



Newsletter Nr. 60 (EN)

The Foreign Contractors Tax in Vietnam

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1. Introduction

In 2008, the Ministry of Finance issued the Circular on Taxation, No. 134-2008-TT-BTC, 31 December, 2008) (“**Circular No.134**”) detailed the implementation of Foreign Contractors Tax. The current general endeavour of the Vietnamese tax authorities to expand the tax basis created considerable and still prevailing in-security about the scope of applicability of the so-called Foreign Contractor Withholding Tax (FCWT).

Therefore, the following newsletter is intended to provide a brief overview of the scope of applicability, the calculation, as well as the collection of the FCWT.

2. Scope of applicability

2.1 Foreign Contractor/Foreign Sub-Contractor

The term Foreign Contractor means any foreign business organisations with or without a permanent establishment in Vietnam, and the foreign business individuals whether they are residents or non-residents of Vietnam doing business in Vietnam or having income arising in Vietnam on the basis of a contract, agreement or undertaking between

such foreign contractor and a Vietnamese organisation or individual/between Foreign Contractor and Foreign Sub-Contractor who perform part of the work of the Foreign Contractor’s contract.

The Foreign Contractors Tax is raised in the case of supplying services or services associated with goods which the Foreign Contractor or Foreign Sub-Contractor supplies in or outside Vietnam and which are consumed in Vietnam.

Summarising, it can be stated that the FCWT applies to companies that are no Vietnamese legal entities under Vietnamese law (i.e. also Representative Offices) and generate an income in Vietnam as well as individuals practicing as freelancer in Vietnam.

2.2 Non-applicable entities

Foreign Contractor’s Tax shall not apply to foreign organisations or individuals:

- Conducting business in Vietnam in accordance with the Law on Investment, Low on Petroleum or Law on Credit Institutions.
- Supplying goods to Vietnamese organisations or individuals not associated

with services provided in Vietnam regarding delivery of goods (i) at a foreign border or (ii) at a Vietnamese border;

- Having income from services performed and consumed outside Vietnam;
- Providing following services for Vietnamese organisations or individuals when such services are performed overseas: (i) repair of transportation means, machinery and equipment with or without replacement spare parts and equipment; (ii) advertising and marketing services; (iii) investment and promotion services; (iv) brokerage services for sale of goods; (v) training services; and (vi) sharing freight charges paid for international post or telecommunications services between Vietnamese party and foreign parties where such services are performed outside Vietnam and services of leasing transmission lines and satellite bans from overseas parties.

3. Scope of Applicability

The Foreign Contractors Tax consists of two elements, namely the collection of a value-added tax element (Value Added Tax/VAT) and a corporate tax element (Corporate Income Tax/CIT). For the in-

dividuals, VAT and Personal Tax shall apply.

The calculation of the tax liability depends on the usage of the Vietnamese Accounting System (VAS) by the salesman/service provider. FCWT applies particularly to companies that do not have an operating legal entity in Vietnam. The further comments are limited to the fiscal treatment of a company or an individual not applying the VAS, i.e. foreign entities doing business in Vietnam.

3.1 Withholding Tax Mechanism

A withholding tax on payments to foreign contractors applies where a Vietnamese contracting party (including foreign owned enterprises) contracts with a foreign party that does not have a licensed presence in Vietnam.

This FCWT generally applies to payments derived in Vietnam for services provided in Vietnam and overseas, except for the pure supply of goods, services performed and consumed outside Vietnam, and various other services performed wholly outside Vietnam (e.g. certain repairs, training, advertising, etc).

Foreign contractors can choose between three methods of tax payment.

a) Method One – Deduction Method

Foreign contractors can register for VAT if they meet the requirements below:

- They have a permanent establishment (“PE”) in Vietnam;
- The duration of the project in Vietnam is more than 182 days;
- They adopt the full Vietnamese Accounting System (“VAS”).

The Vietnamese customer is required to notify the tax office that the foreign contractor will pay tax under the deduction method within 20 working days from the date of signing the contract.

If the foreign contractor carries out many projects, and qualifies for application of the deduction method for one project, the contractor is required to apply the deduction method for its other projects as well. The foreign contractor will pay CIT at 25% of its net profits.

b) Method Two – Direct Method

Direct method foreign contractors do not register for VAT. VAT and CIT will be withheld by the Vietnamese contracting party at deemed percentages of taxable turnover. Various rates are specified according to the nature of the services performed. The VAT withheld by the contracting party is generally an allowable input credit in the Vietnamese contracting party’s VAT return.

c) Method Three – Hybrid Method

The hybrid method allows foreign contractors to register for VAT and accordingly pay VAT based on the conventional method (i.e. output VAT less input VAT), but with CIT continuing to be subject to deemed rates.

