of foreign or Taiwanese shares as a result of a transfer of a foreign company's shares, as long as the shares being transferred are property rich.

Under the New Law, the calculation of the "real property rich" threshold may be different from the calculation under an applicable tax treaty. Instead of using net asset value from financial statements to determine the company's value, tax treaties usually use total asset value without taking into account debts or other liabilities when determining whether a company's shares are "real property rich" and thus a further analysis would be required when the taxpayer's resident jurisdiction has a tax treaty with Taiwan.

3. Reduced deductions when computing capital gains

The incremental value under the "land value incremental tax," based on government-appraised prices, could be deducted when computing capital gains under the pre-amendment law. However, under the New Law, the incremental value permitted to be deducted is limited to the amount accruing since the last transfer of the real property instead of the total incremental amount since the construction of the real property was completed.

Implications

Multinational enterprises with real property situated in Taiwan should consider the impact of the New Law on any potential transfers of real property, including any restructuring.

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Australia tax developments

4 Expansion to Australia's tax treaty network

The Australian Government has announced plans to enter into 10 new and updated tax treaties by 2023, building on the existing network of 45 bilateral tax treaties. It is expected that, post-expansion, Australia's tax treaty network will cover 80% of foreign investment in Australia and $6.3 trillion of Australia's two-way trade and investment. The Government has provided $11.6 million to Treasury and the Australian Taxation Office to support this expansion and submissions from stakeholders are being sought on the key outcomes to be negotiated and any other issues related to Australia's tax treaty network.

The press release has stated that phase 1 negotiations with India, Luxembourg and Iceland are occurring this year, while phase 2 negotiations with Greece, Portugal and Slovenia are scheduled to commence next year. The ratification of a tax treaty with Luxembourg, a domicile jurisdiction of a number of global private equity platforms, should have positive implications for such investors in Australia.

The negotiations are intended to update Australia's existing tax treaties with India and Greece, and establish new tax treaties with Luxembourg, Iceland, Portugal and Slovenia. As of October 2021, the remaining four countries with which negotiations are expected have been locked in but not yet announced.

In addition to OECD standard Limitation of Benefits Articles to be included in the new treaties, Australia has ratified the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) and has existing domestic legislation in relation to General Anti-Avoidance Rule (GAAR) which can apply to treaty shopping. Nonetheless, the expansion of Australia's tax treaty network is welcomed as a positive outcome for inbound investment into Australia.

5 Revised Corporate Collective Investment Vehicles (CCIV) exposure draft (ED) package release

The Australian Government has released a revised tax and regulatory ED package on CCIV, which was finalised in the 2021 budget announcement with an effective date of 1 July 2022. The CCIV is intended to attract foreign investors that are more familiar with corporate structures globally and expand opportunities to explore Australia's funds management expertise. The latest ED package builds on the CCIV regulatory package release in January 2019, and adjusts the 2019 CCIV taxation approach following submissions by EY and other stakeholders.

The tax improvements in the latest ED package are:

- the removal of previous proposals to apply company tax where a CCIV fails to meet eligibility requirements without the ability to frank a distribution;
- removal of proposals to remove the CGT discount at the CCIV level; and
- impose a new penalty, and streamlining the drafting approach.

There are a number of tax issues requiring further consideration, including the failure of widely held tests which would result in application of final CCIV tax of 45% (to some or all of the income), denial of treaty relief where CCIV is treated as trust, complexity of satisfying Attribution Managed Investment Trust (AMIT) widely held tests, competitiveness of non-resident withholding tax rules, and lack of broad tax relief where AMIT restructured into CCIV.

Notwithstanding the continued effort to establish an Australian CCIV vehicle for the domestic funds management industry, it is expected that global capital will continue to invest through global platforms (Corporate and non corporate CIVs) into Australia through existing platforms and vehicles which are typically domiciled offshore. Likewise, Australian private equity fund managers currently raise funds using other vehicles such as Venture Capital Limited Partnerships and Managed Investment Trusts.

