

## LEGAL FRAMEWORK FOR FOREIGN DIRECT INVESTMENT

### 1. Foreign Investment Policy Regime

The growth in FDI to Cambodia from the early 1990s was motivated by the country's shift towards a market economy and growing macroeconomic stability. FDI has brought in the much needed capital investment, technology, and management knowledge, and contributed in a substantial way to reducing poverty as a whole through massive job creation, particularly in the garment and footwear industry. In recognition of the benefits of inward FDI, the Government enacted in 1994 a Law on Investment (LoI) offering generous incentives to investors. According to the IMF, in most respects Cambodia's investment framework compares favourably with that of its regional neighbours.

The LoI establishes an open and liberal foreign investment regime with broad investment guarantees and places very few restrictions on the level of foreign participation in investments. Aside from the specific constitutional restrictions on land ownership, foreign investors can own up to 100% shares of their companies. Foreign and domestic investors are treated in a non-discriminatory manner either at the time of initial investment or after investment. Foreign investors are permitted to hold land through long or short term leases or land concessions. In an effort to entice more foreign investment, a new law was enacted in 2010 allowing foreign ownership of strata titles of condominium properties located above the ground floor.

Cambodia does not apply ownership restrictions on joint ventures, which may be freely established by the parties, unless the joint venture intends to hold land. In that event foreigners can hold a maximum of 49% share in the venture. Joint ventures with the government exist in some regulated sectors like the stock exchange whereby the Ministry of Economy and Finance has teamed up with a Korean listed company to operate the Cambodian Stock Exchanges.

The Government guarantees that it will not adopt a nationalization policy that would adversely affect private properties of investors. Other guarantees include no price fixing of products or services of investors and free purchase and transfer abroad of foreign currencies, including remittance of royalties, management fees, profits and repatriation of invested capital. The LoI permits investors to hire foreign nationals for employment as managers, technicians, or skilled workers if the qualifications and/or expertise are not available in Cambodia. The investment legal framework governing FDI is listed in the endnotes.

The Council for the Development of Cambodia (CDC) was established in 1994 under the LoI as a one-stop decision-making body for private and public sector investment. The Cambodian Investment Board (CIB) is the CDC's operational arm for private sector investment. It is chaired by the Prime Minister and is composed of ministers and senior officials from various government agencies. The CIB reviews investment applications and grants incentives to qualified investment projects meeting the requirements laid out in the Investment Law. As the "One-Stop Service", the CDC coordinates with relevant ministries on investment facilitation measures.

At the provincial level, Provincial/Municipal Investment Sub-Committees (PMIS) are established to regulate the licensing scheme for investments of less than two million US Dollars. For investment projects in Special Economic Zones (SEZs), the government has established the Cambodian Special Economic Zones Board

(CSEZB) under the auspices of the CDC to promote and regulate the SEZ scheme. A Special Economic Zones Administration (SEZA) is established for each respective SEZ and serves as a one-stop service to investors from the registration of investment projects to obtaining routine export-import approvals.

## 2. Investment Registration Procedures

The investment licensing regime was substantially amended in 2003 to achieve greater transparency in the licensing schemes. Qualified Investment Projects (QIPs) are required to submit an application through the CDC/CIB, the PMIS or directly to the CSEZB as the approving authority depending on the type of investment project. The CDC administers projects with an investment capital of USD 2,000,000 or more, while the PMIS administers projects with investment capital of less than USD 2,000,000.

Generally, most sectors are open to foreign investment. Section 1 of Annex 1 of the 2007 Sub-Decree No. 111 (“Negative List”) lists activities prohibited for both Cambodian and foreign entities, namely: (i) Production/processing of psychotropic substances and narcotic substances; (ii) Production of poisonous chemicals, agriculture pesticide/insecticide and other goods by using chemical substances prohibited by international regulations or the World Health Organization, that affect the public health and environment; (iii) Processing and production of electrical power by using any waste imported from a foreign country; (iv) Forestry exploitation business prohibited by the Forestry Law; and (v) other investment activities prohibited by law.

Section 2 of Annex 1 of the Negative List contains a list of investment activities and projects eligible for incentives provided they meet the minimum requirements, a few of which are listed in the table below:

