Chapter 2
Company Taxation Regimes in the Asia-Pacific Region, India, and Russia

2.1 Overview

Generally, as regards the fiscal year 2009, the tax systems in the Asia-Pacific region, India, and Russia follow international standards. In the majority of territories considered, resident corporations are taxed on their worldwide income. In Hong Kong and Malaysia, the definition of taxable income is based on the territoriality principle. In these territories, profits are only taxable if derived from domestic sources. Singapore taxes income based on the concepts of territoriality and receipt. With respect to the integration of the corporation income tax into the personal income tax of the individual shareholders, about half the territories operate a classical system. Referring to the rate structure, the applicable nominal corporation tax rates vary considerably within the Asia-Pacific region, India, and Russia. The lowest rate is levied in Hong Kong (16.5%) whereas Japan and India tax corporate profits at a rate of 30%. The corporation tax is complemented by surcharges in India, Japan, and South Korea and by local profits taxes in Japan and the Philippines. Besides the tax rates, the regulations governing the tax base, e.g. depreciation allowances granted for tax purposes, are an important determinant of the territory-specific tax systems. Some territories (especially Hong Kong) grant generous allowances for tax purposes whereas other territories are more restrictive. Turning to non-profits taxes borne by corporations the majority of territories levy either a real estate tax or a property tax on business assets.

2.2 Corporation Tax Systems

There are various types of corporation tax systems in the Asia-Pacific region, India, and Russia. Regarding the extent of integration of the corporation tax into the personal income tax of the individual shareholder, three main categories can be

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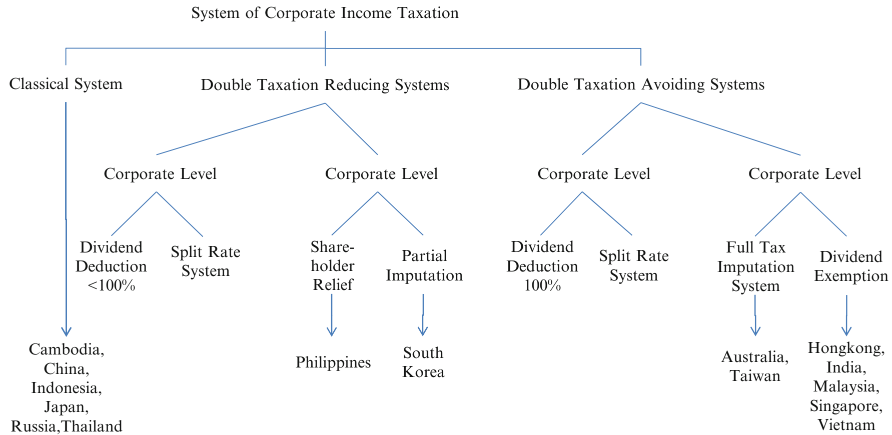

Fig. 2.1 Systems of corporate income taxation in the Asia-Pacific region, India, and Russia

distinguished: the classical system, double taxation reducing systems and double taxation avoiding systems. Figure 2.1 classifies the territories according to the corporation tax system implemented.

The classical system leads to double taxation on dividends by imposing both corporation tax and personal income tax. Cambodia, China, Indonesia, Japan, Russia, and Thailand apply a form of the classical system.

In contrast to the classical system, double taxation avoiding systems ensure that profits are only taxed once – either at the corporate level or at the shareholder level. Both Australia and Taiwan operate a full imputation system, where dividends can be "franked" at the company level with an imputation credit and individual shareholders are required to gross up their dividend income for received imputation credits and use this credit as an offset against their personal income tax liability. Consequently, there is full relief from corporation tax on distributed profits and dividends are subject to personal income tax only.

As another way to eliminate double taxation, Hong Kong, India, Malaysia, Singapore, and Vietnam operate a system of dividend exemption at the shareholder level under which profits are subject only to corporate income tax. Notably, there is a transition period in Malaysia from 1 January 2008 to 31 December 2013 where companies may opt for the old imputation system instead of the newly introduced one-tier corporate tax system. As a result, for these four territories, the corporation tax rate determines the tax burden of both retained and distributed profits.

In order to reduce the economic double taxation on dividends, South Korea implements a partial imputation system in which 12% of the dividend income can be credited against personal income tax liability. The Philippines, by contrast, grant a reduced final withholding tax rate of 10% instead of 32% for dividend income of individual shareholders.

