



MERGERS AND ACQUISITIONS

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Taxation of Cross-Border
Mergers and Acquisitions

2010 Edition

TAX

Vietnam

Introduction

This chapter provides basic information to potential buyers and sellers of Vietnamese businesses through both asset and share purchase deals.

The laws and regulations in Vietnam are at an early stage of development and not well established; investors into Vietnam need to be aware that they cannot expect the same degree of legal certainty available in more developed jurisdictions. Furthermore, as the legal system in Vietnam is itself developing, it is difficult to say how any inconsistencies or gaps in laws and regulations will be dealt with.

The Vietnamese tax rules are characterized by uncertainties and a lack of interpretative guidance. Both the substantive provisions of Vietnamese tax laws and the interpretation and application of such provisions by the Vietnamese tax authorities may be subject to more rapid and unpredictable change than in a jurisdiction with a more developed capital market.

A number of key tax and other reform measures affecting the tax status of taxpayers have been implemented in whole or in part. For instance, the corporate and investment laws have been revised with effect from 1 July 2006 and continue to be supplemented and clarified as issues of interpretation and/or implementation arise. In addition, most major tax laws and regulations have been either revised or enacted effective from 1 January 2009 and are expected to be further amended or supplemented in 2010.

Recent Developments

Current Vietnamese Environment

It is more than two and a half years since Vietnam was admitted as an official member of the World Trade Organization (WTO) on 11 January 2007. As a member of WTO, Vietnam has to adhere to WTO commitments and adopt international rules. There is no doubt that further reforms will take place, especially in the legal framework, to make the country more integrated with the world economy. It is, therefore, to be expected that mergers and acquisitions (M&A) activity will grow rapidly in the coming years. M&A may be an attractive

option for many foreign investors, because Vietnam has begun to open various sectors to foreign ownership.

One of the most significant regulatory developments in 2008 arising from WTO membership obligations was the granting of licenses to wholly foreign-owned banks. The first recipients of such licenses were HSBC, Standard Chartered, and ANZ Bank.

Significant developments also occurred in the area of corporate governance legislation with the enactment in 2007 of new regulations and a model charter for public listed companies. However, although the legislation imposes an obligation on companies to report on their corporate governance status, there is little guidance in the law to help companies implement the necessary processes and procedures. In addition, the lack of publicly available information makes it difficult to assess the extent of compliance with such regulations.

Although many positive changes to the Vietnamese legal environment were committed to under the WTO membership, there remains little guidance on the execution of certain commitments, particularly with respect to the granting of distribution rights to foreign enterprises.

Overall, Vietnam continues to try to live up to the high expectations of international investors that it will be the next Asian tiger by continually pushing through reforms aimed at facilitating the development of the economy. The government's participation and encouragement of forums facilitating consultation between investors and regulators to discuss ways to improve the business climate indicates that this policy will continue.

In recent years, M&A activity in Vietnam had been growing rapidly until 2009 when the financial crisis seemed to put the acquisition plans of many foreign investors on hold. Looking ahead, it is anticipated that M&A activity in Vietnam will pick up again as foreign investors reactivate their previous plans.

Newly Issued Legislation with Effect from 1 January 2009

With effect from 1 January 2009, a number of new laws and regulations have been issued to replace the existing legislation and are likely to have a considerable impact

on Vietnam acquisition structuring. The new legislation includes:

- Law on Corporate Income Tax No. 14/2008/QH12 passed by the National Assembly in May 2008, which reduced the corporate income tax (CIT) rate to 25 percent.
- Law on Value Added Tax No. 13/2008/QH12 passed by the National Assembly in June 2008, which subjects most goods and services to value added tax (VAT) at a standard rate of 10 percent.
- Law on Personal Income Tax No. 04/2007/QH12 passed by the National Assembly in November 2007, which introduced personal income tax to Vietnam for the first time and subjected both expatriate and Vietnamese taxpayers to the same rate.
- Circular 134/2008/TT-BTC dated 31 December 2008 from the Ministry of Finance provided implementation guidance on the tax obligations of foreign organizations and individuals doing business in Vietnam or earning income in Vietnam. The circular broadened the scope of taxable entities and clarified the application of withholding tax (WHT) on important income items, such as income from securities transfers, reinsurance services, etc.
- Decision 121/2008/QD-BTC dated 24 December 2008 of the Ministry of Finance deals with the tax treatment of foreign investors trading on the Vietnam stock market in relation to the acquisition of unlisted shares of domestic companies by foreign investors.

