The 2015 Myanmar Tax Reform: New Rules for Commercial Tax Offset, Branches, Expats and Capital Gains

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Yet another shift in the ever-dynamic landscape of Myanmar taxation promises to improve the situation of many foreign investors. The Union Tax Law 2015 (UTL 2015), just approved by the National Assembly and likely to be signed into law by the President, is the centerpiece of a wider reform spanning income tax Commercial Tax (CT) and Stamp Duty. Equally important are a set of new Ministry of Finance Notifications on depreciations, Commercial Tax offset and undisclosed income. In this briefing note we take stock of the most important new rules, and on how they will affect businesses.

Everyone can now offset Commercial Tax

One of the more challenging and surprising features of the CT, notably that not all taxpayers have the right to offset input CT from output CT, has been significantly improved. Not only manufacturers and traders, but now also service companies can use the offset from 1 April onwards. All taxpayers can as a rule use the CT they paid to suppliers offset with the CT they owe on their sales, but there are still severe limitations on which input CT qualifies for the deduction.

- **Producers:** can offset CT on imported or locally purchased raw materials and semi-finished goods, against CT when it sells the finished goods

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- **Trader:** can offset CT on imported or locally purchased goods, against CT when it sells the same goods

- **Service provider:** can offset the CT he paid while his services are under development, against CT payable on the provision of services (directly related to the services)

However, for the whole seller and importer of cigarettes, tobacco, cured virginia, cheroots, cigar, pipe tobacco, betel chewing preparations, alcohol, beer and wine, offset is not available.

Taxpayers need to claim the input CT on the basis of a customized form (Form 31) which is lodged with the tax authorities.

New rates for cigarettes, alcohol, gems and export of electricity

The UTL 2015 increased CT rates for the followings goods upon importation from 100% to 120% for cigarettes and from 50% to 60% for tobacco, cured virginia, cherrot, cigar, pipe tobaccos, betel chewing preparations (musaki), alcohol and beer.

CT rates for jade, ruby, sapphire, emerald, diamond and other raw precious gem stones are reduced from 30% to 15%. CT on finished goods and jewelries of jade, ruby, sapphire, emerald, diamond and other precious gems are reduced from 15% to 5%.

Surprisingly, an 8% export CT has been added at the eleventh hour of the UTL 2015 for electricity. A power producer in Myanmar can export electricity to Thailand, China or India but apparently a new 8% export tax would be imposed.

IT and consulting becomes 5% more expensive as Commercial Tax exemptions are scrapped

You may recall that when the general 5% CT was introduced in 2014 for all services, a list of exemptions was introduced. A number of important changes have now been made to that list of exemptions: The 26 categories of CT exempted services are reduced to 23 categories under the UTL 2015. Services which were deleted from the exemption list include container services, information and technology service and technical and management consultancy.

No more 35% income tax rate for branches

One of the quirky features of Myanmar's income tax law was that branches of foreign companies in Myanmar are taxed at a higher rate than (foreign owned) companies. The normally applicable corporate income tax rate (CIT) is and remains 25% for companies but was set at 35% for branches. This rate has now been uniformly set at 25%.

The move comes as Myanmar has admitted 9 foreign banks into its market, which will all be operating through branches. It would be a bit difficult to stomach that the new entrants would be subject to a 35% CIT while their domestic competitors are taxed at the general 25% rate. Similarly, the Myanmar Investment Commission, the Attorney General Office and the Internal Tax Department (IRD) lost quite a bit of precious time end 2014 and early 2015 having to reassure the new entrants in the upstream oil and gas sector that their MIC permitted branches would be taxed at 25% and not at 35%. Although this has been the practice since 2012 anyway, some uncertainties were raised by the investors, which led to much debate.

