Corporate tax treatment of zero-balance cash pool (2/38/20)

The corporate income tax (CIT) treatment of cash pools is a grey area when it comes to measuring the company's taxable base. The State Revenue Service (SRS) has still to publish guidance on various situations potentially facing cash pool members in order to make the tax authority's opinion on this issue crystal clear. This article explores how the CIT treatment of zero-balance cash pools is interpreted in an advance tax ruling the SRS has issued to a PwC client.

Background

It is clear that any amounts paid into a cash pool are legally treated as loans, i.e. those transactions are governed by section 11 of the CIT Act.

In practice, though, companies are asking questions about a zero-balance cash pool that involves daily cash movements which the company does not recognise as separate loans. The key question is how the company can trace those amounts and prove they are repaid within 12 months if each separate payment is not recognised as a repayable loan. And the company had a positive cash pool balance at the end of 2018 and 2019, often with an upward trend.

The SRS interpretation

In the advance tax ruling on the CIT treatment of a zero-balance cash pool, the SRS confirms PwC's understanding that the cash movements should be assessed annually under the FIFO (first in, first out) method. If the company's zero-balance cash pool sees continuous cash movements during the year, with repayments exceeding the cash pool balance at the beginning of the year, then the amounts paid during the year should be recognised as loans maturing in up to 12 months. Such loans need not be included in the taxable base because they qualify for the exemption available under section 11(4)(4) of the CIT Act.

The SRS explains that it is up to the company to decide, according to its own accounting policy, how it can account for amounts paid into and withdrawn from the cash pool, and what supporting documents it needs for accounting purposes.

Thus, our experience suggests that it is possible for companies using a zero-balance cash pool to obtain a favourable tax ruling about excluding such loans from their taxable base. However, each case should be assessed on its merits, and consequently each company is advised to seek a separate tax ruling on the CIT treatment in its particular circumstances.