Foreign contractors wishing to adopt the hybrid method must:

- Have a permanent establishment in Vietnam, or be a tax resident of Vietnam; and
- Operate in Vietnam under a contract with a term of 183 days or more; and
- Maintain accounting records in accordance with the accounting regulations and guidance of the Ministry of Finance.

The VAT and CIT rates can be summarised as follows:

Industry	Effective VAT rate	Deemed CIT rate
Trading: distribution, supply of goods, materials, machinery and equipment in Vietnam.	Exempt (*)	1%
Services	5%	5%
Services together with provision of goods	3%	2%
Construction, installation without supply of materials or machinery, equipment.	5%	2%
Construction, installation with supply of materials or	3%	2%

machinery, equipment.		
Leasing of machinery and equipment	5%	5%
Leasing of aircraft, vessels (including components)	Not specified	2%
Transportation	3%	2%
Interest	Exempt	10%
Royalties	Exempt	10%
Insurance	Exempt	2%
Transfer of securities	Exempt	0.1%
Manufacturing, other business activities	3%	2%

(*) on the basis import VAT is paid

3.2 Value-added tax

Initially, the base value, i.e. the explicit added value, has to be determined. This added value is determined on the basis of the total value of the supply of goods and/or services. The total value is then set against a legally fixed percentage wherefrom finally the taxable added value is determined.

An example:

Assuming, the value of the good supplied, amounts to 100,000.00 USD. Now, the Vietnamese legislator presumes that, in case of goods supply, there is an average added value of 10% of the lump sum price. In case of services, the Vietnamese legislator assumes an added value amount of 50% of the total price. Regarding the construction

of buildings, it is to be distinguished whether materials or machines are simultaneously supplied with the construction service or not. In the case of simultaneously supply, an added value of 30% of the total price is acknowledged. If no machines or materials are supplied, the taxable added value amount is 50% of the total price (pure service-provision, see above). For all further business activities or logistical services, the taxable added value accounts for 30% of the total price.

This means, that in our above-mentioned example the added value amount is 10% of 100,000.00 USD = 10,000.00 USD. This amount is now to be set against the value-added tax rate (0, 5, 10 or 20%). Assuming the above-mentioned good consist of electronic devices, a value-added tax rate of 10% should be applied, so that the payable value-added tax amount would be 10% of 10,000.00 USD = 1,000.00 USD.

Furthermore, the costs being carried out by the Vietnamese contracting party for the foreign contractor have to be added to the value-added taxable base.

Assumed, in the above-mentioned example, an additional sum of 30,000.00 USD is

spent by the Vietnamese contractual partner for the lodging of the man-power of the foreign contractor, the value-added taxable base would now amount 130,000.00 USD. Therewith, the value-added tax owed by the foreign contractor would amount to 10% (value-added tax rate) of 50% (taxable added value) of 130.000,00 USD = 6.500,00 USD.

Value Added Rate

Value added rates as a percentage of taxable turnover shall apply to the following business lines:

No.	Business lines	Value added rate as % of taxable turnover
1.	Services, machinery and equipment leasing business, and insurance.	50
2.	a) Construction and assembly and installation where the tender INCLUDED supply of materials, machinery and equipment in the construction work.	30
	b) Construction and	50

	assembly and installation where the tender DID NOT INCLUDED supply of materials, machinery and equipment in the construction work.	
3.	Transportation and other business and production	30

Value added rates as a percentage (%) of VAT-taxable turnover in a number of other specific cases:

- Where a contractor's or sub-contractor's contract comprises different business activities or where a part of the contract value is not subject to VAT, then the application of value added rate as a percentage of VAT-taxable turnover when fixing the amount of VAT payable shall depend on the VAT taxable turnover from each business activity which the foreign contractor or subcontractor performs in accordance with such contractor's or sub-contractor's contract. If the value of each activity cannot be separated, then the highest value added rate applicable to the business line and the highest tax bracket for the whole of the contract value shall apply.
- In the case of a contract for the supply of machinery and equipment accompanied by services being guiding installation, training,

operation and commissioning, if it is possible to separate the value of the machinery and equipment from the value of the services when determining the amount of VAT payable, then a value added rate shall apply to each part of the contract value. If the contract fails to separate the value of each of the two activities referred to above, the deemed value added rate of thirty per cent (30%) of taxable turnover shall apply.

