

For many developing countries, one of the most common types of related party transactions is intra group services. This could be domestic, but is predominantly cross border services provided by Regional or Ultimate Headquarter/Group Service Centers.

AUTHOR



Kieron Gaffney
Director

Kieron is an ACCA-qualified, international tax professional with 10 years of experience, including four years in Cambodia. Recognized as the leading transfer pricing specialist actually located in Cambodia, Kieron established and led KPMG's transfer pricing practice in Cambodia. He has completed thousands of transfer pricing projects, including over 250 in Cambodia, such as preparing transfer pricing documentation in Cambodia and Vietnam for a Japanese-based banking group and saving millions of dollars in tax assessments on a Cambodian transfer pricing audit for a petroleum company. Kieron also has extensive and wide-ranging experience in M&As, IPO readiness exercises, cross-border transaction structuring, and tax regime advocacy across a range of industry sectors, with a particular focus on the energy, banking, real estate, and manufacturing sectors.

INTRA GROUP SERVICES – ARE CAMBODIAN TAXPAYERS WAVING A RED FLAG TO THE GDT? PART ONE

Introduction

For many developing countries, one of the most common types of related party transactions is intra group services. This could be domestic, but is predominantly cross border services provided by Regional or Ultimate Headquarter/Group Service Centers. **Cambodia is no different in this regard, which is acknowledged by the existence of Article 17 in Prakas 986** (Cambodian Transfer Pricing guidelines) which specifically focuses on intra group services. Article 17 is consistent with the most recent guidance on international best practice, namely Chapter VII of Action 10 of the Organization for Economic Co-operation and Development ("OECD") framework for "Base Erosion & Profit Shifting" ("BEPS").

It is therefore important that Cambodian taxpayers are aware of what Article 17 of Prakas 986 outlines in respect of how intra-group service transactions are determined and priced to assess consistency with the "arm's length principle". **The importance of this cannot be overemphasized** as the General Department of Taxation ("GDT") will under audit, scrutinize the charges paid by Cambodian taxpayers in respect of services provided by their related parties (particularly those overseas). To manage this risk correctly, Cambodian taxpayers will

Highlights of this note

- ▶ Introduction
- ▶ Why VDB Loi – How can we help?
- ▶ Background
- ▶ Conclusion

need to pay particular attention to four key points. **This article will focus on two of these**, namely:

- *Whether intragroup services have actually been rendered;*
- *Whether intragroup services rendered justify a charge.*

In the "Background" and "Conclusion" section, further information is given on what Cambodian taxpayers should be aware of, what they should and should not be doing **and how so many Cambodian taxpayers are exposing themselves to a high level of transfer pricing audit risk in respect of their intra group services expense** paid and claimed as an allowable deduction on its Tax on Income ("ToI") Return.

Why VDB Loi – How can we help?

Risk assessment

The devil is very much in the detail and our dedicated transfer pricing team at VDB Loi can complete a document review to determine whether a Cambodian taxpayer has sufficient supporting documentation to prove:

- Services are actually rendered by the related party service provider;
- Services are for the benefit of the Cambodian taxpayer, rather than its shareholder;
- Services are not a duplication of what the Cambodian taxpayer undertakes themselves or is provided to them by a third party;
- Services provided give more than an incidental benefit to the Cambodian taxpayer.

Compliance

Our dedicated transfer pricing team can enhance compliance by producing “Local File” Transfer Pricing Documentation with financial benchmarking (usually within 3 weeks) consistent with the guidance given in Prakas 986.

Audit

In the context of a transfer pricing audit, tax advisors with limited transfer pricing experience will often merely communicate what information the GDT is requesting, rather than guide the process and defend itself. It is therefore important to have **dedicated Transfer Pricing “Subject Matter Experts”** guiding transfer pricing audits. Our dedicated Transfer Pricing Advisory & Audit Team excel at strategically guiding the process and providing technically based defenses to assist Cambodian taxpayers in obtaining the fairest result possible.

Background

Determination on whether intra group services are rendered

The first consideration for Cambodian taxpayers is a test of substance and is outlined in Article 17 (1a) of Prakas 986, stating Cambodian taxpayers should “Analyze the economic and commercial value and the necessary requirements of services provided within the intra-group by comparing between independent

enterprises under similar circumstances.”

This is consistent with international guidance, specifically the benefits test outlined in Section B1.1. of Chapter VII of Action 10 of the OECD framework on BEPS, which outlines that a major focus of the tax authorities will be “determining that a service has been provided.”

The GDT is persistently questioning the validity of services received from related parties; thus, Cambodian taxpayers (service recipients) must be able to prove services have truly been received and they would be willing to pay an independent party for the provision of the same services.

Many Cambodian taxpayers do not retain sufficient documentation to prove that services have actually been rendered by their related party, resulting in the whole amount of their intra-group service expense being disallowed during a transfer pricing audit. This often results in significant tax re-assessment, with an additional 40% penalty plus interest also being charged.

