General tax update for financial institutions in Asia Pacific

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TAX

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AUDIT ▪ TAX ▪ ADVISORY

Country

Australia

Tax update

Legislative developments

- On 29 May 2008, the *Tax Laws Amendment (2008 Measures No 3) Bill 2008* (TLAB 3) was introduced into the House of Representatives

  Broadly, TLAB 3 proposes to amend the *ITAA 1997* to ensure that:

  - No amount is included in the assessable income of a shareholder in a company (or a unitholder in a unit trust) as a result of acquiring certain rights issued by the company to acquire further shares in the company (or as a result of acquiring certain rights issued by the trustee of the unit trust to acquire further units in the trust); and

  - An amount included in the assessable income of a shareholder as a result of acquiring rights issued by the company to dispose of shares is appropriately reflected in the cost base of the rights.

  The amendments are proposed to apply retrospectively to rights issued on or after 1 July 2001.

  These proposed amendments follow on from a media release issued by the Treasurer, Wayne Swan, on 8 April 2008 in which it was announced that the government would amend the income tax law to restore the long–standing income tax treatment of call options issued by companies that existed prior to the decision of the High Court of Australia in *Commissioner of Taxation v McNeil [2007] HCA 5*, which was handed down on 22 February 2007.

Other tax developments

- On 28 May 2008, the Australian Taxation Office (ATO) released Taxation Ruling TR 2008/3 (TR 2008/3) titled, *"Income tax: debt/equity – identification of any 'effectively non contingent obligation' of an issuer of a convertible note to provide 'financial benefits' for the purposes of Division 974 of th*e *Income Tax Assessment A*ct 1997 *if the note can be converted at any time at the issuer's discretion into shares that are equity interests in the issuer company"*.

  TR 2008/3 provides the Commissioner of Taxation's view on whether convertible notes with certain features (see below) will be treated as equity or debt instruments for Australian income tax purposes (i.e., will the convertible note result in payments of interest or dividends for Australian income tax purposes).

  TR 2008/3 applies to a scenario where a company issues a convertible note to a lender for a fixed or indefinite term and the convertible note has the following features:

  - The convertible note is issued under a scheme that is a financing arrangement for the issuer and is issued by a company for an issue price;
  - The issuer has the right to terminate the convertible note at any time by providing shares that are equity interests for Australian income tax purposes; and
  - Alternatively, if the issuer does not exercise its right to terminate the convertible note by providing an equity interest, the issuer must return the issue price to the lender at the end of the life of the convertible note.

The ruling states that the issuer of a convertible note does not have an 'effectively non-contingent obligation' to provide financial benefits for the purposes of the Australian debt/equity rules if the issuer can, at any time of its choosing after issue, exercise a discretion to convert the note into an equity interest in the issuer company. Accordingly, the convertible note will be treated as an equity interest for Australian income tax purposes.

However, the Commissioner notes that there may be an exception to this principle where the option to convert is disregarded upon full consideration of the pricing, terms and conditions of the scheme under which the convertible note was issued.

- On 18 April 2008, the ATO released Taxpayer Alert 2008/7 (TA 2008/7) titled, "*Application of Part IVA of the Income Tax Assessment Act 1936 to 'wash sale' arrangements*". The taxpayer alert was issued after the release of Taxation Ruling TR 2008/1 (TR 2008/1) also titled, "*Application of Part IVA of the Income Tax Assessment Act 1936 to 'wash sale' arrangements*".

  A 'wash sale' is an arrangement under which an asset is disposed of, but there is no substantial change in the economic interest in the asset.

  TR 2008/1 and TA 2008/7 consider wash sale arrangements where a taxpayer disposes of (or otherwise deals with) a CGT asset and generates a capital or revenue loss, but where in substance there is no significant change in the taxpayer's economic exposure in the asset. This may occur where the interest in the asset is in some way reinstated by the taxpayer to apply a resulting capital loss (or a tax deduction) against a capital gain (or assessable income) which has already been derived or is expected to be derived.

  The Commissioner of Taxation has advised taxpayers to be cautious about 'wash sale' arrangements which reduce capital gains or generate tax deductions, as these arrangements may in certain circumstances be considered to be schemes to reduce income tax.

