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Business Transfer in Vietnam

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The Vietnam tax environment for mergers and acquisitions (M&A) has been evolving over the past few years. Before investing in Vietnam, foreign investors who have been targeting established businesses in Vietnam should consider the acquisition purposes, the substance of the target business, economic benefits and the health of the economy before deciding on the type of acquisition: share deal or asset deal.

Tax is one of the most important elements for consideration during transaction structuring; a good tax planning strategy can bring significant benefits in the structuring plan.

In this article, we will discuss popular types of business transfer and our recommendations from a Vietnamese tax perspective.

Types of Business Transfer

When making an investment, an investor may cherry-pick a specific part of a business (e.g. an asset, a business line or a project), or an entire company for acquisition. Technically, an acquisition of a business can appear in the form of an asset transfer or a share transfer.

The choice of method of acquisition is affected by factors such as the potential corporate tax rate on gains, value-added tax (VAT), transfer taxes and other tax attributes. In practice, many M&A investors would select share purchase because of non-tax and licensing issues. However, assets deals may be more appropriate in certain cases due to the potential liability issues and the ability to re-base the asset value for tax depreciation purposes.

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Assets Transfer

The advantage of assets transfer is that the purchaser can avoid historical tax liabilities. The acquisition of assets must be supported by legitimate documents including asset acquisition contract, invoices, and other supporting documents (such as sales invoices and sales contracts).

Purchase price: The value of an asset subject to acquisition is mutually agreed between the seller and the buyer and must be clearly indicated in the asset acquisition contract. The purchase price of the asset is commonly re-valuated by a third-party valuation service provider as appointed by the seller and the buyer.

Notwithstanding this, the transfer price of assets can be subject to challenge by the tax authorities where it can be concluded as not being in line with the market value as deemed by the tax authorities based on their database. This could lead to additional tax payable on the additional gain. Thus, it is important that the transfer valuation should be commercially justifiable.

Goodwill: Acquired goodwill is amortized over a maximum period of 10 years.

Depreciation: Tax regulations allow the cost of acquired assets to be written off against taxable profits in the form of tax depreciation expense, provided that certain conditions are met.

Depreciation of both new and used fixed assets is calculated based on the historical cost and useful life of the fixed assets within the regulated time frame. The depreciation time frame for plant and equipment is from 2 to 30 years, whilst for intangible assets it is from 2 to 20 years, depending on the the particular types of assets or equipment.

VAT: Most assets in Vietnam are subject to VAT upon being transferred. The standard VAT rate is 10%, while other tax rates of 0%, 5% and VAT exemption can be applied to some specific types of assets.

The seller is required to issue VAT invoices for the sale of the assets and VAT must be added to the sales price and indicated in the invoice issued. This VAT becomes input VAT of the buyer provided that the assets are used in business activities that are subject to VAT.

Enterprises are not required to declare and pay VAT in the following kinds of transactions:

- capital contribution in form of assets for establishing an enterprise;
- transfer of assets between dependent accounting entities;
- transfer of assets on de-merger, division, consolidation or conversion of form of the enterprise.

Stamp duty (asset registration tax): Acquisition of assets is subject to asset registration tax. When an asset subject to registration tax is transferred, the newly registered asset owner is required to pay stamp duty.

Specific asset registration tax rates apply to certain kinds of assets listed in the regulations: for instance, the tax rate for land and properties is 0.5%, while for cars or means of transportation it is from 2% to 10%. Asset registration taxes are not applicable to share transfers.

Stamp duty is capped at 500 million Vietnamese dong ($21,600) per asset except for cars with fewer than 10 seats, aircraft and cruisers. In practice, stamp duty payable upon transfer of assets is considered as immaterial.

Asset registration taxes must be declared and paid no later than 30 days from the transaction date.

Tax attributes: In an asset transfer, unused tax losses remain with the company which transfers the assets. Tax losses and tax incentives cannot be transferred in an asset transfer.

In common practice, if an investor wants to preserve the tax attributes upon acquisition, share transfer is required to acquire the entire business, where certain conditions and limitations shall apply, as discussed below.

Share Transfer

The first purpose of acquisition of the target company's shares is to preserve tax attributes of the company.

