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Double Taxation Agreement

1. Introduction

In today's global economy, a person can have several and worldwide sources of income. Difficulties may arise when two or more different states, based on their respective domestic laws, claim a tax over the exact same income. Such situation is known as a double taxation, whereby two or more countries impose taxes on the same income, assets or other financial transaction.

Double taxation occurs because of overlapping tax laws; that is, when two or more countries assume jurisdiction over the same assets, income, or transaction. For example, if one state claims a tax on the basis of a "source of income" and another state claims a tax on the same funds on the basis of "residence". The two states can also both claim taxes on the basis of "residence" by having different legal criteria to qualify a fiscal residence (e.g. length of stay vs. center of vital interests).

To encourage investment and help taxpayers avoid this unfair practice, states are strongly advised to become a party to Double Taxation Agreement ("DTA"), which allows states to agree on rates and tax jurisdictions for specific types of income.

2. Double Taxation Agreement: Objectives and Content

Double Taxation Agreements pursue a "win-win strategy" of encouraging foreign investment and making the foreign market available for locals. States agree on an acceptable basis to share tax revenues and investors benefit from increased legal and fiscal certainty.

Many of the existing DTAs follow models provided by the UN and the OECD. States first determine the scope of the Convention and the tax covered. The next step involves determining an appropriate method for eliminating double taxation.

3. Method of Elimination of Double Taxation

To eliminate double taxation, states can choose between tax exemptions or tax credit. This choice is crucial as it will impact public revenue in different ways.

A. Tax Exemption Method

The exemption method focuses on income. The income earned in the state of source is either fully or progressively exempted in the state of residence. That is to say that, once the taxpayer paid his tax on for an income in the country of source, that income is exempted from tax in the country of residence.

Under full exemption, the income earned in the country source is deduced from the tax basis of the state of residence. Both countries only tax the income earned in their country, according to their respective rate.

With exemption with progression, the amount of income earned in the state of source is taken into consideration in order to determine the tax rate to be applied only to the income earned in the state of residence.

Illustration: a person earned 100,000 USD dollars in total, 80,000 in state of residence (State R) and 20,000 in state of source (State S). If state R tax rates are 30% for income superior to 80,000 and 35% for income superior to 100, 000 USD and if State S tax rate is 20%, we obtain the below result:

	Without double taxation treaty	Full exemption	Exemption with progression
Tax in State R	35,000 USD (35% of 100.000)	24,000 USD (30% of 80,000)	28,000 USD (35% of 80,000)
Tax in State S	4,000 USD (20% de 20,000)	4,000 USD (20% of 20,000)	4,000 USD (20% of 20,000)
Total Tax	39,000 USD	28,000 USD	32,000 USD
Tax relief given by State R	0	11,000 USD	7,000 USD

B. Tax Credit Method

Unlike tax exemption method, the tax credit method focuses on the tax. With full credit, the total tax paid in the state of source is allowed as a credit against any tax payable in the state of residence.

The state of residence can also decide to adopt some restrictions by allowing an ordinary or simple credit. In such situation, the credit allowed can be higher than the amount of tax that would have been paid for the same income, in the country of residence.

ABOUT US

BNG Legal is a leading regional law firm providing comprehensive legal services to foreign and local clients in Cambodia and Myanmar.

Registered with the Bar Association of the Kingdom of Cambodia, our legal professionals combine international standards with local expertise.

We differentiate ourselves by coupling a deep understanding of the local business environment with international professionalism and integrity.

We facilitate business, investment and trade between Cambodia, Myanmar, and the rest of the world through innovative and cost-effective legal services.

Superior knowledge of local protocol, local procedure, and local people is necessary for any business to succeed.

Conducting daily business in Cambodia and Myanmar, BNG Legal is up to date with the newest procedures and requirements, helping clients efficiently and successfully complete any project.

CAMBODIAN LAW BLOG

cambodianlaw.wordpress.com

BNG Legal believes expanding access to legal information is crucial to rule of law. To that end, several of our legal professionals write a blog discussing recent developments in the legal landscape.

