

## The Power of Forgiveness: How Cambodia is Offering Unprecedented Tax Savings for the Confession of Past Unpaid Taxes

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“Love prospers when a fault is forgiven, but dwelling on it separates close friends.”<sup>2</sup>

### 1. Introduction

Early in 2024, the General Department of Taxation (“GDT”) issued a new regulation to incentivize taxpayers to make revisions to their earlier tax returns<sup>3</sup>. The unstated but nevertheless clear objective of the GDT is to encourage taxpayers who are or become aware of past under- or misdeclarations to voluntarily and unprompted make the necessary corrections to their tax filings. To do so, the GDT will, in some circumstances, waive the otherwise due interests for late payment and the “additional taxes” (penalties for non-payment).

This is the crux of Prakas 071: it offers the taxpayer a full exemption on interest for late payment (which is set at 1.5% per month) and a full exemption on the penalties (at 10%, 25% or 40% of the underpaid tax) that would otherwise apply to declaring and paying a tax later than one was supposed to<sup>4</sup>. The below table sets out the interest and penalties that normally apply in the Cambodian tax regime.

	DESCRIPTION	PENALTY
1	<b>Ordinary negligence</b> (late tax payment or taxes underpaid by <10% of the amount due)	Penalty of 10% of the unpaid taxes (plus interest of 1.5% per month).
2	<b>Serious negligence</b> (late tax payment, or taxes underpaid by >10% of the amount due, or failure to pay tax within 15 days after receiving a tax liability collection reminder letter)	Penalty of 25% of the unpaid taxes (plus interest of 1.5% per month).
3	<b>Unilateral tax assessment</b> (This tax assessment may occur when taxpayers does not cooperate to provide information and documentation. Due to lack of required information, GDT may conduct unilateral tax assessment based on currently available information of taxpayers or publicly available information)	Penalty of 40% of the unpaid taxes (plus interest of 1.5% per month).

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<sup>2</sup> The Holy Bible, Proverbs 17:9

<sup>3</sup> Prakas 071 MEF P.GDT dated 30 January 2024 (“**Prakas 071**”)

<sup>4</sup> We discuss below how these exemptions may not apply for correcting tax returns under audit.

This is not the first time the GDT attempts to coax Cambodian taxpayers into correcting their tax compliance out of their own volition. In 2022, a somewhat similar regulation saw the light of day<sup>5</sup> but as we will see, in 2024 the GDT has significantly increased the incentive for voluntary correction of tax returns.

In this note we look into the conditions for applying Prakas 071, and we offer some observations as to its operation. Finally, we draw some conclusions as to which taxpayers and situations are in our view in the best position to make use of this renewed opportunity.

## 2. The conditions to carry out a penalty free correction of tax returns

Several conditions can be read in Prakas 071, relating to different perspectives:

- *Which taxpayers?*

All self-assessment taxpayers can invoke Prakas 071. Cambodian tax regulations categorize taxpayers in the self-assessment regime as “small”, “medium” or “large”<sup>6</sup>. All companies are either “medium” or “large” self-assessment taxpayers, depending on key financial indicators, and are thus allowed to carry out the correction of tax returns.

NGO’s, non-profits and representative offices are “medium” taxpayers in the self-assessment system. Their tax liability is typically limited to withholding taxes and salary taxes. They too can carry out corrections under Prakas 071.

“Small” taxpayers are sole proprietorships below certain revenue and assets thresholds, and these are not included in the regular tax audit program. For that reason, it is difficult to imagine that small taxpayers will be eager to correct their tax declarations.

Withholding agents may also invoke Prakas 071<sup>7</sup>.

- *What kind of corrections are you allowed to make?*

Prakas 071 speaks of “corrections of tax returns due to misunderstanding and uncertainty”<sup>8</sup>. At first glance, this choice of words suggests perhaps that not all corrections are allowed to be implemented under this system. For example, what happens to correcting an intentional omission or act of evasion?

The mechanics of the corrections themselves indicate that any type of correction including intentional omissions, may fall within the scope of Prakas 071. As will be seen below, for the most important taxes the corrections are done in the online filing system of the GDT, which allows for adjustment of earlier uploaded tax declarations. This online system does not have any appreciation for the deeper motive behind the error in the corrected tax return, and it seems to us that regardless of the earlier motive, all corrections are as a principle accepted by the system automatically, if the correction results in more taxes.

- *By which date must the corrections be carried out?*

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<sup>5</sup> Prakas 217 MEF.P dated 14 march 2022 (“**Prakas 217**”)

<sup>6</sup> Prakas 009 MEF Pr.K on Classification of Taxpayers, dated 12 January 2021.

<sup>7</sup> Art. 3 Prakas 071.

<sup>8</sup> Art. 2 Prakas 071.

Unlike its predecessor Prakas 217, Prakas 071 states that corrections must be carried out by end of June 2024. There is thus a limited time window to benefit from the exemptions of interest and penalties set out in Prakas 071.

▪ *For which taxes are corrections allowed?*

Prakas 071 does not state to which taxes it applies. The GDT which has issued this regulation is responsible for the the full wide range of taxes that exist in Cambodia. The most important and regular ones can be filed and corrected online, such as the Value Added Tax, the Tax on Income, Tax on Salary and Fringe Benefit Tax, and the Withholding Tax.

However, Prakas 071 does not say anything about limiting the right to self-correction to these most important taxes which can be filed online. We conclude from this that all taxes may be corrected under Prakas 071. For those taxes that are not filed online, the correction would have to be implemented by refiling corrected hard-copy tax returns. The same can be said for correcting tax returns that preceded the introduction of the online filing facility.