Capital gains tax: For foreign corporate sellers/transferors, the tax treatments on capital gains are different depending on the corporate form of the target company. In particular, the transfer of contributed capital in a Vietnamese limited liability company is subject to corporate income tax (CIT) at 20% on the gain whereas the transfer of securities (bonds, shares of public joint stock companies) is subject to CIT on a deemed basis at 0.1% of the sale price.

A foreign individual investor who is a non-tax resident in Vietnam and earns income from the transfer of capital/securities in a Vietnamese limited liability company/joint stock company is subject to personal income tax at a rate of 0.1% on the sales proceeds.

Tax treaties may provide certain protection from the above taxes. Use of an offshore holding company may also provide certain opportunities for tax mitigation on exit.

Tax indemnities and warranties: Tax exposure of the target company can be transferred to the transferee after the share purchase transaction is complete. Due to the potential negative impact of historical tax liabilities in the target company, tax due diligence exercises are important for identifying significant tax issues in M&A transactions.

As the target company's contingent liabilities may transfer to the purchaser, tax indemnities and warranties for contingent tax liabilities should be thoroughly addressed in the share purchase agreements.

Tax losses: Tax losses of a company can be carried forward for up to five years, starting from the year in which the losses are first incurred. Accordingly, losses incurred by the target company prior to the transaction may continue to be offset against the taxable income of the company after the acquisition.

Tax incentives: The target company shall continue to apply tax incentives for the remaining period after the acquisition.

Consideration of Asset or Share Transfer

As purchase of shares will result in the ownership of the target company, investors normally would select share transfer if the target company is invested in specialized or conditional investment sectors such as heavy-industry manufacturing, pharmaceuticals, logistics, etc., and/or includes land transfer, which leads to preservation of licensing benefits of the target company. Besides the licensing benefits, the investor would also inherit the tax incentives, tax losses or tax refund of the target company.

Another advantage of share purchase is that purchases of shares will not be subject to VAT, stamp duty and other burdensome administrative compliance measures, in comparison to asset purchase.

Meanwhile, the main disadvantage of share purchase is that the purchaser is fully responsible for all the historical or inherent liabilities, including tax and financial liabilities, of the target company.

On the other hand, the most recognizable advantage of asset purchase is that the purchaser will not inherit any historical tax liabilities of the target company but at the same time the current tax loss or tax incentive will not be inherited. The purchase price of assets can also be fully depreciated or amortized for tax purposes. However, the foreign investor will need to establish a legal entity in Vietnam to acquire the assets.

An investor would commonly consider the asset purchase option if the target company is invested in unconditional sectors, is not entitled to tax incentives, and has significant historical tax issues.

Other Factors to Consider

Historical Tax Liabilities A company is required to conduct tax finalization with the local tax authorities up to the time of the decision on the consolidation, division, merger, de-merger or conversion. In the event of assets or shares transfer, tax finalization is not required, unless this involves the liquidation of the target company after acquisition. In a share acquisition deal, the seller may normally request the tax authority to perform tax finalization before the acquisition so that all the historical tax liabilities are completed before the change of shareholder.

Indirect Shares Transfer Many foreign investors invest into Vietnam by acquiring a special purpose vehicle located overseas, aiming not only to achieve convenience in their business management but also tax efficiency for their future exit plan. Transfer of the offshore holding company is considered as indirect shares transfer which is also subject to capital gains tax in Vietnam even where the acquisition occurs outside of Vietnam.

Despite the fact that the offshore capital transfer is difficult to determine, as well as the current regulations being unclear on capital gains tax imposed on such transactions, it is important that the Vietnamese entity being the indirect transferee carefully reviews and has sufficient information and documentation concerning the offshore shares acquisition for tax prudence purposes.

Application of Double Taxation Agreements Vietnam has entered into more than 70 double taxation agreements (DTAs) with other countries for the avoidance of double taxation. Capital gains tax of an offshore entity which transfers shares in a Vietnam target company can be entitled to an exemption or reduction pursuant to the provisions of the DTA signed between Vietnam and its home country, where applicable. The foreign investor can consider applying for protection under a DTA at the time of transferring its shares in a Vietnam target company provided that certain conditions are met.

Disclaimer

This article provides general comments and recommendations in accordance with current Vietnamese laws and regulations in effect as of the publication date. For specific circumstance, readers should seek proper advice with respect to the topic discussed herein.

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