Foreign Contractor Withholding Tax in Vietnam

The tax system of the Socialistic Republic of Vietnam has undergone lots of reforms, is still developing and has become aligned with international rules and practices. A variety of different taxes needs to be kept in mind for foreign companies doing business in Vietnam.

The following brochure will provide you with information on one of the most important, yet underestimated tax schemes in Vietnam, the Vietnamese withholding tax, the *Foreign Contractor Withholder Tax* ("**FCWT**"), a taxation scheme that applies to foreign entities providing services within Vietnam.

1. Legal Basis

The legal basis of the FCWT is Circular No. 103/2014/TT-BTC, on Guidance for fulfillment of tax liabilities of foreign entities doing business in Vietnam or earning income in Vietnam ("**Circular 103**").

2. General Information

If the sale of goods or services is provided by an in Vietnam registered branch ("**subsidiary**"), the subsidiary has to pay corporate income tax ("**CIT**") as well as value added tax ("**VAT**"). The situation differs, if the sale of goods and services is provided by a foreign supplier instead of a Vietnamese subsidiary. In this case, the foreign company has no presence in Vietnam; therefore, it cannot be directly liable for local taxes such as CIT and VAT. Thus, a scheme of FCWT has been implemented and made the foreign entity to be liable to tax itself.

The FCWT contains two components, CIT and VAT. It is usually collected by a clearing system. This means that the Vietnamese contracting party will withhold a percentage of the invoice to pay therefor to the Vietnamese tax office. The foreign party then receives a net amount and, by this, shall not be obligated to register for tax authorities in Vietnam.

3. Getting into details

There are only few exceptions where FCWT is not paid:

1. If the transaction is performed between a subsidiary and a Vietnamese counterpart.
2. If the foreign vendor sells the goods based on EXW-, FCA-, FAS- or FOB. This shall not apply to cases, where the seller provides after sales services related to the product directly. In this case the FCWT is also applicable to the product itself.
3. If the service is offered and rendered outside of Vietnam.

This means in general: For each amount of remunerations generates from services, a foreign entity has to pay FCWT.

1.1 Variety of components – Method of payment

FCWT is a combination of VAT and CIT components. Both are applied together. The rates of VAT and CIT are various, depending on the goods sold or the services provided (see tables below). The commonly applicable rate is 5% VAT and 5% CIT. Pursuant to Art. 4 of Circular 103, foreign entities are not required to conduct the registration and declaration of CIT and VAT in Vietnam. Instead Vietnamese parties are required to withhold the amount of CIT and VAT as computed in accordance with the guidelines in Item 2.1 and 2.2 prior to its payment to foreign entities.

A reverse charge system is possible. This is applied, if the parties agree to apply an individual agreement in relation to the FCWT, and that such tax shall be added the invoiced amount. As the Vietnamese contracting party has to collect and remit the FCWT directly, the incoming remuneration at the Foreign Service Company is – in case of such individual agreement - not the full agreed of 0100%, but the payment less FCWT.

1.1.1 VAT Component

The VAT component is determined as follows:

VAT payable = VAT taxable turnover x VAT rate

The VAT rate depends on the services provided by the foreign contractor, or the goods related to services. VAT on the added value of services, services related to VAT-liable goods is calculated by the turnover for VAT calculation multiplies by the rate (%) of the added value to the turnover. The turnover subjected to VAT is the total turnover from the provision of services, services related to VAT-liable goods which the company receives including the taxes payable, the cost that the customer paid on behalf of the company (if any). According to the nature of business, each VAT rate shall be applied as below:

No.	Business lines	VAT rate (%)
1	Services, rental of machinery and equipment, insurance; construction, installation exclusive of raw materials, machinery and equipment	5
2	Production, transportation, services related to goods; construction, installation inclusive of raw materials, machinery and equipment	3
3	Other activities	2

1.1.2 CIT Component

The CIT liability is determined as follows:

CIT payable = CIT taxable x CIT rate

The turnover for CIT calculation is the total turnover excluding VAT earned by foreign contractors without deduction of any taxes payable. The turnover for CIT calculation includes the costs paid by the Vietnamese party on behalf of foreign contractors. CIT rates are summarized as follows:

No.	Business lines	CIT rate (%)
1	Trading: supply of goods on delivery term (DAP, DDU, etc.) in Vietnam without other services or in the form of on-the-spot export	1
2	Services, lease of machinery and equipment, insurance, lease of drilling platforms	5
	Except for: Services together with supply of machinery and equipment	2
	Services of managing restaurants, hotels and casinos	10
	Derivative financial services	2
3	Lease of aircraft, aircraft engines, aircraft spare parts and sea going vessels	2
4	Construction and installation with or without supply of materials, machinery or equipment	2
5	Other production or business activities and transportation (including sea and air transportation)	2
6	Transfer of securities, certificates of deposit, offshore reinsurance and commission for ceding reinsurance	0,1
7	Loan interests	5
8	Royalties	10

1.2 Services connected to sales

If the contract incorporates multiple parts, e.g. sale of computer (goods) and an afterwards service delivery, e.g. IT services for the computers sold (services), it may be reasonable to have separate invoices for every service activities , so each respective amount of the remuneration is able to be allocated to the actual tax rate. The following example shall demonstrate the advantage of this separate taxation:

a. Invoice without clear indication for each service: 5% VAT for the sale of the computer and the subsequent IT services;
b. Invoice with clear indication for each service: 0% VAT for the sale of the computer and 5% VAT for the subsequent IT services.

1.3 Payments to Vietnamese subcontractors

When a foreign services provider employs a Vietnamese subcontractor to perform (a part of) its services, e.g. within the scope of a major project, the payments of the foreign party to the Vietnamese subcontractor are not subjected to be taxed by FCWT. Instead, the Vietnamese subcontractor is liable to tax therefor. Because of procedural reasons, the foreign service provider has to reveal its contractual agreement with the subcontractor (similar to the agreed upon payment) to its Vietnamese client.

1.4 Tax credit/Tax refund

Because of a double taxation agreement relating to FCWT, tax exemption is available for CIT. The foreign party cannot reimburse Vietnamese subcontractor the amount of VAT for purchased goods or services. A registration for tax purposes is possible, if (1) the foreign party has a subsidiary, (2) the project lasts longer than 183 days and (3) the foreign party maintains its books in accordance with Vietnamese Accounting Standards.

If the foreign party is being registered for tax purposes, it has to pay taxes, like any other Vietnamese companies, especially: (a) VAT related to turnover (basic tax rate of 10%), (b) CIT; the tax rate is either (aa) similar to every other domestic companies (which means 20% of VAT taxable turnover) or (bb) defined on the basis of total turnover in Vietnam plus FCWT (mostly 5% for services) whichever is higher.

4. Concluding Recommendation

With a registration for tax purposes in Vietnam, compliance requirements come along with the foreign party, which may cause a higher tax burden in certain circumstances. Therefore, a registration for tax purposes of a foreign company is only needed if significant indirect tax charges are to be expected.