## A BILL FOR AN ACT

To further amend title 54 of the Code of the Federated States of Micronesia, as amended, by adding a new chapter 5 to establish the Net Profit Tax Act of 2011, and for other purposes.

BE IT ENACTED BY THE CONGRESS OF THE FEDERATED STATES OF MICRONESIA:

- 1 Section 1. Title 54 of the Code of the Federated States of
- 2 Micronesia is hereby further amended by adding a new chapter 5
- 3 entitled "Taxation of Net Profits."
- 4 Section 2. Title 54 of the Code of the Federated States of
- 5 Micronesia is hereby amended by adding a new subchapter I to
- 6 chapter 5 entitled "General Provisions."
- 7 Section 3. Title 54 of the Code of the Federated States of
- 8 Micronesia is hereby further amended by adding a new section 511
- 9 to subchapter I of chapter 5 to read as follows:
- 10 "Section 511. Short title. This chapter may be cited as
- 11 the 'Net Profit Tax Act of 2011'."
- 12 Section 4. Title 54 of the Code of the Federated States of
- 13 Micronesia is hereby further amended by adding a new section 512
- 14 to subchapter 1 of chapter 5 to read as follows:
- "Section 512. Definitions.
- Wherever used in this chapter, except where otherwise
- 17 specified, unless the subject matter, context, or sense
- 18 otherwise requires:
- 19 <u>(1) 'Associate' has the meaning in section 515 of</u>

1	this title.
2	(2) 'Authority' means the Federated States of
3	Micronesia Unified Revenue Authority established by
4	section 711 of this title.
5	(3) 'Board' means the Board of Directors of the
6	Unified Revenue Authority as appointed under Section
7	712 of this title.
8	(4) 'Business' includes any profession, trade,
9	manufacture, or other undertaking carried on for
10	pecuniary profit, but not including employment.
11	(5) 'Business asset' means an asset, whether of
12	revenue or capital nature, used, available for use, or
13	held in carrying on a business, including inventory, a
14	depreciable asset, an intangible, or goodwill.
15	(6) 'CEO' means the Chief Executive Officer
16	appointed under section 731 of this title.
17	(7) 'Consideration received', in relation to a
18	business asset, has the meaning attributed to it in
19	section 553 of this title.
20	(8) 'Cost', in relation to a business asset, has
21	the meaning attributed to it in section 552 of this
22	title.
23	(9) 'Depreciable asset' means any tangible
24	personal property or that portion of a structural
25	improvement to real property that:

1	(a) has a useful life exceeding one year;
2	(b) is likely to lose value as a result of
3	normal wear and tear, or obsolescence; and
4	(c) is used, available for use, or held
5	solely to derive gross revenue.
6	(10) 'Disposal', in relation to a business asset,
7	has the meaning in section 551 of this title.
8	(11) 'Distribution', in relation to an entity,
9	includes a distribution of profits or entitlement to
10	income by an entity to a member of the entity.
11	(12) 'Employee' means any individual who, under
12	the usual common law rules applicable in the FSM in
13	determining an employer-employee relationship, has the
14	status of an employee, and includes the holder of an
15	office.
16	(13) 'Employment' means an employer-employee
17	relationship as determined under the usual common law
18	rules applicable in the FSM and includes activities
19	performed as the holder of an office.
20	(14) 'Entertainment' means the provision of food,
21	beverages, tobacco, amusement, recreation, or
22	hospitality of any kind.
23	(15) 'Entity' means a company, corporation,
24	partnership, unincorporated association or other
25	business entity, trust, or estate.

1	(16) 'Finance lease' means a lease that is treated
2	under generally accepted accounting principles as a
3	finance lease and is so accounted for by the lessor in
4	its financial accounts.
5	(17) 'FSM' means the Federated States of
6	Micronesia.
7	(18) 'Generally Accepted Accounting Principles' or
8	'GAAP' means those accounting principles currently
9	accepted by certified public accountants, which are
10	utilized by auditors operating within the FSM;
11	PROVIDED, HOWEVER, that in the event International
12	Financial Reporting Standards (IFRS) become generally
13	accepted by the financial/auditing entities within the
14	FSM and as prescribed by law or regulations, then GAAP
15	shall be modified by IFRS.
16	(19) 'Gross revenue' has the meaning attributed to
17	it in section 532 of this title.
18	(20) 'Industrial building' means a building that
19	is a depreciable asset used, available for use, or held
20	solely in carrying on:
21	(a) manufacturing operations;
22	(b) research and development into improved
23	or new methods of manufacture;
24	(c) mining operations (other than an
25	accommodation building); or

1	(d) a hotel business.
2	(21) 'Intangible' means:
3	(a) a patent, invention, design or model,
4	secret formula or process, trademark, copyright, or
5	other like property or right;
6	(b) contractual rights (including arising as
7	a result of a prepayment of expenses) with a benefit
8	for a period of more than one year; or
9	(c) an expenditure that provides an
10	advantage or benefit for a period of more than one
11	year, other than expenditure incurred to acquire any
12	tangible personal or real property, provided that the
13	property, right, or expenditure is used, available for
14	use, or held solely to derive gross revenue.
15	(22) 'Interest' means:
16	(a) an amount, whether described as
17	interest, discount, premium, or otherwise, whether
18	periodical or a lump sum, as consideration for the use
19	of money or being given time to pay;
20	(b) an amount that is functionally
21	equivalent to an amount referred to in paragraph (a) of
22	this subsection;
23	(c) any amount treated as interest under
24	section 546 of this title; or
25	(d) a commitment, quarantee, service, or

1	similar fee payable in respect of a debt or other
2	instrument or agreement giving rise to interest under
3	paragraphs (a), (b), or (c) of this subsection.
4	(23) 'Inventory' means anything produced,
5	manufactured, purchased, or otherwise acquired for sale
6	or exchange, and includes livestock, or any raw
7	materials, or consumables used in a production or
8	manufacturing process.
9	(24) 'Liaison office' means an office the sole
10	activity of which is representation.
11	(25) 'Management fee' means an amount as
12	consideration for the rendering of a managerial
13	service, but does not include salary or wages.
14	(26) 'Member', in relation to an entity, means a
15	shareholder in a company, partner in a partnership,
16	beneficiary of a trust or estate, or any other person
17	with an ownership interest in the entity.
18	(27) 'Natural resource amount' means:
19	(a) an amount (including a premium or like
20	amount) as consideration for the right to take minerals
21	or a living or non-living resource from land or sea; or
22	(b) an amount calculated in whole or part by
23	reference to the quantity or value of minerals or a
24	living or non-living resource taken from land or sea.
25	(28) 'Net profit' has the meaning in section 531

1	of this title.
2	(29) 'Net profit tax' means a tax imposed under
3	subchapter II of this chapter.
4	(30) 'Non-resident person' means a person that is
5	not a resident person.
6	(31) 'Permanent establishment' means a fixed place
7	of business through which the business of a person is
8	wholly or partly carried on, and includes:
9	(a) a place of management, branch, office
10	(other than a liaison office), factory, warehouse, or
11	workshop;
12	(b) a mine, oil or gas well, quarry, or
13	other place of extraction of natural resources;
14	(c) a building site, or a construction,
15	assembly or installation project, or supervisory
16	activities connected with such site or project, but
17	only if the site, project or activities continue for
18	more than ninety days;
19	(d) the furnishing of services by the
20	person, including consultancy services, through
21	employees or other personnel engaged by the person for
22	such purpose, but only if activities of that nature
23	continue for the same or a connected project for a
24	period or periods aggregating more than ninety days
25	within any twelve-month period:

1	(e) a person (referred to as an "agent")
2	acting on behalf of another person (referred to as the
3	<pre>"principal"), if the agent:</pre>
4	(i) has and habitually exercises an
5	authority to conclude contracts on behalf of the
6	principal; or
7	(ii) habitually maintains a stock of
8	inventory from which the agent regularly delivers
9	inventory on behalf of the principal, but does not
10	include an agent of independent status; or
11	(f) any substantial equipment used by a
12	person.
13	(32) 'Person' means an individual, entity, a
14	government, a political subdivision of a government, or
15	a public international organization.
16	(33) 'Prescribed' means set forth by the Secretary
17	in regulations.
18	(34) 'President' means the President of the FSM.
19	(35) 'Relative' in relation to an individual,
20	means:
21	(a) an ancestor, a descendant of any of the
22	grandparents, or an adopted child, of the individual;
23	(b) an ancestor, a descendant of any of the
24	grandparents, or an adopted child of a spouse of the
25	individual; or

