EY Asia-Pacific private equity tax network

Quarterly top 10 tax topics
February 2024

Hong Kong

1 Hong Kong's company re-domiciliation regime in 2024

Hong Kong is set to implement a new company re-domiciliation regime (New Regime) in 2024 (*see Legislative Council Panel on Financial Affairs – Company Re-domiciliation Regime: https://www.legco.gov.hk/yr2023/english/panels/fa/papers/fa20230703cb1-708-2-e.pdf for details*), following a similar re-domiciliation mechanism for funds in 2021. This regime will allow foreign companies of different types and scales to change their place of incorporation to Hong Kong, providing a streamlined process for businesses.

Key features and considerations

1. Legislative amendments for inward re-domiciliation

Legislative amendments are expected to be introduced in early 2024 to establish the inward re-domiciliation regime in Hong Kong. The regime aims to attract foreign companies to re-domicile to Hong Kong, offering several advantages over similar regimes, such as in Singapore which targets at more sizable companies. Notably, Hong Kong's regime welcomes companies of all scales and will not require companies to undergo an economic substance test.

Business groups might contemplate utilizing the proposed re-domiciliation regime to relocate their current companies incorporated in offshore jurisdictions to Hong Kong with minimal disruption to their operations. Nevertheless, it is important to consider the potential implications of Hong Kong stamp duty of becoming a Hong Kong incorporated company, i.e., any subsequent transfer of the shares of the applicant after re-domiciling to Hong Kong would potentially be subject to stamp duty in Hong Kong.

2. Streamlined re-domiciliation process

The proposed regime seeks to simplify the re-domiciliation process for businesses. Companies will be able to re-domicile without the need for court intervention, winding-up or re-incorporation processes. The regime will cover all five types of companies that could be formed in Hong Kong under the Companies Ordinance or their comparable types in the company's original place of incorporation.

3. Business continuity and legal identity

Re-domiciled companies will retain maximum business continuity. They will maintain the same legal identity, including their rights, obligations, liabilities, property rights (such as intellectual property rights and existing contractual relationships) and corporate history. This facilitates a seamless transition to the new jurisdiction.

4. Registrar of companies administration

The Registrar of Companies will oversee and administer the proposed re-domiciliation regime. The approval of company re-domiciliation applications will depend on factors such as type of company, compliance requirements fulfillment in the original place of incorporation, integrity, member and creditor protection, and solvency.

The re-domiciled company would be required to de-register in its original place of incorporation within 60 days upon successful application, failing which its company registration in Hong Kong would be revoked. The proposed 60-day time limit for completing the de-registration process in the original place of incorporation aligns with Singapore's re-domiciliation regime. However, foreign incorporated companies with significant business operations in their original places of incorporation may require additional time to handle the tax clearance process, particularly if a tax audit is involved upon exit. It is advisable for the Registrar of Companies to take a practical approach when considering requests for an extension of time, taking into consideration the specific circumstances faced by the applicants.

5. Compliance and amendments for re-domiciled companies

Following successful re-domiciliation and de-registration from its original place of incorporation, the re-domiciled company should observe statutory requirements of its kind as incorporated in Hong Kong.

These include formalities related to annual meeting, protection of creditors' rights, appropriation and distributions. Besides, there are several general considerations that need to be considered when a Hong Kong-redomiciled company is also relocating its business to Hong Kong. These include addressing compliant transfer of assets and liabilities between jurisdictions, addressing employment, immigration, and tax reporting issues related to relocating employees to Hong Kong, obtaining necessary licenses for conducting business in Hong Kong, protecting and registering intellectual property rights, complying with data privacy laws and cross-border data transfer requirements, assessing any potential default events or contractual restrictions related to the re-domiciliation, and understanding the legal framework of Hong Kong along with ongoing compliance obligations and reporting requirements post-re-domiciliation.

6. Tax implications and transition issues

The re-domiciliation process is not expected to affect the Hong Kong profits tax liabilities of a re-domiciled company. A company (regardless of its domicile) that carries on a business, trade or profession in Hong Kong is liable to pay Hong Kong profits tax on profits arising in or derived from Hong Kong from such business, trade, or profession.

EY Asia-Pacific private equity tax network

Private equity thought leadership quarterly top 10 tax topics

1 Hong Kong's company re-domiciliation regime in 2024 (cont.)

However, it is important to note that the re-domiciliation should not result in any change in the beneficial ownership of company assets or trigger any stamp duty implications. The Inland Revenue Ordinance (IRO) is expected to be amended to address and deal with certain transitional tax matters, such as tax deduction for trading stock, bad debts, impairment losses on financial assets and depreciation of fixed assets, and provide greater certainty and guidance to re-domiciled companies.

