CHAPTER 7 **TAXATION AND TRANSFER PRICING**

OVERVIEW

Resolution 43 on supporting the socio-economic recovery and development program,[1] including the policy of reducing the Value-Added Tax ("VAT") rate by 2 per cent, implemented in the past two years, has brought many positive effects for businesses and individuals. We support the decision to extend the VAT rate reduction to 8 per cent until the end of 2023 and hope that it will be extended until 30 June 2024 to provide support due to the impact of slower global growth and trade on the economy.

We also appreciate that the business community has the opportunity to contribute to many important law amendments, including to the Laws on VAT and Corporate Income Tax ("CIT"), and to provide input in relation to the adoption of the Global Minimum Tax. We look forward to continuing to provide our suggestions for improving the tax environment in Vietnam.

I. CORPORATE INCOME TAX POLICIES TO ADAPT WITH THE IMPACT OF GLOBAL MINIMUM TAX RATE – 15 PER CENT (OECD PILLAR 2)

Relevant authorities: Ministry of Finance (MOF), General Department of Taxation (GDT)

Issue Description

The EU member states agreed to implement the Global Minimum Tax Rate of 15 per cent (OECD Pillar 2) for fiscal years beginning 31 December 2023. Other leading investors in Vietnam including Korea and Japan enacted regulations to give effect to Pillar 2 from 2024.

To implement Pillar 2, Vietnam introduced a draft resolution in July 2023 to collect the top-up taxes under 02 mechanisms including the Qualified Domestic Minimum Top-up Tax ("QDMTT") and the Income Inclusion rule ("IIR").

One of biggest concerns in relation to Pillar 2 is the impact on new foreign investment, and for current investors that the benefits of tax incentives previously granted would be lost or reduced.

Potential gains/concerns for Vietnam

Regarding the implementation of extra taxes under Pillar 2, there is significant interest among businesses, notably multinational companies operating in Vietnam and major Vietnamese corporations with overseas investments, about the implications of this global tax reform. Specifically:

- Whether the tax incentives which companies have been or would be entitled will be reduced or lost? This could impact decisions to make investment in Vietnam for current or new foreign investors since tax incentives are an important factor, together with the overall investment environment, in foreign investment attraction, which is a key source of capital, technology, and knowhow.
- What policies the Vietnam Government could introduce to encourage foreign investment for current and prospective investors affected by Pillar 2 when the tax incentive benefits are reduced, lost or no longer available?

This issue is particularly important when Vietnam is currently making efforts to attract the leading global companies in targeted sectors to enable the economic growth strategy of Vietnam in the years to come.

1 Resolution 43/2022/QH15 dated 11 January 2022 of the National Assembly on fiscal and monetary policies for supporting socio-economic recovery and development program.

From recent observations of international developments, many countries which have declared they will adopt Pillar 2, have drafted local corporate income tax laws to consider other tax benefits in response to Pillar 2.

Recommendations

We would like to recommend:

- Vietnam Government take the opportunity presented by Pillar 2 to undertake a comprehensive review of the tax incentives currently in place. This includes studying the impacts of Pillar 2 on current and future investors and considering practical and effective solutions for encouraged sectors so that Pillar 2 adoption does not create negative impacts on the investment environment and Vietnam still meets its commitments under Pillar 2.
    - For example, if expenditure-based incentives were to be introduced instead of income-based, such as tax holidays, there would be less impacts from Pillar 2 adoption on foreign investment. Accordingly, foreign investments could be increased for targeted sectors and locations and the commitments under Pillar 2 would still be met.
    - Examples of expenditure-based incentives that could be considered with reference to international practice including (i) accelerated depreciation for machinery and equipment of the investment projects and (ii) double tax deduction of labour cost or research and development (R&D) costs for encouraged investment projects.
    - Such expenditure-based incentives may increase the likelihood of generating additional investment as they directly target investment expenses.
- In addition to encouraging investment in R&D, innovation and high-technology incentives could be targeted to support policy objectives such as promoting the green transition;
- Tax revenues generated from QDMTT could additionally be spent on areas to continue to improve the overall investment environment such as infrastructure and labour force skills development; and
- Pillar 2 provides a very good opportunity for Vietnam to consider tax incentive reform, and this should be done as soon as possible so as not to lose either tax revenues or foreign investment, as other countries will impose top-up taxes from 2024 and are also considering revising their tax incentive regimes in response.

II. INPUT VALUE ADDED TAX (VAT) CREDITIBLITY AND CORPORATE INCOME TAX DEDUCTIBILITY OF INVOICES FROM RUN-AWAY VENDORS

Relevant authorities: Ministry of Finance (MOF), General Department of Taxation (GDT)

Issue Description

The Vietnam tax authorities publish a list of run-away vendors who have ceased operation without proper notification and contact the direct customers to deny input VAT credits and tax deductions in relation to the invoices issued by those vendors, including invoices issued a long time in the past.

Potential gains/concerns for Vietnam

While enterprises always seek to comply with the prevailing tax regulations and collaborate with the tax authorities to prevent tax fraud, the denial of VAT credit and corporate income tax deductions for all invoices from the run-away vendors is not reasonable because the enterprises (i) have actually bought goods or used services for their business purposes, (ii) have received and fully paid the valid invoices from/to the relevant vendors and (iii) are not in a position to validate/monitor the daily business operations of those vendors.