  Whilst the Commissioner of Taxation appears to be focusing on individual taxpayers (rather than corporate entities) on the basis of the example scenarios and discussion outlined in TA 2008/7 and TR 2008/1, it still has implications for corporate entities undertaking arrangements which may be viewed for Australian tax purposes as wash sale arrangements.

- On 12 March 2008, the Board of Taxation released a Position Paper titled "Review of the Foreign Source Income Anti-Tax-Deferral Regimes" which discusses possible reforms to Australia's foreign source income anti-tax-deferral regimes (i.e., the controlled foreign company (CFC) rules, the foreign investment fund (FIF) rules, transferor trust rules and the deemed present entitlement rules). A further paper was released in May 2008 in relation to the anti-tax deferral regimes.

  The Position Papers outlines the Board of Taxation's views on the high level principles which should apply in the future design of the foreign source income attribution rules.

  The Position Paper puts forward a number of significant proposals to reform the current attribution regimes. Importantly, we note that from a thin capitalisation perspective, there is an issue with controlled foreign entity equity (CFE equity) in that an Australian company which invests overseas is assumed to have funded all of its CFE equity, from equity dollar for dollar. This assumption results in an adverse impact on the thin capitalisation position of Australian companies and represents a disincentive for them to expand overseas. In this context, we understand that some taxpayers have used hybrids in the form of redeemable preference shares that are legal form equity and treated as debt for thin cap purposes.

We further note that in the May 2008 paper, it was indicated that the Section 23AJ dividend exemption may change. There is currently uncertainty as to whether any change to 23AJ would be effected under the Taxation of Financial Arrangements proposals (TOFA proposals).

- On Tuesday 13 May 2008, the Treasurer, Wayne Swan, handed down the Federal Budget for the 2008/2009 financial year (2008 Federal Budget).

  Some of the key proposals announced in the 2008 Federal Budget relating to income tax include:

  - The choice for taxpayers to early adopt the proposals relating to Taxation of Financial Arrangements Stages 3 and 4 (TOFA proposals) which seek to align the tax treatment of financial arrangements with their accounting treatment, are proposed to be removed. The TOFA proposals are now intended to apply from the first income year commencing on or after 1 July 2009;
  - The benchmark interest rate that applies to capital protected borrowing arrangements (and generally determines how much of the interest on the borrowing is attributed to the cost of the capital protection) is proposed to be adjusted. This is expected to increase the capital (i.e., non-deductible) component of the overall expense for arrangements;
  - It is proposed that the 30 percent non-final withholding tax regime for distributions of Australian sourced income (other than dividends, interest and royalties) by managed investment trusts to non-residents will be replaced by a final withholding tax regime.

    For distributions to investors in countries with which Australia has an effective exchange of information arrangement, the final withholding tax regime is proposed to be introduced in a phased manner, with a 22.5 percent non-final rate of withholding intended to apply from the 2009 income year to distributions (net of investors' deductions).

    In the 2010 income year, the rate is proposed to reduce to a 15 percent final rate of withholding tax and a 7.5 percent final rate of withholding tax is intended to apply to subsequent years.

    A final 30 percent rate of withholding is proposed to apply to distributions to investors in countries with which Australia does not have an effective exchange of information agreement.

China

Corporate Income Tax (CIT) consolidated filing for branches of banks incorporated in China

Under the new PRC CIT Law that came into effect on 1 January 2008, banks incorporated in China, including foreign invested banks that are incorporated in China, should file consolidated tax filings in respect of their branches in China. Under a consolidated year-end tax return, the losses of one branch, including losses brought forward from the previous year, may be utilised against the profits of another branch. However, losses brought forward from the previous year may only be utilised at the year end, and not in the quarterly provisional tax filings. As such, where there are losses brought forward, a bank might overpay provisional tax during the year and then apply for a tax refund after the year end.

There is also a new mechanism of sharing out tax revenue among the tax bureaux in charge of the head office and branches in other parts of China. In essence, 50 percent of the total quarterly provisional CIT paid shall be allocated to the tax bureau in charge of the head office, and the remaining 50 percent shall be allocated among the branches using a formula. The formula operates on three allocation keys, namely operating revenue, staff salaries and total assets.