In accordance with the definitions of "resident" found in most of the tax treaties concluded by Hong Kong, a company that is incorporated in Hong Kong would be considered a tax resident of Hong Kong. As a result, it seems that the re-domiciliation regime could potentially allow re-domiciled companies to be recognized as Hong Kong tax residents for the purpose of tax treaties. However, this would be subject to clarification by the Inland Revenue Department (IRD).

Conclusion

The upcoming company re-domiciliation regime in Hong Kong presents an exciting opportunity for businesses seeking to establish a presence in the region. With its streamlined process, business continuity, and favorable tax treatment, re-domiciling to Hong Kong can provide companies with increased flexibility and access to the vibrant market. As this regime takes effect, companies should carefully evaluate their options and consider seeking professional advice for a smooth re-domiciliation process and harness the numerous benefits offered by Hong Kong.

2 Tax certainty enhancement scheme (TCES) for onshore disposal gains

Hong Kong has now introduced safe harbor rules to provide upfront certainty on onshore equity disposal gains under the Inland Revenue (Amendment) (Disposal Gain by Holder of Qualifying Equity Interests) Ordinance 2023, which was enacted on 15 December 2023.

The basic conditions for the TCES are that an investor would need to hold at least 15% of the total equity interests in an investee entity throughout the entire period of 24 months immediately before the disposal of their equity interests in the investee entity. When the basic conditions are satisfied, any gains on their disposal of the equity interests in the investee entity will be regarded as being capital in nature and, therefore, not chargeable to tax in Hong Kong, without the need to determine the capital-versus-revenue nature of such gains by way of the normal "badges of trade" analysis.

What constitutes "closely related" entities

The issue would be what constitutes a "closely related" entity for the purpose of determining whether the 15% threshold is satisfied. Specifically, whether, in addition to the usual 50% beneficial equity interest in an investee entity, the voting rights that an investor can exercise at general meetings of the investee entity will be included as one of the tests for determining the term "closely related".

Such an inclusion would cater to the situation where control over an investee entity is exercised by an investor that holds a class of equity interest that carries a disproportionally higher voting rights than other classes of equity interests issued by the investee entity.

The bill now specifies that the "closely held" relationship would be satisfied simply by virtue of one entity (not being a natural person) holding, directly or indirectly, more than 50% voting rights in the other or a third entity holding, directly or indirectly, more than 50% voting rights in each of the entities concerned.

What constitutes "a business of property trading"

The TCES will not apply to an investor that holds an investee entity which was engaged in "a business of property trading" in the basis period of the investee entity, during which the investor disposed of their equity interest in the investee entity.

The bill provides that "an entity carries on a business of property trading if it carries on a business of acquisition and sale of immovable properties, situated in Hong Kong or elsewhere, unless the acquisition and sale of immovable properties is incidental to the undertaking of any property development by the entity".

The IRD has clarified that "a business of property trading" does not include "an adventure in the nature of trade" in immovable properties. For example, a normal commodity trading entity that only speculated in a residential unit as an isolated transaction in a year for the purpose of making a quick profit would not render the commodity trading entity engaging in "a business of property trading" for the year (*see IRD website: https://www.ird.gov.hk/eng/tax/bus_taxcertainty.htm for details*).

Conversely, the fact that an entity that was normally engaged in a property trading business did not resell any immovable properties for a year would not necessarily render that entity not engaging in "a business of property trading" for that year. This would especially be the case where the entity held unsold property units during the year concerned.

What constitutes "trading stock"

The disposal of an equity interest that is regarded as "trading stock" will not qualify for the TCES. Specifically, the bill provides that if any marked-to-market fair value gains or losses as reflected in the accounts of an investor in respect of an equity interest have been offered for tax assessment or claimed for a tax deduction, such equity interest will be regarded as "trading stock".

In addition, if the disposal gains or losses of part of an equity interest in an investee entity have previously been offered for tax assessment or claimed for a tax deduction, then the remaining equity interest that was acquired on the same occasion as that previously disposed of will also be regarded as "trading stock".

Effective date

The TCES will apply to onshore gains where the disposal occurs on or after 1 January 2024 and the gains accrue in the basis period for a year of assessment beginning on or after 1 April 2023. The legislative provisions for the TCES, unlike the similar scheme in Singapore, have no expiry date.

EY Asia-Pacific private equity tax network

Private equity thought leadership quarterly top 10 tax topics

3 Extension of offshore disposal gains under FSIE regime

The Inland Revenue (Amendment) (Taxation on Foreign-sourced Disposal Gains) Ordinance 2023, enacted on 8 December 2023, expands the scope of offshore disposal gains under the foreign source income exemption (FSIE) regime from equity interests only to cover all kinds of assets. It becomes effective from 1 January 2024.

The change was made in order that the FSIE regime can comply with the updated Guidance on FSIE regimes issued by the European Union (EU) in December 2022. Otherwise, Hong Kong could be subject to certain protective counter measures to be adopted by EU member states.