Since the relief for corporation tax is granted only to domestic shareholders, the type of corporation tax system is only relevant if a subsidiary has resident shareholders. From the perspective of a multinational investor, the local tax burden in the considered location is decisive as well as the tax burden on repatriated profits, i.e. withholding taxes and the method to avoid international double taxation.

2.3 Tax Rates

Table 2.1 illustrates nominal corporation tax rates as well as surcharges and local business tax rates on profits if applicable. The effective statutory profits tax rate is a combined tax rate that comprises corporate income taxes, surcharges and local taxes on profits. The effective statutory tax rate also takes the interrelation of different profits taxes (e.g. deductibility of one profits tax from the tax base of another) into account. The average combined statutory profits tax rate[1] on distributed profits is 26.9% and the spread between the highest and the lowest rate amounts to 28.7% points. The combined statutory profits tax rate is lowest in Hong Kong (16.5%) and highest in India (45.2%). In India, companies face an additional "dividend distribution tax" of 15%. Thus the tax rate on distributed profits largely exceeds the tax rate on retained earnings. The reverse holds true for Taiwan. Taiwan also operates a "split-rate" tax system but in contrast to India levies an additional "retained earnings tax" on undistributed profits.

In all countries with the exception of Japan, Malaysia, Singapore, South Korea, and Taiwan, the corporation tax rate is proportional. In Japan, the standard rate is 30%; however, a special tax rate of 22% is applicable to taxable income of first JPY 8 million (59,435.67 €)[2] on condition that the paid-in capital of the company is equal to or less than JPY 100 million (742,945.91 €). Similarly a special tax rate of 20% on the first MYR 500,000 (98,699.15 €) of taxable income is available in Malaysia for corporations with a paid-in capital of less than MYR 2.5 million (493,495.73 €). In Singapore, South Korea, and Taiwan, the corporation tax rate follows a progressive rate structure regardless of the amount of paid-in capital. As for Singapore, the nominal corporate tax rate is 18% but a 75% exemption applies to the first SGD 10,000 (3,690.99 €) and a 50% exemption applies to the next SGD 290,000 (107,038.72 €). In South Korea, the tax rate in the first income bracket which is defined by a taxable income of up to KRW 200,000,000 (115,604.43 €) is taxed at 11% whereas the excess income is taxed at 22%. Taxable income up to

[1]The combined statutory profits tax rate includes the corporation tax as well as surcharges and local profits taxes. The deductibility of surcharges or local profits taxes for corporation tax purposes is accounted for.

[2]For exchange rates see Table A.1.

Table 2.1 Corporation tax rates and statutory tax rates (%)

Territory	Nominal corporation tax rate	Surcharge	Local profits tax rate (nominal)	Effective statutory profits tax rate
Australia	30	–	–	30
Cambodia	20	–	–	20
China	25	–	–	25
Hong Kong	16.5	–	–	16.5
India	40.5/30	13.3	–	45.21/33.99
Indonesia	28	–	–	28
Japan	30	20.7	7.67	40.75
Malaysia	25	–	–	25
Philippines	30	–	0.75	30.53
Russia	20	–	–	20
Singapore	18	–	–	18
South Korea	22	10	–	24.2
Taiwan	25/32.5	–	–	25/32.5
Thailand	30	–	–	30
Vietnam	25	–	–	25
Average	25.6/25.5			26.9/26.6
Germany	15	5.5	14.98	30.81
USA	35	–	8.84	38.83

India. The nominal corporation tax rate on retained earnings is 30%. Distributed profits are subject to an additional dividend distribution tax of 15%. A surcharge of 10% applies if income exceeds INR 10 m (143,363.42 €). An education cess of 3% also applies on the tax payable (including surcharge)

Japan. The inhabitants' tax of 20.7% is levied on the amount of national corporation tax as a surcharge. There are three additional local taxes which are deductible from corporate income tax. The enterprise tax is levied on the corporate income at a rate of 3.26%. The local corporate tax is 148% of the enterprise tax. A local business tax of 0.48% applies on the value added of the current year

Philippines. Local tax is levied on the annual turnover and is deductible from corporate income tax. The local tax rate is 0.75% in Manila

South Korea. A local surtax of 10% is levied on the corporation tax liability

Taiwan. The corporation tax rate of 25% applies to distributed profits. After-tax retained earnings are subject to an additional "retained earnings tax" at 10% thus yielding a combined statutory profits tax rate on retained earnings of 32.5% (=25% + 10% × (1–25%))

USA. The state profits tax rate of California is the example. In addition to the federal tax and the state tax, a manufacturing deduction for domestic production activities of 6% is taken into account (35% × (1–6%) + 8.84% × (1–35% × (1–6%)) = 38.83%)

TWD 50,000 (1,027.55 €) is exempt in Taiwan. In the second bracket, ranging from TWD 50,000 (1,027.55 €) to TWD 100,000 (2,055.11 €), the applicable rate on the total income is 15%. Any excess income is subject to 25% corporate income tax.

