

## Client Alert

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### Myanmar Introduces a Draft New Income Tax Law

The Myanmar Government has proposed comprehensive amendments to the legislative framework for income tax as part of its sustained strategic reform programme to modernise Myanmar and advance economic transformation. The draft new Income Tax Law ("ITL") was released for public consultation at the end of November 2019.

The deadline for interested stakeholders to provide feedback is 31 December 2019. Following that, it is expected that a public consultation meeting will be held to obtain further feedback.

For now Myanmar is not a member of the Inclusive Framework on Base Erosion and Profit Shifting, nor has it signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting. However, the introduction of the draft new ITL signals the Myanmar Government's intention to align Myanmar's tax laws with international standards while ensuring that it is not disadvantaged vis-à-vis other countries.

We discuss below some key features of the draft new ITL, which may be of interest to multinational enterprises with businesses or other activities in Myanmar.

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### Assessable income

The draft legislation clearly delineates income from employment, business, and investment. It is proposed that assessable income from an employment, business, or investment include amounts derived from an illegal act (such as bribes, kickbacks, or the proceeds of crime).

The proposed list of income from a business, which appears to be non-exhaustive, contains the following:

- (a) gross proceeds from the conduct of the business, including consideration for the disposal of trading stock and gross fees from the supply of services;
- (b) income arising from the capital of a business, including dividends;
- (c) interest, royalties, and rents;
- (d) net foreign currency exchange gains arising from the business;
- (e) gains arising from the disposal of business assets (other than trading stocks);
- (f) amounts derived as consideration for accepting a restriction on the capacity to conduct the business;



- (g) gifts received in respect of the business; and
- (h) amounts derived that are effectively connected with the business and that would otherwise be included in calculating income from an investment.

The proposed list of investment income, which appear to be non-exhaustive, contains the following:

- (a) a dividend, interest, royalty, technical fee, rent, premiums, charges or annuity, or any other amount from the provision, use, or exploitation of any asset;
- (b) a gain on a disposal of real property in Myanmar if it is held for less than the specified period (a period of three years is suggested in the draft legislation, but this has yet to be confirmed);
- (c) an amount derived as consideration for accepting a restriction on the capacity to conduct an investment; and
- (d) a gift received in respect of an investment.

Real property gains is defined to include a gain on the disposal of an option over, or other interest in, real property in Myanmar, and also a gain on the disposal of a membership interest in a resident or non-resident company, if more than 50% of the value of the membership interest is derived, directly or indirectly, from real property in Myanmar held by the company for less than the specified period.

## Capital gains tax

Under the draft legislation, capital gains tax would be payable on gains accruing to a person on the disposal of (i) any chargeable asset in a tax year for which the person is a resident, and (ii) any chargeable asset situated in Myanmar in a tax year for which the person is a non-resident.

## Proposed tax rates

The proposed Schedule 1 to the draft legislation suggests that progressive income tax rates will be applicable to individuals. These tax rates have yet to be specified.

The suggested income tax rate applicable to companies is 25%, but this is yet to be confirmed.

There are no suggestions as yet for withholding tax rates in the draft legislation, nor is there any suggestion in the draft legislation as regards the rate of capital gains tax.



## Residency status

The draft legislation expands the definition of residency for both individuals and companies.

Generally, an individual is a resident for a tax year if (i) his or her home is in Myanmar during the year, (ii) he or she is present in Myanmar for a period of, or periods amounting in aggregate to 183 or more days in any 12-month period commencing or ending in the tax year, or (iii) he or she is a citizen of Myanmar and is an officer or employee of the Government or a public authority.

A resident company is defined to mean a company that is (i) incorporated, registered, formed, settled, or otherwise created in Myanmar, or (ii) managed and controlled in Myanmar.

## Sourcing rules

The proposed amendments introduce detailed sourcing rules for income tax. (Non-resident persons are subject to tax only on Myanmar source income.)


Employment income would generally be sourced in Myanmar to the extent that it is derived by an employee in respect of employment exercised in Myanmar, wherever the income is paid. If the income is paid to an employee by the Myanmar Government, the income would be treated as having a Myanmar source regardless of where the employment is exercised.

A resident's business income would be treated as Myanmar source income except to the extent that it is attributable to a business conducted by the resident through a permanent establishment ("**PE**") outside Myanmar.

For a non-resident, its business income would be regarded as Myanmar source income to the extent that it is attributable to any business, sales, or other business activities conducted through a PE in Myanmar.