Intra-group transfer relief

Conditions applicable to all kinds of assets

Subject to the conditions that the entities concerned must for two years be (i) associated by a 75% threshold and (ii) within the charge to profits tax in Hong Kong, the provisions grant relief for gains derived from an intra-group transfer of all kinds of assets, i.e., such gains would not be taxed at the time of the transfer.

Similar to the "closely related" term discussed under the TCES above, the 75% "associated" relationship would also be satisfied simply by virtue of one entity holding, directly or indirectly, at least 75% voting rights in the other or a third entity holding, directly or indirectly, at least 75% voting rights in each of the entities concerned.

Business facilitating measures

Similar to the current FSIE regime, only essential, high-level information and declarations will be required to demonstrate compliance with the economic substance requirement (ESR) when filing tax returns in relation to the expanded scope of the offshore disposal gains.

To provide greater certainty to taxpayers, the IRD will continue to provide advance rulings on the compliance with the ESR. Such a favorable ruling will be valid for up to five years of assessment.

In addition, a supplementary form is available for taxpayers who have previously obtained a favorable ruling or Commissioner's Opinion in relation to their satisfaction of the ESR for any of their existing FSIE income, so that such a ruling or opinion would be extended to cover their disposal of other kinds of assets under the FSIE regime as amended by the amendment ordinance.

4 Public consultation on BEPS Pillar 2.0

The government has recently issued a consultation paper (the Paper) on the implementation of the global minimum tax and a domestic minimum top-up tax in Hong Kong (HKMTT) starting from 2025 onwards. The consultation will end on 20 March 2024 (*see the consultation paper of the Financial Services and the Treasury Bureau: https://www.fstb.gov.hk/tb/en/others/Consultation%20paper_Global%20minimum%20tax%20and%20HKMTT%20(Eng).pdf for details*).

Background

The global minimum tax under the international reform framework of a two-pillar solution to tackle base erosion and profit shifting (BEPS) risks arising from digitalization of the economy (commonly known as BEPS 2.0) targets multinational enterprise (MNE) groups with annual consolidated revenue of EUR750 million or above. It ensures that these MNEs pay a minimum tax of 15% in respect of profits derived from every jurisdiction they operate in through two interlocking rules, the Income Inclusion Rule (IIR) and the Undertaxed Profits Rule (UTPR), which together referred to as the global anti-base erosion (GloBE) rules. To preserve its own taxing right, a jurisdiction may also impose a domestic minimum top-up tax (DMTT).

The GloBE rules have already been finalized based on the international consensus and there is no room for deviation. As such, the Paper explains the policy considerations and the design features of the GloBE rules which are relevant to Hong Kong and invites views on matters that are left for consideration by the implementing jurisdictions.

Legislative approach to be adopted

Hong Kong will adopt a hybrid legislative approach by directly incorporating the GloBE rules into the IRO with limited adaptions as far as practicable.

For the purposes of the GloBE rules and HKMTT, with retrospective effect from 1 January 2024, an entity is a Hong Kong resident entity if (a) in the case where an entity is a company – the entity is incorporated in Hong Kong or, if incorporated outside Hong Kong, normally managed or controlled in Hong Kong; or (b) in any other case – the entity is constituted under the laws of Hong Kong, or if otherwise constituted, normally managed or controlled in Hong Kong.

Charging UTPR by way of an equivalent adjustment

The GloBE rules provide that the UTPR may take the form of a denial of deduction for otherwise deductible expenses in an amount sufficient to result in the constituent entities located in the UTPR jurisdiction having an additional cash tax expense equal to the UTPR top-up tax amount allocated to that jurisdiction. Alternatively, the UTPR may take the form of an adjustment that is equivalent to a denial of a deduction. Hong Kong will adopt the option of relieving MNE groups from the UTPR in their initial phase of international activity.

Scope and features of the HKMTT

HKMTT will be designed to qualify as a qualified domestic minimum top-up tax (QDMTT). To this end, the HKMTT will mirror all the requirements of the GloBE rules subject to the permitted and optional variations within the OECD's framework. In addition, the HKMTT will be designed to produce a liability for top-up tax that is equivalent to the top-up tax liability that would have arisen under the GloBE rules.