Hong Kong SAR

Negotiations between the government of the Hong Kong Special Administrative Region and the government of Vietnam

The third round of negotiations for an agreement between Hong Kong and Vietnam for the avoidance of double taxation was held on 26-27 May 2008 in Hong Kong. Consensus was reached on all the provisions of the proposed Agreement, except that the Vietnamese Side has to seek approval from its relevant authority on a certain technical issues. The proposed agreement was started after the negotiation and both sides will endeavour to arrange for a formal signing of the proposed Agreement.

India

Cases update

Central Board of Direct Taxes (CBDT) prescribes method for determining expenditure in relation to income which does not form part of total income for disallowance under section 14A of the Income-tax Act, 1961

The CBDT has now prescribed the method to be followed by the tax officer in determining amount of expenditure in relation to income not includible in total income.

Income-tax (Fifth Amendment) Rules, 2008

- **Remittance made to a rating agency for providing commercial information is not 'fees for included services' and not taxable in India**

  ICICI Bank Ltd. v. DCIT *[2008] 20 SOT 453 (Mum)*
  The taxpayer, a banking company had appointed MIS, a credit rating agency, to assess its floating rate Euro notes. The taxpayer did not deduct tax at source from the payment made to MIS due to the fact that the taxpayer contended that MIS's activities were situated outside India and its payment was also settled outside India. The tax officer held that the taxpayer was carrying on its business in India and was not making payment to MIS from any source outside India. Therefore, taking into account the nature of transaction and other available information, the tax

officer held that these payments were technical services and that tax should have been deducted. On appeal, the first appellate authority confirmed the order of the tax officer.

On second appeal, the Mumbai Tribunal was of the view that regardless of what commercial information was gathered by MIS, the information was collected by use of technical expertise outside India and was provided to the taxpayer in return for payment received outside India. The taxpayer only received the related commercial information but not the technical know-how or technical expertise or any other technology on which the information was prepared.

The technical skill, expertise or technical know-how used in preparing the commercial information was not made available to the taxpayer and hence the remittance made by the taxpayer for obtaining such commercial information could not be treated as 'fees for included services' as per Article 12 of the DTAA between India and USA. So the Tribunal held that the taxpayer was not liable to deduct tax at source from the payment made.

- **Cost of acquisition of bonus shares acquired prior to 1 April 1981 can be taken at Fair Market Value as on 1 April 1981**

  Kern-Liebers International GmbH v DIT *(2008)170 Taxman 85 (AAR)*
  The applicant is a company incorporated in Germany which acquired a 26 percent shareholding of an Indian company, SSS Ltd. These shares were allotted to the applicant for the sale of plant and machinery to SSS Ltd. In addition, bonus shares and right issues were also allotted to the applicant. All shares were sold by the applicant to an Indian individual. The applicant computed the capital gain by taking the cost of acquisition of bonus shares allotted before 1 April, 1981 as equivalent to their fair market value on 1 April, 1981. The tax officer passed an order taking the cost of acquisition of the bonus shares as 'nil'.

  The applicant sought an advanced ruling from the Authority of Advance Ruling (AAR) on bonus shares acquired before 1st April 1981, and asked whether the fair market value prevailing on that date can be taken as the cost of acquisition based on the provisions of the Income-tax Act 1961 (the Act) for the purpose of computing capital gains.

  After examining the provisions of the Act, the AAR ruled that it is clear from Section 55(2) that any capital asset falling within the ambit of that clause and acquired before 1 April 1981, the cost of acquisition of the shares can be taken as the fair market value as on 1st April 1981. The AAR also referred to the decision of the Mumbai Tribunal in the case of Heinrich dE Fries GmbH 281 ITR 18 (Mum) (AT) where the same view was also adopted.

- **Concessional tax rate of 10 percent on long-term capital gains of a non-resident company selling original and bonus shares of an Indian company**

  Mcleod Russel India Ltd., *(2008) 299 ITR 79 (AAR)*
  The applicant, a resident Indian company, purchased equity shares of Moran Tea Company (India) Limited. from Moran Holdings Plc, U. K., a non-resident company. The shares sold by Moran Holdings Plc, U. K. to the applicant included original and bonus shares of Moran Tea Company (India) Limited. The transfer of these shares was not effected through the stock exchange.

  The applicant sought an advance ruling from the Authority for Advance

Ruling (AAR) on whether the long-term capital gain arising from the sale of original shares and bonus shares of Moran Tea Company (India) Limited will be subject to tax at the concessionary rate of 10 percent.

