

J.P. MORGAN TSS GLOBAL TAX SERVICES –  
EMERGING MARKETS TAX SEMINAR

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## Brazil – IOF Tax Changes

# Brazil – *Imposto sobre Operacoes Financeiras* (IOF tax) - Overview

The Imposto sobre Operacoes Financeiras (IOF) is a tax on credit, exchange, insurance and securities transactions.

There are two types of IOF:

- IOF tax applicable on Foreign Exchange (FX) transactions
- IOF tax applicable on short term securities.

## **IOF on Foreign Exchange transactions**

The IOF on FX transactions is assessed by applying the rate over the value of the Foreign Exchange value. The Bank carrying out the Foreign Exchange transaction is the withholding agent. The IOF tax changes often and these changes are based on the Monetary Policy of the Brazilian Central Bank. There have been several changes in the IOF tax rate applicable to FX transactions in late 2010 and beginning of 2011. As of January 1, 2011 the IOF tax applies to Resolution 2689 Investments as follows:

### Inflow:

- Foreign Exchange transactions related to equities, derivatives negotiated on the exchange are subject to the IOF at a rate of 2%.
- Foreign Exchange transactions related to Private Equity Funds (FIPs), emerging companies investment funds (FIEEs) are subject to the IOF at a rate of 2%.
- Foreign Exchange transactions related to fixed income instruments and other instruments other than equities, private equity funds, emerging market funds are subject to the IOF at a rate of 6%.

## Brazil – *Imposto sobre Operacoes Financeiras* (IOF tax) - Overview

- Foreign exchange transactions carried out from January 1, 2011, for the entry into Brazil of funds in connection with the cancellation of depositary receipts into local shares, are subject to the IOF Exchange at the rate of 2% (Decree 7,412, clarifies that the rate is 2% and not 6%).
- Foreign exchange transactions carried out as from January 1, 2011, for the entry into Brazil of funds in connection with the change in the investment regime applicable to non-resident investors (from direct investment governed by Law 4,131 to investment in shares traded in the stock exchange market in accordance with the rules provided by the National Monetary Council – Conselho Monetário Nacional, CMN) are subject to the IOF Exchange at rate of 2% (prior to Decree 7,412, the IOF Exchange was levied at the rate of 6%).
- Foreign Exchange transactions related to the funding of taxes, service fees or expense payments are subject to the IOF tax at a rate of 0.38%

### **Outflow:**

- The IOF on FX outflows remains at 0% for the repatriation of cash dividends and interest over capital amounts.
- The outflow IOF rate on both ADR cancelations and investment conversions is 0%.
- Foreign exchange transactions for remittance abroad of proceeds related to foreign credit transactions are subject to the IOF at a 0.0% rate irrespective of the date on which the funds entered into Brazil (prior to Decree 7,412, zero rated IOF Exchange only applied to remittances of funds which have entered into Brazil as from October 23, 2008)

### **Simultaneous FX transactions:**

- The transfer of cash balances from “Equity Accounts” to “Other instruments Accounts” is subject to a 6% IOF tax.
- FX transactions conducted by foreign investors with the purposes of initial or additional cash collateral related to trades at BMFBovespa are subject to a 6% IOF Tax.

## Brazil – *Imposto sobre Operacoes Financeiras* (IOF tax) - Overview

### **IOF on sale of short-term fixed income securities:**

- IOF tax also applies to the sale of short-term fixed income instruments (bonds, investment funds, etc), sold under 30 days from the purchase date.
- The taxes are set on a decreasing scale from 96% overnight to 0% as of day 30.
- The IOF tax is assessed on either 1% per day assessed on the total amount of the redemption amount, or a sliding percentage of the capital gain based on the number of days between the investment date and the redemption date, whichever is lower.
- According to the sliding scale, if the bond is held for 23 days the IOF tax would be 23% and when it reaches 30 days IOF no longer applies. The rates vary according to the progressive table below, considering the percentage over the gains/earnings based on the number of days between the investment/purchase date and the redemption/sell date.
- Under Decree 7412/2010 as of January 1, 2011 the IOF sliding scale on short-term fixed income securities does no longer apply to corporate bonds.