<b>Fields of Investment</b>	<b>Requirement for Investment</b>
Supporting industry, which has its entire production (100%) supplying the export industry.	US\$100,000 - or more
Production of animal feed.	US\$200,000 - or more
Production of leather products and related products; all kinds of metal products; electrical and electronic appliances and office materials; toys and sporting goods; motor vehicles, parts and accessories; ceramic products.	US\$300,000 - or more
Production of food products and beverages; products for textile industry; garments, textiles, footwear and hats; furniture and fixtures that do not use natural wood; paper and paper products; rubber products and plastic products; clean water supplies; traditional medicines; freezing and processing of aquatic product for export; processing of any kind of cereals and crop products for	US\$500,000 - or more

export.	
Production of chemicals, cement, agriculture fertilizer and petrochemicals; modern medicines.	USD 1 Million or more
Construction of modern market or trade centre.	<ul style="list-style-type: none"> <li>• USD 2 Million or more.</li> <li>• More than 10,000 square meters</li> <li>• Adequate space for car park</li> </ul>
Training and educational institutes that provide training for skill development, technology or poly technology that serves industries, agriculture, tourism, infrastructure, environment, engineering, sciences and other services.	USD 4 Million or more
International trade exhibition centre and convention halls.	USD 8 Million or more

### 3. Investment incentives mechanism

The Lol provides a mechanism for various types of incentives for investments that meet specified criteria. QIPs are entitled to receive different incentives such as profit tax exemptions, special depreciation, and duty-free import of production equipment and construction materials. Investment projects located in designated SEZs are also entitled to the same incentives. The approving authority will grant a Conditional Registration Certificate (CRC) to the applicant provided that the investment proposal contains all the required information and the investment activity is not included in the Negative List. The CRC generally specifies the necessary approvals, authorizations, clearances, licences, permits, and registrations required in order to carry out the Qualified Investment Project (QIP). The approving authority will issue subsequently a final registration certificate (FRC) upon completion by the investor of the requirements stipulated in the CRC.

The incentives are not discretionary, in that only QIPs are eligible for incentives. Once QIP status has been granted, then the incentives are guaranteed. The types of investment incentives available for QIPs include:

- (i) Election by QIPs to receive a profit tax exemption or use special depreciation.
  - *Profit Tax Exemption:* Generally, QIPs may elect either for a profit tax exemption (“tax holiday”) or special depreciation. QIPs electing to utilize a tax holiday will enjoy a profit tax exemption during the “trigger period,” the three-year period following the trigger period, and the “priority period.” QIPs are not required to make pre-payment of profit tax and file minimum tax with the GDT during the profit tax exemption period.
  - *Special Depreciation:* QIPs not electing to utilize the profit tax exemption are entitled to a special depreciation allowance of 40 percent of the value of the new or used tangible properties used in production or processing. The special depreciation allowance can be deducted during the first year

of the purchase of the tangible property or the first year of use of such property.

- (ii) Import duty exemptions for production equipment, construction materials and production imports for exported products as shown in the Table 2 below:

**Table 2: Import Duty Exemptions**

Type of QIP	Commodities to be imported free of duty
Domestically oriented QIPs.	Production equipment, construction materials and production input to be used in the production of exports goods
Export oriented QIPs (except those which elect or which have elected to use the Customs Manufacturing Bonded Warehouse mechanism).	Production equipment, construction materials, raw materials, intermediate goods and accessories
Supporting Industry QIPs.	Production equipment, construction materials, raw materials, intermediate goods and production input accessories. In the case where the Supporting Industry QIP fails to supply 100% of its manufactured products to the export industry or directly export its products, the QIP shall pay the customs duties and taxes on production inputs for the quantity that has not been supplied to the export industry or directly exported.

#### **4. Export-Processing Zones and Special Economic Zones**

The key legislative measures regulating SEZs are: (a) Law on the Amendment to the Law on Investment; (b) Sub Decree on the Establishment and Management of the Special Economic Zone; (c) Law on Customs; and (d) Prakas on Custom Bonded Warehouse dated 15 February 2008. To improve the investment climate and increase exports, the Government has established of the CSEZB to promote and attract more investments into the zones. Potential zone developers can apply for the development of special areas into economic zones, which could include general and specialized industries and export processing zones. There are no special restrictions of business activities in SEZs.

The CSEZB, operating under the purview of the CDC, is the “One-Stop Service” in charge of the development, management and supervision of operations of the SEZ. There is also a Special Economic Zones Trouble Shooting Committee (SEZ TSC), mandated to assist zone investors to solve technical or legal issues

occurring in SEZs. Investments located in an SEZ that are approved as a QIP are eligible, in addition to all QIP benefits and incentives, to obtain VAT exemption for imports. Customs regulations generally allow the free flow of materials and products into and out of the SEZ, although goods that move into the stream of commerce in the country are subject to standard import duties. Currently there are more than 20 SEZs, which are engaged mainly in the manufacture of garments, shoes, bicycles, food processing and electrical equipment industries.

The following are summary of the main privileges and incentives offered to general QIPs and QIPs in SEZs and Customs bonded warehouses:

**a) General Qualified Investment Project (QIP):**

*Governing law:* Law on the Amendment to the Law on Investment.