The Authority, after considering the case of Timken France SAS, In re [2007] 294 ITR 513 (AAR) which had similar facts, ruled that the benefit of the concessionary rate of 10 percent should be applied to non-residents/ foreign companies even if they are entitled to another relief in terms of the provisions of the Act.

- **Interest income received from overseas branches by an Indian branch of a foreign banking company is taxable in India**

  DCIT v. British Bank of Middle East *(2008) 19 SOT 730 (Mum)*
  The taxpayer had claimed exclusion of interest received from overseas branches since the taxpayer considered this interest as income from itself. However, the tax officer rejected the claim on the ground that the branch of a foreign company is a separate taxable entity and hence the interest income was taxable in India. On appeal, the first appellate authority reversed the order of the tax officer and decided the issue in favour of the taxpayer.

  On second appeal, the Mumbai Tribunal, after analyzing various conflicting decisions, concurred with the view taken in Dresdner Bank AG v. Asstt. CIT [2007] 108 ITD 3751 (Mum.) and held that the interest income should be taxable in India. The Tribunal restored the addition of interest which was excluded by the first appellate authority in the impugned order.

- **Tax includes "Surcharge" under India-USA Tax Treaty**

  CIT v. Arthusa Offshore Company *(2008) 169 Taxman 484 (Uttaranchal)*
  The Uttarakhand High Court held that for the purpose of comparing a tax rate under the domestic tax law and the difference from the tax rate under a DTAA, the tax rate under domestic tax law should include any surcharge.

  Under Article 14(2) of the DTAA signed with the United States of America, a company which is resident of United States of America is subject to tax in India at a higher rate to the one applicable to domestic companies but the difference in the tax rate cannot exceed 15 percent.

  The US Company offered the income to tax at the rate of 60 percent (i.e. 45 percent (excluding surcharge plus a difference of 15 percent as per Article 14(2) of the DTAA) as against the tax chargeable of 65 percent as per domestic tax law. The High Court held that it is taxable at the rate of 65 percent plus surcharge.

  The High Court distinguished the decision of the Mumbai Tribunal in the case of Bank of America Vs. Deputy Commissioner of Income Tax; (2001) 73 TTJ pg. 51.

  This decision is relevant for prior years since the current difference in rate of tax between a non-resident company and a resident company does not exceed 15 percent.

- **Deposit of share application money and subsequent attempt to convert it into loan would not amount to money lent in the ordinary course of business and thus deduction under section 36(1)(vii) is not allowed**

  DCIT v. Kanchanjunga Advertising (P). Ltd. *[2008] 21 SOT 234 (Del)*
  The taxpayer, a company engaged in the business of advertising, money lending and investment had applied for the shares of a company D and paid INR 50 Lakhs as application money. Since the company did not allot the shares to the taxpayer, it requested to convert the application money into a loan. The company did not accept this request and the taxpayer treated the application money as a bad debt and claimed it as a deduction under section 36(1)(vii). The tax officer held that loss of share application money invested was simply a loss of an investment and, accordingly, disallowed the taxpayer's claim for deduction. On appeal, the first appellate authority allowed the taxpayer's appeal.

  On second appeal, the Delhi Tribunal was of the view that the Memorandum of Association (MoA) of the taxpayer only authorised it to invest surplus funds and not to trade in shares. The deposit of INR 50 lakhs as share application money and subsequent attempt of the taxpayer to get the same converted into a loan would not amount to money lent in the ordinary course of a business of money lending. The Tribunal held that the clause 'in the ordinary course of business of banking or money lending' would not take into its ambit inter-corporate deposits which related to investment of surplus funds as permitted by the MoA of the taxpayer. The amount was never used in the ordinary course of business of advertising and financing nor money lending and the accounting entries made without the consent of D could not change the character of the share application money into loan, so as to fall within money lending business; therefore, the deposits could not be allowed as a bad debt under section 36(1)(vii) of the Act.

- **Receipt on account of 'Fraction Entitlement' is taxable under the head "Income from Capital Gains"**

  Kiran Nagji Nisar v ITO *reported (2008) 300 ITR (AT) 286.*
  Where an Indian company issues bonus shares in a certain ratio and the shareholder does not get a full share but gets a 'fraction entitlement', which is remunerated on sale of full shares by aggregation of all fraction entitlements and the amount proportionately distributed among those shareholders.