The denial of VAT input credits and tax deductions can result in significant tax exposures, including additional tax liabilities, late payment interest and penalties.

Recommendations

We would like to recommend as follows:

- To create fairness and transparency for the enterprises, the tax authorities should consider accepting tax credit and deduction of valid invoices with proper payment and supporting documents from the consumer's perspective. Dealing with the run-away vendors should be handled separately by way of legal investigation.

III. ENHANCING EFFECTIVENESS OF DISPUTE RESOLUTION MECHANISM BY ADVANCE PRICING AGREEMENTS ("APA") AND MUTUAL AGREEMENT PROCEDURE ("MAP")

Relevant authorities: Ministry of Finance (MOF), General Department of Taxation (GDT)

Issue Description

1. Advance Pricing Agreements (APAs)

APA is a prospective dispute resolution mechanism for cross-border transfer pricing transactions. They provide tax certainty for taxpayers and tax administrations by negotiating the terms of transfer pricing transactions upfront. This minimises onerous transfer pricing documentation requirements, as well as mitigating the risk of audit, litigation and double taxation.

Vietnam introduced the APA program in 2013 with Circular 201, which Circular has been replaced by Circular 45 in 2021. Circular 45 is effective from August 2021.

Under the provisions of Circular 45 the APA period of 5 years has been reduced to 3 years, furthermore no roll-back option has been implemented.

Ten years after the implementation of the APA program, despite the numerous APA applications which have been submitted by multinational companies and applications, which have been accepted by the Vietnamese competent authorities to the APA program, Vietnam still has not concluded and implemented APAs. The evaluations and assessment of the APA applications by the Vietnamese competent authority moves slowly, in most of the APA applications in the last years, taxpayers did not experience any developments.

The reduced effective duration of the APA, the lack of the roll back option and the long processing time taxpayers experienced, made the APA application lose its goal as a dispute prevention instrument.

With regards to the numerous APA applications submitted to the Vietnamese competent authority, Vietnam should consider shortening the time spent on evaluation, assessment process, continue the APA negotiation process with the overseas competent authorities and reach agreement in a short period of time.

Furthermore, to enhance the effectiveness of the APA in the future, we recommend that Vietnamese competent authority considers implementing a reasonable timeframe for evaluating, assessing and negotiating the APA applications. Generally, in international practice, an APA application may reach an agreement between two countries' competent authorities in approximately two years after the submission of the application.

In terms of the effective duration, we recommend considering to re-introduce the 5-year effective period, which, in general, is in line with international practice. Furthermore, the roll-back option could provide an effective solution for a potentially longer processing period.

2. Mutual Agreement Procedure (MAP)

The MAP is an instrument for the resolution of international tax disputes whenever a taxpayer considers that the actions of one or both contracting states' tax administrations result in taxation not in accordance with the provisions of a tax treaty.

Vietnam has signed double tax treaties with around 80 countries; therefore Vietnam has the necessary legal framework to manage mutual agreement procedures.

However, in practice based on multinational companies' experience, the applications for a mutual agreement procedure submitted to the Ministry of Finance do not move forward, there have been either little or no developments. There has been no application under mutual agreement procedure in transfer pricing-related matters, which has reached agreement and settlement.

Furthermore, we have seen cases where the provincial tax departments refused to receive the Double Taxation Agreement ("DTA") applications because the taxpayers could not provide the certificates of tax residence for the current year. Such refusals are unreasonable because no tax jurisdictions issue certificates of tax residence for the current year. On the other hand, taxpayers could not declare their tax exemption eligibility on the tax forms because of such unreasonable rejections and had to pay double taxes. After that, taxpayers would have to revise the tax forms to report their tax exemption eligibility, prepare applications for tax rebates and hope that they would get refunds for the overpaid tax portions, which hardly ever happen in reality. It has been observed and reported that the tax refund procedures are extremely slow, strangled with red tape and seem to be done deliberately.

Recommendations

We would like to recommend as follows:

- It is recommended that the time for of evaluating and negotiating the applications is shortened and consideration is given to conclude MAP applications within a reasonable timeframe;
- The procedures for DTA application should also be revised so that taxpayers can declare their eligibility and don't have to pay taxes outright from the beginning, instead of having to pay taxes upfront and expect to receive tax refunds down the line when the supporting documentation is available;
- In addition, if the tax authorities refuse to receive DTA applications, they should be obligated to provide a written explanation of their legal grounds for such refusals based on quotes of tax laws and regulations, instead of advising the taxpayers verbally.

IV. DEDUCTIBILITY OF MARKETING/SALES SUPPORT OFFERING TO INDIRECT CUSTOMERS IN A DISTRIBUTION CHAIN

Relevant authorities: Ministry of Finance (MOF), General Department of Taxation (GDT)

Issue description

To better boost sales in a distribution chain, an enterprise will provide sales supports or conduct promotion programs benefiting its direct distributor's customers ("the indirect customers"). This is a business operation model that is very popular globally and contributes to increasing the enterprise's revenue.

However, the tax authorities currently do not accept tax deductions for to sales support/ promotion expenditures to the indirect customers based on the argument that such expenditures should have been the obligation of the enterprise's distributor, rather than the enterprise.

Recommendations

We would like to recommend as follows:

- Government of Vietnam should amend relevant regulations to allow such expenditure to be acceptable for tax deduction on the basis such expenditure directly contributes in increasing revenue of the enterprises.

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Tax & Transfer Pricing Sector Committee of EuroCham