EY Asia-Pacific private equity tax network

Private equity thought leadership quarterly top 10 tax topics

4 Public consultation on BEPS Pillar 2.0 (cont.)

Other key features of the HKMTT:

- Imposed on the whole amount of the total top-up tax computed in respect of all Hong Kong constituted entities of an in-scope MNE group, irrespective of the ownership interest held in the constituent entities by any parent entity of the group.
- Apply only to MNE groups with an annual consolidated revenue of or above EUR750 million. Small MNE groups and purely local groups are excluded from the scope of the HKMTT.
- All Hong Kong constituted entities of such groups, as well as joint ventures (JVs) and JVs subsidiaries held by the groups, will be subject to the HKMTT regardless of the ownership interest of the ultimate parent entity (UPE) or partially owned parent entity (POPE) in the entities concerned.
- The HKMTT attributable to the JVs and their subsidiaries of an in-scope MNE group will be directly imposed on the JVs and JVs subsidiaries concerned instead of being allocated to other Hong Kong constituent entities of the group.
- The HKMTT payable will, by default, be allocated among Hong Kong constituent entities of an in-scope MNE group pursuant to the formula adopted in Article 5.2.4 of the GloBE rules.
- Substance-based income exclusion will be included.
- The minimum tax rate will be set at 15%, and not higher even it is permitted.
- The same de minimis exclusion provided under Article 5.5 of the GloBE rules will be included.
- The HKMTT will not apply during the initial phase of international activity of an MNE group where no parent entity is required to apply qualified IIR with respect to Hong Kong constituent in-scope MNE groups.

Tax compliance, administration and the general anti-avoidance provisions

The IRD will put in place a dedicated tax administration framework to implement the GloBE rules and the HKMTT. It includes the filing of notifications and returns, payment of top-up tax, record-keeping and penalty for non-compliance, etc. The government proposes that (i) a top-up tax notification will be required to be filed within six months after the end of the fiscal year; and (ii) subject to the transitional year, a top-up tax return be filed no later than 15 months after the last day of the reporting fiscal year. The filing deadline for the transition year is extended to 18 months.

For an in-scope MNE group which is (a) headquartered in Hong Kong; or (b) a non-Hong Kong headquartered jurisdiction that is unable to exchange GloBE Information Return (GIR) with Hong Kong under a qualifying competent authority agreement, the top-up tax return will include the data points required in the GIR. The GIR information reported in the top-up tax return of a Hong Kong headquartered MNE group will be exchanged with other relevant jurisdictions which have a qualifying competent authority agreement in place with Hong Kong.

The government proposes to ride on the existing general and administrative provisions of the IRO, with necessary modifications, for the purposes of the GloBE rules and HKMTT to deal with the record keeping requirements, objection procedures, collection and recovery of tax, and anti-avoidance issues etc.

Singapore

5 Certificate of Residence (COR) in Singapore

Guidance on control and management

The Inland Revenue Authority of Singapore (IRAS) recently has provided guidance on the use of virtual meeting technology (any technology that allows a person to participate in a meeting without being physically present at the place of meeting) for conducting board of directors meeting. It has clarified that that board meetings which involves the use of virtual meeting technology will generally be regarded as having strategic decisions made in Singapore if either of the following conditions is met:

- At least 50% of the directors (with the authority to make strategic decisions) are physically in Singapore during the meetings.
- Chairman of the Board of Directors (if the company has such an appointment) is physically in Singapore during the meeting.

The IRAS has given examples of scenarios where the control and management of a company may be considered not exercised in Singapore:

- There is no board of directors meeting held in Singapore. Instead, the directors' resolutions are merely passed by circulation.
- The local director is a nominee director while the rest of the directors are based outside Singapore.
- No strategic decisions are made by the local director in Singapore.
- No key employees are based in Singapore.

The IRAS has clarified that place of incorporation of a company is not necessarily indicative of the tax residency of a company.

Guidance on COR application for foreign-owned investment holding company

For foreign-owned investment holding company (where 50% or more of its shares are held by (i) foreign companies that are incorporated outside Singapore; or (ii) individual shareholders who are not citizens of Singapore), the IRAS may issue a COR if these companies can show that:

- The control and management of the company's business is exercised in Singapore.
- The company has valid reasons for setting up an office in Singapore.

5 Certificate of Residence in Singapore (cont.)

As per recent guidance from the IRAS, for COR applications in respect of calendar year 2025 and after, apart from demonstrating that decisions on strategic matters are made in Singapore, the company must also:

- Have at least 1 director based in Singapore who holds an executive position and is not a nominee director.
- Have at least 1 key employee (e.g. CEO, CFO, COO) based in Singapore.
- Be managed by a related company based in Singapore (e.g., the related company makes the decisions relating to the operations of the foreign-owned investment holding company or reviews the performance of the investments of the company).

The above change is to allow foreign-owned investment holding companies to better substantiate that they have valid reasons for setting up operations in Singapore.

6 New e-Tax Guide on Section 10L

On 8 December 2023, the IRAS has published the e-Tax Guide on Section 10L of the Singapore Income Tax Act which treats gains from sale or disposal of foreign assets by entities of a relevant group on or after 1 January 2024 and received in Singapore as income chargeable to tax (Section 10L), unless exclusions apply. Foreign assets include shares, equity interests and securities issued by a foreign entity.

