

VAT focus

Asia and Middle East: indirect tax developments

SPEED READ Indirect taxes play an important role in China, representing around 60% of total government revenues. There is a plan to expand their VAT regime, greatly broadening the tax base in China. India's indirect tax regime is made up of a plethora of different tax types. A radical simplification is long overdue but it does now appear to be on the way. Malaysia has seen repeated delays to the implementation of its new GST system. As regards the Middle East, the Gulf Cooperation Council countries decided they would adopt a GST transaction tax, though it would be separately implemented in each country.



Chris Walsh is the Chief International Indirect Tax Officer at Vertex Inc. He is a noted industry leader, bringing 25 years of international indirect tax experience from more than 30 countries to the table. Email: chris.walsh@vertexinc.com; tel: 001 484 595 6355.

Virtually every year over the last decade has seen increases in VAT, Goods and Services Tax (GST) and Sales Tax regulatory activity around the world, peaking in 2010 with more than 10,000 changes in rates, rules and taxability applications. When you add into the mix case law developments, changes to other indirect tax types and amended policy approaches, it is easy to see why we refer to today's indirect tax environment as being a hyper-regulatory situation.

However, the bulk of those changes have originated from the United States' 7,500 federal, state and local taxing jurisdictions and Brazil's additional 5,500 jurisdictions, with the EU also contributing more than its fair share of complexity. While this trend is unlikely to change any time soon in those regions, to find the majority of major new developments in the VAT/GST arena over the coming decade, we need to turn our eyes to the east.

India

Today, India's indirect tax regime is made up of a plethora of individual, narrowly and widely drawn tax types, some of which interact with other taxes and some of which stand alone in their calculation. A radical simplification to this position is long overdue but it does appear to be on the way. The new system has already been delayed several times, making the prediction of an implementation date somewhat hazardous but the official line currently is that a new dual GST system will be in place sometime in Quarter 2 or 3 of 2012.

A new administrative infrastructure is already in place, including a GST Council, which will make recommendations to Parliament on GST; a Technology Group responsible for IT and the tax authority portals; a Dispute Settlement Authority; and the GST Network, which will handle taxpayer

management. It is understood that taxpayer audits will primarily be handled at the local level.

The new GST will operate both at the federal and at the state/territory level, with the federal GST being named Central GST (CGST) and the lower-level version being State GST (SGST). There will also be a third version (Inter-State GST or IGST) that will apply to supplies made between different Indian states. Rates have not yet been announced but 8% CGST and 8% SGST making an overall 16% have been mentioned by some commentators. While this does not seem like much of a simplification, it should be borne in mind that, as a result of the introduction of GST, more than ten other tax types will be subsumed, including Central Excise Tax, Purchase Tax and Service Tax. Others, however, will persist, such as Stamp Duty and passenger and road taxes. There remains some uncertainty over the future of Central Sales Tax, which might yet survive the overhaul.

The lack of clarity on an implementation date is primarily due to a fairly long list of 'open items' that are yet to be settled. Chief among these are:

- whether input SGST incurred in one state can be offset against output SGST due in another state;
- the Indian Constitution does not define 'goods' and 'services'; and
- as things stand, a business operating in all Indian states would require a single CGST registration and multiple SGST registrations (at least one for each state), which represents a significant administrative burden.

One final note on India is that, although the focus of this article has been on the indirect tax changes happening in 2012 and beyond, they will also be revamping their direct taxes system on around the same timelines. The next couple of years will certainly be interesting for those doing business in or providing tax advice in respect of India.