India tax developments

6 Application of Most Favoured Nation (MFN) clause on subsequent OECD memberships

Recently, the Switzerland government issued clarification that the tax rate on dividend under India-Switzerland Double Taxation Avoidance Agreement (DTAA) shall be restricted to 5% pursuant to the MFN Clause. The notification also states "*Should reciprocity in the interpretation of the most favoured nation clause not be guaranteed by the Indian competent authority, the Swiss competent authority reserves the right to reverse this interpretation and to readjust the treaty rates applicable to income accruing as of 1 January 2023.*"

In 2011, India entered into tax treaties with Lithuania and Columbia which contained a lower rate of withholding tax (5%) in the source country. Lithuania became an OECD member on 5 July 2018, and Columbia became an OECD member on 8 April 2020. Given that Lithuania and Columbia became OECD member after treaty negotiations with India, there was an ambiguity on whether MFN clause can be invoked by relying on India-Columbia/ Lithuania DTAA.

The clarification issued by Swiss Government is consistent with the recent High Court rulings in case of Concentrix Services Netherlands BV WP (C) 9051/2020 and Optum Global Solutions International BV WP (C) 882/2021 (in the context of India-Netherlands DTAA) and Nestle SA (in the context of India-Switzerland DTAA) which had upheld 5% tax rate by relying on India-Columbia/ Lithuania DTAA.

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6 Application of Most Favoured Nation (MFN) clause on subsequent OECD memberships (cont.)

Multinationals and Private equity Funds considering an investment in India, and looking to benefit from a lower withholding tax can consider Netherlands, Switzerland and other countries where MFN clause is present as a platform for investing in India especially with the shift to a shareholder level taxation for dividends distributed by Indian companies.

It may be noted that this clarification is not binding on Indian tax authorities. The Indian tax authorities have not issued any guidance on the impact of the MFN in Switzerland, Netherland and other countries where MFN clause is present.

7 Foreign direct investment (FDI) in insurance and telecom sector

Recently, the Government of India have amended the FDI policy to increase the FDI cap in insurance sector up to 74% under automatic route and insurance Intermediaries (i.e. Insurance, re-insurance brokers, insurance consultants, corporate agents etc.) up to 100% under automatic route. Further, based on press release, we understand that the FDI in telecommunication sector will be made 100% under automatic route. The Government is yet to issue press note amending the change in cap of telecommunication sector in the FDI policy.

8 Relaxation in lock-in requirements

The shareholders (including financial / private equity investors) of Indian companies which are being listed and raising money through an initial public offer (IPO) were subject to certain lock-in conditions. In order to facilitate ease of doing business and to increase liquidity in the capital market, the Securities and Exchange Board of India (SEBI) has amended the law to relax the lock-in restriction as under:

- Promoter lock-in period of 3 years (from the date of IPO) of pre-IPO securities to the extent of 20% of post issued capital (Minimum Promoter contribution) have been reduced to 18 months in some cases subject to certain conditions. Further shareholding in excess of Minimum Promoter contribution has been reduced to 6 months from erstwhile lock-in period of 1 year;
- Non-promoter lock-in period of pre-IPO securities has been reduced from 1 year to 6 months from the date of IPO; and
- Minimum holding period of 1 year (from date of acquisition of pre-IPO shares) applicable to Venture Capital Funds, Foreign Venture Capital Investor, Category I and Category II Alternative Investment Fund have been reduced 6 months.

This move of SEBI will likely boost the sentiment of financial and private equity investors holding significant shareholding in Indian companies. Further, these relaxations may also encourage the companies/ promoters to pursue listing of it's shares.

Korea tax development

9 Korea announces 2021 tax reform proposals

Korea's Ministry of Economy and Finance announced the 2021 tax reform proposals (the 2021 Proposals) on 26 July 2021. Unless otherwise specified, the 2021 Proposals will generally become effective for fiscal years beginning on or after 1 January 2022.

Clarification of the deemed beneficial owner rules for overseas investment vehicles (OIV)

The current Korean tax law views an OIV as a deemed beneficial owner of Korean-source income if any of the following conditions are met:

(i) The OIV is subject to taxation in the jurisdiction in which it resides and there is no intention to wrongfully evade Korean tax on the Korean-source income by establishing the OIV in such jurisdiction.

(ii) The OIV is unable to substantiate its investors.

(iii) The OIV is deemed as the beneficial owner under a tax treaty.

The 2021 Proposals clarifies the conditions of (i) and (iii) as follows:

(i) The OIV should be obligated to pay tax in their country of residence and be eligible for tax treaty benefits for the applicable Korean-sourced income in accordance with the tax treaty.

(ii) The OIV is recognized as the beneficial owner of Korean-sourced income by a separate provision in the tax treaty and is subject to the benefits of the tax treaty for the applicable Korean-sourced income in accordance with the tax treaty. The rule will be effective for Korean-sourced income paid on or after 1 January 2022.