An entity is a member of a group of entities if its assets, liabilities, income, expenses and cash flows are:

- Included in the consolidated financial statements (prepared by an entity in accordance with generally accepted accounting standards) of the parent entity of the group.
- Excluded from the consolidated financial statements of the parent entity of the group solely on size or materiality grounds or on the grounds that the entity is held for sale.

In this regard, the e-Tax Guide provides a clarification that an investment holding company which is not included in any consolidated financial statements (such as, of its parent fund or with its investee companies) and the reason is not due to size, materiality grounds, or on the grounds that the entity is held for sale will not fall within the scope of Section 10L.

Where an investment holding company is an entity of a relevant group, foreign-sourced disposal gains from the sale or disposal of a foreign asset will not be brought to tax if the entity has adequate economic substance in the basis period in which the sale or disposal occurs. In context of investment funds, the following economic substance conditions are required to be satisfied:

1. Pure equity-holding entity (it has been clarified that interest income derived from shareholders' loans will not be considered as "income incidental to its activities of holding shares or equity interests in other entities")

   a) The entity submits to a public authority any return, statement or account required under the written law under which it is incorporated or registered, being a return, statement or account which it is required by that law to submit to that authority on a regular basis.

   b) The operations of the entity are managed and performed in Singapore (whether by its employees or outsourced to third parties or group entities). An example has been provided which indicates an employee includes a director of the company (excluding nominee director).

   c) The entity has adequate human resources and premises in Singapore to carry out the operations of the entity (this includes own office, shared office with associated entity or of an outsourced service provider performing core income generating activity).

2. Non-pure equity-holding entity

The economic substance requirement will be determined based on an analysis of the entity's core income generating activities in Singapore (in context of fund management regimes, these are indicated as taking decisions on the holding and selling of investments, calculating risks and reserves, taking decisions on currency or interest fluctuations and hedging positions, preparing relevant regulatory or other reports for government authorities and investors).

   a) The operations of the entity are managed and performed in Singapore (whether by its employees or outsourced to third parties or group entities).

   b) The entity has adequate economic substance in Singapore, taking into account the following considerations:

      - The number of full-time employees of the entity (or other persons managing or performing the entity's operations) in Singapore.
      - The qualifications and experience of such employees or other persons.
      - The amount of business expenditure incurred by the entity in respect of its operations in Singapore.
      - Whether the key business decisions of the entity are made by persons in Singapore.

With respect to the above, key observations are:

- The economic substance requirement takes into account outsourcing arrangements where an entity outsources some or all of its economic activities to third parties or group entities (additional guidance provided on the requirements of the outsourcing arrangement).
- The economic substance requirement will not be applied at a jurisdictional level for a group. It will be assessed at the entity level, except in case of special purpose vehicles, where the economic substance requirements can be applied at the immediate holding entity / ultimate holding company level (subject to conditions).

EY Asia-Pacific private equity tax network

Private equity thought leadership quarterly top 10 tax topics

6 New e-Tax Guide on Section 10L (cont.)

- Entities are required to retain all records (including information on economic substance in Singapore) reasonably required for the IRAS to ascertain the amount of net gains from disposal of foreign assets chargeable to tax. These supporting documents need not be submitted with the income tax returns, but should be submitted to the IRAS for verification upon request.

The e-Tax Guide does not explicitly mention the application of economic substance requirements for entities under Singapore fund tax exemption schemes (i.e., under Section 13D/O/U/V) if such entities are entities of a relevant group. The Monetary Authority of Singapore is expected to issue a circular / guidance for such entities.

Australia

7 Key legislative and administrative changes in Australia

A number of legislative and administrative changes have arisen in Australia in recent months. These key changes include:

- Amendments to the Treasury Laws Amendment (Making Multinationals Pay Their Fair Share Integrity and Transparency) Bill 2023 (Bill), dealing with the new thin capitalization and debt deduction creation measures, as well as delays in the timing for when the Bill is likely to be passed.
- Introduction of legislation preventing the franking of distributions funded by capital raisings.
- The release by the Australian Taxation Office (ATO) of LCR 2023/D1, which provides the Commissioner of Taxation's preliminary view on the operation of the Corporate Collective Investment Vehicle (CCIV) regime.

An overview of each of these key changes is set out below.

Amendments to the draft thin capitalization and debt deduction creation measures

The Australian government has introduced draft legislation into Parliament, which if legislated, will repeal the existing asset based thin capitalization regime and replace it with a new earnings-based test. As currently drafted, the new thin capitalization rules will apply for income years commencing on or after 1 July 2023, while the new debt deduction creation rule will apply from 1 July 2024.