Determination of whether intragroup services rendered justify a charge

The second consideration for Cambodian taxpayers is whether the services received justify a charge being made. When making this consideration, there are three tests of economic substance outlined in Article 17 of Prakas 986, which can be categorized as follows:

- Shareholder Activities;
- Duplication of services;
- Incidental benefits.

Shareholder activities

Article 17 (1b) details Cambodian taxpayers should “Review and consider removing other expenses that are incurred within the intra-group for fulfilment of the shareholders’ functions which are not considered to be services.”

These functions include “activities that relate to the parent company’s structure of jurisdiction such as shareholders’ meeting, parent company’s share publishing, expenses for management services provided to the board of directors, expenses relating to preparation of reports as required by the parent company, expenses for fund raising in order to buy another company’s share, etc.”

This is consistent with Section B1.2. of Chapter VII of Action 10 of the OECD framework of BEPS, which outlines how a service performed by a parent company or a regional holding company **solely because of its ownership interest in one or more group members should not be considered to be an intragroup service, and thus should not justify a charge to other group members.**

Duplication of services

Furthermore Article 17 (1c) details how Cambodian taxpayers should “Review and consider removing expenses for services within the intra-group with



regards to services redundant with those service that another member of the group is already carrying out by themselves or with a third party."

This is consistent with Section B1.3. of Chapter VII of Action 10 of the OECD framework of BEPS, which details how duplication of services occur in instances where the intra-group service provided already exists in the service receiving entity. In effect, the "service receiving" entity may be performing such services for itself or may have engaged a third party to perform such services. Duplicated services should therefore not qualify as intragroup services as they do not add true economic value.

Cambodian taxpayers therefore should assess whether some or all of the services outlined as being provided in its intra-group services agreement is already performed by themselves or a third party. For example, if a Cambodian taxpayer has a highly functioning Human Resources department, they must assess what value their related party is providing for the "human resource service" detailed in the intra-group service agreement. **If they are adding no true economic value and merely duplicating what is already done at Cambodian taxpayer level, no charge should be made for this service.**

Incidental benefits

Article 17 1(d) details how Cambodian taxpayers should "Review and consider removing other expenses for activities or services fulfilled by other members of the intra-group which provide secondary benefits. For example: an enterprise must not consider as expense, the services provided within the intra-group, with regards to the benefits gained for being a part of the intra-group; with which makes it possible to afford goods or service at low prices due to the influence or reputation of the intra-group."

This is consistent with Section B1.3. of Chapter VII of Action 10 of the OECD framework of BEPS, which outlines cases where an intragroup service performed by a group member relates only to some group members but incidentally provides benefits to other group members. The incidental benefits ordinarily would not cause these other group members to be treated as receiving an intragroup service because the activities producing the benefits would not be ones for which an independent enterprise ordinarily would be willing to pay. **Cambodian Taxpayers will therefore not be considered to have received intragroup services attributable solely due to it being part of an MNE or benefiting from group synergies, such as leverage in procurement negotiations.**

Conclusion

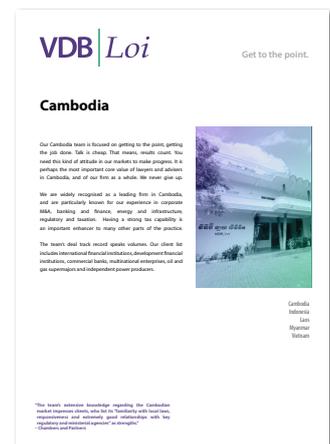
Many Cambodian taxpayers have intra-group service agreements with related parties which either have limited supporting documents or include activities which should be viewed as shareholder beneficial, duplication of services or providing incidental benefit only. This often results in a significant amount of their intra-group service expense being disallowed during a tax audit, which in turn results in large tax re-assessments, with an additional 40% penalty plus interest also being charged. **Cambodian taxpayers should consult with VDB Loi's Transfer Pricing Team** if they believe they may not have sufficient evidence to support their intra group service charges.

Next month we will continue our discussion on this topic and analyze how the methodology being used to determine the intra group service expense for many Cambodian taxpayers is not allowable under Article 17 of Prakas 986.

RELATED ARTICLES

- ▶ [GOOD NEWS FOR INVESTORS: CAMBODIA MOVES MORE LICENSING PROCEDURES ONLINE](#)
- ▶ [LEGAL UPDATE: THE MINISTRY OF COMMERCE CLARIFIES RULES FOR USING A COMPANY NAME](#)
- ▶ [THE MINISTRY OF COMMERCE STEPS UP FINES FOR FAILING TO FILE CORPORATE CHANGES AND FOR UNLICENSED E-COMMERCE ACTIVITIES](#)

DOWNLOAD



<https://bit.ly/2XtrWQU>

CONTACT

No. 33, Street 294 (corner of Street 29), Sangkat Tonle Bassac
Khan Chamkarmorn, Phnom Penh 120101
T: +855 23 964 430~434
F: +855 23 964 154