DEMOCRATIC REPUBLIC OF EAST TIMOR

MINISTRY OF PLANNING AND FINANCE

EAST TIMOR REVENUE SERVICE

Guide
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(English)
Income Tax

INCOME TAX

A guide for Income Tax payers

For the 2002 income tax year

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Attachment: ***SUMMARY OF LEGISLATIVE CHANGES: INCOME TAX***

1. INTRODUCTION

1.1. Income Tax – an overview

Income tax applies to any increase in economic capability received or accrued by a taxpayer, with the exception of salaries subjected to wage income tax.

Gross receipts from some types of business and investment income are subject to a *final* withholding tax upon payment and are not declared in the annual income tax return.

Income tax applies to both individuals and enterprises.

Tax rates for income earned by an individual and not subject to a final withholding tax are progressive:

- 10% for any part of annual income of up to US$ 3,368;
- 15% for any part of annual income between US$ 3,368 and US$ 6,737; and
- 30% for any part of annual income above US$ 6,737.

The tax rate for income earned by other entities and not subject to a final withholding tax is a flat rate of 30%.

Resident individuals are entitled to a deduction against income on the calculated on the basis of:

- US$388 for an individual;
- an additional US$194 for a married individual;
- an additional US$194 for each wholly dependent family member (up to a maximum of three).

Persons conducting business activities are liable to minimum income tax of 1% of total turnover for the year. The amount to be paid is the greater of the person's ordinary income tax or minimum income tax.

Payment of income tax can be made through:

- instalments; and/or
- a self-assessed final payment (to be made with the lodging of the annual income tax form).

Income tax payable for the **2002** tax year is due with the lodgment of an annual income tax form or return on or before **15 March 2003**.

1.2. Structure of the Income Tax Law

UNTAET Regulation 1999/1 continued the operation of Indonesian income tax laws that now apply, subject to the modifications contained in UNTAET Regulation 2000/18 (as amended) and UNTAET Directive 2001/2 (as amended) on the calculation of taxable income of taxpayers and administrative matters relating to income tax. The main Indonesian legislation that applies in relation to income tax is:

- Law on Income Tax (No. 10 of 1994)
- Law on General Rules and Procedures of Taxation (No. 9 of 1994)

Apart from this legislation, the body of Indonesian tax law contains a considerable variety of regulations, decrees and circular letters, each of which has its own characteristics:

- Government Regulations – these typically contain legislative rules on specific aspects of the law.
- Elucidation to Legislation and Regulations – while sometimes merely repeating the law or giving an example, the elucidations sometimes contains additional information or clarification that is not apparent from the law.
- Presidential Decrees – these typically provide an exception or relief from the general provisions of the tax law.
- Minister of Finance Decrees – these are the implementing rules for specific aspects of the law, e.g. depreciation categories for assets. Such decrees will typically state who can apply, what are the conditions, who approves, time limits etc.
- Director General of Taxation Decrees – these contain the detailed forms and procedures to be followed.
- Circular Letters – these cover a wide range of purposes. Some provide detailed guidance on particular issues and others contain clarification of the official position on specific issues.

1.3. Public rulings

The East Timor Revenue Service (ETRS) issues public rulings, which give explanations of how the ETRS Commissioner interprets specific aspects of Regulation 2000/18 and any Directives issued under the Regulation.

The following public rulings have been issued:

Number	**Title**
2001/ 1	The Public and Private Rulings programs
2001/ 2	The Power of the Commissioner of the ETRS to Cancel Taxation Obligations
2001/ 3	When is there employment in East Timor?
2001/ 4	Services tax aspects of vehicle rental
2001/ 5	The meaning of "wages" and "reward for services"
2001/ 6	Construction income and subcontractors
2001/ 7	Depreciation
2001/ 8	Useful lives of depreciable assets
2001/ 9	Apportioning expenses when some income is not subject to withholding tax
2001/10	Auditing, Access and Information Collection
2001/11	Who is a resident of East Timor for tax purposes?
2001/12	Additional Tax
2001/13	The value of “non-wage benefits” for employees of income tax exempt employers
2002/ 1	Timor Sea taxpayers

2. TAX SUBJECTS

2.1. Who is subject to income tax

The following persons and entities are subject to income tax (or are tax subjects) in East Timor:
- an individual;
- an undivided estate as a unit in lieu of the beneficiaries;
- a body in the form of a limited company, limited partnership, other partnership, government business enterprise (including an enterprise owned by the East Timor Public Administration or a political or administrative subdivision of that administration), affiliation, association, firm, cooperative, foundation or similar organisation, institute, pension fund and other forms of business; and
- a permanent establishment of a non resident.

An undivided estate (e.g. deceased estate) constitutes a substitute tax subject, replacing the beneficiaries. Designating an undivided estate as a substitute tax subject is intended to enable tax to continue to be imposed on income derived from the estate.

An individual or other body, as a tax subject, can either be resident or non-resident in East Timor for tax purposes.

2.1.1. Resident Taxpayer

A resident taxpayer is:
- an individual who is present in East Timor for more than 182 days in a tax year and whose permanent place of abode is in East Timor;
- a body established or domiciled in East Timor;
- an undivided estate established or domiciled in East Timor;
- a non-resident conducting business through a permanent establishment in East Timor.

The question of “Who is a resident of East Timor for tax purposes?” is covered in ETRS/SRTL Public Ruling 2001/11.

2.1.2. Non-Resident Taxpayer

A non-resident taxpayer is:
- an individual who is not present in East Timor for more than 182 days in a tax year;
- an individual whose permanent place of abode is outside of East Timor;
- a body which is not established or domiciled in East Timor.

2.1.3. Permanent Establishment

A permanent establishment is any establishment in East Timor used by a non-resident to conduct business in East Timor in the form of, amongst others:
- a place of management;
- a branch office;
- a representative office;
- an office building;
- a factory;
- a workshop;
- a place of mining and extraction of natural resources, and drilling in territory used for mining exploration;
- a fishery, place of animal husbandry, farm, plantation or forest;
- a construction, installation or assembly project;

- the furnishing of services in whatever form by employees or other people, if conducted for more than 60 days in any 12 month period;
- an individual or a body acting as an agent other than an agent of independent status;
- an agent or employee of an insurance company that is not established or domiciled in East Timor and which receives insurance premiums or covers risks in East Timor.

2.2. Who is not subject to income tax

The following are not subject to income tax in East Timor:
- a representative body of a foreign state;
- diplomatic and consular representatives or other foreign officials and the individuals who work for and stay with them at their official residence, provided they are not East Timorese citizens, do not receive or accrue income other than from the performance of their official duties in East Timor, and the foreign state grants reciprocal treatment;
- international bodies as determined by the East Timor Public Administration provided they do not conduct business or engage in other activities to gain income in East Timor
- officials of international bodies as determined by the East Timor Public Administration, provided they are not East Timorese citizens and do not conduct business or engage in activities or other employment to gain income in East Timor
- natural persons whose remuneration is financed out of the Trust Fund for East Timor.

2.3. What is subject to income tax

2.3.1. Income

Income subject to income tax in East Timor is described as any increase in economic capability received or accrued by a taxpayer, in whatever name or form and originating from within or outside East Timor, which can be used for consumption or to increase the wealth of the taxpayer concerned.

Wages received or accrued in the 2001 and subsequent tax years are not subject to income tax but are subject to wage income tax.