The draft legislation has been the subject of significant public consultation in Australia, which has led to a number of amendments to the rules since the last update. Most notably:

- In October 2023, an amended Exposure Draft was released for public consultation.
- In November 2023, proposed amendments to the Bill were published. It is anticipated that these amendments will be the final changes to the Bill, meaning the Bill should be indicative of the final form legislation.
- On 5 December 2023, the amended Bill was referred by the Senate to the Senate Economics Legislation Committee for inquiry, with a report due by 5 February 2024. This inquiry will result in unexpected delays in the passing of the Bill, which was forecast to be passed before year end.

The key features of the amendments are summarized below:

- **Expanded tax Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA):** The calculation of Tax EBITDA in the context of the fixed ratio test (FRT) has been expanded to enable excess tax EBITDA of downstream entities to be included in the tax EBITDA calculation of certain upstream entities. Broadly, this will be available where during the year the upstream entity holds a direct control interest of 50% or more and the controlling entity is an Australian company, unit trust, managed investment trust or Australian partnership (i.e., more than 50% of partners are Australian resident).
- **Other tax EBITDA amendments:** Changes to the method for calculating tax EBITDA for both the FRT and group ratio test (GRT) were introduced. These changes included, inter alia: (a) company dividends are now only disregarded where the receiving entity shareholder is an associate entity of the paying entity, applying a 10% or more thin capitalization control interests associate test; (b) requiring companies to be deemed to use the maximum amount of carried forward tax losses available, even where these losses are not in fact utilized; (c) a new subtraction for notional deductions of R&D entities; (d) specific calculation rules for attribution managed investment trusts.
- **Third-party debt test:** Amendments were made to the third- party debt test (TPDT) to broaden its application. These amendments included, inter alia: (a) expanding recourse of assets conditions to include more Australian assets and disregard recourse to minor or insignificant assets; (b) provide flexibility in the operation of the conduit financing provisions; (c) increase the pool of exemptions available for credit support rights; (d) allow a lender to have recourse to Australian assets that are held by the issuer, membership interests of the issuer or held by an Australian entity that is a member of the obligor group.
- **Choice of test:** Simplified rules were introduced to allow a choice to use the GRT or TPDT to be revoked.
- **Ordering rule:** Amendments to the rules for an entity's ordering of debt deduction considerations. A debt deduction must first be considered under the debt deduction creation rules and are reduced if those rules apply before applying the thin capitalization rules.
- **Debt deduction creation rule timing:** The debt deduction creation rules have been amended such that they should only apply from 1 July 2024. This is important as it provides an opportunity for private equity groups (PE groups) to review the potential impact of the new rules on current and proposed financing arrangements.

EY Asia-Pacific private equity tax network

Private equity thought leadership quarterly top 10 tax topics

7 Key legislative and administrative changes in Australia (cont.)

While a number of the amendments to the Bill are helpful for taxpayers and factor in elements of the public feedback received, the rules may still result in adverse outcomes for a number of PE Groups. Given that the thin capitalization rules as currently proposed are anticipated to apply from 1 July 2023, PE groups should be reviewing their current financing arrangements to ascertain which thin capitalization test is appropriate for their group and what additional debt deduction denials may arise.

The outcomes of the Senate Economics Legislation Committee inquiry should be monitored and may result in unexpected further changes to the Bill.

Distributions funded by capital raisings

In November 2023, the Treasury Laws Amendment (2023 Measure No. 1) Bill 2023 (Cth) received Royal Assent, introducing new specific tax integrity measure that mean certain distributions which are funded by capital raising activities will be unfrankable.

The new rules will apply to distributions made from 28 November 2023. They are intended to capture distributions declared by a company outside or additional to the company's normal dividend cycle, to the extent that they are funded directly or indirectly by capital arising activities that result in the issue of new equity interests.

By way of example, the new rules may apply to arrangements such as certain leveraged distributions (where new equity issuances are issued as part of the transaction), underwritten dividend reinvestment plans or an underwritten rights issue. The rules will be one of the key considerations going forward for PE groups receiving special dividends from their portfolio companies.

CCIV regime

The ATO has released draft Law Companion Ruling LCR 2023/D1, which provides the Commissioner's preliminary view on the operation of the CCIV regime and its application to taxpayers who have either established a CCIV or are interested in establishing a CCIV as an alternative to existing investment structures, such as managed investments trusts and venture capital limited partnerships.

By way of background, a CCIV is a new type of company limited by shares that is available for funds management. A CCIV is a legal form company with all its assets and liabilities segregated into "sub-funds" that are operated by a single corporate director. For tax purposes, each CCIV sub-fund is treated as a separate tax entity, that is a trust. The general trust taxation rules apply to CCIVs, subject to some modifications, where it does not qualify for the attribution managed investment trust (AMIT) regime. From a tax perspective, the intention of the regime is to align the tax outcomes of a CCIV and their investors with the existing treatment of investors in AMIT.