## Brazil – *Imposto sobre Operacoes Financeiras* (IOF tax)

Holding Period in Days	IOF% over gains/earnings	Holding Period in Days	IOF% over gains/earnings
1	96	16	46
2	93	17	43
3	90	18	40
4	86	19	36
5	83	20	33
6	80	21	30
7	76	22	26
8	73	23	23
9	70	24	20
10	66	25	16
11	63	26	13
12	60	27	10
13	56	28	6
14	53	29	3
15	50	30	0

# Brazil IOF Tax – Penalties and Interest Charges

## **Penalties and Interest charges applicable if the IOF is not paid or is not paid on its due date:**

- The penalties of a late payment or incorrect calculation of the IOF Tax are the charge of interest at SELIC rate (BR official interest rate) accumulated (not compounded) beginning the following month in which the payment should have been done until the month before the one in which the payment will effectively take place, plus one percent related to such month in which the payment effectively takes place. Despite that there's also the charge of a past due penalty charged at a rate of 0.33% per day of late payment, limited, however to 20%.
- It's important to notice that i) there's no charge of interest if the late payment is done on the same month it should have been done; and ii) either the interest and the penalty are calculated on the principal amount of tax, not compounded.



Peru – Capital Gains Tax (CGT) New Procedures, Withholding Tax  
on Fixed Income Securities and Financial Transaction Tax Reduction

# Peru – Capital Gains Tax (CGT) New Procedures

## Background

On December 17, 2009 the Peruvian Congress approved a law implementing a Capital Gains Tax (CGT) in Peru

- Effective January 1, 2010, non-resident investors in the Peruvian market are be subject to:
  - 5% CGT for transactions that occur on the Peruvian Stock exchange
  - 30% CGT for over-the-counter (OTC) transactions
- Bonds issued by the Peruvian Government and Central Bank CDs are exempt from both CGT and withholding tax on bond interest
- Currently, the local depository, Central Securities Depository CAVALI (CAVALI), does not act as a withholding agent for CGT and so it remains the Client's responsibility to facilitate the calculation and payment of the tax with the Peruvian Tax Authorities (SUNAT).
- On December 31, 2010 Decree 179-2004-EF was issued and appointed the CAVALI as the withholding agent for CGT resulting from on –exchange transactions. The CAVALI needs to issue regulations for this new Decree to be effective.

## CGT Calculation

- The CGT needs to be paid monthly in arrears by the 12th business day of the following month to the Peruvian Tax Authority
- The calculation methodology is the following:
  - (i) Obtain the gains of the transaction by calculating the difference between the sale amount (sale price x quantity) and the weighted average cost (see formula below) of the securities (weighted average cost x quantity)
  - (ii) Obtain the gains of the transaction by calculating the difference between the sale amount (sale price x quantity) and the value of the securities as of close of 2009 \* (close value x quantity)

# Peru – Withholding Tax Rate Reduction on Certain Interest Payments

(iii) If a positive result is obtained on both assumptions above, the CGT will be calculated using the lowest result between (i) and (ii). Meaning that the lowest gains will be used to calculate the CGT

(iv) If one or two of the results are negative, no CGT will apply

\* The value of securities as of the close of 2009 has been established as the last quoted prices registered during 2009

## **Weighted Average Cost Formula:**

$(P1*Q1) + (P2*Q2) + (P3*Q3) + \dots (Pn*Qn) / Q$  where:

P = cost of the securities bought or received

Q = quantity of shares bought or received at price Pi

Q = Q1 + Q2 + Q3 + ... Qn (total amount of shares bought or received)