India, Japan, and South Korea levy important surcharges on the corporation tax payable. In India, corporations face a surcharge of 10% on the corporation tax if income exceeds INR 10 million (143,363.42 €) and an education contribution of 3% on the tax payable (including surcharge). Japanese companies are subject to a "Prefectural and Municipal Inhabitants Tax". In Tokyo, this surcharge amounts to 20.7%. South Korea also imposes a local "Inhabitants Tax" as a surcharge of 10% on the corporate tax liability.

Only Japan and the Philippines levy additional local taxes. In Japan, there are currently three additional local taxes which are deductible from the corporate income tax. Altogether they amount to 7.67%. A so-called enterprise tax is imposed on the corporate income at a rate of 3.26%. The local corporate tax is 148% of the enterprise tax and a local business tax of 0.48% applies to the value added of the current year. The Philippines impose a local tax on the annual turnover at a rate of 0.75% in Manila.

2.4 Tax Bases

In all territories, the profits liable to corporation tax are determined on the basis of national financial accounting standards and are adjusted to a different extent to obtain the corporation tax base. All territories have in common that the tax base is based upon the accrual principle. Since the regulations governing the tax base might differ significantly from one territory to another, the aim of this section is to take a closer look at important elements of the taxable income, most of which are taken into account in the calculation of effective tax burdens in Chap. 3. Table 2.2 gives an overview of the regulations implemented into the model.

2.4.1 Industrial Buildings

Generally, industrial buildings are valued at acquisition costs. In all territories, industrial buildings can be depreciated for tax purposes. The useful life ranges from 20 to 50 years. In the majority of territories, industrial buildings must be depreciated at a straight-line basis. The declining-balance method is only applicable in India and Taiwan. The Philippines usually allow the sum of the years' digits method[3] for depreciation of industrial buildings; thus the annual depreciation rate varies from year to year. Initial allowances in the first period are granted in Hong Kong (20%), Malaysia (10%), and Singapore (25%) in addition to an annual allowance at a straight-line basis. In Russia, 10% of acquisition costs can be deducted in the first period and the standard straight-line depreciation rate is applied in subsequent years.

2.4.2 Intangibles

In all territories, expenditures for intangibles (e.g. patents) that have been acquired against payment from a third party have to be capitalised and amortised either over their useful life, or as stated in the tax law. Intangibles are treated most favourably

[3]The sum of the years' digits method is an accelerated depreciation method. The numerator of the depreciation rate is the remaining useful life and the denominator equals the sum of the years' digits, i.e. 21 ($1 + 2 + 3 + 4 + 5 + 6 = 21$) if the useful life is 6 years.

Table 2.2 Depreciation and amortisation of assets and valuation of inventories

Territory	Industrial buildings			Intangibles[a]			Machinery[b]			Inventory valuation
	Method	Rate (%)	Length (years)	Method	Rate (%)	Length (years)	Method	Rate (%)	Length (years)	
Australia	SL	4	25	SL	5	20	DB	28.57	ufd	Weighted average
Cambodia	SL	5	20	SL	10	10	DB	20	ufd	Weighted average
China	SL	5	20	SL	10	10	SL	10	10	Weighted average
Hong Kong	SL	24	1	SL	100	1	SL	100	1	Weighted average
		4	19							
India	DB	10	ufd	DB	25	ufd	DB	35	1	Weighted average
								15	ufd	
Indonesia	SL	5	20	DB	12.5	ufd	DB	12.5	ufd	Weighted Average
Japan	SL	2.63	38	SL	12.5	8	DB	25	7	FIFO
							SL	33.33	3	
Malaysia	SL	13	1	SL	20	5	SL	34	1	Weighted average
		3	29					14	4	
								10	1	
Philippines	SD	var	30	SD	var	10	SD	var	7	Weighted average
Russia	SL	10	1	SL	10	10	SL	30	1	LIFO
		3.1	29					11.67	6	
Singapore	SL	28	1	SL	20	m	SL	33.33	3	Weighted average
		3	24							
South Korea	SL	2.5	40	SL	10	10	DB	45.1	ufd	LIFO
Taiwan	DB	4.5	50	SL	10	10	SL	14.29	7	LIFO
Thailand	SL	5	20	SD	var	10	SD	var	7	LIFO
Vietnam	SL	3.33	30	SL	10	10	SL	14.29	7	LIFO
Germany	SL	3	33.3	SL	20	5	SL	14.29	7	LIFO