1	(c) a spouse of the individual or any person
2	specified in paragraph (a) or (b) of this subsection.
3	(36) 'Resident person' means:
4	(a) in the case of an individual, an
5	individual who:
6	(i) has his or her home in the FSM; or
7	(ii) is present in the FSM for a period
8	of, or periods amounting in aggregate to, one hundred
9	eighty-three days or more in any twelve month period
10	that commences or ends during a tax year; or
11	(iii) is an employee of the National or of
12	a State Government of the FSM posted abroad at any time
13	during the year; or
14	(b) in the case of any other person, the
15	person is incorporated, formed, organized, or otherwise
16	established in the FSM.
17	(37) 'Royalty' means an amount, however described,
18	whether periodical or a lump sum, as consideration for:
19	(a) the use of, or right to use any patent,
20	invention, design or model, secret formula or process,
21	trademark, or other like property or right;
22	(b) the use of, or right to use any
23	copyright of a literary, artistic, or scientific work
24	(including films or video tapes for use in connection
25	with television or tames in connection with radio

1	<pre>broadcasting);</pre>
2	(c) the receipt of, or right to receive, any
3	visual images or sounds, or both, transmitted by
4	satellite, cable, optic fiber, or similar technology in
5	connection with television, radio, or internet
6	<pre>broadcasting;</pre>
7	(d) the supply of any technical, industrial,
8	commercial, or scientific knowledge,
9	experience, or skill;
10	(e) the use of or right to use any
11	industrial, commercial, or scientific equipment; or
12	(f) the supply of any assistance that is
13	ancillary and subsidiary to, and is furnished as a
14	means of enabling the application or enjoyment of, any
15	property or right referred to in paragraphs (a) through
16	(e) of this subsection.
17	(38) 'Secretary' means the Secretary of the
18	Department of Finance and Administration of the FSM
19	National Government.
20	(39) 'Small business' means a business that is
21	carried on by a person that is not registered for the
22	VAT, but not including a business making exempt
23	supplies that would be above the VAT registration
24	threshold if the exempt supplies were taxable supplies.
25	(40) 'State' means a State of the FSM.

1	(41) 'Structural improvement', in relation to real
2	property, includes any building, road, driveway, car
3	park, pipeline, bridge, tunnel, airport runway, canal,
4	dock, wharf, retaining wall, fence, power lines, water
5	or sewerage pipes, drainage, landscaping, or dam.
6	(42) 'Tax year' means:
7	(a) in the case of a corporation, the period
8	of twelve months ending on the date of the annual
9	balance of its accounts; or
10	(b) in any other case, the period of twelve
11	months ending on December 31.
12	(43) 'VAT' means the value added tax imposed
13	pursuant to applicable revenue laws.
14	(44) 'VAT Law' means the Value Added Tax Act of a
15	State."
16	Section 5. Title 54 of the Code of the Federated States of
17	Micronesia is hereby further amended by adding a new section 513
18	to subchapter I of chapter 5 to read as follows:
19	"Section 513. Source of income.
20	(1) An amount derived by a resident person in
21	carrying on a business is derived from sources in the
22	FSM except to the extent that it is attributable to a
23	business carried on through a permanent establishment
24	of the person outside the FSM.
25	(2) An amount derived by a non-resident person in

carrying on a business is derived from sources in the 1 FSM to the extent that it is attributable to a business 2. 3 carried on through a permanent establishment of the person in the FSM. 4 5 (3) Notwithstanding subsections (1) and (2) of 6 this section, the following amounts are considered 7 derived from sources in the FSM: 8 (a) a fee for services performed in the FSM; 9 (b) rental from the lease of real property 10 in the FSM; 11 (c) interest, a royalty, or a management 12 fee: (i) paid by a resident person, other 13 14 than as an expense of a business carried on through a 15 permanent establishment of the person outside the FSM; 16 or 17 (ii) paid by a non-resident person as an 18 expense of a business carried on through a permanent 19 establishment of the person in the FSM; 20 (d) a natural resource amount in respect of 2.1 a natural resource taken in the FSM; or 22 (e) an insurance premium in respect of the 23 insurance of a risk in the FSM." Section 6. Title 54 of the Code of the Federated States of 2.4 25 Micronesia is hereby further amended by adding a new section 514

to subchapter I of chapter 5 to read as follows: 1 2. "Section 514. Fair market value. 3 (1) The fair market value of an asset, property, service, or benefit at a particular time is the 4 5 ordinary open market value of the asset, property, 6 service, or benefit at that time. 7 (2) If it is not possible to determine the fair market value of an asset, property, service, or benefit 8 9 at a particular time under subsection (1) of this 10 section, the fair market value is the consideration a 11 similar asset, property, service, or benefit would ordinarily fetch in the open market at that time, 12 13 adjusted to take account of the differences between the similar asset, property, service, or benefit and the 14 15 actual asset, property, service, or benefit. 16 (3) If the fair market value of an asset, 17 property, service, or benefit cannot be determined under subsection (1) or (2) of this section, the fair 18 market value is the amount determined by the CEO." 19 Section 7. Title 54 of the Code of the Federated States of 20 2.1 Micronesia is hereby further amended by adding a new section 515 22 to subchapter I of subchapter 5 to read as follows: 23 "Section 515. Associate. 2.4 (1) Subject to subsection (2) of this section, 25 two persons are associates if the relationship between

1	them is such that one may reasonably be expected to act
2	in accordance with the intentions of the other, or both
3	persons may reasonably be expected to act in accordance
4	with the intentions of a third person.
5	(2) Two persons are not associates solely by
6	reason of the fact that one person is an employee of
7	the other or both persons are employees of a third
8	person.
9	(3) Without limiting the generality of subsection
10	(1) of this section, the following are treated as
11	associates:
12	(a) an individual and a relative of the
13	individual, except if the CEO is satisfied that neither
14	person may reasonably be expected to act in accordance
15	with the intentions of the other;
16	(b) a partner in a partnership and the
17	partnership, if the partner, either alone or together
18	with an associate or associates under another
19	application of this section, controls fifty percent
20	(50%) or more of the rights to income or capital of the
21	<pre>partnership;</pre>
22	(c) a trust or estate and a person who
23	benefits or may benefit under the trust or estate;
24	(d) a shareholder in a company and the
25	company, if the shareholder, either alone or together

1	with an associate or associates under another
2	application of this section, controls either directly
3	or through one or more interposed persons:
4	(i) fifty percent (50%) or more of
5	the voting power in the company;
6	(ii) fifty percent (50%) or more of
7	the rights to dividends; or
8	(iii) fifty percent (50%) or more of
9	the rights to capital; and
10	(e) two companies, if a person, either alone
11	or together with an associate or associates under
12	another application of this section, controls either
13	directly or through one or more interposed persons:
14	(i) fifty percent (50%) or more of the
15	voting power in both companies;
16	(ii) fifty percent (50%) or more of the
17	rights to dividends in both companies; or
18	(iii) fifty percent (50%) or more of the
19	rights to capital in both companies.
20	(4) In applying subsection (3)(b), (d), or (e) of
21	this section holdings that are attributable to a person
22	from an associate are not reattributed to another
23	associate."
24	Section 8. Title 54 of the Code of the Federated States of
25	Micronesia is hereby further amended by adding a new subchapter

II to chapter 5 to be entitled "Imposition of Tax". 1 2. Section 9. Title 54 of the Code of the Federated States of 3 Micronesia is hereby further amended by adding a new section 521 to subchapter II of chapter 5 to read as follows: 4 5 "Section 521. Imposition of net profit tax. 6 Net profit tax is imposed for each tax year at the rate 7 of twenty five percent (25%) on the net profit for the tax year of every business." 8 9 Section 10. Title 54 of the Code of the Federated States of 10 Micronesia is hereby further amended by adding a new section 522 11 to subchapter II of chapter 5 to read as follows: 12 "Section 522. Imposition of presumptive tax. 13 A presumptive tax of eighty dollars (\$80) per tax year is imposed on a business if the gross revenue of the 14 15 business for the tax year does not exceed ten thousand 16 dollars (\$10,000.)" Section 11. Title 54 of the Code of the Federated States of 17 Micronesia is hereby further amended by adding a new section 523 18 19 to subchapter II of chapter 5 to read as follows: 20 "Section 523. General provisions applicable to net 2.1 profit tax and presumptive tax. 22 (1) Net profit tax or presumptive tax is payable 23 by the person or persons carrying on the business. If a 2.4 person carries on more than one business, the net 25 profit tax or presumptive tax payable is computed and