Income that is subject to income tax in East Timor includes the following:
- consideration or other remuneration received or accrued in connection with work or services except for wages received or accrued in the 2001 and subsequent tax years;
- lottery prizes or gifts from work or other activities, and awards;
- profit from business;
- gains from the sale or transfer of property, including:
    - gains from the transfer of property to a corporation, partnership and other body in exchange for shares or capital participation;
    - gains accrued by a corporation, partnership or other body through the transfer of property to shareholders, partners or members;
    - gains from liquidation, merger, consolidation, expansion, separation or takeover of a business;
    - gains from the transfer of property in the form of gift, aid or donation, except when given to blood relatives within one degree of direct lineage, or to religious, educational or other social bodies or to small businesses including cooperatives as determined by the East Timor Public Administration, provided there is no

business, work, ownership or control relationship between the parties concerned;

- refunds of tax payments already deducted as expenses;
- interest, including premiums, discounts and compensation from loan repayment guarantees;
- dividends, in whatever name and form, including dividends paid by an insurance company to policyholders and the distribution of surplus by a cooperative;
- royalties;
- rent and other income related to the use of property;
- annuities received or accrued;
- gains from the cancellation of indebtedness;
- gains from fluctuations in foreign currencies;
- gains from revaluation of property;
- insurance premiums;
- contributions received or accrued by an association from its members who consist of taxpayers engaged in business or independent work, provided the contributions are determined on the basis of volume of business or independent work of the members;
- an increase in net wealth from income which has not been taxed.

2.3.2. Income excluded from Taxable Income (final withholding)

Certain types of income that are subject to final withholding tax are excluded from taxable income depending on whether the relevant income was received by a natural person (ie individual) or not and whether the income relates to a period before or after 1 July 2002.

Information regarding the types of income that is subject to withholding tax can be found in the section of this Guide titled Withholding Tax.

Final Withholding:
For *natural persons* (ie individuals) who received any of the types of income subject to withholding tax and the income in fact has been correctly subjected to final withholding tax, no further liability with respect to income tax will apply and the income will not be included in Taxable Income.

For *persons other than individuals* (ie partnerships, companies or any other form of entity) which received any of the types of income subject to withholding tax relating to a period **before 1 July 2002** and the income has been correctly subjected to final withholding tax, no further liability with respect to income tax will apply and the income will not be included in Taxable Income in the annual income tax form.

For *persons other than individuals* (ie partnerships, companies or any other form of entity) which received any of the types of income subject to withholding tax **except dividends, interest, royalties and rent** relating to a period **after 30 June 2002** and the income has been correctly subjected to final withholding tax, no further liability with respect to income tax will apply and the income will not be included in Taxable Income in the annual income tax form.

Non-final Withholding:
For *persons other than individuals* (ie partnerships, companies or any other form of entity) who received **dividends, interest, royalties or rent** relating to a period **after 30 June 2002,** the amount is to be included in Taxable Income in the annual income tax form and a credit will be allowed for withholding tax that has been paid.

2.3.3. General Deductions from Income

The amount of Income for residents and non-residents who have a permanent establishment in East Timor shall be determined on the basis of gross income reduced by:

a. expenses to earn, recover and secure the income which is subject to income tax;
b. tax (except Income Tax);
c. depreciation of costs to procure tangible property and amortization of costs to obtain rights and any other costs which have a useful lives for more than 1 (one) year;
d. losses due to sales or transfer of property owned and used in business or owned for the purposes of earning, recovering or securing income;
e. losses due to the difference of foreign exchange rate;
f. the company's research and development expenses performed in East Timor;
g. scholarship, apprenticeship, and training costs.

3. TAXABLE INCOME

3.1. Taxable income from business activity

The taxable income from the conduct of a business is the net profit for financial accounting purposes for the year, prepared in accordance with the International Accountings Standards (other than IAS 39), and subject to modifications in Directive No. 2001/2.

3.2. Accounting period

The financial year is a 12-month period starting on 1 January and ending on the following 31 December. Income tax is levied for each financial year by reference to a taxpayer's income for an income year.

3.3. Cash or Accrual Basis

A taxpayer whose annual gross turnover is more than $100,000 shall account for income tax on an accrual basis.

A taxpayer whose annual gross turnover is less than $100,000 may account for income tax either on cash or accruals basis.

A taxpayer accounting for income tax on a cash basis recognizes income when received or made available and incurs expenses when paid.

A taxpayer accounting for income tax on an accrual basis recognizes income when it is receivable and incurs an expense when it is payable. For tax purposes an amount is receivable when the taxpayer becomes entitled to receive it even if the time for discharge of the entitlement is postponed or the entitlement is payable by instalments. An amount is payable when all the events that determine liability have occurred and the amount of the liability can be determined with reasonable accuracy, but not before economic performance occurs. Economic performance occurs:

(a) in the case of acquisition of services or assets, at the time the services or assets are provided,

(b) in case of use of assets, at the time the assets are used; and

(c) in any other case, at the time the taxpayer makes payment in full satisfaction of the liability.

3.4. Aspects of the tax calculation (Directive No. 2001/2)

3.4.1. Inventory

Whatever the basis adopted in valuing trading stock for accounting purposes, for tax purposes inventories are measured at cost and determined according to the absorption-cost method.

Where particular items of inventory are not readily identifiable, a taxpayer may account for inventory under the first-in-first-out or weighted average cost method.

A taxpayer may change its inventory recognition method with the written permission of the Commissioner and subject to any conditions that the Commissioner may impose to ensure that no item is omitted and no item is taken into account more than once.

3.4.2. Depreciation

A taxpayer is allowed a deduction for depreciable assets and business buildings during the tax year.

For this purpose, “business building” is a building used wholly or partly in the conduct of taxable business activities and a “depreciable asset” is any tangible movable property of a taxpayer that has a useful life exceeding one year, which is likely to lose value as a result of wear and tear, or obsolescence and is used wholly or partly in the conduct of taxable business activities.

Expenditure on fixed assets with a useful life of one year or more must be capitalized for accounting and tax purposes. For accounting purposes, depreciation should reflect exhaustion, wear and tear. For tax purposes, depreciation deductions are allowed only in respect of some class of property used during the income year for the purpose of producing assessable income or ready for use for that purpose and held in reserve.

The acquisition or construction costs, and the cost of improvement, renewal, and reconstruction, of business buildings are to be depreciated individually on a straight-line basis.

The cost of a business building does not include the cost of the land on which the building is situated.

Depreciation methods

Depreciable assets may be depreciated:

1. Individually on a straight-line basis or
2. Under a pooling system on a declining balance basis.

For further information, ETRS Public Ruling 2001/7 ‘Depreciation’ gives an explanation and provides examples of these methods of depreciation.

The same method of depreciation shall apply to all depreciable assets of a taxpayer.

A taxpayer may change its method of depreciation with the written permission of the Commissioner and subject to any conditions that the Commissioner may impose with respect to the change.

No depreciation deductions are allowed for a depreciable asset or business building until the asset or building is placed in service. Depreciable property held in reserve is considered as placed in service when it is ready to produce taxable income.

Where a depreciable asset is used only partly in the conduct of taxable business activities, the depreciation deduction shall be proportionately reduced.

If a taxpayer revalues a business building or depreciable asset, no depreciation deduction shall be allowed for the amount of the revaluation.

Pooling system of Depreciation

The depreciation deduction for each depreciation pool for a tax year shall be calculated by applying the depreciation rate for the pool to the written down value of the pool at the end of the tax year. The written down value of a depreciation pool at the end of a tax year shall be the written down value at the end of the previous tax year:

a. increased by the cost of depreciable assets added to the depreciation pool, and the cost of improvement, renewal, and reconstruction of assets in the pool, during the tax year; and

b. decreased by the consideration received or receivable for assets in the depreciation pool alienated during the tax year, including any compensation received for the loss of such assets due to natural calamities or other involuntary disposals.

In the year that an asset is first used the cost price added to the pool is reduced to reflect the fact that the asset was not used for the full year. The remaining value of the asset is added to the pool in the following year.