Laws are passed by the National Assembly and implemented by decrees issued by the government and by circulars, decisions, or rulings of relevant ministerial authorities.

Asset Purchase or Share Purchase

Foreigners cannot directly hold assets in Vietnam. Foreign investors must establish a Vietnamese entity to hold the Vietnamese asset (if not already legally present in Vietnam). If a foreign investor already has a Vietnamese entity, it is likely that the business license of the Vietnamese entity would need to be amended to accommodate the expanded activities following the purchase of assets.

The establishment of a Vietnamese entity or amendment to the business license can be a lengthy process and may entail multiple approvals. In most

cases, therefore, the purchaser is likely to purchase the shares or interests in the target Vietnamese entity, rather than its assets.

Purchase of Assets

Purchase Price

The valuation of assets for transaction purposes is a matter of mutual agreement between seller and buyer. Transactions between related parties, however, are subject to local transfer pricing regulations to ensure fair market value.

A sale of assets is subject to VAT on an itemized basis for each asset. The seller of asset is subject to CIT at 25 percent of the proceeds, after deducting related expenses.

Goodwill

For tax purposes, goodwill can be amortized over a maximum period of three years.

Depreciation

To recognize the assets transferred from the seller to the buyer as fixed assets to which depreciation deductible for CIT purposes can be applied, the following issues must be taken into account.

The acquisition of assets must be substantiated by legitimate tax invoices and other supporting documents, such as a sale invoice and a sale contract.

An asset that satisfies all of the following criteria shall be considered as fixed asset:

- economic profit will be generated by the use of the assets;
- the asset's useful life is at least one year; and
- the asset's value is at least VND 10 million (approximately USD 550).

The original cost of the fixed assets purchased from the seller is the price actually paid plus directly relevant expenses paid when making such fixed assets ready for use (interest on loans taken out to acquire the assets, transport expenses, loading and unloading expenses, expenses for upgrading, installing, commissioning and registering, etc.).

For depreciation purposes, enterprises must register with the local tax department its chosen method of depreciation (such as straight-line method, adjusted reducing balance method, or product quantity and

volume method). The registered methods must be performed consistently during the course of using the fixed assets. In practice, however, the tax authorities accept that an enterprise simply sends a letter to the local tax office indicating its chosen depreciation method. The depreciation method can be changed during the course of operations, provided the company has valid reasons to do so and sends a written notice of such change to the local tax office. Note that only changes in the depreciation method require notification to the tax office. No notification is required of subsequent changes in depreciation rates.

Depreciation of new and used fixed assets is based on the same principles of historical cost and useful life within a prescribed time frame.

Note that an enterprise shall itself determine the useful life of intangible fixed assets, which shall not exceed 20 years. The useful life of land use rights is the term of the lease.

Value-Added Tax (VAT)

The sale of assets is subject to VAT in Vietnam.

Under current VAT law, there are three applicable VAT rates imposed on goods and services: 0 percent, 5 percent, and 10 percent, which is the standard rate.

The seller issues VAT invoices for the sale of assets. The VAT is then added to the sale price and indicated on the invoice issued. This becomes the seller's output VAT, which must be declared and paid on a monthly basis.

For the buyer, the VAT charged by the seller will become creditable input VAT that can be offset against its output VAT on a monthly basis. The buyer has six months to claim creditable input VAT. Input VAT on fixed assets used in the production or trading of both VATable and non-VATable goods and services is creditable in full.

When the buyer of asset is a new business establishment and has not commenced operations, if the capital construction period lasts more than one year, the buyer of asset will be entitled to a refund of VAT on goods or services used for investment on an annual basis. When the accumulated amount of input VAT on goods or services purchased for investment is more than VND 200 million (approximately USD 11,500), the buyer will be entitled to a VAT refund.

Notwithstanding the above, a business establishment shall not be required to declare and pay VAT in the following cases:

- in-kind capital contribution of assets to establish an enterprise;
- transfers of assets between dependent cost accounting entities within an enterprise; and
- transfers of assets on a demerger, division, consolidation, or conversion to another form of enterprise.

