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## Supplying Goods and Services into Vietnam: Tax Implications



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In line with the growth in international trade between Vietnam and other countries, cross-border transactions selling goods and providing services by foreign suppliers to Vietnamese buyers have been a growing concern in terms of the related tax implications.

### Tax Implications

Vietnam Foreign Contractor Tax (FCT) is the tax obligation for overseas contractors who do business in, or receive income from, Vietnam under a contract or agreement with Vietnamese buyers. FCT is imposed on foreign business individuals and foreign organizations earning Vietnam-sourced income (herein referred to as the “foreign contractor”), except for:

- “pure supply of goods” under Incoterms, i.e. where title passed at or before the border of Vietnam and there are no associated services performed in Vietnam;
- services performed and consumed outside Vietnam.

FCT comprises two components, value-added tax (VAT) and income tax: VAT and corporate income tax (CIT) apply to a foreign contractor which is an overseas business entity, and VAT and personal income tax (PIT) apply to an individual business foreign contractor.

The direct method is the most commonly used payment method by foreign contractors due to its adminis-

trative advantages compared to other methods. Under this method, foreign contractors are not required to pay FCT directly to the Vietnam tax authority—the Vietnamese contracting party is required to withhold and file the FCT upon payments made to the foreign contractor, at the deemed percentage of taxable revenue.

The nature of transactions will decide the FCT rate under the direct method; VAT ranging from exemption to 10% for supply of goods (paid at importation phase) or 5% for pure service provision; CIT of 1% for trading activities or 5% for pure service provision.

Tax terms under the contract or agreement could also be a factor that affects the tax liabilities borne by foreign contractors. In particular:

- Gross price: if the contractual price is agreed on a gross of tax basis, the payment under the contracts shall include FCT (VAT and CIT components) that will be withheld by Vietnamese contracting parties before making the payments to foreign contractors.
- Net price: if the contractual price is agreed on a net of tax basis, foreign contractors shall receive the exact net price (i.e. the amount after the FCT). Payments must be grossed up by the Vietnam contracting parties for FCT computation, declaration and payment to the Vietnam tax authorities.
- Mixed price: both parties agree that the foreign contractor shall bear the CIT/PIT component and Vietnamese parties shall bear the VAT component of the FCT. In this case, the Vietnamese contracting party would withhold CIT/PIT before making the payments to a foreign contractor.

### Double Tax Agreement Application

In the context of current fast-growing global trade, tax treaties play a key role in boosting international cooperation by eliminating or reducing double taxation on

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cross-border income. Vietnam has entered into more than 80 double tax agreements (DTAs) with other countries for the avoidance of double taxation.

Foreign contractors and individuals working in Vietnam who are nationals of countries which have entered into tax treaties with Vietnam can apply for either FCT exemption or reduction for the portion of CIT only, or PIT, provided that these foreign contractors/individuals satisfy certain conditions stipulated in the tax treaty, i.e:

- the foreign contractor does not create or have a permanent establishment (PE);

- the individual is not a tax resident and does not receive income from a PE in Vietnam.

If there is any inconsistency in provisions between the DTA and the local tax laws, the provisions of the DTA will prevail. However, if relevant tax obligations stipulated in the DTA do not exist in Vietnam or the DTA requires taxation at higher rates than local tax rates, the local laws shall prevail. Where a term in a DTA is not defined, it will be interpreted as defined by the local laws.

Tax exemption or reduction under a DTA is not automatically granted. Generally, foreign contractors must carry out certain procedures, including submission of a dossier of notification of eligibility for tax exemption or reduction under a DTA to the Vietnamese tax authorities 15 days before commencing an assignment or contract in Vietnam.

Generally, the application requires several documents. These include:

- a notice of eligibility for tax exemption or reduction under the DTA;

- an original copy of the residence certificate granted by the tax authority of the country of residence in the year preceding the year of notification of eligibility for tax exemption or reduction; and

- a copy of the contracts and other relevant supporting documents.

On failure to submit such documents, the Vietnamese parties will be responsible for withholding and paying the taxes on behalf of the foreign contractor but the refund can still be claimed within three years from the date where tax liability has arisen.

The refund procedures are normally onerous, time-consuming, and costly.

## Practical Challenges in Applying Double Tax Agreements

Since DTAs provide comprehensive guidance, the implementation of the provisions on tax protection under a DTA depends on Vietnamese domestic regulations, interpretation and practice of the Vietnamese tax authorities. In addition, DTA application for tax exemption or reduction will be assessed by the provincial tax authority where the project is located instead of the Vietnamese General Department of Taxation.

As a result, the conditions and procedures for DTA application are not consistent nationwide and largely depend on the interpretation of each provincial tax authority. This may be considered as the major obstacle faced by foreign contractors in approaching and using this tool for double tax elimination purposes. As a consequence of not having regular guidance from the top level of the tax authorities, the lack of experience in DTA administration makes the process of DTA relief time-consuming, and it involves much paperwork.

The tight deadline for submitting DTA applications as mentioned above (i.e. only 15 days), is also another challenge that foreign contractors have to contend with. The exchange of tax information from one country to another is not robust and active enough to support the taxpayer in obtaining the necessary documents in a timely manner.

In addition, the tax reduction/exemption under DTAs is mainly conducted on a self-declaration and self-responsibility basis, without the opinion of the tax authorities being provided at the time of submitting the DTA application dossier. This exposes foreign contractors to the risk of being challenged by the tax authorities on the tax audit and will likely lead to tax claw back, interest for late payment and penalties imposed on wrong declaration if the taxpayers have made a wrong interpretation and assessment in applying the DTA.

**Going Forward** One point to note is that the Vietnamese General Department of Taxation has started to understand the difficulties of foreign contractors when doing business in Vietnam and is trying to reduce the volume of paperwork by issuing regulations, issuing guidance on the implementation of DTAs from central to provincial tax departments, and reducing the complicated administrative procedure for taxpayers, in order to encourage international cooperation and to attract foreign investment to Vietnam.

However, the side effect of updating and changing regulations continuously is that it causes confusion for taxpayers, who are not able to follow and adopt the new laws in a timely manner.

In light of the above, it is recommended that foreign contractors, as well as Vietnamese parties, review all business contracts carefully to assess the PE risk and the possibility of applying DTAs, before preparing and submitting the notification of tax exemption under the DTA.

### Disclaimer

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