Where the written down value at the end of a tax year of a depreciation pool is a negative amount, that amount shall be included in the income of the taxpayer for the year, and the written down value of the pool shall be zero.

Where the written down value at the end of a tax year of a depreciation pool is less than $US100, a further deduction for the tax year shall be allowed equal to the amount of that written down value. The written down value of the pool at the end of the tax year shall be zero.

If all the depreciable assets in a depreciation pool are alienated before the end of the tax year, a deduction is allowed for the amount of the written down value (if any) of the pool at the end of the year. The written down value of the pool at the end of the tax year shall be zero.

Individual Basis of Depreciation

The following rules apply to a depreciable asset depreciated on a straight-line basis and to a business building:

(a) where the cost of a depreciable asset is less than $100, the depreciation deduction in the year that the asset is acquired is equal to the cost of the asset and no depreciation deduction is allowed for that asset in a subsequent year;

(b) the cost of an improvement, renewal, or reconstruction of a depreciable asset or business building shall be treated as the cost of a new asset with a useful life equal to the original useful life of the asset or building;

(c) where the depreciable asset or business building is used only partly in the conduct of taxable business activities and partly for another purpose, the amount of depreciation allowed as a deduction shall be reduced by the proportion of the non-business use;

(d) where the depreciable asset or business building is acquired and put in service in the conduct of taxable business activities in a tax year, the amount of depreciation allowed as a deduction in that year is reduced by a fraction equal to the fraction of the year prior to the time the asset or building was put in service and the amount reduced shall be allowed as a deduction in the year after the asset or building has been depreciated; and

(e) where the depreciable asset or business building is alienated by a taxpayer, the cost of the asset or building shall be reduced by the depreciation deductions allowed under this section.

3.4.3. Amortization of Intangibles

A taxpayer is also allowed a deduction for the amortization of intangible assets and expenditure.

"Intangible asset" is any property (other than tangible movable property or immovable property) that:

(a) has a useful life exceeding one year; and

(b) is used wholly or partly in the conduct of taxable business activities;

"Intangible expenditure" is any expenditure incurred other than in the acquisition of any tangible or intangible movable or immovable property.

The acquisition or creation cost, and the cost of improvement or renewal, of intangible assets for use by a taxpayer shall be amortized individually on a straight-line basis at the relevant rate.

The amount of any intangible expenditure with a useful life exceeding one year incurred by a taxpayer in the conduct of taxable business activities shall be amortized individually on a straight-line basis.

Where an intangible asset or expenditure is used only partly in the conduct of taxable business activities, the amount allowed as a deduction shall be reduced by the proportion of the non-business use. Where an intangible asset or expenditure is used only for part of the tax year in the conduct of taxable business activities, the amount allowed as a deduction shall be reduced by the proportion of the tax year that the asset was not used in the conduct of taxable business activities.

Where an intangible asset has been alienated by a taxpayer during a tax year, the cost of the asset shall be reduced by any deductions allowed in respect of the asset.

Expenditures with a useful life of more than one year incurred before the commencement of taxable business activities shall be capitalized and amortized individually on a straight-line basis

Examples of such expenditures include the cost of feasibility studies, construction of prototypes, and trial production activities and exclude the cost of acquiring land, or expenditures depreciated or amortized under another provision.

3.4.4. Depreciation and amortization rates

Part A
Business Buildings

The rates of depreciation of business buildings are:

Type of Building	Useful Life	Straight-line Depreciation Rate
Permanent	20 years	5%
Non-permanent	10 years	10%

"permanent building" means any business building other than a non-permanent building; and

"non-permanent building" means any business building constructed of materials of a temporary nature, or for temporary purposes, including any movable building.

Part B
Depreciable Assets

1. Where pooling applies, depreciable assets shall be divided into the following depreciation pools:

Pool 1	Assets with a useful life of 1-4 years
Pool 2	Assets with a useful life of 5-8 years
Pool 3	Assets with a useful life of more than 9 years

2. Depreciation rates for depreciation pools:

Pool	*Depreciation rate*
1	50%
2	25%
3	12.5%

3. Depreciation rates where assets are depreciated individually on a straight-line basis:

Useful Life	*Depreciation Rate*
Assets with a useful life of 1-4 years	25%
Assets with a useful life of 5-8 years	12.5%
Assets with a useful life of more than 9 years	6.25%

4. The classification of depreciable assets in accordance with their useful life is set out in ETRS Public Ruling 2001/8.

Taxpayers who acquire an asset that is not listed in the Public Ruling may request the Commissioner to provide advice by way of private ruling on the useful life of the asset.

The Public Ruling sets out the useful life for the following assets:

Depreciable Assets with a useful life of 1-4 years

All business types:	a) Furniture and equipment of wood or rattan including tables, desks, chairs, cabinets and the like, which are not part of a building; b) Computers, printers, scanners and the like;
	c) Office equipment, such as typewriters, duplicators, photocopy machines, accounting machines and the like;
	d) Electrical equipment such as amplifiers, tape/cassette players, video recorders, televisions and the like;
	e) Motorcycles, bicycles, tricycles;
	f) Specific tools for the relevant industry/ services;
	g) Kitchen tools for cooking, food and drinks;
	h) Dies jigs and moulds.
Agriculture, plantation, forestry, fishery:	Non-mechanically operated equipment.
Food and Beverage industry:	Lightweight movable machinery such as hullers, peeling equipment, rice hulling processors, dryers, pallets, and the like.
Transportation, warehouse, and communication:	Taxis, buses, and trucks used for passenger transportation.

Depreciable Assets with a useful life of 5-8 years

All business types:	a) Furniture and furnishings of metal including tables, benches, chairs, armoires and the like which are not part of a building;
	b) Temperature regulators such as air conditioners, fans, and the like;
	c) Automobiles, buses, trucks, speedboats and the like;
	d) Containers and the like.
Agriculture, plantation, forestry, fishery:	a) Agriculture/plantation machinery such as tractors, ploughs, rakes, planters, seed broadcasters and the like;
	b) Machines that process, produce or manufacture material or agricultural items, forestry, plantation and fishery.
Food and beverage	a) Machines that process industry animal products, poultry and fishery, e.g. in a dairy factory, a fish-canning factory;
	b) Machines that process plant products, e.g. coconut oil machines, margarine, coffee grinders, candies, machines to process kernels such as to mill rice, corn, tapioca;
	c) Machines that produce drinks and all types of beverage material.
Machine industry	a) Machines that produce food material and any type of food;
	b) Machines which produce light machines (e.g. sewing machines, water pumps).
Carpentry	Machines and wood chopping equipment.
Construction	Equipment used such as big trucks, dump trucks, cranes, bulldozers and the like.
Transportation, warehousing and communication.	a) Work trucks for transportation, loading, and other such trucks;
	b) Passenger ships, cargo ships, specific ships made for the transportation of specific goods (e.g. corn, stone, mining ores and the like) including refrigerated ships, tankers, fishing boats and the like, which weigh up to 100 DWT;
	c) Ships made specifically to pull or push other ships, lightships, fireships, dredgers, floating cranes and the like, which weigh up to 100 DWT;
	d) Sailboats with or without any motor having a

	weight up to 250 DWT;
	e) Airships.
Telecommunication	a)Telephone sets;
	b) Telegraph sets, including dispatch equipment and radio telegraph and radio telephone receiver sets.