Transfer Taxes

Transfers of houses, land, means of transportation, shotguns, and sport guns are subject to stamp duty payable on the transfers by the new registered owners.

The stamp duty rates are 0.5 percent for land and buildings, 2 percent for motorcycles and larger automobiles, and 10 percent to 15 percent for cars with less than 10 seats.

The amount of stamp duty payable on any one transaction on any one asset shall not exceed VND 500 million (approximately USD 28,500), except for cars of less than 10 seats where there is no such cap.

Stamp duty must be declared and paid no later than 30 days after the transaction date.

Purchase of Shares

The Prime Minister's Decision No.55/2009/QĐ-TTg of 15, April 2009 (Decision No.55), which allowed foreign investors to hold a maximum of 49 percent of the shares of a public joint stock company from 1 June 2009 has opened up Vietnam's investment environment significantly. This decision and the gradual removal of restrictions on the capital holding ratio of foreigners in specific sectors in line with the WTO commitment has also created more investment opportunities for foreign purchasers. Some services sectors, such as banking, remain capped at a current 30 percent of foreign ownership.

Tax Indemnities and Warranties

In accordance with prevailing Vietnamese regulation, the tax exposure of the target company will be transferred to the purchaser after the deal. It is, therefore, advisable for the purchaser to pay careful consideration to the target company's tax compliance status, to reduce the risk of contingent tax payables post-deal. For this reason, tax due diligence exercises

often play an important role in identifying and locating significant tax issues in M&A transactions.

As the target company's legal rights and related liabilities will also be transferred to the purchaser, the buyer would be well-advised to seek tax indemnities and warranties for contingent tax liabilities in the M&A contract.

Tax Losses

Tax losses of the target company remain after the transaction. Accordingly, losses incurred by the target company prior to the transaction could be offset against the taxable income of the company after the transaction. In principle tax losses can be carried forward for a period not exceeding five years from the loss year.

In principle, losses to be carried forward for deduction from taxable income are self-assessed by the target company under the Vietnam self declaration tax regime. However, in the case of a tax audit by the tax authority, only the losses determined by the local tax authority can be used.

Pre-Sale Dividend

In certain circumstances, the seller may prefer to realize part of the value of his/her investment as income by means of a pre-sale dividend. The rationale here is that the dividend may be subject to no (in the case of a company) or only a low tax rate (in case of an individual who is taxed at 5 percent).

Transfer Taxes

Currently there is no stamp duty on the transfer of shares in Vietnam.

Tax Clearances

The target company is required to conduct tax finalization with the local tax authorities up to the time of the decision on the merger.

Choice of Acquisition Vehicle

There are several potential acquisition vehicles available to a foreign purchaser in Vietnam.

Local Holding Company

Because that laws and regulations in Vietnam are at an early stage of development, the use of this vehicle by foreign investors is rare, because it may require license from the Vietnam authorities that will be hard and time-consuming to obtain. Moreover, since there is no tax

group consolidation in Vietnam, there is no tax group benefit for such a vehicle.

Foreign Parent Company

This structure is normally chosen by foreign purchasers. It has a number of tax benefits. Dividends paid to a foreign parent company are not subject to Vietnam CIT or WHT as long as they are paid from the subsidiary's after-tax profits. However, interest payments to a foreign parent company are subject to WHT at 10 percent and, in addition, the foreign parent is subject to CIT at 25 percent on gains when selling its capital contribution in the subsidiary, or WHT of 0.1 percent on the total sale proceeds, when selling shares of the subsidiary (provided that such shares are deemed securities under Vietnam law).

The foreign investor may seek tax exemption for transfers of capital or securities in Vietnam under the double taxation agreement (DTA) between Vietnam and the country in which it is resident.

Currently, Vietnam has no anti-treaty shopping legislation.

Local Branch

A Vietnam branch is subject to Vietnam corporate income tax at 25 percent. A branch is not a popular form of business presence at present because of the ambiguity of its tax status and disadvantages in many tax and regulatory respects. As a result, use of this form of business has typically been confined to law firms and foreign banks with their distinctive professional regulatory requirements.