- In cases of lease of machinery, equipment and means of transportation, VAT-taxable turnover shall be the total rent and if turnover from the lease includes costs directly paid by the lessor such as insurance of means of transportation, maintenance, certification of registration of means and persons operating means of transportation or machinery, and costs of bringing such machinery and equipment into Vietnam from overseas, then VAT-taxable turnover shall exclude such costs if there are documents proving actual expenditure.

VAT Rate

Law on VAT and its implementing guidelines shall apply on taxable goods and services.

NOTE: Foreign contractors and foreign sub-contractors which pay VAT DIRECTLY on the basis of added value SHALL NOT PERMITTED TO CREDIT VAT on goods and services purchased for performance of the contractor's or sub-

contractors contract (including VAT on a sub-contractor's contract performed by a Vietnamese sub-contractor).

However, the following exceptions must be noted:

As far as services (service, installation and construction) are provided in combination with the supply of machines, equipment objects, and consumable materials, the following objects are exempted from the VAT:

- Machinery, equipment, or specialised materials which are imported for direct use in scientific research and technological development activities;
- Machinery, equipment, replacement accessories, specialised means of transportation and materials required to carry out prospecting, exploration and development of gas or oil fields;
- Airplanes (including aircraft engines), drilling platforms, and watercraft imported to form fixed assets of enterprises or leased from foreign parties for use for production, business or for lease.;

The question, which machinery, equipment, or consumable materials can be produced in Vietnam or not, is to be determined in accordance with a list of the Ministry or Plan-

ning and Investment from time to time. It is important to follow up the schedule.

If a Vietnamese subcontractor is used, the foreign contractor is exempted of the value added tax amount of the Vietnamese subcontractor's service. However, it is to note that this exception is not applicable if the Foreign Contractor signs contracts with suppliers in Vietnam for the purchase of goods and services serving performance of the foreign contractor's contract.

3.3 Corporate Income Tax

The corporate income tax rates vary between 0.1 and 10%, depending on the type of the work perform and/or the supplied goods. If the respective contract offers no itemisation, the highest applicable tax rate is used. Therefore, it is recommendable to draft contract accordingly.

Corporate Income Tax Rate:

No.	Business lines	CIT rates as a percentage (%) of taxable turnover
1.	Trading: distribution and supply of goods, raw materials. Supplies, machinery and equipment associated with services in Vietnam.	1

2.	Services, lease of machinery and equipment, insurance.	5
3.	Construction.	2
4.	Other production or business activities and transportation (including sea and air transportation).	2
5.	Lease of aircraft, aircraft engines, aircraft spare parts and seagoing vessels.	2
6.	Reinsurance.	2
7.	Assignments of securities.	0.1
8.	Loan interest.	10
9.	Income from royalties.	10

CIT rates as a percentage (%) of taxable turnover in some specific cases:

- For the purpose of calculating the amount of CIT payable on a contractor's or subcontractor's contract for a number of different business activities, CIT rates shall apply on the basis of the CIT-taxable turnover from each business activity performed by the foreign contractor or foreign sub-contractor under the contract. Where the value of each business activity is not able to be calculated separately, the CIT rate for the line of business which is subject to the highest tax rate shall apply to the total value of the contract.

- In the case of contracts for supply of machinery and equipment which include services of providing instructions on guiding installation, training, operating and test trials where the value of the machinery and equipment is separable from the value of the services, then tax shall be assessed as the percentage applicable to each activity. If the contract does not separate the value of the machinery and equipment from the value of the services, then the CIT rate of 2% shall apply to the total value of the contract.

Following positions are exempted from the corporate income tax:

- In the case of lease of machinery, equipment, or logistical means, those costs that the leasing giver verifiably spends for insurances support, for the registration of the logistical means, or for the logistical leader are also exempted from the corporation tax;
- Further exceptions exist in the area of the aviation, shipping, and the loan award.

However, it is to note that expenses paid by the Vietnamese contractual party for the foreign contractor are to be added to the taxable base.