## **CGT Payment Procedure**

- J.P. Morgan offers clients a service to help them to comply and pay the CGT in Peru. Clients also have the option to appoint a local tax agent in the market for them to do their calculations and submission of the CGT payment.
- Clients can instruct J.P. Morgan Tax Operations via SWIFT MT599 (BIC address CHASGB2LTAX) or by an authorized fax to 44 1202 342713, to request the local subcustodian to make the CGT payment by check and to complete Form 1073.
- Clients should submit these instructions to J.P. Morgan by the 4th business day of the month following the relevant liability being incurred. Moreover, clients are required to ensure their PEN cash accounts at J.P. Morgan are funded appropriately, including the relevant Peru Financial Transactions tax (which is currently 0.005%) at the point the instruction is submitted.
- Clients that do not pay the CGT to the Peruvian Tax Authorities on the due date will be subject to a 1.2% monthly interest charge. Moreover, the Tax Authorities plan to revise Form 1073 so that the Form will constitute a sworn affidavit and when this new Form is in effect, a late submission will cause a 1,200 USD penalty. The current Form is not considered an affidavit by the Tax Authorities and therefore, the described penalty cannot be applied until the Tax Form 1073 is updated.

# Peru – Withholding Tax on Fixed Income Securities

## **Reduced withholding tax on interest payments of certain fixed income securities.**

- Effective January 1, 2011, Decree 179-2004-EF set forth a 4.99% withholding tax applicable on interest payments received from:
  - Corporate Bonds
  - Other debt instruments
  - Deposits in the Peruvian financial system.
- This reduced withholding tax applies to all fixed income instruments traded both on exchange and over the counter, with the exception of government bonds, (i.e, interest from government bonds continues to be exempt from withholding).
- This reduced withholding tax applies to non Peruvian individual or corporate residents.
- Under the previous legislation the general withholding rate was 30% and the 4.99% only applied to interest paid on corporate bonds issued by a non-Peruvian entity.

# Peru – Reduction of Financial Transaction Tax

## **Reduction of Financial Transaction Tax**

- The Financial Transaction Tax (FTT) is a tax over the nominal value of each transaction and applies to all debits and credits made to a client's local cash account in either local or foreign currencies. The movement of funds between the same beneficial owner accounts are not be subject to the FTT.
- On February 10, 2011 the Peruvian Congress approved the proposed legislation submitted by the Executive Power to reduce the FTT rate from 0.05% to 0.005%. This reduction will be effective beginning April 1, 2011.
- The purpose of this reduction is to achieve an increase in the banking and formalization of the economy in order for the SUNAT to be able to monitor all the financial activity.

## Chile – Capital Gains Tax (CGT) Update

# Chile – Capital Gains Tax

## Chile Capital Gains Tax (CGT)

- The general rate of capital gains tax is 35%.

## CGT Exemption

- **Listed Stock (Article 107 of Law 20,448):** There is a capital gains tax exemption on the sale of exchange-listed shares of securities if they have stock “exchange presence” and provided the shares of these securities were purchased on or after April 19, 2001. Exchange Presence means that: i) the shares of the company are duly registered with the Superintendencia de Valores de Seguro (SVS) and listed on a local stock exchange and ii) the shares must have a daily traded amount over 200 U.F. (approx. USD 5,550) during at least 25% of the prior 180 trading days (i.e., 45 days).
- **Mutual Fund Units: Article 107 of Law 20,448):** There is a new capital gains tax exemption on the sale of Mutual Funds Units (including ETFs) if they have stock “exchange presence” and the mutual funds must invest at least a 90% of their portfolio in local or foreign securities that comply with a set of conditions that include periodic payment of income to their shareholders.
- **Bonds and Fixed Income Securities and Stock:** Under article 106 of Law 20, 448 (previously Article 18bis of Law 19,768) investors must meet the following requirements in order to benefit from this exemption:
  - The investor must be incorporated outside of Chile and must not have domicile therein and
  - Certification must be submitted: Must certify that it is a foreign institutional investor complying with at least one of the following characteristics:
    - \* A Fund whose shares are publicly traded in an investment grade country, as rated by an international rating agency and qualified as such by the Chilean Superintendence of Securities and Insurance ("SVS").
    - \* A Fund registered with a regulatory authority of an investment grade country, as rated by an international rating agency and qualified as such by the SVS, provided that the fund's investments in Chile represent less than 30% of its capital (portfolio) including securities issued abroad that represent Chilean securities.
    - \* A Fund whose investments in Chile represent less than 30% of its capital (portfolio), including securities issued abroad that represent Chilean securities, provided that proof is given that no more than 10% of the share value of the fund is directly or indirectly owned by Chilean residents.
    - \* A Pension Fund.
    - \* A foreign investment capital fund regulated in Chile by Law No. 18,657, in which case all shareholders must reside abroad.
    - \* Other types of foreign institutional investors complying with the characteristics defined by the by-laws for each category of investor, with prior notice to the SVS and the Tax Authority.