USA	SL	2.46	1	SL	6.66	15	DB	14.29	1	LIFO
		2.56	38				DB	24.49	6	
		0.11	1				SL	8.92	1	

The kind of capital allowances and valuation of inventories represent the most tax efficient possibility; other possibilities are ignored. If multiple methods and rates are given, they represent the development of depreciation allowances over the lifetime of the asset. *DB* declining balance method, *SD* sum of years' digit method, *SL* straight-line method, *ufd* until fully depreciated, *FIFO* first-in-first-out, *LIFO* last-in-first-out, *var* varying depreciation rate

Hong Kong. An immediate 100% first year allowance is granted for machinery that qualifies as prescribed fixed assets, e.g. machinery or plant used specifically and directly for any manufacturing process, and for expenditure on patents provided that the rights are not purchased wholly from an associate

India. New plant and machinery acquired by a company engaged in manufacturing or production is entitled to an additional depreciation of 20% of the actual cost in the year of acquisition

Malaysia. For buildings and machinery an initial allowance is granted in the first period that amounts to 10/20% of the acquisition cost

Russia. For assets with a useful life of less than 3 years and more than 20 years a deduction equal up to 10% of the acquisition costs of fixed assets is available in the year of acquisition. This rate amounts to 30% for assets with a useful life of more than 3 years and less than 20 years

Singapore. An accelerated depreciation of 33 1/3% is available for plant and machinery. For buildings an initial allowance of 25% is granted

Taiwan. If the declining balance method is used, the residual value of the asset is fixed at 10% of its cost and depreciation is granted throughout its service life on the remaining 90%

Vietnam. Profitable companies are granted accelerated depreciation of machinery. The depreciation rate is twice the depreciation rate under straight line depreciation

[a]The purchase of a patent is assumed. If depreciation depends on the useful life of the patent and no period is specified in the national tax codes, a period of 10 years is assumed for the calculation of the allowance rate

[b]If depreciation depends on the useful life of the machinery and no period is specified in the national tax codes, a period of 7 years is assumed for the calculation of the allowance rate

Table 2.3 Treatment of losses for tax purposes

Territory	Loss carry-forward		Loss carry-back	
	Available	Periods	Available	Periods
Australia	Yes	Indefinite	–	–
Cambodia	Yes	5	–	–
China	Yes	5	–	–
Hong Kong	Yes	Indefinite	–	–
India	Yes	8	–	–
Indonesia	Yes	5	–	–
Japan	Yes	7	Yes	1
Malaysia	Yes	Indefinite	–	–
Philippines	Yes	3	–	–
Russia	Yes	10	–	–
Singapore	Yes	Indefinite	Yes	1
South Korea	Yes	5	Yes, for SME	1
Taiwan	Yes	10	–	–
Thailand	Yes	5	–	–
Vietnam	Yes	5	–	–

in Hong Kong due to an immediate 100% first year allowance. Besides Hong Kong, the average useful life of patents ranges from 5 years in Malaysia and Singapore to 20 years in Australia. In India and Indonesia, intangibles are depreciated according to the declining balance method. The sum of the years' digits method defines the tax depreciation path on the Philippines and in Thailand (Table 2.3).

2.4.3 Tangible Fixed Assets

Tangible fixed assets such as plant, machinery, and office equipment can be depreciated in all territories. In Hong Kong, machinery that qualifies as a prescribed fixed asset, e.g. machinery or plant used specifically and directly for any manufacturing process is eligible for an immediate 100% first year allowance. From a tax-minimising perspective, this regulation is by far the most generous compared to the depreciation allowances granted in other territories. Australia, Cambodia, India, Indonesia, Japan, and South Korea allow tangible fixed assets to be depreciated according to the declining balance method. As opposed to the straight-line method, the declining balance method enables the corporation to deduct a higher amount of the acquisition costs in earlier periods, thus reducing the tax burden. Among the countries allowing the declining balance method, only Japan permits a switch-over to the straight-line method once the depreciation expense under the declining-balance method falls below the respective value under the straight-line method. The respective rates for declining balance depreciation might vary according to the predefined useful life of certain types of machinery. For some standard machinery with a medium lifetime, the applicable rates range between 12.5% in Indonesia and 45.1% in South Korea. Machinery is depreciated according to the straight-line method in China, Malaysia, Russia, Singapore, Taiwan, and Vietnam at an allowance rate ranging from 10% in China to 14.29%