There is not much justification to go on taxing branches at a higher rate than subsidiaries. Both are in principle subject to the same rules on net profit calculation, financial reporting and profit repatriation. The principle of non-discrimination, comprised in all of Myanmar's double taxation, trade and investment agreements will in many cases actually prevent the Internal Revenue Department (IRD) from imposing a less favorable tax on a foreign enterprise than is imposed on a local enterprise in the same circumstances. So, this 35% rate had to go sooner or later anyway. The Government is basically taking the entry of the 9 foreign bank branches and the oil and gas exploration companies as the opportunity to do it, which makes sense to us.

Does that mean the 3.5% withholding will also be reduced?

As a result, we think the withholding tax (WHT) for non-residents will also have to come down. That is to say, the current WHT rate for payments to non-residents is fixed at 3.5%. The rationale for this particular percentage is that it 35% tax on a 10% deemed profit rate. In other words, non-residents receiving for example a service income from Myanmar are deemed to make a 10% net profit on that income, which is taxed at the 35% tax rate for

non-residents. Mind you, this is not exactly how the Myanmar tax law fixes the WHT rate, it is just the legislator's rationale behind setting forth a 3.5% rate.

Nevertheless, this logic, the connection between the non-resident rate of 35% and the WHT rate of 3.5% is fairly entrenched on the IRD's thinking. That is why we believe that there is more good news to come for foreign businesses. For the moment, however, the WHT rate remains at 3.5%.

Capital gains tax for non-residents slashed from 40% to 10%

Another remarkable feature of Myanmar's income tax system is its disproportionate capital gains tax (CGT) rate for non-residents, which was fixed at 40%. A foreign company selling shares in a Myanmar company, or assets it holds in Myanmar was subject to this 40% rate unless it was reduced by DTA (on which more later). The domestic rate is and remains 10% for CGT, and now the UTL 2015 has uniformly set the rate for non-residents at the same 10%.

There are no special rules safeguarding pre-2015 gains, so even gains realized from now on which were basically built up during the past years when the 40% rate was still in effect, are now taxed at just 10%. This is quite a stroke of good luck for many investors, we believe. Most of the existing offshore structures (including the ones through Singapore where the potential seller of shares cannot evidence to be a Singapore resident for tax purposes) may have considerable potential capital gains which will now go untaxed.

This will not apply to oil and gas assets, though. Anyone (both residents and non-residents) deriving a gain from an oil and gas asset or a company holding an oil and gas asset, is subject to a special CGT at rates of 40%, 45% and 50%.

Is there still a point in investing through the Singapore route?

It has become commonplace to invest in Myanmar through a Singapore SPV. The Myanmar-Singapore DTA has everything to do with that, particularly since it is the only DTA presently in force which caps Myanmar's CGT at a maximum of 10%. The provision concerned, art. 13 of the DTA, is entirely written with Myanmar in mind as Singapore does not even have a CGT to begin with. Under art 13 DTA, Myanmar cannot impose its 40% in any event. Myanmar can tax at 10%, but there are also cases where the gain has to be exempt by Myanmar. Simply put, if a Singapore resident sells at least 20% of its shares in a Myanmar company, and holds minimum 35% of that company, Myanmar may impose its 10% CGT. If not, Myanmar has to exempt, except in case the Myanmar company principally holds immovable property.

So, now Myanmar has harmonized its CGT rate for residents and non-residents at 10% (except oil and gas), how will this affect the popularity of the Singapore route? First of all, one should note that without a DTA, an exemption of CGT is not possible in the first place (except for the exempt gain up to 5 million MMK). Singapore remains an attractive structuring option in and of itself for minority shareholders holding less than 35% and selling less than 20% of a Myanmar company. Those shareholders would have to pay 10% CGT without a Singapore structure, but they can claim an exemption with it. Other cases such as the typical scenario of a 100% shareholder do not qualify for the 0% CGT and they end up paying 10% CGT instead, which is now the normal rate.

Personal income tax for non-resident expats is dropped from 35% to maximum 25%

Presently non-resident foreigners' Myanmar sourced income is taxed at 35%. The only exception now is the non-residents who work for an MIC company. Under the UTL 2015, non-resident foreigners' Myanmar sourced salary income would be taxed at the same progressive rates as residents.