16 of 63

1	reported separately for each business. For this
2	purpose, if a business has operations in more than one
3	State, the operations in each State are treated as a
4	separate business.
5	(2) No net profit tax or presumptive tax is
6	payable if the gross revenue of a business for a tax
7	year does not exceed two thousand dollars (\$2,000).
8	(3) Notwithstanding subsection (1) of this
9	section, in determining whether the gross revenue of a
10	business carried on by a person does not exceed ten
11	thousand dollars (\$10,000) for the purposes of section
12	522 of this title, or two thousand dollars (\$2,000) for
13	the purposes of subsection (2) of this section, account
14	is taken of the gross revenue of all businesses carried
15	on by the person or by associates of the person in the
16	FSM."
17	Section 12. Title 54 of the Code of the Federated States of
18	Micronesia is hereby further amended by adding a new section 524
19	to subchapter II of chapter 5 to read as follows:
20	"Section 524. Imposition of tax on transportation or
21	insurance income of non-resident person.
22	(1) Tax is imposed at the rate of three percent
23	(3%) on the gross revenue derived by a non-resident
24	person without a permanent establishment operating a
25	ship or aircraft for the carriage of passengers

1	livestock, mail, merchandise, or goods embarked in the
2	FSM.
3	(2) Tax payable under this section shall be
4	payable by the non-resident person deriving the amount
5	subject to tax. The tax payable is discharged if the
6	tax has been paid in accordance with section 575 or 576
7	of this title."
8	Section 13. Title 54 of the Code of the Federated States of
9	Micronesia is hereby further amended by adding a new section 525
10	to subchapter II of chapter 5 to read as follows:
11	"Section 525. Imposition of tax on certain payments to
12	non-resident persons.
13	(1) Tax is imposed at the rate specified in
14	subsection (2) of this section on the gross amount of
15	interest, a royalty, natural resource amount, insurance
16	premium, or management fee derived by a non-resident
17	person from sources in the FSM.
18	(2) The rate of tax imposed under subsection (1)
19	of this section is:
20	(a) five percent (5%) of the gross amount of
21	the insurance premium; or
22	(b) fifteen percent (15%) of the gross
23	amount of the interest, royalty, natural resource
24	amount, or management fee.
25	(3) Subsection (1) of this section does not apply

1	<u>to:</u>
2	(a) an amount that is exempt income; or
3	(b) interest, a royalty, natural resource
4	amount, insurance premium, or management fee that is
5	attributable to a business carried on by the non-
6	resident person through a permanent establishment of
7	the person in the FSM and, in that case, the interest,
8	royalty, natural resource amount, insurance premium, or
9	management fee is taxable under section 521 of this
10	title.
11	(4) The tax payable under subsection (1) of this
12	section is discharged if the tax has been paid in
13	accordance with section 581 of this title."
14	Section 14. Title 54 of the Code of the Federated
15	States of Micronesia is hereby further amended by
16	adding a new subchapter III to chapter 5 to be entitled
17	"Computation of Net Profit".
18	Section 15. Title 54 of the Code of the Federated States of
19	Micronesia is hereby further amended by adding a new section 531
20	to subchapter III of chapter 5 to read as follows:
21	"Section 531. Net profit.
22	The net profit of a business for a tax year is the
23	gross revenue of the business for the year reduced by
24	the total amount of deductions allowed to the business
25	for the year."

1	Section 16. Title 54 of the Code of the Federated States of
2	Micronesia is hereby further amended by adding a new section 532
3	to subchapter III of chapter 5 to read as follows:
4	"Section 532. Gross revenue.
5	(1) The gross revenue of a business for a tax year
6	is the sum of the following amounts (other than an
7	amount that is exempt income) derived by the business
8	during the year from sources in the FSM:
9	(a) the gross receipts from the carrying on
10	of the business, including the gross proceeds from the
11	disposal of inventory and the gross fees for the
12	provision of services;
13	(b) the gross receipts from the employment
14	of the capital of the business, including interest,
15	royalties, and rentals;
16	(c) the net gain on disposal of a business
17	asset (other than inventory);
18	(d) the net gain on satisfaction or
19	cancellation of a debt of the business; and
20	(e) the amount of an expense, loss, or bad
21	debt previously allowed as a deduction that has been
22	reimbursed or recovered by the business.
23	(2) For the purposes of subsection (1)(c) of this
24	section, the net gain on disposal of a business asset
25	is the consideration received on disposal of the asset

1	less the cost of the asset at the time of disposal.
2	(3) For the purposes of subsection (1)(d) of
3	this section, the net gain on disposal of a debt
4	of a business is the amount of the debt less the amount
5	received on satisfaction or cancellation of the
6	debt.
7	(4) The gross revenue of a business does not
8	include any amount subject to tax under sections 522,
9	524, or 525 of this title."
10	Section 17. Title 54 of the Code of the Federated States of
11	Micronesia is hereby further amended by adding a new section 533
12	to subchapter III of chapter 5 to read as follows:
13	"Section 533. Exempt income.
14	(1) The following amounts are exempt income:
15	(a) a distribution by an entity;
16	(b) interest paid by a resident company to a
17	non-resident person in respect of debentures if the
18	following conditions are satisfied:
19	(i) the debentures were issued by the
20	company outside the FSM for the purpose of raising a
21	loan outside the FSM;
22	(ii) the debentures were issued with a
23	view to public subscription or other wide distribution;
24	(iii) the debentures were issued for the
25	purpose of raising funds for use by the company in a

1	business carried on in the FSM; and
2	(iv) the interest is paid outside the
3	FSM; and
4	(c) an amount exempt from tax under an
5	international agreement between the Government of the
6	FSM and a foreign government or a public international
7	organization.
8	(2) A provision in another law providing that an
9	amount is exempt income does not have legal effect
10	unless also provided for in this chapter."
11	Section 18. Title 54 of the Code of the Federated
12	States of Micronesia is hereby further amended by adding a new
13	section 534 to subchapter III of chapter 5 to read as follows:
14	"Section 534. Deductions.
15	(1) Subject to this chapter, the total amount of
16	deductions allowed to a business for a tax year is the
17	<pre>sum of:</pre>
18	(a) subject to section 535 of this title,
19	the expenses or losses incurred during the year solely
20	in deriving amounts included in the gross revenue of
21	the business;
22	(b) the cost of inventory for the year as
23	determined under this chapter;
24	(c) the total amount, as determined under
25	section 536 of this title, by which the value of the

1	depreciable assets of the business have declined during
2	the year by reason of wear and tear from use in
3	deriving amounts included in the gross revenue of the
4	business;
5	(d) the total amount, as determined under
6	section 537 of this title, by which the value of the
7	intangibles of the business have declined in value
8	during the year from use in deriving amounts included
9	in the gross revenue of the business; and
10	(e) the net loss on disposal of a business
11	asset (other than inventory) during the year.
12	(2) For the purposes of subsection (1)(e) of this
13	section, the net loss on disposal of a business asset
14	is the cost of the asset at the time of disposal less
15	the consideration received on disposal of the asset."
16	Section 19. Title 54 of the Code of the Federated States of
17	Micronesia is hereby further amended by adding a new section 535
18	to subchapter III of chapter 5 to read as follows:
19	"Section 535. Non-deductible expenses.
20	(1) No deduction is allowed for:
21	(a) a distribution by an entity or capital
22	withdrawn from a business;
23	(b) an expense or loss of a capital nature
24	except as provided in section 534(1)(c), (d), or (e) of
25	thic title.