In addition to the Commissioner's views on the general operation of the CCIV regime, the draft ruling also covers specific matters, such as: (1) the deeming principle and its effect on the tax treatment of a CCIV, a CCIV sub-fund trust and investors; and (2) the Commissioner's views on specific tax interpretive issues.

The draft ruling will be effective from 1 July 2022, being the commencement date of the CCIV regime. The ATO has flagged that further guidance may be provided going forward as new interpretive issues arise.

The draft ruling will be beneficial for PE groups that are looking to establish a new fund vehicle that will register as a CCIV. The draft ruling will provide clarity around how the Commissioner will apply and interpret the regime, providing greater certainty to fund managers. This clarity around the ATO's approach will be beneficial for PE groups given the regime and its concepts are new in Australia and remain relatively untested.

New Zealand

8 Draft legislation of digital services tax

The New Zealand government introduced a Digital Services Tax Bill (DST Bill) on 31 August, which was subsequently allowed to lapse pending the 2023 New Zealand general election. Following the formation of a new coalition government and the reconvening of Parliament, the DST Bill has now been reinstated in New Zealand, meaning work on its enactment can resume.

The DST Bill allows the government to implement a 3% DST on the gross digital services revenue of large multinational groups (MNE groups) where the revenue is attributable to New Zealand users or land.

The proposed commencement date is 1 January 2025. However, this date could be deferred by up to five years, providing legislative flexibility. A deferred commencement date would give the government time to monitor implementation of Pillar One of the OECD's Two-Pillar multilateral solution and decide whether the DST Bill is necessary.

Design of the proposed DST

The proposed DST is conceptually similar to those introduced or proposed in other countries, including Canada and the United Kingdom.

It will be charged at a rate of 3% on an MNE group's gross "taxable digital services" revenue attributable to New Zealand users or New Zealand land. The DST will apply to an MNE group if both of these conditions are met:

- One of the group's business activities or services includes in-scope "taxable digital services" (principally the provision of intermediation platforms, social media and content sharing platforms, and internet search engines).
- The group's global annual gross "taxable digital services" revenue is at least EUR750 million.

The New Zealand DST will then apply if the annual gross taxable digital services revenue attributable to New Zealand users or New Zealand land exceeds NZ$3.5 million.

8 Draft legislation of digital services tax (cont.)

As the DST is intended to target certain highly digitalized business models that derive significant value from active user participation, some activities are specifically excluded from its scope. For example, loyalty programs accessed via online platforms would be excluded in certain circumstances.

New Zealand users

The DST Bill has adopted the concept of a "New Zealand user" as opposed to looking at tax residency, as the latter would be difficult to determine in the context of a DST. A "New Zealand user" is defined to include any user of the digital services normally located in New Zealand.

Under this approach, it would be possible for a New Zealand user to use an in-scope taxable digital service while not being physically present in New Zealand. Conversely, a foreign user that uses a digital service while visiting New Zealand would generally not be considered a New Zealand user if they are not normally located in New Zealand.

Filing and payment obligations

The DST will be administered by the New Zealand Inland Revenue Department (Inland Revenue). If the DST Bill is implemented in its current form, the following key filing and payment obligations will apply:

- The ultimate parent entity of an in-scope MNE group must nominate one of its members to act as the "DST representative member“.
- The representative member must register with Inland Revenue within 90 days of the end of the first revenue year in which the MNE group meets the global revenue threshold.
- The representative member must file an annual DST return, due six months after the end of the group's revenue year. This obligation generally exists regardless of whether there is any DST tax liability (i.e., nil returns are also generally required to be filed).
- Any DST tax liability must be paid to Inland Revenue within six months of the end of the MNE group's revenue year.
- Group members will be jointly and severally liable for any DST tax liability.

The DST Bill proposes a new penalty of up to NZ$100,000 where a DST representative member does not comply with the registration requirements. This penalty will apply at the discretion of Inland Revenue. A new penalty of NZ$500 for failing to file a DST return is also proposed. Other existing penalties may also apply in certain circumstances.

If implemented, the DST is expected to raise NZ$222 million over a four-year forecast period.

Next Steps

The DST Bill has not yet been referred to Select Committee for consideration of public submissions. This may occur in the first quarter of 2024.

Korea

9 Korea’s 2023 tax reform proposals

On 27 July 2023, Korea's Ministry of Economy and Finance announced the 2023 tax reform proposals (the 2023 Proposals). Unless otherwise specified, the 2023 Proposals will generally become effective for fiscal years beginning on or after 1 January 2024.

Significantly, the supplementary rules for income inclusion (known as Undertaxed Profit Rule (UTPR)) are proposed to have a 12-month delay, extending the effective date to 1 January 2025.

Revision of the global minimum tax rule (GloBE)

The 2023 Proposals include new and additional GloBE rules on top of Korean GloBE regulations under the current Adjustment of International Taxes Act (AITA) to reflect the OECD's Pillar Two GloBE rules, including the relevant administrative guidance, as well as other member countries' Pillar Two legislation activities.