Joint Ventures

The tax treatments of joint ventures are similar to that for foreign parent companies (see above).

Choice of Acquisition Funding

When considering an acquisition, a purchaser needs to decide how to fund the deal; by means of debt or equity, or even a hybrid method which includes elements of both.

Debt

Vietnamese legal entities and individuals, and foreign legal entities and individuals can choose to fund their acquisitions by debts arranged locally or from offshore.

For legal entities established under the Vietnamese Law using debt, one of the most considerable advantages is that interest expenses would be allowed as deductible expenses for CIT calculation purpose (please refer to Deductibility of Interest). Other expenses relating to the

costs of debt, such as guarantee fee and bank commissions are also considered deductible expenses.

There is a wide range of debt funding sources available to purchasers – banks, third parties, or even related parties. Given that debt is to be used to fund the acquisition, a further decision has to be made about how it should be structured.

Under domestic tax regulations, debt financing arranged locally would not attract WHT, but WHT of 10 percent of the interest would apply to cross-border financing.

Of approximately 50 DTAs currently in force, only the treaty with France provides straightforward tax exemption on interest for commercial loans. The other treaties generally specify a maximum interest WHT rate equal to or higher than the 10-percent Vietnamese domestic rate.

Deductibility of Interest

Interest expenditure is deductible against taxable income in the Vietnamese company. There are no thin-capitalization rules as such; however, the debt-to-equity ratio is specified in the business registration certificate by virtue of specifying the charter capital (equity) and investment capital (total project size – total of equity and debt). In the past, this was restricted to 30:70. There is now no such restriction.

The tax deductibility of interest rate is limited to 150 percent of the basic interest rate announced by the State Bank at the date of the loan. Foreign loans must be registered with the State Bank of Vietnam before the interest and related expenses are allowed as deductible for the borrower's CIT purposes.

Interest payments on loans for contribution to legal capital or to registered legal capital that is not yet fully paid up, as per the schedule for capital contribution set out in the enterprise charter, including cases when the enterprise has commenced production and business, are not deductible expenses for CIT calculation purposes.

Withholding Tax on Debt and Methods to Reduce or Eliminate

Interest payments to non-resident parties are subject to WHT at 10 percent unless reduced under a DTA between Vietnam and approximately 50 countries.

Please note that DTA relief is not automatically granted to beneficiaries unless the conditions for tax exemption or reduction are met. The prior approval of the Vietnamese tax authorities must be obtained before the

exemption becomes effective. Professional advice should be sought on how to comply with requirements for DTA claims under both domestic laws and DTA provisions.

Checklist for Debt Funding

All foreign debts must be registered with the State Bank of Vietnam.

The interest payment on debt from foreign lenders shall be subject to WHT at 10 percent.

Equity

Under Vietnamese regulations, only joint-stock companies can issue shares either to current shareholders or outsiders and only under certain conditions.

There is no capital duty, no stamp duty, and no stamp duty reserve tax on new share issues and no WHT is levied on dividends paid from after-tax profits by a Vietnamese company to corporate investors. However, after-tax dividends paid to individual investors shall be further subject to 5-percent personal income tax on capital investment on the part of such individual investors, to be withheld and paid by the dividend paying entity on behalf of the individual investors.

Moreover, a purchaser may prefer equity for non-tax purposes. For instance, in some circumstances it may be necessary to maintain a relatively low debt-equity ratio for financial reasons. In such cases, a buyer may prefer to use a hybrid.

When carrying out a reorganization or merger, any difference between the book value and reassessed value of assets shall be treated as other income and taxed at the standard corporate income tax rate of 25 percent, regardless of any tax incentives that the reorganized or merged company may have. Reorganization or mergers of companies at book value of assets should be tax neutral transactions.

As stated earlier in this chapter, transfers of assets on a demerger, division, consolidation, or conversion to another form of enterprise shall not be subject to VAT.

The post-reorganized or post-merger entity shall be responsible for tax debts of the enterprise prior to such reorganization or merger, and shall inherit tax incentives of the former enterprise for the remaining period if the new enterprise continues to satisfy the relevant conditions.

Hybrids

A purchaser may use a hybrid instrument, incorporating attributes of both debt and equity, to fund its acquisition, to take advantage of interest deduction for CIT calculation purposes.