  The Mumbai Tribunal held that since any profit on sale of bonus shares received by a taxpayer is taxable under income from capital gains, this receipt of a 'fraction entitlement' is also taxable under the same head.

Indonesia

Recent regulations issued - Discounts on Treasury Bills (Surat Perbendaharaan Negara)

On 4 April 2008, the government of Indonesia issued regulation number 27/2008. Under this regulation, discounts on treasury bills will no longer be subject to 20 percent final withholding tax when derived by:

- An Indonesian bank or Indonesian branches of foreign banks with permanent establishments in Indonesia;
- Pension funds approved by the Minister of Finance (MoF);
- Mutual funds registered in the Capital Market Supervisory Agency within the first five years from the date of establishment.

The discounts derived by banks mentioned above will be included as taxable income and subject to corporate income tax.

While existing regulations exempt certain income of Pension Funds & Mutual Funds, and the nature of discounts is similar to the exempt income, the discounts are not specifically exempted. There is currently no further regulation clarifying these matters.

Use of book value for transfer of assets in merger transactions

On 13 March 2008, the MoF issued regulation 43/PMK.03/2008 regarding the use of book value in merger transactions, consolidations and expansions. A taxpayer undertaking a merger, consolidation or expansion is entitled to use the book value of assets, for transfer of those assets, provided that the following requirements are met:

- All tax liabilities of each business entity must be settled;
- An application must be filed to the Director General of Taxation stating the reason for/ purpose of the merger; and
- The business purposes test is met. (There is no current regulation clarifying this requirement).

Criteria for a taxpayer undertaking an expansion to be entitled to use book value of the assets for transfers are as follows:

- The taxpayer is not listed on the Indonesian Stock Exchange but intends to conduct an initial public offering;
- The taxpayer is listed on the Indonesian Stock Exchange and intends to "hive-off" a division by conducting an initial public offering.

The regulation also stipulates that the transferor of the assets is not allowed to transfer any tax losses to the transferee. This regulation is different from the previous regulation where unutilised tax losses of the transferor could be carried over to the transferee.

Korea

Reduction of Corporate Income Tax rate and alternative minimum tax rate

The current corporate tax rates (13 percent for first 100 million won of taxable income; 25 percent on taxable income exceeding 100 million won) will be reduced with changes being phased in over three years until 2010. In addition, the income brackets for each tax rate will also be expanded. Please refer to the table below:

Phased Reduction of Corporate Income Tax Rates

Current		Proposed Revision		
Tax Base	Rate	Tax Based	2008 to 2009	2010
Up to 100 million Won	13%	Up to 200 million Won	11%	10%
Exceeding 100 million Won	25%	Exceeding 200 million Won	22%	20%

The minimum tax rate (alternative minimum tax) on small and medium enterprises will also be reduced from the current 10 percent to 8 percent.

The Korean National Assembly is expected to pass the revision before the end of June 2008.

Signing bonus not considered a non-business purpose payment (Seomyun2team-125, 2008.01.17)

A recent ruling states that a signing bonus paid in accordance with an employment contract, which stipulates the payment is conditional on the employee working for a specified minimum period (i.e., if the employee fails to satisfy the conditions, a certain portion of the signing bonus would have to be returned) shall not be considered as a 'non-business purpose payment' under Article 53 of the Enforcement Decree of the Corporate Income Tax Law and therefore deductible for Korean tax law purposes.

A previous ruling (Seomyun1team-402, 2006.03.29) stated that an employer is required to withhold tax on signing bonus paid to an employee over the specified period over its respective employment contract for salary tax purposes. The previous ruling also stated if the signing bonus exceeds the respective employee's monthly salary amount and is thus not considered as an advance payment of salary, the signing bonus would be treated as a 'non–business purpose payment' and not deductible for Korean tax purposes.

