

WHAT ARE THE TAX ISSUES AFFECTING CROSS BORDER TRANSACTIONS?



Increasingly, companies in Thailand seek to use these treaties to minimize tax exposure associated with cross-border transactions. Thai law attaches a withholding tax on many types of payments made by Thailand parties to parties offshore. This withholding tax is paid to the Revenue Department by the Thailand party making the payment offshore. This article uses the Thailand-US Tax Treaty and the Thailand-Singapore Tax Treaty as examples to show how qualifying Thailand parties can minimize withholding taxes and how provisions of tax treaties vary.

1. Business Profits

A business profit is most commonly a fee paid by a Thai party to a party offshore for a service benefiting the Thai party. Common example of a service fee payment that may qualify as a business profit is a payment for market research. Ordinarily, the Thai party's payment for this service would be subject to a 15% withholding tax.

If, however, the service provider qualifies under the treaty, this payment would qualify for exemption from withholding tax as a business profit.

2. Royalties

The Thai Revenue Code defines a royalty as "value received for goodwill, copyright, or any other right" Payments that fall under the definition of a royalty are subject to a 15% withholding tax. Royalties are most commonly licensing fees and other fees paid by the Thai party for the use of patents, designs, trademarks, formulas, and other intellectual property rights.

Whether a service fee falls under the definition of a royalty or qualifies as a business profit is not an exact science. The following points are some of the factors Thai courts have used when making a determination:



i. Type of Knowledge Transferred

If the knowledge to be transferred is more general in nature, it tends to be a business profit. If the knowledge is confidential, it tends to be a royalty.

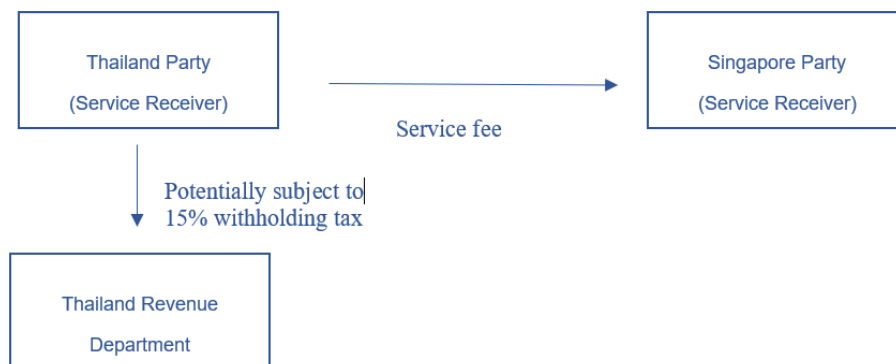
ii. Imparting Principle

If the purpose of the service being performed is for the offshore party to impart knowledge to the Thai party, so that the Thai party can perform the service next time, the service fee tends to be a royalty. If the exchange is for the service provider to use its own resources and know-how solve the Thai party's problem, it tends to be a business profit.

iii. Substance over Form

The court will look at the real relationship between the parties to determine whether the payment is a royalty or business profit. The court will not merely rely on the way the parties characterize the relationship in the contract.

In a technical service agreement, the Thai party is outsourcing specific services to a party offshore. In return for the service, the Thai party pays a fee. Normally, such a fee would be subject to withholding tax.



Note VAT (7%) also applicable.

EXAMPLE: A Thailand company engages a US company to source raw materials for use in its factory in Thailand. The purpose of this transaction is not for the US company to teach the Thai Company how to do anything. Instead, the US company would use its own knowledge and resources to solve the Thai company's problem, which here is finding raw materials. This transaction would qualify as a business profit, making it exempt from withholding tax. If we changed the facts in the example to make the service provider sourcing raw materials a Singapore party rather than a US party, the outcome would be the same. Under both treaties the transaction would qualify for exemption as a business profit.

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