Depreciable Assets with a useful life of 9-16 years

Mining other than oil and gas:	Machinery used in the mining field, including machinery which processes mineral products.
Spinning, Weaving and Dyeing:	a) Machinery which processes/produces textile products (e.g. cotton cloth, synthetic silk, wool and other animal hair, linen, carpet, fuzzy cloth, tulle);
	b) Machinery for yarn preparation, bleaching, dyeing, printing, finishing, texturing, packaging and the like.
Carpentry:	a) Machinery which produces wood products, items of straw, grass and other plait work;
	b) Machinery and wood sawing equipment.
Chemical Industry:	a) Machinery and equipment that processes/produces chemical industry products and industries which are related to the chemical industry (e.g. non-organic chemical matter, organic chemical fusion and non-organic from precious metal, radioactive elements, isotopes, organic chemical matter, pharmaceutical products, fertilizer, dyeing materials, colouring materials, paint, varnish, etheric oil and fragrance resinoids, beauty products and makeup products, soap, detergent and other organic cleaners, albumin substance, adhesive, explosives, pyrotechnical products, matches, pyroforis, photographic and cinematographic equipment;
	b) Machinery that processes/produces other industrial products (e.g. artificial resin, plastic material, ester and ether from cellulose, rubber, synthetic rubber, tanning leather, hide and raw leather).
Machinery Industry:	Machinery that produces/manufactures medium size and heavy-weight machinery (e.g. automobile machine/engine, ship's engines).
Transportation and Communication:	a) Navigational radio sets, radar and long distance control sets;
	b) Passenger ships, cargo ships, specific ships made for the transportation of specific goods (e.g. corn, stone, mining ores and the like) including refrigerated ships and tankers, fishing boats and the like, which weigh over 100 DWT up to 1000 DWT;
	c) Ships made specifically to pull or push other ships, lightships, fireships, dredgers, floating cranes and the like, which weigh over 100 DWT up to 1000 DWT;

	d) Sailboats with or without any motor, which weigh over 250 DWT;
	e) Airplanes and helicopters of any kind.
Others:	Other tangible assets which are not included in the other asset classes.

Depreciable Assets with a useful life of more than 16 years

(**Note**: With effect for the 2002 and subsequent income tax years, the categories of assets with useful lives of 9-16 years and more than 16 years have been combined. There is now no separate treatment for assets with a useful life of more than 16 years.)

Construction	Heavy machinery for construction
Transportation and Telecommunication	a) Steam, electric or other locomotives and tenders on railroad tracks;
	b) Car trains, passenger and cargo cars, including containers specifically made and equipped to be pulled by one or several types of transportation equipment;
	c) Passenger ships, cargo ships, specific ship made for the transportation of specific goods (e.g. corn, stone, mining ores and the like) including refrigerated ships, tankers, fishing boats and the like, which weigh over 1000 DWT;
	d) Ships made specifically to pull or push other ships, lightships, fireships, dredgers, floating cranes and the like, which weigh over 1000 DWT;
	e) Floating docks.

Part C
Intangible Assets and Expenditures, and Pre-commencement Costs

1. The rates of amortization of intangible assets and expenditures are:

Useful Life	Straight-line Amortization Rate
1-4 years	25%
5-8 years	12.5%
9-16 years	6.25%
16-20 years	5%

2. Useful life of intangibles

Types of Intangible Property	Useful Life	Straight-line Amortization Rate
1. Research and development	4 years	25%
2. Installation costs	4 years	25%
3. Copyrights, patent, design or		

model, plan, secret formula or process, trademark, or other like property or right,	(a)	(a)

(a) The useful life and amortization rate of this type of property shall be determined in accordance with the period of time for which the intangible property exists.

3. An intangible asset or intangible expenditure with a useful life of more than twenty years shall be treated as if it has a useful life of twenty years.

4. An expenditure with a useful life of more than one year incurred before the commencement of taxable business activities shall be capitalized and treated as if it has a useful life of four years.

5. An intangible asset or intangible expenditure that does not have a defined useful life shall be treated as having a useful life of twenty years.

3.4.5. Reserves

Even though accounting practice may require that the potential liability be reflected in the taxpayer's accounts, no deduction is allowed for any amount retained by a taxpayer from profits to create a reserve or provision for expected expenses or losses.

Only banks are allowed a deduction for a provision for doubtful debts provided the amount of the provision has been determined in accordance with the prudential requirements prescribed by instruction of the Banking and Payments Authority under Section 26 of UNTAET Regulation No. 2000/8 and as defined by Government.

3.4.6. Bad Debts

A taxpayer is allowed a deduction in a tax year for a bad debt if the amount of the debt was previously included in taxable income, the debt is written off in the accounts during the tax year and the taxpayer has reasonable grounds for believing that the debt will not be recovered.

3.4.7. Long-term Contracts

A "long-term contract" is a contract for manufacture, installation, or construction, or services related thereto, that is not completed in the tax year in which work under the contract commenced, other than a contract estimated to be completed within six months of the date on which work under the contract commenced.

The annual profit arising from a long-term contract shall be determined by applying the percentage-of-completion method.

3.4.8. Finance Leases

A finance lease shall be treated as a sale and purchase of the leased asset. The lessor is treated as having made a loan to the lessee equal to the purchase price of the asset and the lessee is treated as the owner of the asset. Each payment by the lessee to the lessor is treated as in part a repayment of principal and in part a payment of interest. The interest part shall be calculated on the principal outstanding at the time each payment is made.

A lease is a finance lease if:

(a) the lease term (including any period under an option to renew) is 75% or more of the useful life of the asset for depreciation purposes;

(b) the lessee has an option to purchase the asset for a fixed or determinable price at the expiration of the lease;

(c) the estimated residual value of the asset at the expiration of the lease is less than 20% of its market value at the start of the lease;

(d) in the case of a lease that commences before the last 25% of the useful life of the asset, the present value of the minimum lease payments equals or exceeds 90% of the market value of the asset at the commencement of the lease term; or

(e) the asset is custom made for the lessee and, after the expiration of the lease, the asset will be of no practical use to any person other than the lessee.

3.4.9. Interest Expense

Interest paid by a person on loans and advances is not deductible in a tax year to the extent that the total amount of interest exceeds the sum of the interest income and 50% of the net non-interest income for the year. A taxpayer's net non-interest income is the gross income for the year other than interest income less the total amount of deductions allowed to the taxpayer for the year, other than for interest expense.

This does not apply to financial institutions.

Examples

(1) Taxpayer has gross income for a tax year of $20,000, which includes $1000 of interest income. Taxpayer has total deductible expenses of $15,000 for the year, including $2,000 of interest expense.

The ceiling on the amount of interest deductible for the year is:
Interest Income + (50% x ((Gross Income – Interest Income) – (Total Deductions – Interest Expense))
ie ($1,000 + (50% x ($19,000-$13,000)) which is $4,000.

As the interest expense ($2,000) is below the ceiling ($4,000), all the interest expense is deductible.

(2) Assume the same facts as for (1) except that the interest expense is $10,000.

Interest Income + (50% x ((Gross Income – Interest Income) – (Total Deductions – Interest Expense))
ie $1,000 + (50% x ($19,000 - $5,000)).
The ceiling on the deductibility of interest is $8,000

Taxpayer's interest expense for the tax year exceeds the ceiling so that only $8,000 is deductible. The other $2,000 may be carried forward as interest expense incurred in the next tax year. This means that it may be deducted in that year subject to the application of the ceiling for that year. Any carry forward interest expense is taken into account in determining the ceiling for that year.

3.4.10. Deduction Denial

Where a person is required to withhold tax from a payment that is a deductible expense of the person, the deduction is not allowed until the person pays the withheld tax to the Commissioner.

A person is not allowed a deduction for any commission, rebate, discount, spotters fee, or similar payment that is East Timor-source income of the recipient unless:

(a) the person discloses the name and address of the recipient by notice in writing to the Commissioner; and

(b) the Commissioner is satisfied that tax has been or will be paid in respect of the payment.

3.4.11. Recouped Deductions

Where a taxpayer recovers a previously deducted expense, loss, or bad debt, the amount recovered shall be included as income in the calculation of the taxable income of the taxpayer for the tax year in which the amount was recovered.