CAN BE AMENDED ONLINE	SHOULD PRESUMABLY BE AMENDED BY SUBMITTING HARDCOPY
<ul style="list-style-type: none"> <li>▪ Value Added Tax (“VAT”)</li> <li>▪ Tax on Salary (“TOS”)</li> <li>▪ Tax on Fringe Benefit (“TOFB”)</li> <li>▪ Withholding Tax (“WHT”)</li> <li>▪ Prepayment of Tax on Income (“PTOI”)</li> <li>▪ Specific Tax (“ST”)</li> <li>▪ Public Lighting Tax (“PLT”)</li> <li>▪ Accommodation Tax (“AT”)</li> <li>▪ Tax on Income (“TOI”)</li> <li>▪ Minimum Tax (“MT”)</li> </ul>	<ul style="list-style-type: none"> <li>▪ Advertisement Tax (“AdT”)</li> <li>▪ Tax on Immovable Property Rental (“TOIPR”)</li> <li>▪ Transfer Tax (“TT”)</li> <li>▪ Tax on Immovable Property (“TOIP”)</li> <li>▪ Unused Land Tax (“ULT”)</li> <li>▪ Capital Gains Tax (“CGT”)</li> <li>▪ Tax on Transportation Means (“TOTM”)</li> <li>▪ Advance Tax on Dividend Distribution (“ATDD”)</li> </ul>

▪ *For which tax years are corrections allowed?*

Prakas 071 only states that tax returns related to transactions occurring before 01 January 2024, thus up to and including 31 December 2023.

There does not seem to be any limitation as to how far back tax returns can be corrected. Typically in Cambodia an audit can be commenced for a financial year of a taxpayer up to 3 years ago, or in case of evidence of tax evasion, a total of 5 years ago. Accordingly, when it comes to yet to be audited financial years, the taxpayer would likely be focused on the past 5 years, and not beyond<sup>9</sup>.

**3. Correction of tax returns pending an audit**

The voluntary correction of tax returns which are already under a tax audit present several administrative and practical questions. On the one hand it is beneficial for the GDT that taxpayers volunteer to pay underpaid taxes which are already reassessed by officials in the course of a tax audit, instead of appealing them and delaying payment. Granting taxpayers benefits such as waivers of interest

<sup>9</sup> Correction of years already under audit is a separate issue, which we discuss below.

and penalties maybe justifiable from that perspective. Enforcement and seizures can be lengthy and costly for all involved.

On the other hand, granting blanket exemptions of interests and penalties for reassessed taxes unjustly prejudices those taxpayers who have declared and paid their taxes as they were due. Why would taxpayers pay on time if there is no cost for failing to do so?

This tension between on the one hand seeking to incentivize wrongly declaring taxpayers without disincentivizing timely compliance is palpable in Prakas 071.

Prakas 071 allows correction of tax returns for periods which are already under audit, but it distinguishes the incentives -somewhat vaguely- between two situations:

- The issue that is to be corrected has not yet been found in the audit: in this case the 1.5% interest for late payment, and the additional penalty (of 10% or 25% or 40%) are all exempted, identical to where there is no audit at all; or
- The issue that is to be corrected has already been found in the audit: in this case the 1.5% interest for late payment is NOT exempted. With respect to the additional penalty a penalty of 10% is payable and this can be offset with the final penalty imposed at the closing of the audit, which could be at 10% or 25% or 40%. In this situation, assuming the GDT would seek to impose a 25% or 40% penalty in any event for the underpaid tax issue, it is difficult to see any incentive for the taxpayer to self-correct.

The notion “not yet been found in the audit” is somewhat in need of a better definition. Although tax authorities are required to explain their reassessments to the taxpayer<sup>10</sup> this is -in practice- not necessarily the case in the Notice of Tax Reassessment itself<sup>11</sup>. It may thus be difficult to determine what issue has been “found”, although the common practice of drafting meeting minutes may serve as evidence in this regard.

#### 4. Concluding remarks

Prakas 071 is a highly interesting initiative by the GDT for a significant group of taxpayers in a wide range of circumstances. It is a lot more powerful and better conceived than its predecessor Prakas 217.

Taxpayers which are dedicated to transparency and compliance are able to fix earlier mistakes, omissions, misunderstandings and calculation errors in a way that does not cost more than paying the unpaid tax at the time it was due. In other words, it would be as if the error never happened, even without any late payment interest or penalty. This is a significant benefit. Particularly for taxes that should have been paid many years ago, and which would enter in the 25% or 40% penalty range, the savings are very substantial<sup>12</sup>. Taxpayers in this situation should definitely look into moving forward with voluntary self-correction. This is also the case, for example, when the GDT has reassessed the same mistake or omission in several subsequent years of tax audits.

In all cases taxpayers should make a careful, calculated analysis of their past compliance and weigh the cost of the interests and penalties as the risk of “doing nothing”, to possibly seize this unique moment of penalty free corrections.

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<sup>10</sup> Art. 14 Prakas nr. 270 MoEF. Brk on Tax Audit dated 13 March 2019

<sup>11</sup> Art. 15 Prakas nr. 270 MoEF. Brk on Tax Audit dated 13 March 2019

<sup>12</sup> For example, an underpaid tax of 100,000 in January 2019 plus a penalty of 40% can have increased to 230,000 or more by January 2024.

The question whether or not to move toward self-correction is more complicated for the (often numerous) tax years that are under tax audit. The benefits of self-correcting errors that are not yet detected in an audit are the same as if there is no audit, and therefore certainly worth considering. But if an issue is “found”, self-correcting becomes much less attractive. The complications associated with whether or not something is already found may present an obstacle to taxpayers from taking the leap in favor of voluntarily revising their own tax returns.