Details regarding the GloBE rules in the 2023 Proposals are outlined below.

Introduction of filing obligation for overseas stock-based compensation

The 2023 Proposals introduce a filing obligation for domestic corporations (including the PE of foreign corporations) on transactions in which its executives or employees receive share-based compensation from foreign controlling shareholders.
Domestic corporations must submit the transaction details (e.g., details of grant, exercise, and payment of share-based compensation) by the 10th of March of the year following the taxable period to which the date of exercise or payment of stock-based compensation belongs. This rule will be applied to stock-based compensation exercised (or paid) on or after 1 January 2024.

Changes to when the statute of limitation starts to run for treaty rectification

Under the current Korean Corporate Income Tax Law, if a beneficial owner (foreign individual or foreign corporation) seeks to apply a tax treaty exemption in respect of its Korean-sourced income, either the beneficial owner or income payer may request the refund claim within five years from the last day of the month in which the tax is withheld. The 2023 Proposals provide that, effective 1 January 2024, the statute of limitations for the treaty rectification is within five years after the 10th day of the month following the month to which the withholding date belongs.

Introduction of special tax rules for omnibus accounts for foreigners

Under the 2023 Proposals, when foreign individuals or corporations invest through an omnibus account, the income payer must withhold tax from the payment. Reduced or exempted withholding tax rates under the treaties do not apply. However, either beneficial owners or income payers who wish to receive an exemption or reduced tax rate under tax treaties may apply for its rectification after the withholding taxes have been deducted. The new rule will be effective for income paid on or after 1 January 2024.

EY Asia-Pacific private equity tax network

Private equity thought leadership quarterly top 10 tax topics

Malaysia

10 Malaysia's capital gains tax update

Further to the Malaysia Budget 2024 announcement on 13 October 2023, the Finance (No. 2) Act 2023 (Finance Act) was gazetted into law on 29 December 2023. Pursuant to the Finance Act, the following will be subject to Malaysian capital gains tax (CGT):

- Disposal of shares of a company incorporated in Malaysia not listed on the stock exchange.
- Disposal of shares of a company incorporated outside Malaysia (foreign company), where the foreign company directly or indirectly owns real property in Malaysia exceeding certain thresholds, as determined based on the parameters of the law.
- Disposal of all capital assets situated outside Malaysia (not limited to shares), where the gains are received in Malaysia.

Effective date

Based on the Finance Act, CGT would apply on all disposals listed above from 1 January 2024. However, pursuant to an Exemption Order issued on 29 December 2023, gains or profits from the disposals of shares in a Malaysian incorporated company not listed on the stock exchange will be exempted from tax, if the disposal takes places between 1 January and 29 February 2024. Hence, CGT will only be payable on disposals of unlisted shares in Malaysian-incorporated companies from 1 March 2024.

Rates of tax

For disposals under categories 1 (disposals of unlisted shares in Malaysian-incorporated companies) and 2 (disposals of shares in foreign companies deriving value from real property in Malaysia) above, the rates of tax would be as follows:

- If the shares were acquired before 1 January 2024, the disposer has the option of paying CGT of either 10% of the gain (as calculated based on CGT principles) or 2% on the gross disposal price.
- If the shares were acquired on or after 1 January 2024, the CGT rate would be 10% of the gain.

For disposals under category 3 (disposal of capital assets situated outside Malaysia), the rate of tax will be the prevailing tax rate of the disposer, for example, generally 24% for a Malaysian company.

EY Asia-Pacific private equity tax network

Private equity thought leadership quarterly top 10 tax topics

EY Asia-Pacific key Private Equity Tax contacts

Ian Scott
EY Asia-Pacific Private Equity Tax Co-leader
+61 2 9248 4774
ian.scott@au.ey.com

Adam Williams
EY Asia-Pacific Private Equity Tax Co-leader
+852 9400 4535
adam-b.williams@hk.ey.com

Darryl Kinneally
EY ASEAN Private Equity Tax Leader
+65 6309 6800
darryl.kinneally@sg.ey.com

Matt Weerden
EY Oceania Private Equity Tax Leader
+61 2 8295 6788
matt.weerden@au.ey.com

Masako Kanaya
EY Japan Private Equity Tax Leader
+81 3 3506 2430
masako.kanaya@jp.ey.com

Subramaniam Krishnan
EY India Private Equity Tax Leader
+91 226 192 1949
subramaniam.krishnan@in.ey.com

This quarter's contributors

Adam Williams
Anil Kumar Puri
Brad Wheeler
Chai Yee Ng
Christy Ngai
Kim Cunningham
Matt Weerden
Michelle Chua
Mriganko Mukherjee
Tammy Tan
Yoohyun Baik

EYG Number 000860-24Gbl
ED None