Additionally, the draft legislation prescribes a list of gains/income that would be regarded as Myanmar source income, such as:

- (a) rent from the lease of real property located in Myanmar;
- (b) gains arising from the disposal of a Myanmar asset;
- (c) insurance premiums relating to the insurance or reinsurance of a risk in Myanmar;
- (d) natural resource amounts that are derived from the taking of minerals, petroleum, or other living or non-living resource from Myanmar;

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- (e) dividends paid by a resident company; and
  - (f) interest, royalties, annuities, management fees, or technical fees paid by a resident (other than as an expenditure of a business conducted by the resident through a PE outside Myanmar) or a non-resident (as an expenditure of a business conducted by the non-resident through a PE in Myanmar).

## Definition of a PE

The draft new ITL includes a definition of PE where previously there was none. A PE is defined as "a place of business through which the business of a person is wholly or partly conducted".

The draft legislation includes a list of what would be regarded as giving rise to a PE:


- (a) a place of management, branch, office, factory, warehouse, or workshop, but not including an office that has representation of the person's business as its sole activity;
- (b) a mine site, oil or gas well, quarry, or other place of exploration for, or exploitation of, natural resources, including an installation, structure, drilling rig, boat or ship used for the exploration or exploitation of natural resources; and
- (c) the furnishing of services, including consultancy services, by a person, including through employees or other personnel engaged by the person for such purpose, but only if the activities of that nature continue for the same or a connected project of the person or an associate of the person for a certain period of time.

It is proposed that a building site, construction, assembly, or installation project, or a supervisory activity connected with such site or project be regarded as a PE only if the site, project, or activity continues for more than three months. This would also take into consideration any connected activity conducted by an associate of the person.

The draft legislation does not include a list of exceptions to PE status where a place of business is used solely for specific activities (such as the maintenance of a stock of goods for storage, display, delivery, or processing).

A dependent agent PE would arise when an agent acting on behalf of another person (i.e., the principal):

- (a) regularly negotiates contracts on behalf of the principal, whether the contracts are concluded in the name of the principal or the agent; or



(b) maintains a stock of goods from which the agent regularly delivers goods on behalf of the principal;

unless the agent is a general agent of independent status acting in the ordinary course of business.

## Foreign tax credits

Another proposed key feature of the new ITL is the introduction of a foreign tax credit system. A resident would be allowed foreign tax credits of an amount equivalent to the lower of:

- (a) the foreign income tax paid; or
- (b) the Myanmar income tax otherwise payable in respect of the assessable foreign income.

This tax credit may be applied to reduce the amount of income tax payable in respect of the taxable income of the resident for the tax year in which the assessable foreign income was derived. However, any unapplied foreign tax credit cannot be carried back to an earlier tax year or carried forward to a subsequent tax year.

The foreign tax credit for a tax year is to be calculated separately for the foreign business income and other foreign income of the resident.

A foreign tax credit is allowed only if the foreign income tax is paid within two years after the end of the tax year in which the foreign income to which the tax relates was derived by the resident person. However, an application in writing for an extension of time may be made to the Director General of the Inland Revenue Department ("IRD").

## Tax treaties

The proposed amendments clarify that the terms of a tax treaty would prevail over the provisions of the ITL in the event of any conflict.

However, an entity that is a resident of the other contracting state may not rely on the tax treaty to reduce its taxes in Myanmar where 50% or more of the underlying ownership or control of that entity is held by non-resident individuals of that other contracting state for the purposes of the tax treaty. This restriction would not apply to an entity that is either (i) a company listed on a stock exchange in that other contracting state, or (ii) a company carrying on an active business in that other contracting state where the Myanmar source income derived by the company is attributable to that business.



## Taxation of recharged technical fees and royalties

It is proposed that recharged technical fees and royalties be subject to taxation if the following conditions are satisfied:

- (a) a non-resident supplies technical services or the lease of equipment other than through a PE in Myanmar;
- (b) the technical services are supplied, or equipment leased, to a person who is:
  - (i) a resident, other than in relation to a business conducted by the resident through a PE outside Myanmar; or
  - (ii) a non-resident conducting business in Myanmar through a PE;
- (c) the technical fee or royalty in respect of the supply or lease is paid to the supplier by a non-resident that is an associate of the recipient; and
- (d) the technical fee or royalty is recharged by the associate to the recipient.

If these criteria are met, the ITL would apply as if the associate is supplying the technical services or leased equipment to the recipient and the recharged amount is the technical fee for the services or royalty for the leased equipment.

## Withholding taxes

The draft legislation introduces more detailed rules for withholding tax as regards payments to both residents and non-residents.

A licensed financial institution or prescribed entity would be required to withhold an amount from the gross amount of interest payment made to a resident individual at a yet to be specified rate.

A non-profit body, or a company that was formerly a non-profit body, making a payment of a dividend out of exempt income to a resident would generally be required to withhold an amount from the gross amount of the dividend at a yet to be specified rate. This would be a final tax on the dividend.