3.4.12. Assets

For the purposes of calculating taxable income, any gain arising on the disposal of an asset is the excess of the gross consideration received over the cost of the asset, and any loss arising from the disposal of an asset is the excess of the cost of the asset over the gross consideration received.

The cost of an asset is the total amount paid or incurred by a taxpayer in the acquisition, creation, or construction of the asset. It includes any non-deductible incidental expenditures incurred in acquiring the asset and the market value of any in-kind consideration given for the asset. The cost is reduced by the amount of any deductions, including depreciation or amortization, allowed in respect of the asset.

Non-deductible expenditures incurred to alter or improve an asset shall be added to the cost of the asset.

The consideration received on disposal of an asset is the total amount received or receivable for the asset. It includes any non-deductible incidental expenditures incurred in alienating the asset and the market value of any in-kind consideration received for the asset.

Where a part of an asset is alienated, the cost of the asset shall be apportioned reasonably between the part of the asset retained and the part alienated.

Where an asset is transferred between associates in a non arm's length transaction, the transferor is treated as having received, and the transferee is treated as having given, the market value of the asset as consideration for the transfer.

3.4.13. Currency Translation

Any amount taken into account for income tax purposes shall be calculated in United States dollars only.

Where an amount is in a currency other than United States dollars, the amount shall be converted at the Banking and Payments Authority's mid-exchange rate applying between the currency and United States dollars on the date the amount is taken into account for tax purposes, but with the prior written permission of the Commissioner, a taxpayer may use the average rate of exchange for the tax year or a part of the tax year.

3.4.14. Market Value

An amount-in-kind shall be accounted for at its fair market value on the date it is taken into account for tax purposes. The fair market value of an asset shall be determined without regard to any restriction on disposal.

3.4.15. Foreign Currency Exchange Gains and Losses

A taxpayer shall account for transactions in foreign currency in accordance with International Accounting Standard IAS 21. No foreign currency exchange loss is recognized to the extent that the exposure to such loss is hedged.

3.5. Special deductions for resident individuals

In calculating the taxable income of a resident individual taxpayer, the following amounts shall be deducted from net income:

a. US$388 for an individual Taxpayer;
b. An additional US$194 for a married Taxpayer;
c. US$194 for each family member of the same blood or by marriage in a straight descent line, including any adopted child, who is a fully dependent, up to a maximum of 3 individuals per family.

These deductions only relate to income included in an annual tax form or return. No deduction is allowed in relation to income subject to wage income tax or a final withholding tax.

A taxpayer who has a member of the family of the same blood and by marriage in straight descent line who becomes their full dependent (eg. parents, parents-in-law, child, adopted child) shall be given extra deductions of US$194 for each dependant up to a maximum of 3 dependants. The members of a family who become fully dependent shall be members of a family who are not receiving income whose living costs are borne by the Taxpayer.

Example:

For the 2002 tax year, taxpayer A has a wife and 4 dependent children. The total deduction as a resident individual that taxpayer A is entitled to is US$1164 (US$388 + US$194 + (3 x US $194)).

The amount of deduction for resident individuals shall be determined in accordance with the circumstances of the taxpayer at the beginning of a tax year.

Example:

On 1 January 2002, taxpayer B is married with one dependent child. If a second child is born after 1 January 2002, the amount of the deduction for a resident individual that taxpayer B would be entitled to for the 2002 tax year shall be based on the taxpayer B's married status with 1 child.

3.6. Income and Deductions for Permanent Establishments

A person neither residing in East Timor or established or domiciled in East Timor, yet conducting business or engaged in activities through a permanent establishment in East Timor, is subject to Income Tax in East Timor.

The tax will be calculated by reference to the income attributable to any:

a. business or activities and property owned or controlled by the permanent establishment;
b. sales in East Timor of goods or merchandise of the same or similar kind as those sold through the permanent establishment; and
c. any other business activities carried on in East Timor of the same or similar kind as those effected through the permanent establishment.

Head office income arising from business activities or sales which are similar to the ones performed by the permanent establishment is considered income of the permanent establishment, since such business or activities are included in the scope of business or activities that may be performed by the permanent establishment.

Business activities similar to those of a permanent establishment occur, for example, where a non-resident bank having a permanent establishment in East Timor provides a loan directly to a company in East Timor and not through its permanent establishment or where a head office of a consultancy services firm outside East Timor directly provides the same kind of consultancy services as those offered by the permanent establishment to clients in East Timor.

Sale of goods similar to those sold by a permanent establishment occur, for example, where a overseas head office having a permanent establishment in East Timor sells directly in East Timor, products of the same kind as those sold by its permanent establishment.

The profit of the permanent establishment shall be calculated on the basis that it is a distinct and separate person engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the non-resident person of which it is a permanent establishment.

Expenses incurred for the purposes of the business activities of the permanent establishment including executive and administrative expenses so incurred, whether in East Timor or elsewhere are allowed as deductions.

However no deduction is allowed for amounts paid or payable by the permanent establishment to its head office or to another permanent establishment of the non-resident person (other than towards reimbursement of actual expenses incurred by the non-resident person to third parties) by way of:

(a) royalties, fees, or other similar payments for the use of any tangible or intangible asset by the permanent establishment;

(b) compensation for any services (including management services) performed for the permanent establishment; or

(c) interest on moneys lent to the permanent establishment, except in connection with a banking business.

No account shall be taken in the determination of the income of a permanent establishment of amounts charged by the permanent establishment to the head office or to another permanent establishment of the non-resident person (other than towards reimbursement of actual expenses incurred by the permanent establishment to third parties) by way of:

(a) royalties, fees, or other similar payments for the use of any tangible or intangible asset;

(b) compensation for any services (including management services) performed by the permanent establishment; or

(c) interest on moneys lent by the permanent establishment, except in connection with a banking business.

3.7. International taxation

Resident taxpayers are subject to tax on their income from all sources. This includes income received or earned from abroad. To alleviate double taxation, which may occur because of the imposition of tax abroad on income received or obtained from abroad, the amount of tax paid abroad on that income may be credited against the tax owed in East Timor.

This credit is referred to as a “foreign tax credit”.

The foreign tax credit shall be calculated separately for each foreign country from which income is derived by a taxpayer. The amount of the credit in respect of income from sources in a foreign country shall be limited to the East Timor tax payable on that income. There is no deduction or carry forward of any excess foreign tax credit.

The amount of foreign tax paid has to be substantiated by appropriate evidence, such as payment under a tax assessment, a tax withholding certificate, or other similar document accepted by the Commissioner for this purpose.

Deductible expenses incurred in deriving income from sources in a foreign country shall be deducted only against that income. If deductible expenses exceed the income derived from sources in a foreign country for a tax year, the amount of the excess shall be a foreign country loss allowed as a deduction against income from sources in the foreign country (until expired) for a maximum of five tax years. Where a taxpayer has a foreign country loss carried forward for more than one year, the loss for the earliest year shall be deducted first.

3.8. Losses

If the determination of the taxable income of a taxpayer results in a loss for a tax year, that loss may be deducted as an expense in calculating the taxable income of the taxpayer, until the amount is expired, for a maximum of five tax years. Where a taxpayer has a loss carried forward for more than one tax year, the loss for the earliest year shall be deducted first.

4. TAX RATES

Income tax, at the specified rate, applies –

(1) at the time of payment of certain types of payments (as a withholding tax),
(2) at the time of lodgement of annual income tax, (as an annual income tax), or
(3) both 1 and 2 (with a credit allowed for withheld tax).

