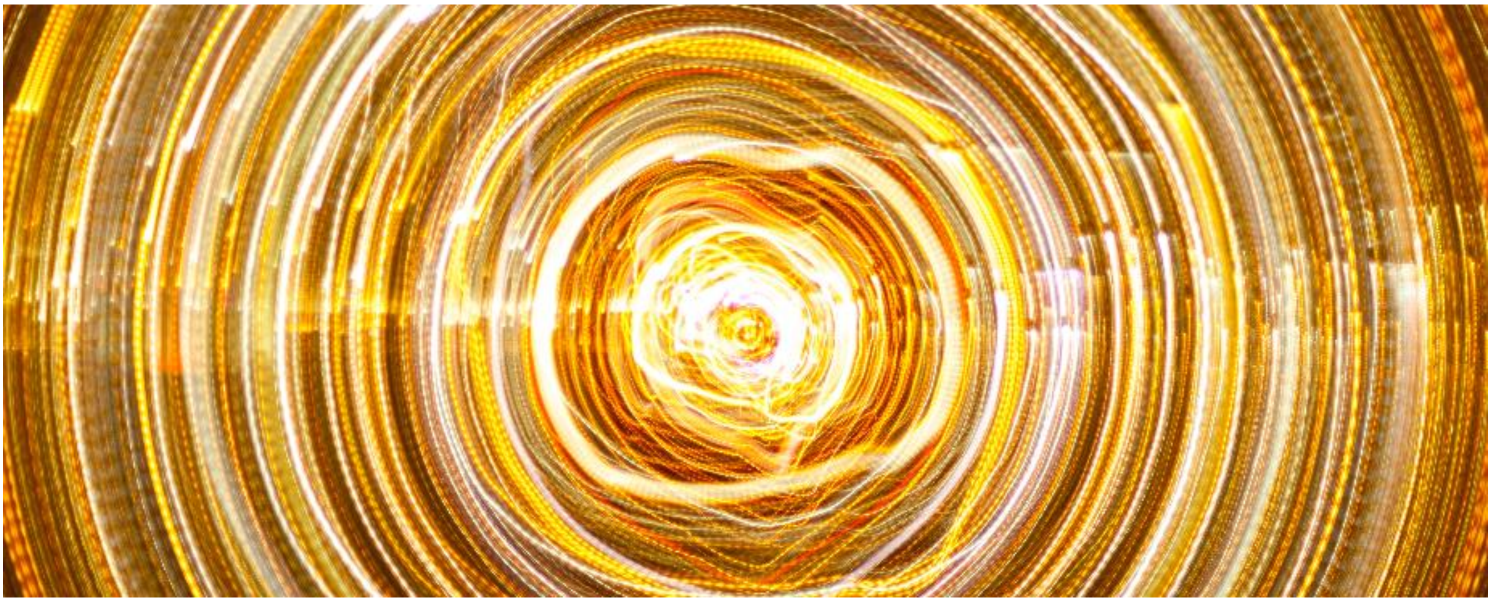

Transfer Pricing Sharing Series

Episode No. 03: Decree amending the cap on deductible interest expenses: Matters to consider and proposed action

20 July 2020

Our sharing series will cover the following key areas:

1. Supply chain disruption due to Covid-19 – How existing group supply chain model may require long-term changes and what potential risks may be involved. Please refer the link for details.
2. Pre-Covid-19 intra-group pricing arrangements may potentially become irrelevant and the need to revaluate them. Please refer the link for details.
3. Amending regulations on interest deductibility cap: What enterprises should consider and proposed action.
4. Planning ahead for loss-making or fluctuating profitability in periods impacted by Covid-19.
5. Business re-structuring from the perspective of specialists.
6. Are low-risk classified entities actually less impacted by Covid-19?
7. Covid-19's impact on APA negotiation and/or implementation process.
8. Transfer pricing audit trends: relaxation in approach for taxpayers or aggressive plan for State budget?