1	(c) an amount placed in a reserve fund, a
2	provision for expected expenses or losses, or an amount
3	capitalized in any way;
4	(d) an expense or loss to the extent
5	recoverable under a policy of insurance or contract of
6	<pre>indemnity;</pre>
7	(e) an expense incurred in providing
8	entertainment except:
9	(i) if the entertainment was provided
10	in the ordinary course of a business carried on to
11	provide the entertainment and the entertainment was not
12	provided to an employee or an associate of the person
13	carrying on the business;
14	(ii) if the entertainment was provided
15	to an employee, it was provided while the employee is
16	traveling on business in course of the employee's
17	employment; or
18	(iii) if the entertainment is a meal or
19	refreshment provided to an employee on the business'
20	premises and which is available to all full-time
21	employees on equal terms;
22	(f) interest payable to an associate other
23	than that interest included in the gross revenue of a
24	business carried on by the associate or taxable under
25	section 525 of this title;

1	(g) the net profit tax, including any
2	penalty or interest payable in respect of net profit
3	<pre>tax payable;</pre>
4	(h) a fine or penalty imposed for violation
5	of any law, rule, or regulation; or
6	(i) a bribe, kickback, or other expense
7	incurred to accomplish an illegal transaction or
8	activity.
9	(2) A person required to withhold tax under
10	subchapter VII of this chapter in respect of an amount
11	paid to a non-resident person is not allowed a
12	deduction for the amount paid until the withheld tax
13	has been paid to the CEO."
14	Section 20. Title 54 of the Code of the Federated States of
15	Micronesia is hereby further amended by adding a new section 536
16	to subchapter III of chapter 5 to read as follows:
17	"Section 536. Depreciable assets.
18	(1) A business is allowed a deduction for a tax
19	year for the amount by which the value of the
20	depreciable assets of a business has declined during
21	the year.
22	(2) The decline in value of a depreciable asset
23	of a business for a tax year is computed by applying
24	the rate specified in subsection (3) of this section
25	against the cost of the asset.

1	(3) The rate of depreciation is:
2	(a) in the case of motor vehicles, buses and
3	minibuses, goods vehicles, trucks, tractors, trailers,
4	and trailer-mounted containers, computers and data
5	handling equipment, construction equipment and
6	earthmoving equipment, and plant and machinery used in
7	manufacturing, mining, or farming operations, fifty
8	percent (50%);
9	(b) in the case of industrial buildings, ten
10	percent (10%);
11	(c) in the case of any other structural
12	improvement, five percent (5%); or
13	(d) in the case of any other depreciable
14	asset, thirty three and one-third percent $(33^{1}/_{3}\%)$ .
15	(4) If a depreciable asset of a business is not
16	used, available for use, or held in carrying on the
17	business for the whole of the year, the amount computed
18	under subsection (2) of this section is reduced by the
19	proportion of the year that the asset was not so used.
20	(5) The total decline in value allowed as a
21	deduction under section 534(1)(c) of this title for a
22	depreciable asset for the current tax year and all
23	previous tax years must not exceed the cost of the
24	asset."
25	Section 21 Title 54 of the Code of the Federated States of

Micronesia is hereby further amended by adding a new section 537 1 to subchapter III of chapter 5 to read as follows: 2. "Section 537. Intangibles. 3 (1) A business is allowed a deduction for a tax 4 5 year for the amount by which the value of the 6 intangibles of a business has declined during the year. 7 (2) The decline in value of an intangible of a 8 business for a tax year is computed by dividing the 9 cost of the intangible by its useful life. 10 (3) An intangible is treated as having a useful 11 life of ten years if: 12 (a) it has a useful life of more than ten 13 years; or 14 (b) it does not have an ascertainable useful 15 life. (4) If an intangible of a business is not used, 16 17 available for use, or held in carrying on the business for the whole of the year, the amount computed under 18 19 subsection (2) of this section is reduced by the 20 proportion of the year that the intangible was not so 2.1 used. 22 (5) The total decline in value allowed as a 23 deduction under section 534(1)(d) of this title for an 2.4 intangible for the current tax year and all previous 25 tax years must not exceed the cost of the intangible."

Section 22. Title 54 of the Code of the Federated 1 2. States of Micronesia is hereby further amended by adding a new 3 section 538 to subchapter III of chapter 5 to read as follows: "Section 538. Net loss carry forward. 4 5 (1) If the total amount of deductions of a 6 business allowed for a tax year (other than under this 7 section or section 540(3) of this title) exceeds the 8 gross revenue of the business for the year, the amount 9 of the excess is the net loss of the business for the 10 year. 11 (2) If a business has a net loss for a tax year, 12 the amount of the loss is carried forward to the 13 following tax year and allowed as a deduction in 14 computing the net profit of the business for that 15 following year. (3) If a net loss is not wholly deducted under 16 17 subsection (2) of this section, the amount not deducted 18 is carried forward to the next following tax year and 19 applied as specified in subsection (2) of this section 20 in that year, and so on until the loss is fully 2.1 deducted, but no loss can be carried forward for more 22 than three tax years after the year in which the loss 23 was incurred. (4) If a business has a net loss carried forward 2.4 25 under this section for more than one tax year, the loss

of the earliest year is deducted first. 1 2. (5) If a business has a net loss carried forward 3 under this section and an interest expense carried forward under section 540 of this title for a tax year, 4 5 the net loss carried forward is deducted first. 6 (6) If a person carries on more than one 7 business, this section applies separately to each 8 business." Section 23. Title 54 of the Code of the Federated States of 9 10 Micronesia is hereby further amended by adding a new section 539 11 to subchapter III of chapter 5 to read as follows: 12 "Section 539. Currency translation. (1) An amount taken into account under this 13 14 chapter must be expressed in United States dollars. 15 (2) Subject to subsection (3) of this section, if 16 an amount is in a currency other than United States 17 dollars, the amount must be translated to United States 18 dollars at the United States Federal Reserve exchange rate applying between the foreign currency and United 19 20 States dollars on the date the amount is taken into 2.1 account for the purposes of this chapter. 22 (3) With the prior written permission of the CEO, 23 amounts taken into account in computing the net profit or net loss of a business for a tax year may be 2.4 25 translated to United States dollars at the average mid-

1	exchange rate for the tax year between the foreign
2	currency and United States dollars."
3	Section 24. Title 54 of the Code of the Federated States of
4	Micronesia is hereby further amended by adding a new section 540
5	to subchapter III of chapter 5 to read as follows:
6	"Section 540. Interest expense.
7	(1) Subject to section 535(1)(f) of this title
8	and subsection (2) of this section, a business is
9	allowed a deduction for any interest expense incurred
10	by the business during a tax year to the extent which
11	the business has used the proceeds or benefit of the
12	debt or other instrument or agreement giving rise to
13	the interest solely to derive income included in the
14	gross revenue of the business.
15	(2) The total amount of interest allowed to a
16	business as a deduction under this section for a tax
17	year must not exceed the amount computed according to
18	the following formula:
19	$A + (50\% \times (B - C))$
20	Where:
21	A is the total interest income derived by the
22	business during the year;
23	<b>B</b> is the total gross income of the business
24	for the year, other than interest income; and
25	<b>c</b> is the total amount of deductions allowed to the

1	business for the year, other than for interest
2	incurred.
3	(3) If an amount of interest is not deducted in a
4	tax year as a result of subsection (2) of this section,
5	the undeducted amount of the interest is carried
6	forward and treated as interest incurred by the
7	business in the next following tax year and deducted in
8	accordance with this section in that year, and so on
9	until the interest is fully deducted.
10	(4) Subsection (2) of this section does not apply
11	to a financial institution."
12	Section 25. Title 54 of the Code of the Federated States of
13	Micronesia is hereby further amended by adding a new subchapter
14	IV to chapter 5 to be entitled "Tax Accounting".
15	Section 26. Title 54 of the Code of the Federated States of
16	Micronesia is hereby further amended by adding a new section 541
17	to subchapter IV of chapter 5 to read as follows:
18	"Section 541. Simplified tax accounting for small
19	<u>businesses.</u>
20	(1) The net profit of a small business is computed in
21	accordance with generally accepted accounting
22	principles subject to the following modifications:
23	(a) the revenues and expenses of the business are
24	accounted for on a cash basis under which an amount of
25	revenue is derived when it is received and an expense

