

# Technical Update

## Tax and Corporate Services

January 2016

### Prakas on the extension of Prepayment of Profit Tax (PPT) suspension validation for Garment and Footwear production enterprises

(Prakas no. 1818.MEF.Prk dated 25 December 2015)

The Ministry of Economy and Finance (MoEF) recently issued a **Prakas no. 1818 MEF.Prk** dated 25 December 2015 to extend the suspension of the 1% PPT for garment and footwear production enterprises until the end of 2017. This is further to the Prakas 988, dated 23 November 2011, that extended the validation until the end of 2015.

To extend the suspension, the enterprises shall comply with the conditions as follows:

1. Enterprises shall properly keep accounting records, declare Tax on Profit (ToP) and comply with other tax obligations;
2. Enterprises shall submit an independent audit report to the tax administration annually.

The Tax Office has the right to invalidate this temporary suspension and impose other penalties if enterprises fail to comply with the above conditions.

Additionally, the Tax Office has also issued a letter to Garment Manufacturers Association in Cambodia (GMAC) to further clarify the above two conditions as below:

- The bookkeeping shall follow the Law on Enterprise Accounting, Enterprise Accounting Audit and Profession and shall pay other taxes as stipulated in applicable tax regulations.
- The independent audit report shall be prepared by accounting and auditing firms licensed by the National Accounting Council of the MoEF and submitted to the GDT starting from 2015 fiscal year onwards and must be provided no later than 3 months of the following tax year.

On the other hand, *supporting industries*, undertaking the supply of goods or services to the export industries including garment, textile, footwear, bag and wallet, and hat producing industries, and subject to 0% VAT in accordance with Prakas 311 dated 19 March 2014 are still obligated to pay other taxes as already in force. (Notably the 1% PPT is not specifically mentioned. But it would seem that supporting industries would be subject to the 1% PPT).

#### Our comment

We note that the objective of this Prakas could be to assist the garment and footwear production enterprises by extending the suspension period of payment of the monthly 1% PPT until end of 2017, albeit this was also extended previously.

In view of the above Prakas, we would think that the above suspension of the monthly 1% PPT would help garment and footwear production enterprises in term of their cash flow management as they are not required to pay PPT on a monthly basis and then set off with their annual ToP payable if any. Furthermore, if they still maintain their Qualified Investment Project status after their tax holiday expiration, the minimum tax which is required to be paid at 1% of annual turnover would still be exempted.

Thus, they will have no tax to be paid, if they make any taxable loss at year end. However, it should also be noted that this new Prakas also stipulates *two new conditions* as indicated above for such garment and footwear production enterprises to comply with in order to be eligible for the suspension of the 1% PPT.

# Prakas on Tax Mechanisms on Financial Lease Transactions

(Prakas no. 1704.MEF.Prk dated 9 December 2015)

The MoEF recently issued a Prakas no. 1704 MEF.Prk dated 9 December 2015, on the Tax Mechanism on Financial Lease Transactions. The Prakas details tax mechanism to be implemented for both lessor and lessee being entered into a financial lease agreement.

The terms used in this Prakas include:

- **Financial Lease:** Lessor and Lessee agree to give the lessee the right to possession and use of a movable property, for a specified period and paying a periodic leasing fee or an equivalent value to the lessor. The property is either purchased or returned at the end of the period.
- **Lessor:** The person licensed by or holding the financial lease license from the National Bank of Cambodia and a Real Regime taxpayer and must be considered a Financial Institution.
- **Lessee:** The person who is a taxpayer under Real Regime or Estimated Regime or Physical person granted the right to possession and use of the movable property
- **Supplier:** the person who supplies the movable property
- **Movable property:** properties, machineries and equipment, **except for** land and building
- **Movable property value:** net price after discount from the supplier, excluding finance costs and other expense charged by Lessor.

The requirement for a financial lease transaction shall be:

- Lessee can clearly specify the movable property and select the supplier regardless of the Lessor's skill and judgment;
- Lessor acquires the movable property;
- Term of the lease must be at least one year; and
- Lessee must pay to Lessor at least 75% of the movable property value including deposit and down payment

We summarize main clarifications on tax mechanism as follows:

Financial Lease Transactions		
Items	Lessor	Lessee (who is under real regime taxpayer)
<b>Value Added Tax (VAT)</b>	<ul style="list-style-type: none"> <li>• Charge 10% VAT for all revenue related (i.e. underlying periodic payment, lawyer's fees, leasing service fees, document fees; and transportation fees... etc ), except for interest income.</li> <li>• Issue Tax invoice for a Real Regime taxpayer and Commercial invoice for a non-Real Regime taxpayer.</li> </ul>	<ul style="list-style-type: none"> <li>• Claim VAT input as per Tax invoices issued by the Lessor;</li> <li>• Record in monthly purchase record the principle amount, other charges and interest per Tax/Commercial invoice.</li> </ul>
<b>Prepayment of Profit Tax (PPT)/Minimum Tax (MT)</b>	<ul style="list-style-type: none"> <li>• Apply 1% PPT and MT on all charges and interest (exclusive of VAT) received under the finance lease excluding principal amount.</li> </ul>	N/A
<b>Tax on Profit (ToP)</b>	<ul style="list-style-type: none"> <li>• Recognize at either the date at which payment is due, or the date at which payment is made, whichever is the earlier.</li> </ul>	N/A
<b>Withholding Tax (WHT)</b>	N/A	<ul style="list-style-type: none"> <li>• Exempted from WHT as per Article 25 (New) of the Law on Taxation. (i.e. principal amount and interest payment)</li> </ul>
<b>Capitalization and Depreciation</b>	N/A	<ul style="list-style-type: none"> <li>• Record as fixed asset based on the amount stated in the financial lease agreement, exclusive of VAT;</li> <li>• Deprecate the principal amount in accordance with Article 13 (New) of the Law on Amendment of Law on Taxation.</li> </ul>

The Tax Office has also set out various tax mechanism for both lessor and lessee, in case the financial lease is terminated before the expiration date and movable property is confiscated as detailed in the Prakas above.

## Our comment

As noted, the Tax Mechanism on Financial Lease Transactions has been promulgated after a long period of discussion and consultation between the bodies mainly represented by the Tax Office and the Private Sector Working Group. This Prakas clarifies a number of tax issues as indicated above that were previously unclear with respect to financial lease transactions in Cambodia for both the Lessor and Lessee.

A key consideration arises on the Financial Lease Transactions that have been entered into before introduction of this tax law and a further clarification with the Tax Office may be required.

As a committed tax advisor to our clients, we welcome any opportunity to discuss the relevance of the above matters to your business.

## Contact Us

### KPMG Cambodia Ltd

PO Box 2352  
4<sup>th</sup> Floor, Delano Center  
No.144, Street 169  
Sangkat Veal Vong  
Khan 7 Makara, Phnom Penh  
Kingdom of Cambodia

### Michael Gordon

Senior Partner  
T: +855 23 216 899 (ext 7222)  
E: [mgordon@kpmg.com.kh](mailto:mgordon@kpmg.com.kh)

### Tan Mona

Director  
T: +855 23 216 899 (ext 7221)  
E: [tmona@kpmg.com.kh](mailto:tmona@kpmg.com.kh)

### So Dary

Director  
T: +855 23 216 899 (ext 7277)  
E: [daryso@kpmg.com.kh](mailto:daryso@kpmg.com.kh)

### Song Kunthol

Senior Manager  
T: +855 23 216 899 (ext 7202)  
E: [skunthol@kpmg.com.kh](mailto:skunthol@kpmg.com.kh)

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