in Taiwan and Vietnam.[4] Regardless of the depreciation method applied, an initial allowance of 20% is granted in India and Malaysia. In Russia, 30% of acquisition costs are deductible from the tax base in the year of acquisition if the useful life of the asset ranges between 3 and 20 years. The remaining costs are depreciated according to the straight-line method in subsequent years. As for intangible assets, the Philippines and Thailand apply the sum of the years' digit method for an assumed useful life of machinery of 7 years.

2.4.4 Inventories

Inventories are valued at production cost. The concrete amount at which inventories are included in the accounts depends on the extent to which overhead is allocated to the products. Changes in stock of finished goods and work in progress are valued on the basis of alternative simplifying assumptions. In the majority of territories, the weighted-average cost method prevails for inventory valuation. Russia, South Korea, Taiwan, Thailand, and Vietnam, however, permit the last-in-first-out (LIFO) method. In times of rising prices LIFO is the most tax efficient method. The items most recently purchased at the higher price are matched against taxable revenues. Consequently, the taxable income decreases in earlier periods and payment of corporation tax is deferred. In Japan, the LIFO method as well as the weighted-average cost method are no longer accepted since 2009. Thus the first-in-first-out (FIFO) method is the only method for a simplified valuation of inventories.

2.4.5 Provisions

Due to the diversity of the tax treatment of provisions, it is not possible to provide a comprehensive overview. Rather, the focus is on provisions for bad debts or uncertain (contingent) liabilities. In each of the territories, the creation of provisions or reserves for bad debts is allowed. In Japan, Malaysia, Russia, Singapore, South Korea, and Taiwan, provisions for bad debts are deductible for corporation tax if certain prerequisites are fulfilled. In Malaysia, for example, provisions for bad debts are only deductible if they are specifically identified as irrecoverable.

2.4.6 Losses

All of the territories allow a loss carry-forward. Australia, Hong Kong, Malaysia, and Singapore offer an indefinite loss carry-forward. Among the other territories, the period of loss-carry forward ranges between 3 years on the Philippines and 10 years in Taiwan, and Russia. Cambodia, China, Indonesia, South Korea, Thailand, and

[4] Again a standard machinery with a medium useful life is assumed.

Vietnam allow a loss carry-forward for 5 periods. Slightly more attractive loss regulations offer Japan with 7 years and India with 8 years. Japan, Singapore, and South Korea even grant a loss carry-back of one period. In South Korea, however, the loss carry-back is only available for small and medium sized corporations.

2.4.7 Interest Deductibility

Interest expenses are generally deductible if incurred for the production of services or goods. Yet, several territories restrict the extent to which interest payments can reduce the tax base. In Cambodia, interest payments can only be deducted up to an amount that equals the total interest income plus 50% of non-interest income of the year. On the Philippines, the amount of deductible interest expenses is reduced by 42% of the company's taxable interest income. In Russia and Taiwan, interest expenses are only deductible if the interest rates do not exceed predefined thresholds. In Russia the threshold is based on similar loans. In Taiwan, the threshold is set by the ministry of finance.

2.5 Non-Profits Taxes for Corporations

In addition to corporation tax on profits and local business taxes on profits, companies may be subject to certain non-profits taxes. In Table 2.4, the nominal tax rates already account for possible valuation effects of the taxable asset. The effective tax rates, in contrast, account for the deductibility of real estate tax or other property taxes from corporate income tax.[5]

A real estate tax is levied in China, India, Indonesia, Japan, Singapore, South Korea, Taiwan, and Thailand. The taxable value is derived either from the market value, a standardised value or from the rental value. The effective tax rates range from an almost negligible 0.1% in Indonesia to a more substantial 1% in Thailand and 1.6% in India.

Japan, the Philippines, and Russia levy a property tax on fixed assets. In contrast to real estate tax, these property taxes are also levied on other fixed assets than real estate. The market value or a standardised value represents the taxable base for the respective property taxes. In Japan, land, buildings, and depreciable assets are subject to an effective property tax of 0.8%. Russia imposes a property tax on all fixed assets except intangibles. The rate is subject to regional variations, e.g. in Moscow, the effective tax rate on property is 1.8%. On the Philippines, the property

[5]Other indirect taxes, e.g. stamp tax or duties, are not considered as the study only examines direct taxation of profits. Real estate and assets tax are usually deductible from the corporate tax base and can therefore have an impact on the tax burden of profits.