1	is incurred when it is paid;
2	(b) no deduction is allowed for an amount
3	specified in section 535 of this title;
4	(c) subject to paragraph (e) of this section, the
5	amount allowed for the depreciation of depreciable
6	assets or the amortization of intangibles is computed
7	in accordance with sections 536 and 537 of this title;
8	(d) the amount allowed as a deduction under
9	section 534(1)(b) of this title for a tax year is the
10	total amount paid by the business for the cost of
11	inventory acquired during the year and section 544 of
12	this title does not apply; and
13	(e) an intangible that is a prepayment of a
14	business expense is deductible in the tax year in which
15	it is paid."
16	(2) Reserved.
17	Section 27. Title 54 of the Code of the Federated States of
18	Micronesia is hereby further amended by adding a new section 542
19	to subchapter IV of chapter 5 to read as follows:
20	"Section 542. Tax accounting for businesses other than
21	small businesses.
22	(1) The net profit of a business (other than a
23	small business) is computed in accordance with
24	generally accepted accounting principles subject to the
25	following modifications:

1	(a) the revenues and expenses of the
2	business are accounted for on an accrual basis under
3	which an amount of revenue is derived when it is due
4	and an expense is incurred when it is payable;
5	(b) no deduction is allowed for any amount
6	specified in section 535 of this title;
7	(c) the amount allowed for the depreciation
8	of depreciable assets or the amortization of
9	intangibles is computed in accordance with sections 536
10	and 537 of this title;
11	(d) the deduction allowed for inventory is
12	computed in accordance with section 544 of this title;
13	(e) the gross revenues and expenses arising
14	under a long-term contract are determined under section
15	545 of this title;
16	(f) a finance lease is treated as the
17	equivalent of a sale and purchase of the leased asset
18	in accordance with section 546 of this title; and
19	(g) a deduction for a bad debt is allowed in
20	accordance with section 547 of this title.
21	(2) For the purposes of subsection (1)(a) of this
22	section:
23	(a) an amount is due when the business is
24	entitled to receive it even if the time for discharge
25	of the entitlement is nostnoned or the amount is

1	payable by installments; and
2	(b) an amount is payable when all the events
3	that determine liability have occurred and the amount
4	of the liability can be determined with reasonable
5	accuracy, but not before economic performance occurs.
6	(3) For the purposes of subsection (2) of this
7	section, economic performance occurs:
8	(a) in the case of the acquisition of
9	services or assets, at the time the services are
10	provided or assets delivered;
11	(b) in the case of the use of assets, at the
12	time assets are used; and
13	(c) in any other case, at the time payment
14	is made in full satisfaction of the liability."
15	Section 28. Title 54 of the Code of the Federated States of
16	Micronesia is hereby further amended by adding a new section 543
17	to subchapter IV of chapter 5 to read as follows:
18	"Section 543. Change in tax accounting method.
19	(1) If a business that is a small business ceases
20	to be a small business or a business that is not a
21	small business becomes a small business, the business
22	shall apply, in writing, to the CEO for a change in the
23	method of accounting used by the business in computing
24	the net profit of the person's business and the CEO
25	shall in writing, approve or disapprove the

application. 1 2. (2) If the method of accounting used by a 3 business in computing the net profit of a business changes, adjustments must be made in the tax year of 4 5 change to items of revenue, deduction, or credit, or to 6 any other items affected by the change so that no item 7 is omitted and no item is taken into account more than 8 once." Section 29. Title 54 of the Code of the Federated States of 9 10 Micronesia is hereby further amended by adding a new section 544 11 to subchapter IV of chapter 5 to read as follows: 12 "Section 544. Inventory. (1) The amount allowed as a deduction under 13 14 section 534(1)(b) of this title for a tax year to a 15 business accounting for net profits tax on an accrual 16 basis for the cost of inventory is the cost of 17 inventory disposed of during the year as computed under 18 this section. 19 (2) The cost of inventory disposed of by a business during a tax year is computed in accordance 20 2.1 with the following formula: 22 (A + B) - C23 Where: A is the opening value of the inventory for the 2.4 25 tax year;

1	<b>B</b> is the cost of inventory acquired during the
2	tax year; and
3	c is the closing value of inventory for the tax
4	year.
5	(3) The opening value of inventory for a tax
6	<pre>year:</pre>
7	(a) is the cost of inventory on hand at the
8	end of the previous tax year; or
9	(b) if the business commenced during the
10	year, the cost of inventory (if any) acquired by the
11	owner of the business prior to commencement of the
12	business.
13	(4) The closing value of inventory for a tax year
14	is the lower of cost or fair market value of inventory
15	on hand at the end of the tax year.
16	(5) The cost of inventory on hand at the end of a
17	tax year is computed under the absorption-cost method.
18	The absorption-cost method is the generally accepted
19	accounting principle under which the cost of an item of
20	inventory is the sum of direct material costs, direct
21	labor costs, and factory overhead costs. Direct
22	material costs are the cost of materials that become an
23	integral part of the inventory manufactured or
24	produced, or which are consumed in the manufacturing or
25	production process. Direct labor costs are the labor

costs directly related to the manufacture or production 1 of inventory. Factory overhead costs are the total 2. 3 costs of manufacturing or producing inventory, other than direct labor and direct material costs. 4 5 (6) If particular items of inventory are not 6 readily identifiable, the cost of inventory on hand at 7 the end of a tax year may be accounted for on the first-in-first-out method. The first-in-first-out 8 9 method is the generally accepted accounting principle 10 under which the valuation of inventory is based on the 11 assumption that inventory is sold in the order of its acquisition." 12 Section 30. Title 54 of the Code of the Federated States of 13 14 Micronesia is hereby further amended by adding a new section 545 15 to subchapter IV of chapter 5 to read as follows: 16 "Section 545. Long-term contracts. 17 (1) A business accounting for net profit tax on an accrual basis must compute the net profit arising 18 19 under a long-term contract during a tax year under the 20 percentage of completion method. The percentage of 2.1 completion method is the generally accepted accounting 22 principle under which revenues and expenditures arising 23 under a long-term contract are recognized by reference 2.4 to the stage of completion of the contract. 25 (2) In this section, 'long-term contract' means a

1	contract for manufacture, installation, or
2	construction, or, in relation to each, the performance
3	of related services, that is not completed within the
4	tax year in which work under the contract commenced,
5	other than a contract estimated to be completed within
6	six months of the date on which work under the contract
7	commenced."
8	Section 31. Title 54 of the Code of the Federated States of
9	Micronesia is hereby further amended by adding a new section 546
10	to subchapter IV of chapter 5 to read as follows:
11	"Section 546. Finance leases.
12	(1) If a business has entered into a finance
13	lease, the net profit of the business is computed on
14	the basis that:
15	(a) the lessee is the owner of the asset;
16	(b) the lessee acquired the asset at the
17	commencement of the lease, except in cases when the
18	lessee already was the owner of the asset; and
19	(c) the lessor has made a blended loan to the
20	lessee at the commencement of the lease and each lease
21	payment is in part repayment of principal and in part
22	payment of interest under that loan.
23	(2) The cost of an asset treated as owned by the
24	lessee under subsection (1)(a) of this section is:
25	(a) if the lessor and lessee are not

1	associates and an amount is stated as the cost or value
2	of the asset in the lease agreement, that amount; or
3	(b) in any other case, the fair market value
4	of the asset at the commencement of the lease.
5	(3) The amount of the loan referred to in
6	subsection (1)(c) of this section is the amount
7	determined under subsection (2) of this section as the
8	cost of the asset.
9	(4) The interest part of each payment made under
10	the loan is computed by reference to the interest rate
11	implicit in the lease agreement.
12	(5) In this section, a blended loan is a loan
13	under which payments by the borrower represent in part
14	a payment of interest and in part a repayment of
15	principal when the interest part is calculated on the
16	principal outstanding at the time of each payment."
17	Section 32. Title 54 of the Code of the Federated States of
18	Micronesia is hereby further amended by adding a new section 547
19	to subchapter IV of chapter 5 to read as follows:
20	"Section 547. Bad debts.
21	(1) A deduction is allowed for a tax year for a
22	bad debt of a business if the following conditions are
23	satisfied:
24	(a) the amount of the debt:
25	(i) was previously included in the

1	gross revenue of the business; or
2	(ii) is money lent by the business in
3	the normal course of carrying on a business of money
4	<pre>lending;</pre>
5	(b) the debt or part of the debt is written
6	off in the accounts of the business in the tax year;
7	<u>and</u>
8	(c) there are reasonable grounds for
9	believing that the debt is irrecoverable.
10	(2) The amount of the deduction allowed under
11	this section for a tax year must not exceed the amount
12	of the debt written off in the accounts of the business
13	for that year."
14	Section 33. Title 54 of the Code of the Federated States of
15	Micronesia is hereby further amended by adding a new subchapter V
16	to chapter 5 to be entitled "Business Assets".
17	Section 34. Title 54 of the Code of the Federated States of
18	Micronesia is hereby further amended by enacting a new section
19	551 to subchapter V of chapter 5 to read as follows:
20	"Section 551. Disposal and acquisition of business
21	assets.
22	(1) Except as otherwise provided in this chapter,
23	this section establishes when a business asset is
24	disposed of or acquired for the purposes of this
25	chapter.