In the case of a payment to a non-resident, if the payer is a resident or a PE in Myanmar of a non-resident and the payment is subject to income tax under the ITL, the payer would be required to withhold an amount from the payment at a yet to be specified rate.

Further, a resident or a PE in Myanmar of a non-resident would generally be required to withhold an amount from the gross amount of a rental



payment to a non-resident person at a yet to be specified rate. If the rental payment is made to a real estate agent in Myanmar acting for the non-resident, the obligation to withhold would be imposed on the real estate agent and not the tenant. In the case of a tenant who is an individual paying rent directly to a non-resident, the obligation to withhold applies only if the tenant uses the leased property to derive assessable income.

## Thin capitalization rule

The proposed amendments introduce a thin capitalization rule, which may apply to any foreign-controlled entity (other than a financial institution). The rule disallows a deduction for a portion of the interest the entity incurs in relation to its debt if its average debt to average equity ratio exceeds the specified ratio for a tax year. For the purpose of the threshold, a ratio of two to one is suggested, but this has yet to be confirmed.

However, the thin capitalisation rule would not apply if the amount of the average debt of the company for the year does not exceed the arm's length debt amount. The "arm's length debt amount" is defined to mean the amount of debt that a financial institution not being an associate of the foreign-controlled resident company would be prepared to lend to the company in an arm's length transaction having regard to all the circumstances of the company.

In addition, it is proposed that a PE in Myanmar be treated as a foreign-controlled resident company. The average debt to average equity ratio of the PE would be calculated by reference to (i) the debt obligations of the non-resident company attributable to the PE; and (ii) the equity of the non-resident company attributable to the operations of the company conducted through the PE.

## Transfer pricing related provisions

The draft legislation provides for transfer pricing and transfer-pricing related rules.

Generally, if a party to a non-arm's length transaction is located in and subject to tax in Myanmar and the other party to the transaction is located outside Myanmar, the allocation of income, deductions, losses, or tax credits must be made in accordance with yet to be issued regulations.

Further, the allocation of income and deductions to a PE in Myanmar of a non-resident person or to a PE of a resident person outside Myanmar must be made in accordance with yet to be issued regulations.

It remains to be seen what would be the extent and scope of the transfer pricing regulations (e.g., as regards the methodology for any benchmarking



requirement), and what would be the requirements for documentation and reporting.

Additionally, the draft legislation includes a provision to empower the Director General of the IRD ("**Director General**") to make an adjustment in the case of a transaction between associates by apportioning or allocating income, gains, deductions, losses, or tax credits between the parties to the transaction to properly reflect that which would have been realized in an arm's length transaction.

If any person disposes of an asset to an associate, the transferor would be treated as having disposed of the asset for consideration equal to the open market value of the asset at the time of disposal or the net book value of the asset, whichever is higher. Likewise, the transferee would be treated as having acquired the asset for consideration equal to that amount.

## General anti-avoidance provision

Chapter VII of the draft legislation introduces a general anti-avoidance rule, which operates by empowering the Director General to undo the effect of a tax benefit that is obtained by a taxpayer in connection with a scheme where, having regard to the substance of the scheme, it would reasonably be concluded that a person, or one of the persons, who entered into or carried out the scheme did so for the sole or dominant purpose of enabling the taxpayer to obtain a tax benefit.

If an amended assessment is issued to give effect to an adjustment under this provision, the notice of the amended assessment must be served within the specified time limit.

## Other anti-avoidance provisions

The draft legislation specifically targets the reduction of income tax through income splitting opportunities such as (i) the transfer of income or property, directly or indirectly, to an associate, or (ii) the making of a payment for services in excess of the open market value of the services or when the recipient has no economic need for the services. In such instances, the Director General of the IRD may adjust the taxable income and tax credits of both persons to prevent any reduction in tax payable as a result of the splitting of income.

Further, the draft legislation introduces a provision targeting the use of tax havens to avoid Myanmar income tax. If a resident enters into a transaction that, directly or indirectly, has the effect that income is foreign income derived through an associate that is a non-resident company connected to a tax haven, the Director General is empowered to adjust the income and





foreign tax credit position of the resident to undo the tax effect of the transaction.

The proposed definition of a tax haven appears somewhat simplistic. A foreign country (or part of a foreign country) would be treated as a haven if it has (i) an effective corporate tax rate that is less than the specified rate (the suggested rate is 10%, but this is yet to be confirmed), or (ii) secrecy laws that facilitate the concealment of the identity of the real owner of any income or asset.

## Record-keeping

The draft legislation also introduces record-keeping requirements to enable the calculation of income tax and provide evidence of exempt income. It is expected that regulations will be issued to specify the accounts, documents, and records that must be maintained.

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