Table 2.4 Summary of nominal and effective tax rates on property and real estate (%)

Territory	Real estate tax		Property tax	
	Nominal[a]	Effective[b]	Nominal[a]	Effective[b]
Australia	–	–	–	–
Cambodia	–	–	–	–
China	0.96	0.72	–	–
Hong Kong	–	–	–	–
India	2.48	1.63	–	–
Indonesia	0.2	0.14	–	–
Japan	0.3	0.18	1.4	0.83
Malaysia	–	–	–	–
Philippines	–	–	2.4	2.4
Russia	–	–	2.2	1.76
Singapore	0.5	0.41	–	–
South Korea	1.06	0.8	–	–
Taiwan	1.5	1.01	–	–
Thailand	1.0	0.7	–	–
Vietnam	–	–	–	–
Germany	0.39	0.27	–	–
USA	–	–	1.0	0.62

China. Real property tax is imposed on the original cost net of allowance deduction which ranges from 10 to 30%. In this study a deduction of 20% is assumed

Hong Kong. Corporations carrying on a business in Hong Kong can apply for an exemption from property tax or a credit against corporate tax if property is used by the company for producing the profits chargeable to profits tax

India. The law on real estate tax varies from one state to another. In the state of Karnataka, the applicable tax rate on real estate is 31% (including surcharge). The net annual value of the property is approximated with 8% of acquisition cost. Real estate tax is deductible for corporation tax purposes. An additional net wealth tax is levied on the aggregate value of specified assets but any assets used for conducting business are exempt

Indonesia. The actual tax due is calculated by applying the tax rate of 0.5% to the assessment value of taxable property. The assessment value of taxable property is determined as a percentage of the deemed fair market value. It is 40% for any land or building which have a sale value of more than IDR 1 billion (70,634.92 €)

Japan. Property tax is levied on real estate property as well as depreciable assets at a rate of 1.4%. Moreover city planning tax is imposed on land and buildings at a rate of 0.3%

Philippines. Real property tax is based on the assessed value of the property. It is determined based on the fair market value of the real property multiplied by the assessment level. For buildings the assessment level varies between 30 and 80% according to the value of the building. In this study an assessment level of 80% is assumed. For industrial machinery the assessment level is 80%. The nominal rate is 2% for Manila. In addition to the real property tax, a 1% Special Education Fund is levied on the same tax base

Russia. The corporate property tax is imposed on the average aggregate annual depreciated value of fixed assets. The rate is 2.2% for Moscow

Singapore. Property tax of 10% is imposed on the annual value of all immovable properties. In this study a rental value of 5% of acquisition cost is assumed as annual value

South Korea. The tax base is the current standard value of the industrial building. It is assumed that the current standard value corresponds to the acquisition costs. The rate is 2.5% in the first five periods (regulation for newly built factory) and 0.5% afterwards

Taiwan. Building tax is levied annually on the taxable present value of the building. For registered factories which are used for manufacturing 50% of the market value are taxable. The rate is 3% for commercial usage of buildings

Thailand. The tax base is the assessed economic rental value of the building. It is assumed to be 8% of acquisition costs. The nominal rate is 12.5%

USA. A net wealth tax is imposed on tangible assets, i.e. on industrial buildings and machinery. The tax rate may not exceed 1%. The tax base is the market value

[a]The nominal tax rate already accounts for possible valuation effects

[b]The effective rate accounts for the deductibility of real estate tax from corporate income tax

tax is levied on real estate and industrial machinery at an effective rate of 2.4%. It is not deductible from corporate income tax.

2.6 Conclusion

A comparison of the company tax regimes in the Asia-Pacific region, India, and Russia reveals differences in the tax system, the types of taxes relevant for corporations, the respective tax bases and – above all – a remarkably great variation in corporation tax rates. The impact of the different taxes, tax rates and tax bases on the effective tax burdens differs according to the type of investment, the source of finance and the profitability of an investment. A qualitative comparison of the different elements of the tax regimes cannot identify their impacts on the effective tax burdens. It is therefore unclear as to whether favourable allowances in the tax base compensate for higher tax rates and vice versa. Therefore the following quantitative analysis will determine the effective average tax levels at the subsidiary level and the parent company level in the different territories. Moreover, the analysis will provide insights into the weights of the respective tax drivers and how they explain the cross-territory differences in the effective average tax burdens.