LEGAL ALERT

Cambodia issues Guidelines on Implementation of Double Taxation Agreement with Singapore and Thailand

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Although the DTAs were signed some time ago, the relevant implementing regulations were only issued earlier this year. On 2 February, the Ministry of Economy and Finance ("MEF") issued Ministerial Directive (or "Prakas") No. 116 on the Implementation of International Treaties regarding the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Tax on Income. Pursuant to this Prakas, the Singapore and the Thai Treaty entered into force on 1 January 2018. (We note that three further DTAs signed with China, Brunei and Vietnam are yet to come into force as at the date hereof).[1] These first two DTAs are important milestones for attracting more foreign investments into Cambodia.

Although bilateral investment agreements between Cambodia and Singapore, and Cambodia and Thailand were signed decades ago,[2] and all three counties enjoyed the advantages of being ASEAN members, the lack of DTAs were a significant negative issue to investors looking to invest in Cambodia. In the absence of a DTA between the two countries, there remained a high risk that the investor would have to pay tax on the same income not only in the country of his residence, but also in the host country where the investment takes place. Although the lack of DTAs between the investor's residence and the host country is rarely a deal breaker, it is still highly considered and strongly taken into account when assessing the financial concerns of investing and ultimately, in making the final decision on whether to pursue investing into a foreign country.

DTAs clarify the tax levying rights of both countries on different forms of income arising from cross-border business activities and minimises the double taxation of such income. Consequently, this is expected to further assist in facilitating cross-border investment and boost trade and economic flows between countries. Apart from reducing the possibility of double taxation of the same income, the provisions also aims to eliminate tax evasion. In addition, the DTAs provide for the cooperation of the signatories' tax authorities, setting up a communication protocol for the authorities on unresolved tax issues based on the provisions of the DTAs.

Both DTAs in question follows the structure and recommendations of the Model Double Taxation Convention of the United Nations (rather than the OECD Model Convention). The United Nations Model Convention represents an understanding between the source principle and the residence principle. Notably, it gives more weight to the source principle. As a result of this, the DTAs promote foreign investment into a developing country more than the OECD Model Convention.

Providing Clarity for Taxpayers

The DTAs provide a clear definition of "residence", placing emphasis on the center of vital interests. It also specifies when a business is considered as a "permanent establishment" in a country.

Taxes covered under the scope of the DTAs are as follows:

- Cambodia –Tax on Profit including Withholding Tax, Additional Profit Tax on Dividend Distribution, Capital Gains Tax and Tax on Salary;
- Singapore – Income Tax; and
- Thailand – Income Tax and the Petroleum Income Tax.

Regarding income from *immovable properties,* both DTAs provides that income derived by a resident of a contracting state from immovable property (including income from agriculture or forestry) situated in the other contracting state may be taxed in that other state.

As principal rule in both cases, business profits of an enterprise are taxable only in that state unless the enterprise carries on business in the other contracting state through a permanent establishment situated therein.

Provisions on the taxation of income or profit derived from the operation of international traffic are similar in both cases, although the Thai DTA expanded the scope of the traffic involved from aircrafts and ships to rail and road vehicles.

For dividends, both DTAs provide for the same. Dividends paid by a company which is a resident of a contracting state to a resident of the other contracting state may be taxed in that other state. However, such dividends may also be taxed in the contracting state of which the company paying the dividends is a resident, but if the beneficial owner of the dividends is a resident of the other contracting state, then the tax charged shall not exceed ten percent of the gross amount of the dividends. This will not affect the taxation of the company in respect of the profits out of which the dividends are paid.

The same applies in the case of royalties, including but not limited to payments of any kind received as consideration for the use of a copyright, trade mark or patent. Such royalties arising in a contracting state and paid to a resident of the other contracting state may be taxed in that other state. However, as with dividends, such royalties may also be taxed in the contracting state in which they arise, but if the beneficial owner of the royalties is a resident of the other contracting state, then the tax charged shall not exceed ten percent of the gross amount of the royalties.

Correspondingly, any kind of consideration, including without limitation for the rendering of any managerial, technical or consultancy services, jointly referred to as fees for technical services is treated in the same way as dividends and royalties.

However, there is a slight difference between Singapore and Thailand in the case of Interest. If accruing in one contracting state and paid to a resident of the other contracting state, such interest payments may be taxed in that other state. Then again, such interest may also be taxed in the contracting state in which it accrues, but if the beneficial owner of the interest is a resident of the other contracting state, then the tax charged shall not exceed ten percent of the gross amount of the interest in the case of the Singapore Treaty (with the exception of financial institutions and insurance companies), and 15 percent in the case of the Thai Treaty.

According to both DTAs, capital gains derived by a resident of one contracting state are taxable in principal only in the state of residence. However, there are important exceptions that differ under the Singapore and Thai Treaties.

Apart from some exceptions, with regard to tax rates as between the pre-DTA and post-DTA situations, the main difference is the reduction in withholding tax from 14 percent to ten percent on Dividends, Interest, Royalties and Technical Service Fees paid to Thai and Singapore residents.

Cooperation and Exchange of Information

Both DTAs improve the cooperation between the tax authorities of the respective countries. In both cases, the lawmakers have set up a procedure in order to reach mutual agreement in cases where a resident of one contracting state considers that the action of one or both states results in taxation not in accordance with the DTAs. The mutual agreement procedure is designed not only to furnish means of settling questions relating to the interpretation and application of the DTA, but also to provide a forum in which residents of the states involved can seek redress for actions not in accordance with the DTA and a mechanism for eliminating double taxation in cases not provided for in the DTA.

Both DTAs enforce the possibility of the exchange of tax related information between the tax authorities of the contracting states. Although the UN Model Convention on the Avoidance of

Double Taxation proposes such, neither of the DTAs in question includes methods for providing assistance to the other contracting state in tax collection.

In Practice

Recently, the General Department of Taxation of the Ministry of Commerce ("GDT") issued an Instruction on the Implementation of International Treaties regarding the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Tax on Income dated 26 March 2018. The GDT Instruction provides for more detail on the persons under the scope of the DTA, the types of tax regimes applicable and procedures for implementing the DTA, rules regarding determination of resident taxpayers, and guidelines on procedures for determining which country the tax payer shall pay taxes to in case of persons having residency in both countries.

For the exemption from double taxation, an application shall be submitted to the Department of Law, Taxation Policies and International Cooperation of the General Department of Taxation of Cambodia.

If you have any questions or require any additional information, please contact Matthew Rendall, Eszter Papp or the ZICO Law partner you usually deal with.

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