# Chile – Capital Gains Tax

## CGT Exemption

- **Certain Chilean Corporate Bonds, Central Bank bonds and Treasury Bonds (Article 104 of Law 24,448)** Effective January 1, 2010, Chilean Corporate Bonds, Central Bank bonds and Treasury bonds that meet certain requirements set forth by the Ministry of Finance qualify for exemption from the 35% Capital Gains Tax (CGT). Under Article 104 all debt securities (issued by corporate entities or government entities) that comply with the following requirements are exempt from the 35% CGT.
  1. Bonds and commercial paper should be registered with the Superintendencia de Valores de Seguro (SVS);
  2. Debt must be in a Company subject to Corporate Tax with full accounting;
  3. Listed on at least one local exchange;
  4. Placed at a value equal or higher than the face value set up in the issuance agreement; and
  5. The issuance agreement states that this security is subject to the conditions of the Law 20,343.
  6. It should be noted that according to Decree No. 1,686 from the Minister of Finance, Central Bank and Treasury debt securities will be exempt from CGT even if they don't comply with the requirements mentioned in (1) and (2).

For this exemption to apply, clients must purchase and sell the securities on a local Chilean exchange and through a local Chilean broker broker-dealer, bank or registered OTC dealer.

The Ministry of Finance has published a list of the securities that to date qualify for the CGT exemption. This list is provided below.

Name	Local Code	ISIN Code
Central Bank of Chile	BCP0300112	CLP0000006941
Central Bank of Chile	BCP0600115	CLP0000006966
Treasury General of Chile	BTP0600120	CLP0000006974
Treasury General of Chile	BTU300115	CLP0000006982
Treasury General of Chile	BTU300120	CLP0000006958
Treasury General of Chile	BTU300140	CLP0000007006



Colombia – Abolishment of Debit Tax on Repatriations

# Colombia – Abolishment of Debit Tax on Repatriations

## **Reduction of Financial Transaction Tax**

- Repatriation of funds from Colombia has been subject to a debit tax of 40bsp and has been withheld on all repatriations of local funds.
- On March 2011, the Minister of Revenue issued Decree 660/2011 amending the current rules on the Debit Tax.
- Under the Decree the purchase of foreign currency will no longer be subject to the Debit Tax as of March 10, 2011 as long as the funds are credited to an account under the same legal entity's name.

## China – Recent Developments

# China – Recent Developments

## Capital Gains Tax

- Despite 10% CGT on non-residents being included in legislation effective January 1, 2008, it has not been implemented to date on sales of securities by portfolio investors and there is no mechanism to make payments.
- Clarification still expected from Chinese Tax Authorities (SAT), but not sure whether will exempt certain categories of investors or broadly confirm implementation of tax.
- Recent reports that liquidation of a QDII caused taxation of realized capital gains.
- Various accounting practices to reflect this uncertainty.

## B-share Exercise

- Effective January 1, 2008, the 10% withholding tax on passive income paid to non-residents was gradually implemented to different types of income, including B-shares. Nevertheless, a number of B-share issuers did not withhold tax on dividends paid in 2009 (i.e., out of profit generated in 2008).
- J.P. Morgan's sub-custodian reached out to the 50 B-share companies who paid dividends to our clients in 2008-2009 but failed to withhold tax. Of these, only 9 companies initially accepted to assist J.P. Morgan clients in paying the tax retrospectively to the relevant local tax offices. That repayment exercise took place in March 2010.
- Subsequently, SAT released a notice aimed at ensuring that all issuing companies (including B-share issuers) fulfill their obligations as withholding agents, which led to further retrospective payment exercises.
- Current status: after 7 successive repayment exercises, only 2 of the original 50 issuers have not accepted to facilitate retrospective payments by non-resident investors.