Malaysia

Recent Exemption Order gazetted

Tax Exemption on Income Received by Non-resident Experts in Islamic Finance

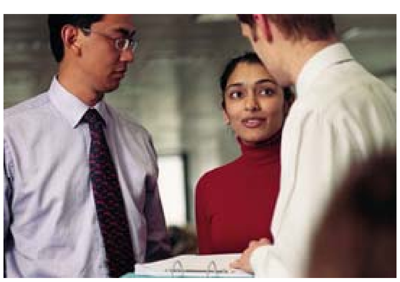
The tax exemption on income received by non resident experts in Islamic Finance announced in the 2008 Budget proposal has been gazetted. The exemption covers income under paragraph 4A(ii) of the Income Tax Act, 1967 which includes technical and advisory fees. To qualify for this exemption, the individual must be verified by the Malaysia International Islamic Financial Centre Secretariat as an expert in the field of Islamic Finance. This exemption is effective from 8 September 2007 until 31 December 2016.

Recent rules gazetted

Tax Treatment of Life Insurance Business – Transfer of Actuarial Surplus

It was announced in the 2008 Budget proposal that where an amount of actuarial surplus from the life fund is transferred to the shareholders' fund, any amount of tax charged on the portion of that surplus under the life fund will be allowed as a set-off against the tax charged on the chargeable income from the shareholders' fund of the insurer in respect of life business. The set-off rule has now been gazetted. The set-off amount is computed based on a specific formula. The amendment is effective from Year of Assessment 2008.

New Zealand



Individual income tax rates

The income tax rate thresholds for individuals are to be adjusted, with changes being phased in over three and a half years. The new structure, effective from 1 October 2008, is as follows:

0 – 14,000	12.5%
14,001 – 40,000	21%
40,001 – 70,000	33%
70,001 +	39%

These thresholds are to be gradually increased over a period between 1 October 2008 and 1 April 2011.

NZ-US Double Tax Agreement

The New Zealand government will soon enter into negotiations with the United States regarding the updating of the current double tax agreement between the countries. The negotiations are expected to begin in June, and will likely include technical improvements as well as possible changes to the non-resident withholding tax rates.

June Tax Bill

The government proposes to issue draft legislation in June which will, once passed, bring into effect the active/passive income distinction for offshore income for New Zealand companies. This will mean that active income earned by the overseas subsidiaries of a New Zealand resident company will be exempted from taxation in New Zealand.

At present New Zealand companies are not taxed on their subsidiaries' offshore earnings if the subsidiary is in a "grey list" country. This list of originally eight countries is to be reduced to only one – Australia – as a result of the introduction of the active/passive exemption. Australia remains on the grey list as it is usually the first choice to which the New Zealand companies wish to expand overseas, and is therefore expected to reduce compliance costs.

Interest allocation rules are also to be introduced, to prevent New Zealand companies from excessively borrowing in New Zealand where a deduction is available for the interest expense, and from investing the funds in active offshore operations as the income of which will not be subject to tax in New Zealand.

Philippines

Tax developments

- On 21 February 2008, the Bureau of Internal Revenue (BIR) issued Revenue Memorandum Circular (RMC) No. 21-2008 which clarified the persons liable to the Stock Transaction Tax (STT) and Initial Public Offering (IPO) Tax.

- For the STT, it is the duty of the stockbroker to file the tax return (BIR Form 2552) and pay the tax due after collecting the same from the seller, within five banking days from the date of collection.

  For the IPO tax, the person liable in the case of a "primary offering" is the issuing corporation, while the seller is the one primarily liable in the case of a "secondary offering".

- On 24 March 2008, the BIR issued Revenue Memorandum Circular No. 26-2008 to notify taxpayers that the BIR subscribes to the Organization for Economic Co-operation and Development (OECD) Transfer Pricing Guidelines as its Interim Transfer Pricing Guidelines while revising the final draft of the Revenue Regulations on Transfer Pricing.

  The circular further provides that until the Revenue Regulations on Transfer Pricing are issued, any and all concerns/ issues related to transfer pricing shall be resolved in accordance with the principles laid down by the OECD Transfer Pricing Guidelines.

- On 1 April 2008, the BIR issued Revenue Memorandum Circular No. 30–2008 which clarified the taxability of insurance companies for minimum corporate income tax (MCIT), business tax, and documentary stamp tax (DST) purposes.

MCIT of Life and Non-Life Insurance Companies

For purposes of computing the 2 percent MCIT of life and non-life insurance companies, gross revenue shall include direct premium and reinsurance assumed (net of returns, cancellations), miscellaneous income, investment income not subject to final tax, released reserve, and all other items treated as gross income under Section 32 of the Tax Code.