A tax-efficient structure normally requires an appropriate mix of debt and equity, but the position is constantly changing and professional advice should be obtained.

Discounted Securities

When securities are sold at a discount, the actual discounted purchased price is the basis for assessing the tax obligations of the seller. The discounted price also serves as the cost base for the buyer for tax purposes in the event of a subsequent sale. The taxation in this case is similar to that of non-discounted securities.

Deferred Settlement

An acquisition often involves an element of deferred consideration, the amount of which can only be determined at a later date on the basis of the business's post-acquisition performance. However, the seller only exposes to Vietnamese taxation once realizing income/gain from selling the unknown future amount.

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Other Considerations

Given the changeability of the M&A tax environment in Vietnam, investors would be well-advised to seek advice before proceeding with acquisitions, in such areas as foreign exchange control, repatriation of funds, limitations on foreign ownership, etc.

Concerns of the Seller

Corporate Seller of Shares/Interest

Under the Law on corporate income tax, Vietnamese corporate sellers would ordinarily be subject to 25 percent tax on the gain. Foreign organizations are subject to 25-percent tax on the gain when selling capital contributions in the subsidiary, or WHT of 0.1 percent on the total sale proceeds when selling shares of the subsidiary provided that are considered securities under Vietnam law.

Individual Seller of Shares/Interest

Pursuant to the Law on Personal Income Tax, an individual seller should be subject to tax on capital investment, capital assignment, and real estate transfers as follows

Taxable Income	Tax Rate	
	Resident ¹	Non-resident ²
Capital investment income (including dividends and interest) ³	5%	5%
Capital assignment income (direct interest, that is, holding an interest in a limited liability company)	20% on gains	0.1% on gross sale proceeds
Capital assignment income (securities where taxable gain can be determined)	20% on gains	0.1% on gross sale proceeds
Capital assignment income (securities where taxable gain cannot be determined)	0.1% on gross sale proceeds	0.1% on gross sale proceeds
Real estate transfer income (where taxable gain can be determined) ⁴	25% on gains	2% on gross sale proceeds
Real estate transfer income (where taxable income cannot be determined)	2% on gross sale proceeds	2% on gross sale proceeds

Notes

1. Appears to include also all offshore sourced income/gains/transactions
2. Only on Vietnam sourced income/gains/transactions
3. Note interest on deposit with credit institutions is classified as a tax exempt income item
4. Exemption applies on certain transaction such as sole dwelling property, family members' transaction, among others.

The above may have a substantial impact on M&A activity, including acquisitions of shares traded on stock exchanges, over the counter trades, and real estate transactions

Company Law and Accounting

Company Law

Vietnamese legal entities incorporated and operating in Vietnam are mainly governed by two laws; Law on Investment 59-2005-QH11 (LOI) and the Law on Enterprise 60-2005-QH11 (LOE).

Vietnamese legal entities take one of the following forms: multi-member limited liability company, one-member limited liability company, shareholding company, partnership, proprietary business, or corporate group. Enterprises may be divided, separated, consolidated, merged, converted, or dissolved. Each entity is generally subject to CIT at 25 percent of the profits of the business (subject to a range of incentives).

In general, foreign businesses set up in Vietnam are not required to contribute after-tax profits to any compulsory reserves apart from banks and insurance businesses. After tax profits can, therefore, be fully remittance overseas.

A foreign investor is entitled to contribute capital to and/or purchase shares of a company in Vietnam, but the proportion of capital contributions/share purchase in certain sectors and industries is prescribed by the government. The prevailing regulation affirms a general principle that business entities and individuals, irrespective of nationality, are entitled to make capital contributions and purchase shares without any limitation of ownership in all enterprises in Vietnam, except for:

- public companies, including listed companies (the 49-percent cap remains);
- businesses operating in certain specialized industries;
- capitalized state-owned enterprises (SOEs); and
- many service companies as set out in Vietnam's commitments to the WTO.

Accounting Standards

The Vietnamese accounting standard No. 11 mainly determines the accounting treatment of a business combination. This standard should be applied to business combinations using the purchase method.