Revision of the 30% EBITDA interest limitation rule

The current 30% EBITDA interest limitation rule provides an ordering rule for the calculation of non-deductible interest. If interest is calculated with different interest rates, the interest deduction denial is applied starting with the highest interest rate.

The 2021 Proposals introduce additional ordering rules for the non-deductible portion of interest:

- For interest where the same interest rate is applied, the most recent borrowing date takes precedence.
- If the interest rate and borrowing date are the same, the non-deductible portion is bifurcated based on the ratio of the borrowed amounts.

9 Korea announces 2021 tax reform proposals (cont.)

In addition, the 2021 Proposals introduce a new rule that if the amount of EBITDA is negative, the deductible amount of interest is deemed to be nil.

This rule will be effective for fiscal years beginning on or after 1 January 2022.

Introduction of new rules for international transactions

The 2021 Proposals introduce the following new rules to mitigate potential tax evasion through international transactions:

- New obligation to submit information regarding the status of a liaison office of a foreign company (e.g., basic information of the liaison office, status of foreign headquarters and other domestic branch, among others).
- New obligation to submit transaction details by foreign companies supplying electronic services.
- Establishment of grounds for ex officio cancellation of simplified VAT registration.
- The current Enforcement Decree of Adjustment of International Taxes Act applies a penalty for late or false filing of transfer pricing (TP) documentation (e.g., Master/local files, Country by Country Report, etc.) for the maximum penalty of KRW100 million (US$87,000).
- The 2021 Proposals introduce new rules for reducing penalties for negligence for submitting revised or late TP documentation.

Amendment to transfer pricing under special economic conditions

To rationalize TP taxation under special circumstances such as COVID-19, the 2021 Proposals revise the TP rules under the current Law for the Coordination of International Tax Affairs (LCITA).

Extension of the deadline for submitting documents related to international transactions

The current Enforcement Decree of the Korean Corporate Income Tax Law (CITL) requires a permanent establishment (PE) of a foreign corporation to submit documents such as a statement of internal transactions, expense allocation, etc. for the transactions between a PE of a foreign corporation and its overseas headquarters and other branches within the statutory deadline for the CIT return.

The 2021 Proposals allows an extension of the above submission deadline from the statutory deadline of CIT return to within six months from the last day of the month containing the fiscal year end date.

This rule applies to submissions made on or after 1 January 2022.

Extension of the application period for special taxation for foreign workers

Under the current Restriction of Special Taxation Act, a foreign executive or employee (excluding workers hired on a daily basis) initially working in Korea before 31 December 2021 may elect to apply for a flat tax rate of 19% (excluding local income tax) on wage income without deductions, for five years from the first day of work in Korea.

The 2021 Proposals extend the application period from 31 December 2021 to 31 December 2023.

EU tax development

10 Global: OECD announces conceptual agreement in BEPS 2.0 project with G20 endorsing key components

On 1 July 2021, at the conclusion of two days of virtual meetings of the OECD/G20 Inclusive Framework on BEPS (the Inclusive Framework), the OECD released a Statement on a Two-Pillar Solution to Address the Tax Challenges Arising From the Digitalisation of the Economy (the Statement), which reflects agreement of 130 of the member jurisdictions of the Inclusive Framework in connection with the BEPS 2.0 project. The nine members of the Inclusive Framework that have not joined the Statement are Barbados, Estonia, Hungary, Ireland, Kenya, Nigeria, Peru, Saint Vincent and the Grenadines, and Sri Lanka.

The Statement describes agreed components with respect to both elements of the BEPS 2.0 project: Pillar One on revisions to nexus and profit allocation rules and Pillar Two on new global minimum tax rules. The Statement further indicates that remaining issues and a detailed implementation plan will be finalized by October 2021.

On 9–10 July 2021, the G20 Finance Ministers also endorsed the key components of the Statement.

The Statement is an important step in advancing the work on the BEPS 2.0 proposals for fundamental changes to global tax rules. However, it reflects a conceptual agreement and there is significant work to be done to flesh out the technical details and address the remaining open questions.

It is important for companies to follow these developments closely as they unfold in the coming months and to evaluate the potential impact of the proposals to their businesses. In addition, looking ahead, companies will need to monitor activity in relevant countries related to the implementation of these proposed rules through changes in domestic tax rules and bilateral or multilateral agreements.

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APAC Number 03013424
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