The cost of services or direct costs and identifiable direct revenue-related deductions are those costs which are exclusively related, or otherwise considered indispensable to the creation of the revenue from their business activity as an insurance company, which include the generation of investment income not subject to final income taxes, and shall be limited to the following:

1. Claims, losses, maturities and benefits net of reinsurance recoveries;
2. Additions required by law to reserve fund; and
3. Reinsurance ceded.

Business Tax of Life Insurance Companies

Premiums received, as well as re-insurance fees, reinstatement fees, renewal fees and penalties paid to a life insurance company which are incidental to or in connection with the insurance policy contracts issued are subject to premium tax at the rate of 5 percent, based on the gross amount received.

Management fees, rental income or other income from unrelated services which can be pursued independently of the insurance business activity are not subject to the 5 percent premium tax. Rather, these are treated as income for services subject to VAT or to the percentage tax, as the case may be.

Investment income realised from the investment of premiums earned by life insurance companies is considered exempt from the further imposition of business tax since the premiums which are the source of the funds invested have already been subject to the 5 percent premium tax.

Income earned from the use of funds solicited and pooled from policyholders to invest in various marketable securities, instruments, and other financial products which funds are recognised as liabilities by the life insurance company and which can be withdrawn by the policyholders anytime are considered as income earned from performing quasi-banking functions and is subject to the gross receipts tax imposed under Section 121 of the Tax Code.

The circular also clarified the taxability of other financial services sold by life insurance companies such as the Variable Unit Link and the Premium Deposit Fund.

DST of Life Insurance Companies

With respect to life insurance policies issued, the same is subject to DST pursuant to Section 183 of the Tax Code.

For group insurance policies issued, the premium collected is also subject to DST pursuant to Section 183. However, for the individual certificates issued to each employee covered by a group insurance policy, the issuance of each certificate is subject to DST under Section 188 of the Tax Code. With regard to health and accident insurance, the same is subject to DST pursuant to Section 185 of the Tax Code.

Business Tax of Non-Life Insurance Companies

The "gross receipts" of non-life insurance companies (except crop insurance) are subject to the imposition of VAT. This includes the total premiums collected and premiums received from a health and accident insurance contract underwritten by the non-life insurance companies.

The following non-life insurance companies are subject to VAT on gross premiums received:

a. Marine, fire and casualty insurance companies;
b. Surety, fidelity, indemnity and bonding companies;
c. Mutual benefit associations;
d. Government owned or controlled corporations engaged in the business of non-life insurance;
e. Non-stock, non-profit organisations and cooperatives engaged in the business of non-life insurance; and
f. All other persons, whether individual, trust/estate, partnership, association, joint venture, or corporation engaging in the non-life insurance business, such as but not limited to resident foreign persons rendering non-life insurance services in the Philippines in the course of trade or business.

"Gross receipts" however do not include the following:

a. Premiums refunded within 6 months after payment on account of rejection of risk or returned for other reasons to the person insured (return premiums);
b. Premiums on reinsurance of a company that has already paid the tax;
c. Premiums on account of any reinsurance, if the risk insured against covers property located outside the Philippines;
d. DST and local taxes passed on by the insurance company to the insured; and
e. VAT passed on to the insured.

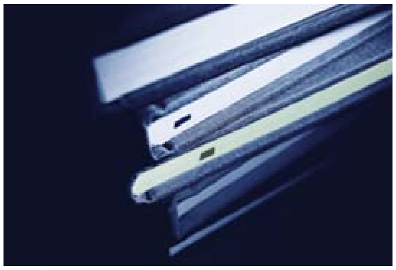
DST of Non-Life Insurance Companies

With respect to insurance policies other than health and accident insurance policies, the same is subject to DST pursuant to Section 184 of the Tax Code.

With regard to health and accident insurance policies the basis for the payment of DST is Section 185 of the Tax Code.

For certificates including Certificate of Cover pertinent to motor vehicle insurances, the same is subject to DST pursuant to Section 188 of the Tax Code.

Singapore



Renewal of Financial Sector Incentive (FSI) Awards

(a) FSI-Standard Tier (FSI-ST)

The FSI-ST awards for companies that were automatically transited into FSI-ST on 1 January 2004 would end on 31 December 2008. To renew their FSI-ST awards for a further five years with effect from 1 January 2009, these companies must have a minimum of six professionals substantially engaged in qualifying activities.