1	(2) A business is treated as having made a
2	disposal of an asset at the time the business parts
3	with the ownership of the asset, including when the
4	asset is:
5	(a) sold, exchanged, transferred, or
6	distributed; or
7	(b) cancelled, redeemed, relinquished,
8	destroyed, lost, expired, or surrendered.
9	(3) A disposal includes the disposal of a part of
10	an asset.
11	(4) The transmission of an asset by succession or
12	under a will is treated as a disposal of the asset by
13	the deceased at the time the asset is transmitted.
14	(5) The application of a business asset to
15	personal or domestic use is treated as a disposal of
16	the asset by the owner at the time the asset is so
17	applied.
18	(6) A business acquires an asset at the time the
19	owner of the business begins to own the asset,
20	including at the time the owner is granted any right.
21	(7) The application of a personal asset by the
22	owner of a business to business use is treated as an
23	acquisition of the asset by the business at the time
24	the asset is so used.
25	(8) In this section, 'personal asset' means an

1	asset held wholly for personal or domestic use."
2	Section 35. Title 54 of the Code of the Federated States of
3	Micronesia is hereby further amended by adding a new section 552
4	to subchapter V of chapter 5 to read as follows:
5	"Section 552. Cost.
6	(1) Except as otherwise provided in this chapter,
7	this section establishes the cost of a business asset
8	for the purposes of this chapter.
9	(2) Subject to this chapter, the cost of a
10	business asset is the sum of the following amounts:
11	(a) the total consideration given by a
12	business for the asset, including the fair market value
13	of any consideration in kind determined at the time the
14	asset is acquired and, if the asset is constructed or
15	developed, the cost of construction or development;
16	(b) any incidental expenditure incurred by
17	the business in acquiring or disposing of the asset; or
18	(c) any expenditure incurred by the business
19	to install, alter, renew, reconstruct, or improve the
20	asset.
21	(3) Subject to this chapter, the cost of a
22	business asset that is an intangible is:
23	(a) in relation to an intangible referred to
24	in paragraph (a) or (b) of the definition of
25	'intangible' in section 512 of this title, the total

expenditure incurred in acquiring, creating, improving, 1 2. or renewing the intangible; or 3 (b) in relation to an intangible referred to in paragraph (c) of the definition of 'intangible' in 4 5 section 512 of this title, the amount of the 6 expenditure. 7 (4) The cost of a business asset is reduced by the amount of any deduction allowed to the business in 8 9 respect of amounts included in the cost of the asset, 10 including a deduction allowed under section 536 or 537 11 of this title. 12 (5) If a business disposes of a part of a business asset, the cost of the asset is apportioned 13 between the part of the asset retained and the part 14 15 disposed of in accordance with their respective fair 16 market values determined at the time the business 17 acquired the asset. 18 (6) The cost of a business asset does not include the amount of any grant, subsidy, rebate, commission, 19 or other assistance received or receivable by a 20 2.1 business in respect of the acquisition or holding of 22 the asset, except to the extent to which the amount is 23 included in the gross revenue of the business. The 2.4 reference to 'other assistance' in this subsection does 25 not include a loan repayable with or without interest.

1	(7) The cost of a business asset treated as
2	acquired under section 551(7) of this title is the fair
3	market value of the asset determined at the date it is
4	applied to business use.
5	(8) If the acquisition of a business asset is the
6	derivation of an amount included in gross revenue of a
7	business, the cost of the asset is the amount so
8	included plus any amount paid by the business for the
9	asset.
10	(9) If the acquisition of a business asset is the
11	derivation of exempt income, the cost of the asset is
12	the exempt amount plus any amount paid by the business
13	for the asset."
14	Section 36. Title 54 of the Code of the Federated States of
15	Micronesia is hereby further amended by adding a new section 553
16	to subchapter V of chapter 5 to read as follows:
17	"Section 553. Consideration received.
18	(1) Except as otherwise provided in this chapter,
19	this section establishes the amount of consideration
20	received on disposal of a business asset for the
21	purposes of this chapter.
22	(2) The consideration received by a business on
23	disposal of a business asset is the total amount
24	received by the business for the asset, including the
25	fair market value of any consideration received in kind

determined at the time of disposal. 1 2. (3) If a business asset has been lost or 3 destroyed, the consideration received by a business for the asset includes any compensation, indemnity, or 4 5 damages received by the business as a result of the 6 loss or destruction, including amounts received as a 7 consequence of: (a) an insurance policy, indemnity, or other 8 9 agreement; 10 (b) a settlement; or 11 (c) a judicial decision. 12 (4) The consideration received for a business asset treated as disposed of under section 551(5) of 13 this title is the fair market value of the asset 14 15 determined at the time it is applied to personal or 16 domestic use. 17 (5) If two or more business assets are disposed of by a business in a single transaction and the 18 19 consideration received for each asset is not specified, 20 the total consideration received by the business is 2.1 apportioned among the assets disposed of in proportion 22 to their respective fair market values determined at 23 the time of the transaction." Section 37. Title 54 of the Code of the Federated States of 2.4 25 Micronesia is hereby further amended by adding a new section 554

1	to subchapter V of chapter 5 to read as follows:
2	"Section 554. Non-arm's length transaction.
3	(1) For the purposes of this chapter, if a business
4	asset is disposed of in a non-arm's length transaction:
5	(a) the business disposing of the asset is
6	treated as having received consideration equal to the
7	fair market value of the asset determined at the time
8	the asset is disposed of; and
9	(b) the business acquiring the asset is treated
10	as having a cost equal to the amount determined under
11	paragraph (a) of this section.
12	(2) Reserved. "
13	Section 38. Title 54 of the Code of the Federated
14	States of Micronesia is hereby further amended by adding a new
15	section 555 to subchapter V of chapter 5 to read as follows:
16	"Section 555. Gain or loss not recognized.
17	(1) For the purposes of this chapter and subject
18	to subsection (2) of this section, no gain or loss is
19	taken to arise on the disposal of a business asset:
20	(a) between spouses as part of a divorce
21	settlement or under an agreement to live apart, but
22	only if the asset is used, available for use, or held
23	by the recipient spouse in carrying on a business;
24	(b) by reason of the transmission of the
25	asset on the death of a person to an executor or

beneficiary, but only if the asset is used, available 1 2. for use, or held by the executor or beneficiary in 3 carrying on a business; or (c) by reason of the compulsory acquisition 4 5 of the asset under any law if the consideration 6 received for the disposal is reinvested by the 7 recipient in an asset of a like kind (referred to as a 8 'replacement asset') within one year of the disposal. 9 (2) Subsection (1) of this section does not apply 10 if the person acquiring the asset (including a 11 replacement asset) is a non-resident person at the time 12 of the acquisition. (3) If subsection (1)(a) or (b) of this section 13 applies, the person acquiring the asset is treated as 14 15 acquiring an asset of the same character as the person disposing of the asset for an amount equal to the cost 16 17 of the asset for the person disposing of the asset at the time of the disposal. 18 19 (4) A person's cost of a replacement asset or 20 intangible referred to in subsection (1)(c) of this 2.1 section is the cost of the asset or intangible at the 22 time it is compulsorily acquired plus the amount by 23 which any consideration given by the person for the 2.4 replacement asset exceeds the consideration received by 25 the person for the asset or intangible compulsorily

1	acquired."
2	Section 39. Title 54 of the Code of the Federated States of
3	Micronesia is hereby further amended by adding a new subchapter
4	VI to chapter 5 to be entitled <u>"Anti-avoidance"</u> .
5	Section 40. Title 54 of the Code of the Federated States of
6	Micronesia is hereby further amended by adding a new section 561
7	to subchapter VI of chapter 5 to read as follows:
8	"Section 561. Transfer pricing.
9	(1) The CEO may, in respect of:
10	(a) a transaction between businesses carried
11	on by persons who are associates; or
12	(b) a transaction between businesses carried
13	on by the same person, distribute, apportion, or
14	allocate revenue and expenses between the businesses as
15	is necessary to reflect the outcome that would have
16	arisen in a transaction between independent persons
17	dealing with each other at arm's length.
18	(2) In applying subsection (1) of this section,
19	the CEO may be guided by international standards, case
20	law, and guidelines on transfer pricing issued by
21	international organizations concerned with taxation."
22	Section 41. Title 54 of the Code of the Federated States of
23	Micronesia is hereby further amended by adding a new section 562
24	to subchapter VI of subchapter 5 to read as follows:
25	"Section 562. General anti-avoidance provision.