4.1. Withholding tax rates

The rates of tax applicable to amounts payable to **residents** or **non-residents who have a permanent establishment** in East Timor are as follows:

TYPE OF INCOME	RATE
dividends	15 %
interest	15 %
royalties	15 %
rent from land and buildings	10 %
income from prizes and lotteries	15 %
income from construction and building activities	2 %
income from construction consulting services including project management, engineering design and site supervision services	4 %
income from the provision of air or sea transportation services	2.64 %
income from petroleum and geothermal drilling and drilling support services	4.5 %
income from mining and mining support services	4.5 %

Certain types of business income (see table below) were subject to a non-final withholding tax. The income was subject to a 5% withholding at the time of payment, but was still subject to annual income tax with a credit being available for the amount of tax withheld. Regulation No. 2001/20 retrospectively, from 1 January 2001, reduced the non-final withholding rate to nil. While there is no longer a requirement to withhold tax from these payments, the income is required to be declared in the annual income tax form.

These types of income are now subject to income tax instalments.

TYPE OF INCOME
income from hiring or lease of movable property
income from the provision of the following services: technical management interior and landscape design accounting and book-keeping cleaning pest eradication forest clearing

film dubbing appraisal actuarial architectural surveying legal automated data processing advertising marketing secretarial stevedoring shipping and customs agent travel agent storage and warehousing

The rate of tax applicable to amounts payable to **non-residents without a permanent establishment** in East Timor is as follows:

TYPE OF INCOME	RATE
all income	20 %

4.2. Annual Income Tax rates

For *natural persons* ie individuals -

AMOUNT OF INCOME	RATE
0 –$3,368	10%
in excess of $3,368 - $6,737	15%
in excess of $6,737	30%

> ***For example**, an individual with a taxable income of $5,000 would pay income tax of $581.60 ie[$3,368x10%] + [$1,632x15%]*

For *any other person* ie partnership, company or any other entity – 30%

> ***For example**, a company with a taxable income of $5,000 would pay income tax of $1,500 ie $5,000x30%*

5. MINIMUM INCOME TAX

For the 2002 income tax year and subsequent years, the law provides for the imposition of a minimum income tax on taxpayers conducting business activities.

The minimum income tax payable for a tax year is one percent (1%) of the taxpayer's total turnover for that year. The tax is payable even if the taxpayer has no taxable income for the year ie there is a loss for the year.

"Turnover" has its ordinary meaning, namely the taxpayer's total revenue from business activities without deduction for any expenses (including the cost of inventory sold). Where a taxpayer has disposed of a non-inventory asset in the tax year, total revenue includes the net gain from disposal of the asset. Total turnover does not include any amount derived by the taxpayer that is subject to a final withholding tax.

Taxpayers that conduct business activities are subject to both the ordinary income tax and to the minimum income tax but will be required to pay, in effect, the higher of the two amounts. The ordinary income tax for the tax year is computed first. The amount of the ordinary income tax payable for the year is credited against the minimum income tax payable for the year. If a taxpayer's ordinary income tax liability for the year exceeds the taxpayer's minimum income tax liability, then the minimum income tax payable is reduced to zero.

Where the minimum income tax liability for the year exceeds the ordinary income tax liability, only the amount of the excess is payable. Any instalments of income tax paid by a taxpayer in a tax year in excess of the taxpayer's ordinary income tax liability shall be credited against the taxpayer's minimum income tax liability for the year.

Example

Suppose a taxpayer's total turnover for a tax year is $100,000. The taxpayer has a minimum income tax liability for the year of $1,000 (1% x $100,000). Suppose further that the taxpayer also has an ordinary income tax liability of $1,200 on its taxable income. The ordinary income tax liability is credited against the minimum income tax liability reducing it to zero. The taxpayer pays only the $1,200 ordinary income tax liability on its taxable income.

If the taxpayer's ordinary income tax liability for year is only $800, then this is credited against the minimum income tax liability reducing it to $200. This amount is payable by the taxpayer (in addition to the ordinary income tax liability of $800).

6. ASSESSMENT

6.1. Self-assessment

As a general rule, taxpayers are required to deliver an annual income tax form. The tax due (if any) according to this tax form shall be treated as an assessment.

6.2. Commissioner's assessment

The Commissioner may determine the amount of the tax due and issue to the person liable for payment of the tax an assessment notice for the amount due if the information provided on the tax form does not correctly disclose the tax due or the required tax form has not been delivered.

Tax specified in a Commissioner's assessment notice, in the case of a required tax form not being delivered, is treated as due and payable on the date a tax form correctly disclosing the tax due was to be delivered to the Banking and Payments Authority.

The Commissioner also may amend an assessment notice issued.

Where a taxpayer has delivered a tax form, or has received an assessment notice, and believes that the tax form or assessment is incorrect, they can either deliver an amended tax form, or request the Commissioner to amend the assessment.

Where the Commissioner agrees to amend an assessment or where an overpayment of tax has arisen, the Commissioner shall, to the extent there has been an overpayment:

- (a) apply that overpayment against any other taxes then due; and
- (b) refund the remainder to the person who paid it

and shall pay to the person interest in respect of each whole calendar month between:

- (a) the later of:
  - (i) the date of payment by the person; and
  - (ii) the date the Commissioner first became aware that an overpayment has arisen; and
- (b) the date of the application of the overpayment to other taxes due, or its refund.

6.3. Time limits for assessments

The Commissioner can only issue assessment notices, or amend assessment notices, within five years of the date on which the tax form to which the notice relates was due.

The Commissioner may make or amend an assessment at any time where:

- (a) a person with the intent of evading tax has failed to deliver a tax form;
- (b) a person with the intent of evading tax has delivered a tax form which the Commissioner considers to be incorrect; or
- (c) fraud has been committed by or on behalf of a person in relation to tax due.

6.4. Jeopardy assessments

Where the Commissioner believes that the collection of tax that will become due is in jeopardy because a person is about to depart from East Timor, to cease business, or to transfer property, or is in jeopardy for other reasons, the Commissioner may at any time issue an assessment notice for any tax period in the current or preceding tax year.

7. WITHHOLDING TAX

For certain types of income, there is an obligation (either on the payer or the recipient) to withhold tax at the prescribed rate and pay that amount to the ETRS.

The following types of income are subject to withholding tax:

TYPE OF INCOME	RATE
dividends	15 %
interest	15 %
royalties	15 %
rent from land and buildings	10 %
income from prizes and lotteries	15 %
income from construction and building activities	2 %
income from construction consulting services including project management, engineering design and site supervision services	4 %
income from the provision of air or sea transportation services	2.64 %
income from petroleum and geothermal drilling and drilling support services	4.5 %
income from mining and mining support services	4.5 %

7.1. Withholding Obligations

7.1.1. Payments for Services

A person (other than a natural person) making a payment to which a final rate applies shall withhold tax from the gross payment at the rate prescribed. If the person making the payment is a natural person, the recipient of the payment shall withhold tax from the gross payment received at the same rate.

7.1.2. Non-resident Withholding Tax

A person making a payment of East Timor-source income to a non-resident shall withhold tax from the gross amount of the payment.

7.1.3. Obligations of a Person Withholding Tax from a Payment

A person who has withheld a tax shall remit it to the Commissioner by the 15th (or next business day if the 15th is not a business day) of the month following the month in which the tax was withheld.

At the time of payment, the payer shall issue to the recipient of the payment a withholding tax notice setting out the amount of the payment made and the amount of tax withheld from the payment.

A person who fails to withhold a tax from a payment is personally liable to pay the amount of tax that has not been withheld and become entitled to recover this amount from the recipient of the payment.

A person who has withheld tax from a payment and remitted the amount withheld to the Commissioner shall be treated as having paid the withheld amount to the recipient of the payment for the purposes of any claim by that person for payment of the amount withheld.

Any tax withheld by a person is held as agent for the Commissioner. In the event of the liquidation or bankruptcy, any amount of tax withheld does not form a part of the estate of the payer in liquidation or bankruptcy, and the Commissioner shall have a first claim to the tax withheld before any distribution of property is made.