Similarly, for (i) fund managers that were automatically transited into the FSI (Fund Management) (FSI-FM) awards on 1 January 2004 and (ii) companies that were approved for the FSI-ST awards after 1 January 2004, they may renew their FSI-FM and FSI-ST awards if they can demonstrate incremental commitments to Singapore.

(b) FSI-Enhanced Tier (FSI-ET)

The renewal of these awards would similarly depend on the incremental commitments to Singapore.

Qualifying Base (QB)

The initial QB for companies that were automatically transited into FSI-ST (excluding those carrying out fund management or investment advisory services only) on 1 January 2004 would be applicable until 31 December 2008. Thereafter, companies are required to compute the subsequent QB.

As a concession, if the FSI award for these companies is renewed for a further five years effective from 1 January 2009, the initial QB may continue to be used during the renewal period until 31 December 2010. However, this does not apply to companies with an initial QB of 100 percent or 0 percent.

Enhancement to FSI Scheme re: Project and Infrastructure Finance (FSI-PF)

The tax incentives for project financing which are due to expire after 31 December 2008 will be renewed as follows:

i. exemption of qualifying income from qualifying project debt securities issued during the period 1 January 2009 to 31 December 2013;

ii. exemption of foreign-sourced interest income of qualifying entities (including companies incorporated in Singapore, business trusts registered in Singapore and trusts established in Singapore) listed on the Singapore Exchange that invest in offshore qualifying infrastructure projects/assets;

iii. remission of stamp duty payable on the instrument of transfer (executed the period from 1 January 2009 to 31 December 2011) relating to qualifying infrastructure projects/assets to entities listed or to be listed on the Singapore Exchange; and

iv. concessionary tax rate of 5 percent on income derived by a FSI (Project Finance) company from specified qualifying activities and from project finance advisory services related to a qualifying infrastructure project, provided that application is made on or before 31 December 2011.

In addition to the above, a concessionary rate of tax of 10 percent will be granted for a period not exceeding 10 years on the following:

a. In the case of a qualifying Registered Business Trust, the concession would be accorded to an approved Trustee Manager on qualifying income from offshore infrastructure assets in connection with the management and operation of the qualifying Registered Business Trust.
b. In the case of a qualifying infrastructure fund, the concession would be accorded to an approved fund manager on qualifying income from offshore infrastructure assets in connection with managing the qualifying infrastructure fund.

Enhancement to FSI Scheme re: Credit Facilities Syndication (FSI-CFS)

The FSI-CFS award would be enhanced to allow more lending arrangements to qualify for the 5 percent concessionary tax rate.

The Monetary Authority of Singapore is expected to release details of the enhancements to the FSI-CFS award at a later date.

Merging of the FSI (Bond Market) (FSI-BM), FSI-CFS and FSI-PF

The existing FSI-BM, FSI-CFS and FSI-PF awards will be merged into a new FSI (Debt Capital Market) (FSI-DCM) award. All the existing qualifying criteria and conditions for the respective awards remain applicable.

Enhancement to FSI Scheme re: Islamic Finance

A new FSI(Enhanced Tier) (FSI-ET) award for Islamic finance (known as "FSI–IF") to grant a concessionary tax rate of 5 percent (subject to conditions) on the qualifying income derived from qualifying Shariah-compliant activities such as lending and related activities and fund management and other fund investment advisory services has been introduced.

In addition to the above, a 5 percent concessionary tax rate will also be granted under the Offshore Insurance Business (OIB) Scheme – Takaful (Islamic Insurance) and Retakaful (Islamic Reinsurance) to the relevant income derived from Shariah-complaint activities performed by a qualifying insurer. The approval period for the OIB award is from 1 April 2008 to 31 March 2013. The award is for a period of five years.

Sri Lanka

New regulations on transfer pricing rules

Sri Lanka imposed arm's length pricing on transactions between associated undertakings effective from 1 April 2006.

Regulations prescribing the following and thus endorsing the practical application of transfer pricing was however gazetted only on 22 April 2008 and covers the following areas.

- "Control" for triggering associated undertaking status
- Transaction thresholds for application of transfer pricing
- Pricing methodologies
- Prescribed documentation
- Advanced pricing agreements.

Transfer pricing covers both cross border and domestic transactions.

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