48 of 63

1	(1) In this section, 'tax avoidance scheme' means
2	any transaction or arrangement where one of the main
3	purposes of a person in entering into the transaction
4	or arrangement is the avoidance or reduction of the tax
5	liability of a business under this chapter.
6	(2) For the purposes of determining the tax
7	liability of a business under this chapter, the CEO
8	may:
9	(a) determine the character of a transaction
10	or an element of a transaction that was entered into as
11	part of a tax avoidance scheme;
12	(b) disregard a transaction that does not
13	have substantial economic effect;
14	(c) determine the character of a transaction
15	if the form of the transaction does not reflect the
16	<pre>substance; or</pre>
17	(d) treat separate businesses carried on by
18	the same person as a single business if business
19	activity has been fragmented under a tax avoidance
20	scheme."
21	Section 42. Title 54 of the Code of the Federated States of
22	Micronesia is hereby further amended by adding a new subchapter
23	VII to chapter 5 to be entitled "Procedures".
24	Section 43. Title 54 of the Code of the Federated States of
25	Micronesia is hereby further amended by adding a new section 571

1	to subchapter VII of chapter 5 to read as follows:
2	"Section 571. Filing of tax return.
3	(1) A person liable for tax under section 521 of
4	this title in respect of a business must file a net
5	profit tax return for the business for each tax year
6	within three months after the end of the tax year.
7	(2) A person liable for tax under section 522 of
8	this title in respect of a business must file a
9	presumptive tax return for the business for each tax
10	year within three months after the end of the tax year.
11	(3) A tax return must be in the prescribed form
12	and filed in the prescribed manner."
13	Section 44. Title 54 of the Code of the Federated States of
14	Micronesia is hereby further amended by adding a new section 572
15	to subchapter VII of chapter 5 to read as follows:
16	"Section 572. Self-assessment of net profit tax or
17	presumptive tax due.
18	(1) A person that files a net profit tax return
19	in respect of a business for a tax year is treated as
20	having made a self-assessment of:
21	(a) if the business has a net profit for the
22	year, the amount of the net profit of the business and
23	the net profit tax payable thereon as specified in the
24	return; or
25	(b) if the business has made a net loss for

1	the year, the amount of the net loss of the business as
2	specified in the return.
3	(2) A person that files a presumptive tax return
4	in respect of a business for a tax year is treated as
5	having made a self-assessment of the presumptive tax
6	payable for the year as specified in the return."
7	Section 45. Title 54 of the Code of the Federated States of
8	Micronesia is hereby further amended by adding a new section 573
9	to subchapter VII of chapter 5 to read as follows:
10	"Section 573. Payment of tax.
11	The net profit tax or presumptive tax payable by a
12	person for a tax year in respect of a business carried
13	on by the person is payable by the date that the tax
14	return of the business for the year is due."
15	Section 46. Title 54 of the Code of the Federated States of
16	Micronesia is hereby further amended by adding a new section 574
17	to subchapter VII of chapter 5 to read as follows:
18	"Section 574. Installments of tax.
19	(1) A person must pay installments of net profit
20	tax for a tax year in respect of a business carried on
21	by the person on the last working day of the third,
22	sixth, ninth, and twelfth months of the tax year.
23	(2) The amount of each installment is one-quarter
24	of the amount of net profits tax estimated by the
25	nergon to be navable in respect of the business for the

tax year. An estimate of net profit tax payable by the

person for a tax year in respect of a business must be

filed with the CEO by the due date for payment of the

first installment for the year.

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- subsection (2) of this section remains in force for the whole of the tax year unless a revised estimate is filed with the CEO. A revised estimate applies to the calculation of installments of net profit tax for a tax year due both before and after the date the revised estimate was filed. The amount of any underpayment of installments made prior to filing the revised estimate must be paid by the person together with the first installment due after the revised estimate is filed. The amount of any overpaid installments is applied against future net profit tax installments due.
- (4) If a person fails to file an estimate of net profit tax in respect of a business as required under subsection (2) of this section, the estimated net profit tax payable in respect of the business for the tax year is such amount as estimated by the CEO. The CEO's estimate remains in force for the whole of the tax year unless revised by the business in accordance with subsection (3) of this section.
  - (5) Each installment of net profit tax paid by a

person in respect of a business during a tax year is 1 credited against the assessed net profit tax of the 2. 3 business for the year. If the amount of the credit allowed exceeds the net profit tax due for the year, 4 5 the amount of the excess is credited against the 6 assessed net profit tax liability of the person in 7 relation to any other business carried on by the 8 person. Any remaining excess is refunded to the person, 9 or at the person's election, may be credited against 10 the next year's tax assessment. 11 (6) If the estimate (including any revised 12 estimate) of net profit tax payable by a person in 13 respect of a business for a tax year is less than 14 ninety percent (90%) of the assessed net profit tax 15 liability of the person in respect of the business for the year (the difference is referred to as the 16 17 'installment shortfall'), the business is liable for a 18 penalty equal to: 19 (a) if the under-estimate is due to fraud or 20 willful neglect, fifty percent (50%) of the installment 2.1 shortfall; or 22 (b) in any other case, ten percent (10%) of 23 the installment shortfall. 2.4 (7) No penalty is imposed under subsection (6)(b) 25 of this section if the CEO is satisfied that the reason

1	for the installment shortfall was due to circumstances
2	beyond the control of the business (such as a
3	significant price fluctuation) and all reasonable care
4	was taken in making the estimate."
5	Section 47. Title 54 of the Code of the Federated States of
6	Micronesia is hereby further amended by adding a new section 575
7	to subchapter VII of chapter 5 to read as follows:
8	"Section 575. Collection of tax from non-resident ship
9	owners or charterers.
10	(1) Subject to subsection (3) of this section,
11	before the departure of a ship owned or chartered by a
12	non-resident person from a port in FSM:
13	(a) the master or agent of the ship must
14	file with the CEO a return showing the gross revenue
15	derived from the carriage of passengers, livestock,
16	mail, merchandise, or goods embarked in the FSM in
17	respect of the ship; and
18	(b) the CEO must determine the amount of tax
19	due under section 524(1)(a) of this title in respect of
20	the ship and pursuant to regulatory guidelines, notify
21	the master or agent, in writing, of the amount due.
22	(2) The return required under subsection (1)(a)
23	of this section must be in the prescribed form and
24	filed in the prescribed manner.
25	(3) The master or agent of a ship is liable for

the tax notified under subsection (1)(b) of this 1 2. section. 3 (4) If the CEO is satisfied that the master or agent of a ship or the owner or charterer of the ship 4 5 is unable to file the return required under subsection 6 (1)(a) of this section before the departure of the ship 7 from the FSM, the CEO may allow the return to be filed 8 within 30 days after departure of the ship provided the 9 non-resident owner or charterer has made satisfactory 10 arrangements for the payment of the tax due under 11 section 524(1)(a) of this title in respect of the ship. 12 (5) The CEO must not grant a port clearance for a ship owned or chartered by a non-resident person until 13 14 satisfied that any tax due under section 524(1)(a) of 15 this title in respect of the ship has been paid or that 16 arrangements for its payment have been made to the 17 satisfaction of the CEO. 18 (6) This section does not relieve the owner or 19 charterer of the ship from liability to pay any amount 20 due under section 524(1)(a) of this title that is not 2.1 paid by the master or agent of the ship." 22 Section 48. Title 54 of the Code of the Federated States of 23 Micronesia is hereby further amended by adding a new section 576 to subchapter VII of chapter 5 to read as follows: 2.4 25 "Section 576. Collection of tax from non-resident