7.1.4. Self-withholding

Every recipient of payment who is required to withhold tax from the payment in accordance with Directive 2001/2 shall remit the tax withheld to the Commissioner by the 15th (or next business day if the 15th is not a business day) of the month following the month in which the payment was received.

7.2. Withholding Tax – final

Withholding tax is a **final tax** in the circumstances summarized in the following table:

Type of Payment	***Period during 2002 year to which payment relates***	
	Received by ***Natural Person***	*Received by* ***Non-natural persons***
Dividends	Any period	Pre 1 July 2002
Interest	Any period	Pre 1 July 2002
Royalties	Any period	Pre 1 July 2002
rent from land and buildings	Any period	Pre 1 July 2002
income from prizes and lotteries	Any period	Any period
income from construction and building activities	Any period	Any period
income from construction consulting services including project management, engineering design and site supervision services	Any period	Any period
income from the provision of air or sea transportation services	Any period	Any period
income from petroleum and geothermal drilling and drilling support services	Any period	Any period
income from mining and mining support services	Any period	Any period

Where the tax withheld is a **final tax** on the income of the recipient of the payment:

(a) no further income tax liability is imposed upon the recipient in respect of the income to which the tax relates;

(b) that income is not aggregated with the other income of the recipient for the purposes of ascertaining taxable income;

(c) no deduction (including a depreciation or amortization deduction) is allowed for any expenditure or losses incurred in earning the income; and

(d) no refund of tax shall be made in respect of the income.

7.3. Withholding Tax – non final

Where the tax withheld is a **non-final tax** on the income of the recipient of the payment:

(a) further income tax liability is imposed upon the recipient in respect of the income to which the tax relates;

(b) that income is aggregated with the other income of the recipient for the purposes of ascertaining taxable income;

(c) deductions (including a depreciation or amortization deduction) are allowed for any expenditure or losses incurred in earning the income; and

(d) credit will be allowed for amounts withheld from the payment and paid to the ETRS.

Withholding tax is a non-final tax where the income of the recipient is dividends, interest, royalties or rent from land or buildings and relates to a period after 30 June 2002.

8. PAYMENTS

8.1. Instalments of Tax

The basis for calculating instalments of tax changed with tax amendments made during the 2002 year. An explanation of the both the current and future instalment calculation processes is provided below.

8.1.1. Instalments of Tax for the 2002 year

Taxpayers with a turnover of more than one million US Dollars shall pay instalments of tax for a tax year on the 15th day of each month starting in the fourth month of the tax year and ending in the third month after the end of the tax year.

The amount of each instalment is one-twelfth of the amount of tax due for the previous tax year.

For taxpayers with a turnover of one million US Dollars or less, these instalments of tax will be cumulated quarterly and paid by 15th May 2002, 15th August 2002, and 15th November 2002, and 15th February 2003.

If a taxpayer commenced carrying on business activities in the previous tax year, the instalment for each month of the current tax year shall be the amount of tax due for the previous tax year divided by the number of months the taxpayer carried on business activities in that year. If a taxpayer commenced carrying on business activities in the current tax year, the instalment for each month of the current year shall be the estimated tax for the current year divided by the number of months remaining in the current year.

Where a taxpayer can substantiate at any time during a tax year to the Commissioner that the tax on taxable income for the year will be substantially lower than the tax due for the previous tax year, the Commissioner shall reduce the amount of each instalment accordingly.

If the Commissioner estimates that the tax due for the current tax year to be more than 10% in excess of the tax due in the previous tax year, the Commissioner may adjust the instalments according to the estimated tax.

For the instalment calculation, "tax due" does not include tax credits, other than instalment payments.

> ***Example 1:***
>
> *A taxpayer owed Income Tax of $22,500 based on the Annual Income Tax Return of 2001 before allowing for a foreign tax credit of $7,500.*
>
> *The tax instalment, which must be paid by the taxpayer each month is US$ 1,250 (US$ 15,000 / 12).*
>
> ***Example 2:***
>
> *If the Income Tax as referred to in the above example related to income received or obtained for part of a fiscal year which covers 6 (six) months in the year 2001, the monthly instalment which must be paid by the Taxpayer each month in the year 2002 is US$ 2,500 (US$ 15,000/ 6).*

8.1.2. Instalments of Tax for the 2003 and subsequent years

The previous system of instalments is now replaced with a system based on the taxpayer's turnover. Under the new system, monthly instalments of income tax are payable commencing with the first month of the tax year. The amount of each instalment is 1% of the taxpayer's total turnover for the period. "Turnover" has its ordinary meaning, namely the taxpayer's total revenue from business activities without deduction for any expenses (including the cost of inventory sold). Where a taxpayer has disposed of a non-inventory asset in the tax year, total revenue includes the net gain from disposal of the asset. Total turnover does not include any amount derived by the taxpayer that is subject to final withholding tax.

> ***Example****:*
>
> *A taxpayer conducts a business as a new car retailer. For the month of January 2003, its total income from this activity is $100,000. During the month, the taxpayer sold some office equipment for a net gain of $2,000. Total turnover for the month is therefore $102,000. The instalment payable for January is $1002 being 1% of the turnover for the month.*

Taxpayers with a total turnover for the previous tax year of $1 million or less may pay instalments of tax quarterly rather than monthly. The quarterly periods are three months ending on 31 March, 30 June, 30 September and 31 December.

Instalments of income tax are payable on the 15th day after the end of the period (month or quarter) to which they relate. Instalments are creditable against the taxpayer's ordinary income tax payable each year.

The new instalment system applies for the tax year ending on 31 December 2003 and subsequent tax years. For taxpayers permitted to use a substituted tax year, the new instalment system applies for the first such year ending after 31 December 2003.

8.2. Final payment

8.2.1. Due Date

Income tax is due on **15 March** of the year following the year of the income.
For companies with a substituted tax year, income tax is due on the fifteenth day of the third month after the end of the substituted tax year.

8.2.2. Allowable credits

For a resident taxpayer and permanent establishment of a non-resident, the tax due for the year concerned shall be reduced by any tax credits in the form of:

a) amounts withheld from payments subject to non-final withholding;
b) instalments paid by the taxpayer;
c) tax paid or due on income from abroad that may be credited as foreign tax credits.

8.2.3. Underpayment or Overpayment

If the tax due for a tax year is greater than the tax credit, the underpaid tax must be paid, along with the lodgment of an annual income tax form, on or before the 15th day of the third month after the tax year (or substituted tax year) ended.

If the tax due for a tax year is less than the amount of tax credit, the overpayment will, after verification, be applied against any other taxes then due (if any) or refunded.

9. ANNUAL INCOME TAX FORM

Tax returns for the year ended 31 December 2002, together with any payments must be lodged on or before **15 March 2003**. Two copies of the form should be completed, one for the taxpayer's records and the other for the ETRS.

If a tax payment is not required, one copy of the completed income tax return is to be delivered to the ETRS District Office. The ETRS Dili District Office is located the Justice Building on the corner of Don Fernando and Jacinto de Candido Streets, immediately south of the former LGR building and west of the Lyceum. The office is open between the hours of 9am and 5 pm Monday to Friday (holidays excepted).

If a taxpayer is required to make a tax payment, two copies of the completed income tax return and payment are to be presented to the Banco Nacional Ultramarino (BNU).

For taxpayers based outside of Dili, the income tax return can be delivered to the:

- ETRS Baucau office (Vilanova Street, Baucau) with payment to the Baucau District Finance Officer, or

- ETRS Maliana office (Holsa Street, Maliana) with payment to the Maliana Microfinance office.

The income tax form of a taxpayer conducting business activities shall be accompanied by the taxpayer’s income statement, balance sheet and cash flow statement for the tax year.