This will mostly affect expats coming to work in Myanmar for their first year. As residence is defined strictly on presence in Myanmar (not less than 183 days) for foreigners, an expat who comes to work in Myanmar often cannot qualify for the residents rate right from the outset in the first tax year. In such case, the 35% flat rate was applicable, increasing the cost for employers significantly.

The UTL 2015 has also reduced the tax rate for non-residents deriving business income from Myanmar.

The reduction in the rates is illustrated by the below example.

Example: Mr. A is a German national residing in Hong Kong. He works in Myanmar on an irregular basis as an employee while remaining a non-resident in Myanmar. He received 100,000 USD as an income for

this year. Separately he also received a fee USD 20,000 as an architect for a project.

	Before the Union Tax Law 2015		After the Union Tax Law 2015
Salary from A Co	100,000	Salary from A Co	100,000
PIT @ 35% flat rate	(35,000)	Progressive rate (0%-25%)	(22,000)
Net salary from A Co	65,000	Net salary from A Co	78,000
Architect fee	20,000	Architect fee	20,000
PIT @ 35% flat rate (20,000*35%)	(7,000)	PIT @ 25% flat rate (20,000*25 %)	(5,000)
Income from profession	13,000	Income from profession	15,000
Net Income (Before)	78,000	Net Income (After)	93,000

Sale of buildings and construction subject to Commercial Tax at 3%

For some time now, it has been difficult in Myanmar to predict the exact tax implications on real estate development projects. In 2014, the Commercial Tax (CT) was expanded to apply to all services, including construction services, at 5%. The sale of apartments and villas was however not specifically mentioned in the CT regulations, leaving a massive uncertainty on the subject. It seems to us that few if any apartment sellers in fact paid the CT up to now.

The 2015 tax reform again changes the tax architecture by amending the CT rules in connection with real estate. The UTL 2015 now provides that from 1 April 2015 onwards, "3% Commercial Tax shall be charged on sale proceeds from the construction and sale of buildings". Construction companies and developers are both clearly targeted and have little argument now for not paying the CT.

Unfortunately the drafting of the UTL 2015, which is limited to just one sentence to describe an entire new category of taxable events, again leaves considerable uncertainty. What if buildings are not "sold" but leased with an upfront payment? After all, foreign purchasers will usually lease immovable property instead of purchasing it. Or, what if not the building itself but an occupancy right to that building is sold? In fact, all apartments are legally speaking lease or occupancy rights. We are clarifying these issues with the IRD, but it is certain that some issues will remain unclear given the limited guidance in the text of the law itself.

Real estate sector gets the right to offset input Commercial Tax, but in a funny way

Having subjected the real estate development and construction sector to CT, the legislator had little choice but to give those same companies the right to offset input CT from their output CT. The UTL 2015 now grants that right to companies selling construction and buildings. In addition, companies building for the purpose of leasing the building to third parties can claim input CT based on the recent CT regulations. The mechanics on how this will work in practice is not clear yet.

A developer will now have to take into account that he will pay 3% CT on proceeds, minus the CT on supplies made to him. However, the supplies made to the developer, such as services by construction companies and materials, likely taxed at 5% rather than the 3% rate for the developer's output. That means that the developer actually has a serious advantage out of the rate difference in and of itself. In other words, a develop can have a huge margin on the sale of the building without having to pay any additional CT, which is remarkable.

New depreciation rates for tax purposes

The new tax rules increase the annual depreciation rates for buildings, furniture and in some cases for machinery. So, in most cases the depreciation rates go up rather than down. This means that taxpayers which are profitable right now will have a benefit from the extra deduction. Taxpayers which are in their tax holiday period or which have losses do not benefit from the higher depreciation rates.

Assets	Old depreciation rates (per annum)	New depreciation rates (per annum)
Factory buildings (first class)	3%	10%
Factory buildings (second class)	5%	15%
Furniture, fixtures, silver wares and kitchen wares used in hotels, cinemas and apartments	5% or 6.25%	10%
Machinery	2.5%, 6.25% or 20%	10%

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