China

Indirect taxes play a particularly important role in China, representing around 60% of total government revenues. The main consumption-type taxes are:

- Value Added Tax: administered at the federal level, VAT applies to most supplies of goods and a few related services, such as processing and repair services. The current rates are 17% (standard rate), 13%, 3% and 0% (mostly on exports).
- Business Tax: administered at the local level, Business Tax applies to a limited range of services, such as transportation, construction, financial services, telecoms, entertainment, sales of immovable property and hotels/catering. The current rates are 20%, 5% (standard rate) and 3%. Business Tax is not reclaimable by the purchaser (unlike VAT), so it is a direct cost to the purchaser.
- Consumption Tax: applies to 'luxury goods' such as cars, tobacco products, alcoholic

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beverages, cosmetics, jewellery and oil products. Rates can vary widely between 1% and 50%.

It has been announced that there is a plan in place to effectively abolish the Business Tax and to expand the VAT regime to cover both goods and a far wider range of services, greatly broadening the tax base in China. This means that all the main transaction taxes will be administered at the federal level and the federal authorities will then share the tax revenues with the local levels, to ensure that they continue to be funded.

The pilot for this change is scheduled to take place in 2013, with the fully implemented system targeted for 2015. There are likely to be multiple VAT rates under the new structure and the standard rate is expected to reduce to somewhere in the 13%–15% range. Even with the standard rate being lowered from the current 17%, the much broader tax base is probably going to see an overall increase in government tax revenues. There have been no announcements around any change to the Consumption Tax system.

Malaysia

Like India, Malaysia has seen repeated delays to the implementation of its new GST system, which is due to replace the existing Sales Tax and Service Tax regimes. Currently the legislative framework is in place and draft taxpayer GST guidebooks are already being circulated. Further, the tax authorities have launched an externally facing website to help acquaint taxpayers with the coming changes (www.gst.customs.gov.my). There remains uncertainty around an implementation date for Malaysian GST but the first half of 2013 is probably a safe bet.

As far as rates are concerned, we are expecting to see a 4% standard rate; a zero rate applicable to exports, fruit, raw meat and supplies of power and water to residential properties; and exemptions that will apply to financial services, residential property, mass public transport, healthcare and education.

Middle East

The main area of activity in the Middle East is the Gulf Cooperation Council (GCC) countries, namely Saudi Arabia, Oman, Bahrain, Kuwait, United Arab Emirates and Qatar (Yemen may

join in 2016). The GCC is similar in its goals to the EU, including moving to a common currency and the Member States decided some years back that they would adopt a GST transaction tax, though it would be separately implemented in each country.


[In China] there is a plan in place to effectively abolish the Business Tax and to expand the VAT regime

Today, none of the GCC countries have any equivalent to a transaction or consumption tax, so the adoption of GST will be something entirely new for the tax authorities, taxpayers and the general public alike. However, the global economic downturn and more recent unrest in North Africa and the Middle East have pushed back implementation dates, which are now likely to start from some as-yet-unspecified time in 2013.

Conclusion

It appears inevitable that the next few years will see the emergence of GST as the clearly preferred transaction tax system in the Middle East and Asia Pacific regions, challenging VAT as the pre-eminent global consumption tax. Not that there is any meaningful difference between VAT and GST, but the latter tends to be somewhat simpler if for no other reason than GST systems tend to have fewer exemptions and tax rates.

However, the critical point for international VAT advisers and in-house indirect tax specialists alike is that, in addition to today's hyper-regulatory environment, they are going to have to contend with major changes to or introductions of new transaction tax systems in some of the fastest growing parts of the world. Not only that but these regions are, for many advisers and companies, somewhat unknown both culturally and from a tax perspective. With the exponential economic growth of countries such as India, China and Malaysia over the last decade, it is essential that Europe-based tax professionals start gearing themselves up for a crash course in Far Eastern and Middle Eastern tax and business systems. ■

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Indirect tax management and globalisation (Chris Walsh, 26.7.10)

2010 international review (various authors, 20.12.10)

Tax consulting 2.0 (Chris Walsh, 15.3.10)

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Phone 020 7405 3404 or email vat@blт.co.uk

Quality House, 5/9 Quality Court, Chancery Lane, London WC2A 1HP www.blт.co.uk