A taxpayer may apply in writing to the Commissioner for an extension of time to deliver an income tax form. An application must be accompanied by a statement estimating the amount of income tax due for the tax year and proof of settlement of the tax due. The Commissioner may, by notice in writing, grant the taxpayer’s application for an extension of time for delivering an income tax form. The granting of an extension of time does not alter the due date for payment of tax.

10. TAXPAYER OBLIGATIONS

Enterprises, permanent establishments and other persons liable to pay or withhold taxes, are required to obtain a Tax Identification Number in East Timor.

The Commissioner may require the inclusion of the tax identification number in any form, notice, or other document used for tax purposes. The Commissioner may also designate other documents or registrations including but not limited to a licence, permit, passport, registration certificate as documents or registrations requiring presentation of a tax identification number prior to its issue.

Anyone liable to pay or withhold tax shall create and maintain records of account suitable to determine their liability to pay or withhold tax, in Tetum, Portuguese, English or Indonesian, for a period of at least five years after the tax year in which the tax liability to which they relate arose.

Where records needed by taxpayers are unavailable, mainly because of damage and destruction, the Commissioner may determine on a reasonable basis any amounts that would have been calculated by reference to any other available information.

11. POWERS OF INVESTIGATION

Any officer authorized by the Commissioner in writing for this purpose:

(a) shall have at all times and without any prior notice full and free access to any premises, place, book, record, or computer where there are reasonable grounds for concluding that access may provide the Commissioner with materials relevant to an understatement of tax due;

(b) may make an extract or copy from any book, record, or computer-stored information to which access is obtained under paragraph (a);

(c) may seize any book or record that, in the opinion of the Commissioner or authorized officer, affords evidence which may be material in determining the liability of a person to tax, additional tax, or to a penalty under the present Regulation;

(d) may retain any such book or record for as long as it may be required for determining a person's liability or for any proceeding under the present Regulation; and

(e) may, where a hard copy or computer disk of information stored on a computer is not provided, seize and retain the computer for as long as is necessary to copy the information required.

These powers may be exercised only during ordinary business hours, unless the Commissioner determines that the collection of tax is in jeopardy and that their exercise outside ordinary business hours is necessary to protect the collection of the tax.

The owner, manager, or any other person on the premises or place entered or proposed to be entered shall provide all reasonable facilities and assistance for the effective exercise of power.

A taxpayer whose books, records, or computer have been removed and retained may examine them and make copies or extracts from them during regular office hours under such supervision as the Commissioner may determine.

To collect information about the liability of a specific taxpayer the Commissioner may, by notice in writing, require anyone, even if not liable to pay the tax to:
(a) provide to the Commissione*r* such information as may be required by the notice; or
(b) attend at the time and place designated in the notice for the purpose of being examined on oath before the Commissioner or any officer authorized by the Commissioner for this purpose, concerning the tax liability of that person or any other person, and for that purpose require such person to produce any book, record, or computer-stored information in the control of that person.

12. RIGHTS AND GUARANTEES

A taxpayer who disputes a tax or additional tax liability set out in an assessment or amended assessment or who considers that a decision or assessment by the Commissioner is incorrect, may appeal to the ETRS Appeals Office within 60 days from the date of receiving, from the Commissioner, notice of the assessment, amended assessment or decision which they wish to appeal.

Decisions of the Appeals Office shall be delivered in writing to the person making an appeal.

Whether or not a person has lodged an appeal to the Appeals Office, tax due shall remain due and payable, and may be recovered notwithstanding that appeal.

Where a person becomes entitled to a refund of tax following an appeal to the Appeals Office, the Commissioner shall refund the tax and interest calculated from the day of payment by the person to the day of refund.

Summary of Legislative Changes: Income Tax (Revenue System Amendment Act 2002)

During the 2002 year, the *Revenue System Amendment Act 2002* was enacted. By virtue of this amendment Act, a number of provisions relating to income tax, as well as other taxes, were changed. While the income tax changes are addressed as appropriate throughout this Guide, for convenience a summary of relevant changes is provided below:

Item	***Previous Law***	***New Law***	***Date of Effect***	***Reference***
Withholding Tax (for other than a natural person)	Final withholding on: -dividends (15%), -interest (15%), -royalties (15%), and -rent on land or buildings (10%) (applies for all taxpayers)	Credit for amount withheld on: -dividends -interest -royalties and - rent (For a taxpayer other than a natural person [ie partnerships, companies, unincorporated associations, non-government organizations etc], the amount must be declared in the income tax return and a credit will be allowed for amounts previously withheld.)	1 July 2002	Reg. 2000/18 Section 38
Income Tax Rates (for legal persons other than natural persons)	Graduated rate as follows: 0 - $3,368….. 10% $3,369 - $6,737….. 15% in excess of $6,737… 30%	Flat rate of 30% on total taxable income	For the year ended 31 December 2002 and later years	Reg. 2000/18 Schedule 1 Section 6 Part A (b)
Minimum Income Tax (for business activities)	No provision	Taxpayers conducting business activities to pay the higher of the Minimum Income Tax and Actual Income Tax for the year. Minimum Income Tax is 1% of total turnover for the year. Actual Income tax is the tax payable on income after deductions.	For the year ended 31 December 2002 and later years	Reg. 2000/18 Section 36A
Installments of Income Tax	Installments of current year income tax based on previous year's tax liability and payable monthly or quarterly	Installments of current year income tax are 1% of turnover. If previous turnover exceeds $1 million, then monthly installments payable. Otherwise, quarterly installments payable. Installments are due to be paid by the 15th day after the end of the month or quarter.	For the year ending 31 December 2003 and later years	Dir. 2001/2 section 38

Item	*Previous Law*	*New Law*	*Date of Effect*	*Reference*
Depreciation Rates (DBB = **declining balance basis** and applies to pooled assets) (SLB = **Straight line basis** and applies to individual assets)	Categories of Asset life: Pool 1- asset useful life 1-4 years Pool 2- asset useful life 5-8 years Pool 3- asset useful life 9-16 years Pool 4- asset useful life over 16 years Depreciation Rates: Pool 1: 50% DBB or 25% SLB Pool 2: 25% DBB or 12.5% SLB Pool 3: 12.5% DBB or 6.25% SLB Pool 4: 10% DBB or 5% SLB	Categories of Asset life: Pool 1- asset useful life 1-4 years Pool 2- asset useful life 5-8 years Pool 3- asset useful life over 9 years Depreciation Rates: Pool 1: 50% DBB or 25% SLB Pool 2: 25% DBB or 12.5% SLB Pool 3: 12.5% DBB or 6.25% SLB	For the year ending 31 December 2002 and later years	Directive 2001/2 Schedule 1 Part B
Reserves (provision for doubtful debts for banks)	-	Government at a later date shall define the amount of the deduction for a bank's doubtful debts.	For the year ended 31 December 2002 and later years	Dir.2001/2 section 12.2
Interest Deduction (thin capitalization) **(for other than financial institutions)**	Deduction for interest not allowable on amount of loans and advances exceeding twice the amount of capital.	Deduction for interest not to exceed the total of interest income and 50% of net non-interest income. Interest expense not deductible may be carried forward for up to 5 years.	For the year ended 31 December 2002 and later years	Dir. 2001/2 section 16
Transactions between Associates	Transactions between associates adjusted to amount expected had persons not been associates	Transactions between associates adjusted to amount expected had persons been dealing at arm's length.	1 July 2002	Reg. 2000/18 section 91
Exempt Remuneration (T.F.E.T. consultants)	No provision	Exemption from wages and income tax for remuneration financed from the Trust Fund for East Timor and received by natural persons for services provided.	1 January 2000	Reg. 2000/18 Section 38A