A business combination may be structured in a variety of ways. It may involve the purchase by an entity of the equity of another entity, the purchase of all the net assets of another entity, the assumption of the liabilities of another entity, or the purchase of some of the net

assets of another entity that together form one or more businesses. It may be effected by the issue of equity instruments, the transfer of cash or cash equivalents, other assets, or a combination of all of the above.

An acquirer must be identified for every business combination. The acquirer is the combining entity that obtains control of the other combining entities or businesses.

A business combination may result in a parent-subsidiary relationship in which the acquirer is the parent and the acquiree is a subsidiary of the acquirer. In such circumstances, the acquirer applies this standard in its consolidated financial statements. The parent includes its interest in the acquiree in any separate financial statements it issues as an investment in a subsidiary.

Group Relief/Consolidation

There is no tax group relief/consolidation in Vietnam at present.

Transfer Pricing

After M&A activities are completed, the purchaser and the target shall be considered related parties if the purchaser holds more than 20 percent of the share capital of the target. Transactions between related entities must be on an arm's-length basis (that is, based on market prices). Transfer pricing documentation must also be maintained properly, otherwise the local tax authorities may challenge the position of the two parties involved.

Foreign Investments of a Local Target Company

The Vietnam target company (VTC) will be allowed to remit invested capital abroad to carry out investment activities if it satisfies the following conditions:

- it has been issued with an outbound investment certificate by the Vietnamese Ministry of Planning and Investment;
- the investment project has been approved by the competent state body of the investment recipient country in accordance with the law of that country; and
- it has fulfilled all financial obligations towards the State of Vietnam.

The VTC is required to repatriate to Vietnam all profit and/or income earned from investment projects within six months of the date of completion of the tax

finalization report in accordance with the law of the investment recipient country.

If income from an investment overseas has been subject to CIT (or a tax similar to CIT) overseas, the VTC can deduct the tax paid overseas or paid on its behalf by the foreign party, when computing CIT payable in Vietnam, but the tax deducted must not exceed the tax amount otherwise payable in Vietnam. If the VTC, pursuant to the foreign law, is entitled to a tax reduction or exemption on part of the profit earned from the offshore investment project, the amount of such exemption or reduction shall also be deductible from the CIT payable in Vietnam.

Loss arising from an offshore investment cannot be deducted from the amount of income arising in Vietnam when the VTC calculates its Vietnam CIT liabilities.

All transactions on the transfer of foreign currencies from Vietnam abroad or vice versa, which are related to investment projects, should be conducted via a foreign currency account opened at a credit institution licensed to conduct foreign exchange activities in Vietnam and be registered with the State Bank of Vietnam.

In addition, remittance of invested capital overseas must adhere to laws and regulations on foreign investment, foreign exchange control, and other international agreements in which Vietnam has taken part.

Comparison of Asset and Share Purchases

A share purchase leads to ownership partly or wholly of the target company, not just its assets. The key difference is that the purchase of assets is subject to VAT, whilst the purchase of shares is not. In addition, to be able to purchase Vietnamese assets, the buyer must establish a Vietnamese entity to hold the assets. A sale of assets is taxed at 25 percent of gain on the part of

the seller, while share transfers can be taxed at either 25 percent of the gain or at 0.1 percent of the gross sale proceeds, depending on the type of shares being transferred.

Advantages of Asset Purchases

- The purchase price can be depreciated or amortized for tax purposes (including goodwill).
- No previous liabilities of the company are inherited.

Disadvantages of Asset Purchases

- A foreign investor must establish an entity in Vietnam for purchasing assets. Purchasing assets does not lead to the ownership of the entity that owned the assets.
- The possible need arises to renegotiate supply, employment, and technology agreements, etc.
- Accounting profits may be affected by the creation of acquisition goodwill.
- The benefit of any losses incurred by the target company remains with the seller (but may be lost altogether).

Advantages of Share Purchases

- The purchaser may gain benefit not only from tax losses but also that from any CIT incentives of the target company.
- Share purchases are not subject to VAT.

Disadvantages of Share Purchases

The purchaser will have to assume all remaining liabilities including tax and debts of the target company in correspondence with their portion of ownership in the target company. In addition, if the seller no longer has a business presence in Vietnam after the completion of the deal, the buyer will be liable for withholding and paying capital gains tax to the government of Vietnam on behalf of the seller.

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