## RMB Securities Traded in Hong Kong

- Recent trend to issue RMB-denominated securities traded in Hong Kong: bonds and soon REITs and equities
- In some cases, issuers are Chinese residents (or offshore companies deemed resident of China) with a potential 10% withholding tax applying to income paid to non-residents.
- Gross-up clauses are often included but investors must be aware of possible contingent liability.

India – 2011-2012 Budget and Direct Tax Code

# India – 2011-2012 Budget and Direct Tax Code

- Draft version of new Direct Tax Code (DTC) released in August 2009. Direct Tax Code (DTC) bill cleared by Government on August 26, 2010 and introduced in Parliament on August 30, 2010. When finally adopted, it will replace the existing Income Tax Act of 1961.
- Union Budget for 2011-2012 proposes to implement the new Direct Tax Code (DTC) from April 1, 2012.
  - Key measures that could have an impact on the taxation of non-resident investors:
    - Capital Gains Tax (CGT) and Securities Transaction Tax (STT): Under the DTC bill, securities held by FII's would always be regarded as investment assets and therefore any income that would be derived by an FII from the transfer of securities would be characterized as capital gain (i.e., impossible to have them treated as business profits).
    - In its current state, the DTC bill proposes to maintain the CGT exemption in the case of long term capital gains (holding period over 1 year) on the transfer of listed equities, despite previous proposals to abolish the distinction between long and short term. On the other hand, short term capital gains on the transfer of listed equities would be taxed at 50% of the normal rate, (i.e., an effective rate of 15%).
  - Treaty Benefits and Anti Avoidance Rules: The DTC bill provides that the beneficial provisions of tax treaties prevail over the less favorable provisions of domestic legislation (unlike the previous draft), except for anti avoidance rules. The DTC bill includes some General Anti Avoidance Rules (GAAR) under which the tax authorities would have the power to declare impermissible any transaction entered into with the objective of obtaining a tax benefit where it lacks commercial substance (or meets other similar criteria). The GAAR would override provisions of tax treaties.
  - Rules on Indirect Transfers: The DTC bill proposes that the income derived from the transfer of an interest in a non-Indian company would be taxable in India whenever at least 50% of the fair market value of its assets is attributable to assets located in India. In that case, the income taxable in India would be proportional to the assets located in India.

Indonesia – Update on Requirements for Treaty Relief

# Indonesia Treaty Relief – Overview

## Background

- Standard rate on dividends, interest and capital gains is 20%, reduced under tax treaties to 10% or 15% (dividends); capital gains are exempt under some treaties.
- Under the rules effective January 1, 2010, treaty relief is conditioned upon timely submission by the beneficial owner of Form DGT-1 or DGT-2 in the case of banks or pension funds.
- Nominees are no longer recognized
- Page 1 of Form DGT-1 is completed and signed by the beneficial owner and certified by the tax office of its domicile. It is valid for 12 months commencing from the month of the certification. One original must be submitted to each withholding agent:
  - In the case of government bonds, the withholding agent is the sub-custodian
  - In the case of equities or corporate bonds, the withholding agent is the issuer
- Page 2 of Form DGT-1 is completed and signed by the income recipient (non-resident tax payer). It is either used on a per event basis to report the income for which relief is sought, or on a monthly basis.