Assuming in the above-mentioned example that the Vietnamese contractual party pays another additional amount of 30.000,00 USD for the lodging of the manpower of the foreign contractor, this sum would be added to the contractual sum of 100,000.00 USD, so that the corporate tax would be calculated to a total amount of 130,000.00 USD. As a result, the corporate tax owed by the foreign contractor would amount to 5% (corporate tax rate in case of service supply) of 130,000.00 USD = 6,500.00 USD.

3.4 Elevation of the FCWT

The FCWT is raised as a source tax, i.e. the tax guilt of the foreign contractor is to be balanced by the Vietnamese party. If the respective contract shows a net sum, a conversion into a gross sum has to be done. The tax on the gross amount is then to be kept by the Vietnamese contractual party and has to be paid to the tax authorities.

4. Impact of the agreement between Germany and Vietnam to avoid double taxation (DTA Vietnam)

Vietnam has signed a DTA with 60 countries, whereas various others are not in force.

In accordance with the protocol to the DTA Vietnam, the foreign contractor tax is deemed a profit taxes named in the DTA. Therewith, the DTA Vietnam is applicable.

Companies that do not maintain a branch in Vietnam (for example: Place of management, branch, office, manufacturing site etc.) can demand direct protection via the DTA since the taxation of business profits in Vietnam is prohibited according to Article 7.1.

Tax regulations in Vietnam allow taxpayers to self-determine to access DTA's entitlements and lodge the application to tax authority at least 15 days prior to commencement of the contract. Of note, taxpayers are not required to pay tax in advance before tax authority has a final decision. If taxpayers miss the deadline, taxpayers will submit the application at the later date to claim or offset the taxes paid.

Withholding tax rates under DTA:

	Recipient	Interest %	Royalties %	Notes
1	Algeria (*)	-	-	-
2	Australia	10	10	-
3	Austria (*)	10	7.5/10	1, 3
4	Bangladesh	15	15	1, 2
5	Belarus	10	15	1, 2
6	Belgium	10	5/10/15	1, 2, 3
7	Brunei Darussalam	10	10	1, 2
8	Bulgaria	10	15	1, 2
9	Canada	10	7.5/10	3
10	China	10	10	2
11	Cuba	10	10	-
12	Czech Republic	10	10	2
13	Denmark	10	5/15	1, 2, 3
14	Egypt (*)	-	-	-
15	France	Nil	10	-
16	Finland	10	10	-

17	Germany	10	7.5/10	2, 3
18	Hong Kong	10	7/10	2, 3
19	Hungary	10	10	-
20	Iceland	10	10	2
21	India	10	10	2
22	Indonesia	15	15	1, 2
23	Israel	10	5/7.5/15	1, 2, 3
24	Italy	10	7.5/10	2, 3
25	Ireland	10	5/10/15	2
26	Japan	10	10	1, 2, 3
27	Korea (South)	10	5/15	-
28	Korea (North)	10	10	1, 2
29	Kuwait (*)	-	-	-
30	Laos	10	10	-
31	Luxembourg	10	10	2
32	Malaysia	10	10	2
33	Mongolia	10	10	2
34	Morocco (*)	-	-	-
35	Myanmar (*)	10	10	1, 2, 3
36	Netherlands	10	5/10/15	2
37	Norway	10	10	1, 2
38	Oman	10	10	1, 2
39	Pakistan	15	15	1
40	Philippines	15	15	1, 3
41	Poland	10	10/15	1, 2
42	Qatar (*)	-	-	-
43	Romania	10	15	1
44	Russia	10	15	-
45	Seychelles	10	10	1, 2, 3
46	Singapore	10	5/15	2
47	Slovakia	-	-	-
48	Spain	10	10	1, 2
49	Sri Lanka	10	15	1, 2, 3

50	Sweden	10	5/15	2
51	Switzerland	10	10	1
52	Taiwan	10	15	1, 2
53	Thailand	10/15	15	2
54	UAE (*)	-	-	-
55	Ukraine	10	10	2
56	United Kingdom	10	10	1, 2
57	Uzbekistan	10	15	-
58	Venezuela	-	-	-

(*) *not in force yet*

Notes:

1. In some cases the limits set by the treaty are not lower than the present withholding rate under domestic law. Therefore the domestic rates will apply.
2. Interest derived by certain government bodies is exempt from withholding tax.
3. Royalty withholding tax rates vary for certain types of royalties.

5. Summary

Except of the extension of the scope of the FCWT to offshore services, hardly any basic changes have been made. Worth pointing out is the possibility to demand DTA protection. This should be considered in advance and in due to the specific individual case.