*Investment incentives, duties and taxes exemption:* Investment incentives granted to QIP shall be as follows:

- QIPs may elect to receive a profit tax exemption or use special depreciation
- Profit tax exemption (Selective): A tax holiday period is composed of “Trigger period” + 3 years + Priority Period (Maximum total 9 years)
- Maximum Trigger Period: commencing on the issuance of the Final Registration Certificate (FRC) and ending on the last day of the taxation year immediately preceding the earlier of:
  - if the QIP derives a profit, the taxation year that the profit is first derived; and
  - if the QIP derives income from investment activities in respect of the sale of goods or services, the third taxation year after the taxation year in which the income is first derived.
- An annual Certificate of Obligation Satisfaction (or “Certificate of Compliance”) has to be obtained by the QIP to be entitled “Profit Tax Exemption
- A QIP shall be subject to a profit tax rate after its tax exemption period as determined in the Law on Taxation.
- Special depreciation (Selective): 40% special depreciation allowance on the value of the new or used tangible properties used in the production or processing
- Duty free import of production equipment, construction materials, etc.
- A QIP located in a designated SEZ or Export Processing Zone are entitled to the same incentives and privileges as other QIP stipulated in the Amendment to the LOI.
- A QIP is entitled to 100% exemption of export tax, except for activities as stipulated in other laws in effect.

**b) Special Economic Zones**

*Governing law:* Sub Decree on the Establishment and Management of the Special Economic Zone.

Investment incentives:

- The Zone Developer may request, under the form of a temporary admission, the import of means of transport and machineries used for the construction of infrastructures.
- Zone developers, investors or foreign employees have the right to transfer all the income derived from the investment and salaries received in the zone to banks located in other countries after payment of tax liabilities.

Duties and taxes exemption:

- The exemption period for the Tax on Profit is a maximum period of 9 years, in compliance with Article 14.1 of the Law on the Amendment to the Law on Investment.
- The import of equipment and construction materials to be used for infrastructure construction in the zone is allowed and exempted of import duties and other taxes.
- The Zone Developer is entitled to receive custom duty exemption on the import of machinery and equipment for the construction of roads connecting the town to the zone and other public services infrastructures, such as water treatment plant and sewage system.
- Entitlement of the same incentives on customs duty and tax as other QIPs.
- The Zone Investor is entitled to a Zero percent on Value Added Tax (VAT) incentive rate for its import provided the production outputs are re-exported. If the production outputs are imported into the domestic market, the Zone Investor shall refund the appropriate VAT amount.

**c) Custom Bonded Warehouse (CBW)**

*Governing law:* Law on Custom; Prakas on Custom Bonded Warehouse.

Investment incentives:

- Goods may be stored in the customs bonded warehouse for up to two years from the date of registration of the customs declaration. Before its expiry of the two years period, owners of the goods may request an extension of this time limit for storage of goods of up to twelve months if the goods are still in good condition.

Duties and taxes exemption:

- Goods removed for export shall be subject to the filing of a customs export declaration, and no import or export duties and taxes are charged, except for domestic goods, which may be subject to export duty.
- Applicable duties and taxes on goods removed for domestic use are charged according to the rates of duties and taxes in effect on the date of the filing of the customs declaration.

**d) Custom Bonded Manufacturing Warehouse (CBMW)**

Investment incentives:

- In a specific circumstance, the MEF may issue a licence for the operation of custom manufacturing bonded warehouse.

- Such licensed operators are authorized to carry out processing and manufacturing of approved products under the control of Customs. Operators of such warehouses are allowed to import certain types of dutiable raw materials/components, and machinery and equipment, whose payment of duties and taxes are suspended, to be directly used in the manufacturing or processing of goods.

## **5. Bilateral Reciprocal Investment Promotion and Protection Agreements**

Cambodia has signed numerous bilateral investment promotion and protection agreements, the following of which have entered into force comprise: Australia, China, Croatia, Cuba, the Czech Republic, France, Germany, Indonesia, Kuwait, Japan, Laos, Malaysia, the Netherlands, Democratic People's Republic of Korea, the Overseas Private Investment Corporation (OPIC), Pakistan, the Philippines, Singapore, South Korea, Switzerland, Thailand, and Vietnam.

The agreements generally provide reciprocal national treatment to investors, excluding benefits deriving from membership in future customs unions or free trade areas and agreements relating to taxation. The agreements preclude expropriations except those that are undertaken for a lawful or public purpose, are non-discriminatory, and are accompanied by prompt, adequate and effective compensation at the fair market value of the property prior to expropriation. The agreements also guarantee repatriation of investments and provide for the settlement of investment disputes via arbitration. As of today, Cambodia has not signed any agreement on avoidance of double taxation.

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*\* Article courtesy of Dr. Sok Siphana, Advisor to the Royal Government of Cambodia*

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