## Timeframes for submission of original DGT Form to J.P. Morgan

- Relief at source:
  - Dividends: Pay Date - 10 business days at the latest.
  - Coupon or redemption : Pay Date - 7 business days at the latest.
  - Sale or transfer of government or corporate bonds: Settlement Date - 5 business days at the latest
- Quick refund : 2 business days (at the latest) before the end of the month
- In the case of Form DGT-2 our sub-custodian needs 7 days to legalize the copies of the form before they can be transmitted to the various withholding agents. Therefore, Form DGT-2 covers (within its 12 month validity date) all income payments where the pay date is no less than:
  - \* 17 business days after submission to J.P. Morgan in the case of dividends;
  - \* 14 business days after submission to J.P. Morgan in the case of bond coupon (or redemption).



# Indonesia Treaty Relief – Enhanced Service

## Description

- J.P. Morgan enhanced service developed with its Indonesian sub-custodian makes it easier to meet deadlines in case of beneficial owners who must use Form DGT-1
- Under that enhanced service offering, J.P. Morgan's sub-custodian:
  - keeps an inventory of DGT-1 Page 2s pre-completed and signed by clients, with the exception of Part VI and the date section, and
  - adds the relevant income information into Part VI (as well as the date) and utilizes the form for claiming treaty relief whenever possible.

## Clients who wish to receive the enhanced service should provide:

- An original completed, signed and certified DGT-1 Page 1 for each withholding agent they expect to receive payments from.
- As many original completed and signed (but un-dated) Page 2s as they expect will be required during the validity period of Page 1 (i.e., 12 months from the month of tax office certification in Part III). It is recommended that clients provide an additional number (e.g., +50%) of Page 2s to cover additional income events that could occur or unforeseen bond trades. In all cases, clients should ensure that no less than 5 additional Page 2s are provided. J.P. Morgan will send a report of form utilization to clients where more than 70% of the forms provided are expected to be utilized in the current month.
- A completed and signed "Acknowledgment Letter for Indonesia Form DGT-1 Partial Completion Service".

# Indonesia Treaty Relief – Retrospective Reclaim Process

## Background

- Due to lack of a defined process, historically impractical to file retrospective reclaims in Indonesia, and the industry (including J.P. Morgan through the Association of Global Custodians and the British Bankers' Association) had called in early 2010 for the adoption of clear guidelines, as the newly published rules for treaty relief made it more likely that relief at source would be missed.
- In August, the DGT issued regulation No. PER-40/PJ/2010 effective August 9, 2010.

## Procedure

- A tax reclaim application must be made in writing by the beneficial owner by using Form DGT-3 completed in English. The reclaim is submitted to the relevant district tax office through the Indonesian withholding agent.
- A Power of Attorney must be given to the withholding agent using Form DGT-4.

## Supporting Documentation

- Certificate of Domicile: Form DGT-5 should be signed by the beneficial owner and certified by its tax office. Form DGT-5 similar in appearance to Form DGT-1 but does not include questions in Part V of DGT-1 (in particular as to whether the Indonesian income is subject to tax in the country of residence of the investor)
- Original Tax Vouchers
- Letter from the beneficial owner stating that the amount of tax being reclaimed has not been credited against residence country tax liability, or used to reduce taxable income in the country of residence.
- Additional Income Specific Documents: In the case of dividend income, a declaration of dividend distribution by the issuing company is required as well as a bank statement showing the receipt of income and a statement by the issuing company that the non-resident taxpayer filing the reclaim is the actual owner of the dividend.
- In case the applicable treaty includes a beneficial ownership language, 7 additional items are required (including detailed information about shareholders and employees, etc).

## Current Status

- Above process is too onerous. J.P. Morgan is working closely with its sub-custodians to clarify the process and has requested, in particular through the BBA, that the requirements should be simplified, as it is currently not workable.
- Statute of Limitations confirmed as 5 years from income pay date.
- New guidance is expected in April 2011.