LEGAL DATABASE

The laws and regulations in our database are based upon the Official Gazettes, law compendiums and other collections from the ministries and institutions of the Royal Government of Cambodia. These are available to the public through our partner site, www.bnglaw.net.

4. Practice in Cambodia

For taxation purposes, a person living in Cambodia for more than 182 days is considered as a resident. Under Cambodian taxation law, a resident is taxed on any income from any source (both earned in Cambodia and abroad) and a non-resident is taxed on the income earned in Cambodia.

At this time, Cambodia has not entered into any Double Taxation Agreement with other countries. However, Cambodia law provides for a unilateral tax credit system. According to Article 36 and 50 of the Law on Taxation (LoT), a taxpayer who has received income or salary from foreign sources and who has paid taxes according to foreign tax law, shall receive a tax credit for deduction from the tax on profit or salary to be paid in Cambodia. Cambodia chooses to allocate a simple tax credit. The amount of the credit should be the smaller between the tax amount actually paid in a foreign country and the amount obtained by multiplying the total tax on profit /salary from all sources, calculated according to Cambodian tax rate with the ratio of income received in that foreign country to the total income/salary from all sources.

To be granted the tax credit, the taxpayer needs to comply with the formalities set out in Article 50 of the LoT. He needs to supply various documents, including certification of payment from the foreign tax administration.

In the progress to conclude the DTA with the other countries, the Ministry of Economy and Finance has issued a Decision No. 93 dated 18 April 2014 on Establishment of Inter-ministerial Committee for Negotiating on Double Tax Agreement. This Inter-ministerial Committee is chaired by a Secretary of State of Ministry of Economy and Finance (MoEF), with 8 members from other ministries and the Director General of General Department of Taxation (GDT) is a permanent member. This Committee has main duties:

1. To ensure the success of negotiation on double taxation agreement with partners in ASEAN and other country that requested to make this agreement.
2. To review and make decision on the policy of agreement.
3. To review and make decision on the draft of agreement
4. To review and make decision on the negotiation procedure on double taxation agreement for selecting the priority country for negotiating.
5. To review and make decision on the strategy for negotiating with each partner
6. To make regular and special report to Minister of MoEF for reporting to Government to request the opinion and make decision related to policy.
7. To attend meeting requested by Chairman of the committee in case of urgent matter.

This committee has the right to use MoEF's stamp on formal documents if the documents are approved by committee. In addition, the committee has a technical team to support for reviewing on national and international tax and scheduling the meeting on technical. This team is chaired by Director General of GDT, and has 25 members and 2 assistants.

Legal Update

Prakas No. 283 dated 11 November 2014 on Minimum Wage Determination for Workers in Textile, Garment and Footwear Industry for year 2015

The Ministry of Labour and Vocational Training in its Prakas on "Minimum Wage Determination for Workers in Textiles, Garment and Footwear Industry for year 2015" increases the minimum wage from US$100 to US$128 per month for workers in the said sectors for 2015. Under this Prakas, the set minimum wage must be implemented from 01 January 2015.

It should be noted that to finalize the above minimum wage, there were a triangle meeting on 12 November among the representative of employers, representative of employees and the Royal Government. The employers would like to offer the minimum wage of US$110 while the employees would like US$140. To compromise, the Labor Advisory Committee ("LAC") in the name of the Royal Government proposed a minimum wage of US$123 to have three options for vote.

As a result of the vote, 16/25 voted for a minimum wage of US$ 123 and this amount has been increased to US$128 upon the recommendation from Prime Minister Hun Sen.

Finally, several issues have been discussing regarding the increasing of minimum wage in Cambodia. Some say that this can bankrupt some employers who cannot afford the new minimum wage. Also, it is the employees' concern that increased minimum wage will be meaningless if food and especially renting fee are also increased as usually the landlords near factories usually increase their price when the minimum wage is increased. Therefore, it is their suggestion that the Royal Government should take action in order to avoid this problem happened.