Introduction

Decree No. 20/2017/ND-CP ("Decree 20") issued on 24 February 2017, which stipulates the deductible interest expenses cap for Corporate Income Tax ("CIT") purpose in Clause 3, Article 8, has triggered numerous comments and questions from domestic and foreign business entities/economic organizations due to vague areas as well as significant impacts on the cash flows and tax expenses of companies, especially companies having a high leveraged capital structure.

In the aftermath of the Covid-19 pandemic, considering measures to support businesses in maintaining and developing production and business activities as well as promoting economic development, the Government has officially issued Decree No. 68/2020/ND- CP ("Decree 68") to amend Clause 3, Article 8, Decree 20. Accordingly, in Episode 03 of the series, Deloitte would like to provide detailed analysis and multi-dimensional perspectives related to Decree 68 to provide enterprises with a comprehensive viewpoint and proposed solutions in line with post-pandemic business strategy.

Notable changes

Subject	The regulation relates to the tax deductibility of interest expenses
Net interest	The rule applies to cap deductibility of the net interest expense (after deduction of interest income from bank deposits and lending incurred in the period). Previous regulation in Decree 20 does not allow the taxpayer to offset interest expense with interest income from bank deposits and lending.
30%	The deductible interest expense for CIT calculation purposes (after deduction of interest income from bank deposits and lending) over EBITDA – the total net profit from business activities plus interest expenses (after deduction of interest income from bank deposits and lending) and depreciation expenses within the tax period.
5 years[1]	The period for the non-deductible interest expenses (after deduction of interest income from bank deposits and lending) to be carried forward consecutively.
Form 01	This form replaces Form 01 under Decree 20.
Effectiveness	The Decree takes effect from 24 June 2020 and applied from tax period 2019 onwards. The Decree does not apply to credit, insurance institutes, and Government preferential loans.
2017-2018 period	
01 Jan 2021	The taxpayer re-determines deductible interest expense and CIT payable, and submits adjustment CIT returns to directly managing tax authority before 01 Jan 2021. Non-deductible interest expense of FY17-FY18 (after the re-determination) is not allowed to be carried forward into next tax periods.
5 years[2]	Overpaid CIT (including late payment interest, if any) after re-determination per Decree 68 can be **offset** into CIT payable **up to five (05) years from 2020**
Tax audited cases	In case tax audits/inspections have been conducted, taxpayers request local tax authorities to re-determine tax liability and corresponding late payment interest to offset against CIT liability within 5 years from 2020. This process will be carried out at tax authority site, not at taxpayer site. Tax investigation will not be re-opened.

Positive impacts

- Reduce certain tax burden, create opportunities to centralize resources to recover, maintain and promote business and production after the Covid-19 pandemic.
- Allow the interest income from bank deposit and lending to offset against the interest expense to calculate the interest cap, which optimizes the interest expense cap and relieve pressure on post-pandemic cash flow.
- Approaching international practice level in order to create a uniform mechanism for determining the deductible interest expense among subsidiaries from Group's perspective.

Notable considerations

- How to determine the interest expenses, interest income from deposits and loans
- Treatment in cases of tax periods that have been audited
- How to determine deductible interest expenses for taxpayers having multiple business segments with different tax rates/ incentives?

What should enterprises do?

Accounting – Tax Team

Board of Directors/ headquarters

2017 – 2018

Accounting – Tax Team

- Review, re-determine non-deductible interest expense exceeding the cap and overpaid/underpaid CIT amount;
- Submit adjustment CIT return;
- Work with the tax authority to re-determine tax duty in case of tax audited periods.

Board of Directors/ headquarters

- Evaluate the impact of the amended Decree on financial/tax plans and business activities in the short and long run to manage cash flow to recover, maintain and promote business activities after the pandemic.

2019

Accounting – Tax Team

- Review, re-determine non-deductible interest expense exceeding the cap and overpaid/underpaid CIT amount;
- Determine the impact of deferred income tax on the financial statements;
- Submit adjustment CIT return.