Korea – Repeal of KTB and MSB Exemption / Review  
of Beneficial Ownership Concept

# Korea – Repeal of KTB and MSB Exemption

- Exemption on Korea Treasury Bonds (KTBs) and Monetary Stabilization Bonds (MSBs) introduced in May 2009
  - Covered interest and capital gains
  - Applied to non-residents
- Introduction late 2009 of mechanism to hold exempt KTBs and MSBs outside Korean market (e.g., in Euroclear) via QFIs
  - J.P. Morgan applied for QFI status with the regulator KSD
- Repeal of the exemption passed in the National Assembly on December 9, 2010
  - Measure applies to KTBs and MSBs purchased on or after November 13, 2010. Bonds purchased before that date will remain exempt
  - Interim period between November 13, 2010 and January 1, 2010 where exemption continued to apply
  - Interest taxed at 15.4% (but Government can decide to reduce rate in the future in line with market conditions). Lower treaty rate is applied at source.
  - Capital gains
    - Taxed at 22% of net gains (or 11% of gross sales proceeds, whichever the lower) or lower treaty rate (generally full exemption)
    - Tax is calculated and withheld by the executing broker. Method applied is “moving average”.
    - No tax on transactions between non-resident investors.
  - QFI status discontinued.

## Korea – Review of Beneficial Ownership Concept

- Current practice to implement treaty relief at the level of the IRC holder (i.e., the entity approved for investment in the market).
- Several recent exercises by tax authorities suggest the Government may be reviewing the concept of beneficial ownership (i.e., potentially to look behind the IRC holder).
  - Request received from Korean NTS in November 2010 to verify that some U.S.-resident investors should not be denied treaty benefits under Article 17 of the Korea-U.S. treaty, which applies when two conditions are cumulatively met:
    - Tax applied by the U.S. to Korean passive income derived by the investor is ‘substantially less’ than the tax generally imposed by the U.S. on corporate profits, and
    - More than 25% ultimate ownership directly or indirectly owned by investors who are not U.S. resident individuals.
  - Request received from Seoul Regional Tax Office in January 2011
- In both cases, information initially requested included list and details of funds’ underlying investors. However, depending on the profile and residency of the investor, lighter requirements applied in many cases.
- J.P. Morgan contacted impacted clients individually and proactively made suggestions, in conjunction with our sub-custodian and external tax advisor, to simplify the requirements and streamline the process.
- To date, no feedback as to the potential outcome of these exercises.

## Philippines – Recent Developments on Tax Relief

# Philippines – Recent Developments on Tax Relief

## Background

- Philippine law allows foreign investors to apply for preferential tax rates under treaties or under the Internal Revenue Code (NIRC), (e.g., tax exemption for sovereign entities under Sec. 32 or 15% tax sparing rate under Sec. 28).
- Historically, lack of official guidelines from the Philippine Bureau of Internal Revenue (BIR) with respect to required supporting documentation for foreign investors to apply for preferential tax rates at source. Local issuers (acting as withholding agents) used to only require foreign investors to provide a certificate of tax residence (COTR) in order for the issuers to grant preferential tax rates.
- Starting from September 2009, more and more Philippine issuers have started requiring foreign investors to apply for a pre-approved ruling from the BIR for tax treaty relief purposes (i.e., a BIR ruling). However, ambiguous documentation requirements and extremely tight deadline made it virtually impossible to apply for a BIR ruling.
- On August 25, 2010, the Bureau of Internal Revenue (BIR) issued Revenue Memorandum Order No. 72-2010 (RMO 72-2010), which provides foreign investors with guidance of documentary requirements and deadlines to apply for tax treaty relief at source. To date, however, still no official guidelines of documentation requirements and procedures for foreign sovereign entity and tax sparing rate investors to obtain a BIR ruling.
- Further to the RMO 72-2010, major sub-custodian banks in the Philippines (including J.P. Morgan's sub-custodian bank HSBC) adopted a stricter policy of documentation requirements. In particular, it requires that all foreign investors (including foreign sovereign entities) must provide a pre-approved ruling from the BIR.
- For tax treaty relief application, the RMO 72-2010 provides an official list of documentation requirements. However, it also exerts new onerous burdens on foreign investors (e.g., consularized copy of COTR, Article of Incorporation (AOI), special power of attorney (SPA), etc). Also, the BIR verbally confirmed that foreign investors (at beneficial owner level) are still required to apply for a BIR ruling for each dividend/interest distribution event.