1 aircraft owners or charterers. 2. (1) The owner or charterer of an aircraft liable 3 for tax under section 524(1)(a) of this title must file a return with the CEO for each quarter within fifteen 4 5 days after the end of the quarter. 6 (2) The return required under subsection (1) of 7 this section must be in the prescribed form and filed 8 in the prescribed manner. 9 (3) A person that files a tax return under 10 subsection (1) of this section is treated as having 11 made a self-assessment of the gross revenue derived for 12 the carriage of passengers, livestock, mail, merchandise, or goods embarked in the FSM during the 13 14 quarter and the tax payable thereon under section 15 524(1)(a) of this title as specified in the return. (4) The tax payable by the non-resident person 16 17 under section 524(1)(a) of this title is collected 18 quarterly and is due on the due date for filing the 19 return for each quarter. 20 (5) If the tax payable for a quarter is not paid 2.1 within three months of the due date, the CEO may issue 22 to the relevant airport authority a certificate 23 specifying the name of the non-resident person and the 2.4 amount of tax due, and the relevant airport authority 25 must refuse clearance from any airport in the FSM to

1 any aircraft owned or chartered by the person until the tax due has been paid." 2. Section 49. Title 54 of the Code of the Federated States of 3 Micronesia is hereby further amended by adding a new section 577 5 to subchapter VII of chapter 5 to read as follows: "Section 577. Records. 6 7 (1) A person carrying on a business must: (a) keep such accounts, documents, and 8 9 records as enable the computation of the net profit of 10 the business for a tax year; and 11 (b) retain the records required under 12 paragraph (a) of this subsection for six (6) years 13 after the end of the tax year to which they relate. 14 (2) The records that must be maintained by a 15 person liable to pay presumptive tax or tax under section 524 of this title may be prescribed. 16 (3) The CEO may disallow a claim for a deduction 17 18 for an expense if a business is unable, without reasonable excuse, to produce a receipt or other record 19 20 of the expense, or to produce evidence relating to the 2.1 circumstances giving rise to the claim for the 22 deduction." 23 Section 50. Title 54 of the Code of the Federated States of 2.4 Micronesia is hereby further amended by adding a new subchapter 25 VIII to chapter 5 to be entitled "Withholding Tax".

1	Section 51. Title 54 of the Code of the Federated States of
2	Micronesia is hereby further amended by adding a new section 581
3	to subchapter VIII of chapter 5 to read as follows:
4	"Section 581. Withholding of tax from payments to non-
5	resident persons.
6	(1) A person paying interest, a royalty, natural
7	resource amount, insurance premium, or management fee
8	that is liable to tax under section 525 of this title
9	must withhold tax at the rate of:
10	(a) in the case of an insurance premium,
11	five percent (5%) of the gross amount of the premium;
12	<u>or</u>
13	(b) in any other case, fifteen percent (15%)
14	of the gross amount of the payment.
15	(2) A person must withhold tax from the gross
16	amount paid at the rate of ten percent (10%) if:
17	(a) a person is liable to pay a fee to a
18	non-resident person for the rendering of independent
19	services;
20	(b) the fee is derived by the non-resident
21	person from sources in the FSM; and
22	(c) the fee is not attributable to a
23	business carried on by the non-resident person through
24	a permanent establishment of the person in the FSM.
25	(3) Tax required to be withheld by a person under

1	this section must be paid to the CEO within 15 days
2	after the end of the month in which the person was
3	required to withhold the tax.
4	(4) A person is personally liable to pay the
5	amount of the tax to the CEO if that person:
6	(a) fails to withhold tax as required under
7	this section; or
8	(b) having withheld tax fails to pay the tax
9	to the CEO as required under this section.
10	(5) A person personally liable for an amount of
11	tax under subsection (4) of this section as a result of
12	failing to withhold the tax is entitled to recover the
13	tax from the recipient of the payment.
14	(6) A person who has withheld tax from a payment
15	under this section and paid the tax to the CEO is
16	indemnified against any claim by the recipient for
17	payment of the withheld amount."
18	Section 52. Title 54 of the Code of the Federated States of
19	Micronesia is hereby further amended by adding a new section 582
20	to subchapter VIII of chapter 5 to read as follows:
21	"Section 582. Withholding tax documentation.
22	(1) A person withholding tax under section 581 of
23	this title must give to the recipient of the payment a
24	tax withholding certificate as prescribed.
25	(2) A non-resident person required to file a net

1	profit tax return for a tax year must attach to the
2	return any tax withholding certificate received for the
3	applicable tax period.
4	(3) A person withholding tax under section 581 of
5	this title shall, within two months after the end of
6	the calendar year, file with the CEO an annual
7	withholding tax statement as prescribed."
8	Section 53. Title 54 of the Code of the Federated States of
9	Micronesia is hereby further amended by adding a new section 583
10	to subchapter VIII of chapter 5 to read as follows:
11	"Section 583. Priority of tax withheld.
12	(1) Tax withheld from a payment by a person under
13	section 581 of this title:
14	(a) is held by the person in trust for
15	the National Government; and
16	(b) is not subject to attachment in respect
17	of any debt or liability of the person.
18	(2) In the event of the liquidation or bankruptcy
19	of a person who has withheld tax under section 581 of
20	this title, any amount withheld does not form part of
21	the estate of the person in liquidation or bankruptcy
22	and the CEO has first claim for that amount before any
23	distribution of property is made.
24	(3) An amount that a person is required to
25	withhold from a payment under section 581 of this title

1	<u>is:</u>
2	(a) a first charge on the payment; and
3	(b) deducted prior to any other amount that
4	the person may be required to deduct from the payment
5	by virtue of an order of any Court or under any other
6	<pre>law."</pre>
7	Section 54. Title 54 of the Code of the Federated States of
8	Micronesia is hereby further amended by adding a new section 584
9	to subchapter VIII of chapter 5 to read as follows:
10	"Section 584. Credit for tax withheld.
11	(1) If tax has been withheld under section 581(2)
12	of this title:
13	(a) the gross revenue of the non-resident
14	person deriving the fee is the amount of the fee before
15	the withholding of the tax; and
16	(b) the non-resident person deriving the fee
17	is allowed a credit for that tax against the net profit
18	tax payable by the person for the tax year in which the
19	tax was withheld.
20	(2) If the amount of the credit allowed under
21	subsection (1)(b) of this section for a tax year
22	exceeds the net profit tax due for the year, the amount
23	of the excess must be refunded to the non-resident
24	person."
25	Section 55 Title 5/ of the Code of the Rederated States of

Micronesia is hereby further amended by adding a new subchapter 1 2. IX to chapter 5 to be entitled "Final Provisions". Section 56. Title 54 of the Code of the Federated States of 3 Micronesia is hereby further amended by adding a new section 591 4 5 to subchapter IX of chapter 5 to read as follows: "Section 591. Regulations. 6 7 (1) The Secretary shall, subject to approval of 8 the President, prescribe and have printed reasonable 9 regulations for the enforcement of this chapter and 10 such regulations shall have the force and effect of law 11 if they are not in conflict with the express provisions 12 of this chapter or other laws of the FSM. (2) The regulations shall also provide for 13 14 matters prescribed under the chapter to be made by 15 regulation. 16 (3) Such regulations shall be promulgated in 17 accordance with law." 18 Section 57. Title 54 of the Code of the Federated States of 19 Micronesia is hereby further amended by adding a new section 592 20 to subchapter IX of chapter 5 to read as follows: "Section 592. Transition. 2.1 22 Any tax liability that arose before this chapter came 23 into force may be recovered under chapter 9 of this title, but without prejudice to any action already 2.4 25 taken for the recovery of the tax."

62 of 63

1	Section 58. Title 54 of the Code of the Federated States of
2	Micronesia is hereby further amended by adding a new section 593
3	to subchapter IX of chapter 5 to read as follows:
4	"Section 593. Commencement of administration.
5	Administration of this act shall commence six (6)
6	months after the commencement of administration date of
7	the Unified Revenue Authority Act as determined by
8	section 769 of this title."
9	Section 59. This act shall become law upon approval by the
10	President of the Federated States of Micronesia or upon its
11	becoming law without such approval.
12	
13	Date: 5/27/11 Introduced by:
14	Florencio S. Harper (by request)
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63 of 63