From 2020

Accounting – Tax Team

- Estimate the impact of Decree 68 on tax obligations of 2020 based on business and production plans;
- Update and standardize the method of determining deductible interest expenses for the purposes of tax declaration.

Board of Directors/ headquarters

- Discuss with headquarters to consider appropriate strategies related to the establishment/restructuring of the group's financial transactions/group's internal capital arrangement to optimize the interest net-off and five-year carried forward scheme;
- Consider the strategy to optimize tax costs of the Group for different levels:
  - Restructure the value chain/ financial transaction flow;
  - Restructure capital and cash flow;
  - Review and re-establish internal borrowing/lending policies to optimize the interest net-off scheme or carry-forward scheme.

In summary, we have provided our analysis and recommendations for your consideration in the context of applying Decree 68 on interest cap rule. We are pleased to discuss and clarify any concerns you may have. We are looking forward to working with you to overcome the difficult periods and future prosperous development.

Compliance review

- ❑ Assist in determination/review on the accuracy on determining deductible net interest expenses in accordance to Decree 68;
- ❑ Consult/assist in fulfilling tax compliance requirements for the tax periods 2017, 2018 and 2019;
- ❑ Determine the tax impact on the financial statements of relevant years (e.g. deferred income tax).

Assistance in working with Tax authority

- ❑ Assist in discussing and working directly with Tax authorities to clarify tax payer's concerns when determining deductible net interest expenses in accordance to Decree 68; and
- ❑ Assist in working with Tax authorities to request Tax authority to re-calculate the amount of payable CIT liabilities in 2017, 2018 and 2019.

Strategic advisory

- ❑Advise to develop strategy/restructuring financial transaction model in order to optimize the deductible net interest expenses/non-deductible net interest expenses during the current tax period which are carried forward to the next tax periods;
- ❑Advise to establish internal control policy for lending and borrowing activities with related parties from the company/group's perspective to implement new scheme;
- ❑Advise to establish internal control policy for other intragroup transactions for the Group to enhance the compliance position and optimize tax liability.

Next episode of our sharing series

In our subsequent sharing, we will discuss in more details how to plan ahead for the consequences of loss-making or fluctuating profitability in periods impacted by Covid-19.

Contact us

Thomas McClelland
National Tax Leader
+84 28 7101 4333
tmcclelland@deloitte.com

Dinh Mai Hanh
National TP Leader
+84 24 7105 0050
handinh@deloitte.com

Bui Ngoc Tuan
Tax Partner
+84 24 7105 0021
tbui@deloitte.com

Phan Vu Hoang
Tax Partner
+84 28 7101 4345
hoangphan@deloitte.com

Nguyen Thi Khanh Ha
Director
+84 28 710 14470
hatkng@deloitte.com

Tat Hong Quan
Director
+84 28 710 14341
quantat@deloitte.com

Hoang Thi Le Phuong
Senior Manager
+84 28 710 14373
phuongthoang@deloitte.com

Mukherjee Supratik
Senior Manager
+84 28 710 14450
supmukherjee@deloitte.com

Ha Duc Thanh
Senior Manager
+84 24 710 50105
thanhha@deloitte.com

Le Na
Senior Manager
+84 24 710 50035
nale@deloitte.com

Nguyen Trung Ngan
Manager
+84 24 710 50098
ngantnguyen@deloitte.com

Tang Minh Tung
Manager
+84 28 710 14363
tungtang@deloitte.com

Tran Hong Anh
Manager
+84 24 710 50063
anhtran@deloitte.com

Hanoi Office
15th Floor, Vinaconex Building,
34 Lang Ha Street, Dong Da District,
Hanoi, Vietnam
Tel: +84 24 7105 0000
Fax: +84 24 6288 5678

Ho Chi Minh City Office
18th Floor, Times Square Building,
57-69F Dong Khoi Street, District 1,
Ho Chi Minh City, Vietnam
Tel: +84 28 7101 4555
Fax: +84 28 3910 0750