# Philippines – Recent Developments on Tax Relief

## **Latest Development**

- In March 2011, J.P. Morgan's sub-custodian has agreed to accept documents other than a BIR ruling, subject to a number of conditions, in particular that the issuing company itself should not be requiring a BIR ruling.
- We are currently seeing a few companies (e.g., PLDT) announcing requirements not including a BIR ruling. However, these companies impose onerous documentation requirements on investors, which must be met within very challenging timeframes.

## **Actions to Date**

- J.P. Morgan has issued over 40 flashes to promptly notify clients of important market updates in the Philippines.
- Lobbying efforts with the BIR for less onerous documentation requirements on foreign investors, including the possibility of one BIR ruling per beneficial owner (or 1 BIR ruling per issuing company), instead of the current requirement of 1 BIR ruling per distribution event.
- Lobbying efforts with respect to an official guidelines from the BIR, with respect to foreign sovereign entity clients and tax sparing clients to apply for a BIR ruling.
- J.P. Morgan is working with its sub-custodian in order to provide extended services to help clients to apply for a BIR ruling for tax treaty relief (under RMO 72-2010). A proposed enhanced product is currently being reviewed.



## Thailand – Reintroduction of Government Bond Taxation

# Thailand – Reintroduction of Government Bond Taxation

## Background

- Announcement on October 12, 2010 that Thai Government approved the Finance Ministry's proposal to remove the previous tax exemption on interest and gains derived by foreign investors from government bonds and to impose withholding tax at the standard 15% rate (or at a lower rate under a tax treaty).
- Confirmed by Royal Decree of December 14, 2010.
- These instruments had been benefiting from withholding tax exemption since January 25, 2005.
- Effective date of the measure is October 13, 2010 and refers to the “trade date”. Therefore, the new tax regime applies to bonds purchased on or after that date.
- As there was initially some uncertainty as to the implementing date, no tax was applied by market participants in the weeks following the announcement. Subsequently, a tax had to be applied retroactively to certain transactions but, as expected, the late tax payment fees were waived by the Revenue Department.

## Scope

- The scope of interest withholding tax is narrow: only interest paid on bonds issued by certain state-owned enterprises have become taxable. In particular, the following bonds remain exempt from interest withholding tax:
  - Bonds issued by the Government of Thailand (including T-Bills)
  - Bonds issued by the Bank of Thailand
  - Bonds issued by other Government organizations established under the State Agencies Establishment Act
  - Bonds issued by the following financial institutions;
    - Bank for Agriculture and Agricultural Cooperative
    - Small and Medium Enterprise Development Bank of Thailand
    - Government Savings Bank
    - Islamic Bank of Thailand
    - Export-Import Bank of Thailand
    - Small Business Credit Guarantee Cooperation
- Capital gains tax will apply on the sale of all types of government bonds.

# Thailand – Reintroduction of Government Bond Taxation

## **Withholding obligation**

- In the case of interest, the registrar of the bond is responsible for withholding and remitting the tax to the Revenue Department.
- In the case of capital gains, the payer (i.e., a resident buyer or its broker) is responsible for withholding and remitting the tax, but this seldom happens in practice

## **Capital gain calculation**

- Capital gains calculation is on a transaction-by-transaction basis and capital losses cannot be used to offset capital gains.
- According to Revenue Department, for discounted bonds that are held to maturity, the difference between the principal value on redemption date and the purchasing price is treated as interest. However, if the bonds are sold prior to maturity, the Revenue Department will treat the difference between the selling price and the purchasing price as capital gain.

## **J.P. Morgan Thai CGT Services**

- New rules have no implication on the current account structure
- J.P. Morgan has worked with its sub-custodian to ensure that clients can receive the same elective services as are available for equities CGT. This includes in particular treaty accounts and a full CGT calculation and payment service.
- Clients who are not exempt from Thai CGT under a tax treaty, and have not made an election to receive one of the available levels of service, are responsible for calculating and paying CGT to the Thai Revenue Department.

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