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Tax issues related to commercial contracts

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Outline

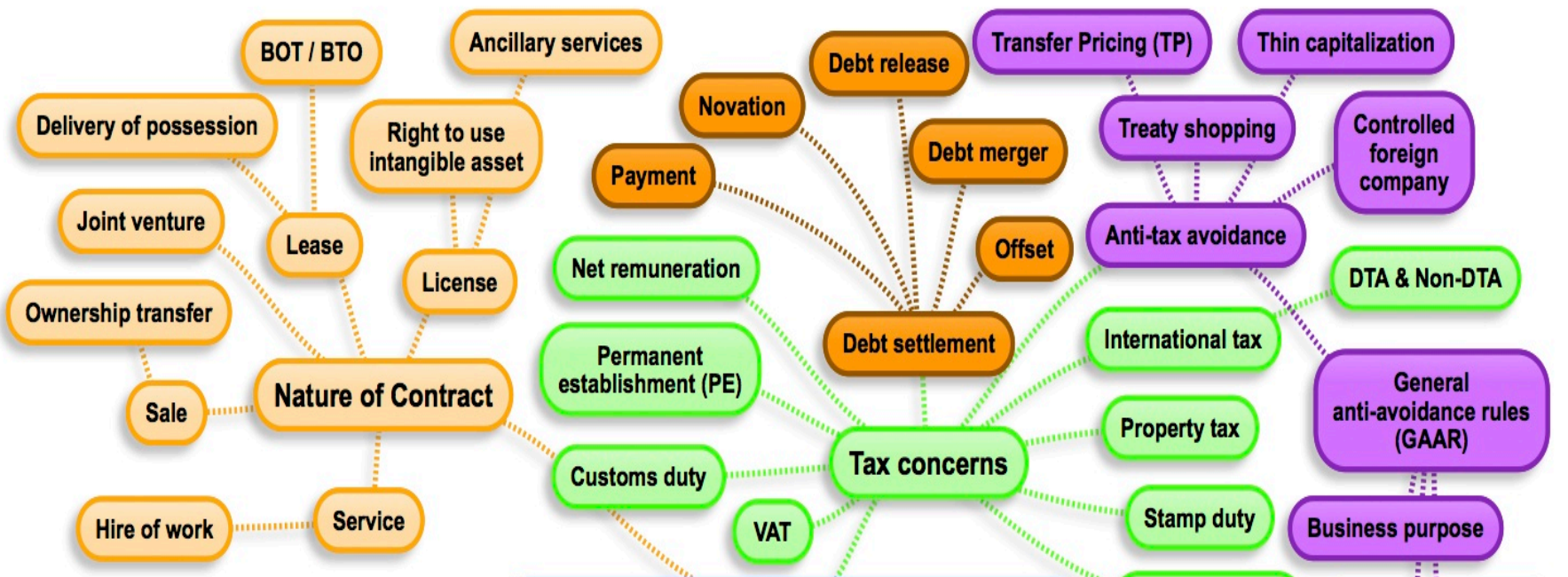
2

- Tax consideration on contract drafting and reviewing
- Basic tax consideration under Thai laws
- Key tax problems on contract practices and case study
 - Lease: Build Transfer Operate (BTO) / (BOT)
 - Franchise: Pizza Hut case / License: Nestle case
 - Service: Philips case
 - OEM: Nike case
 - M&A: Hana Semi-conductor case

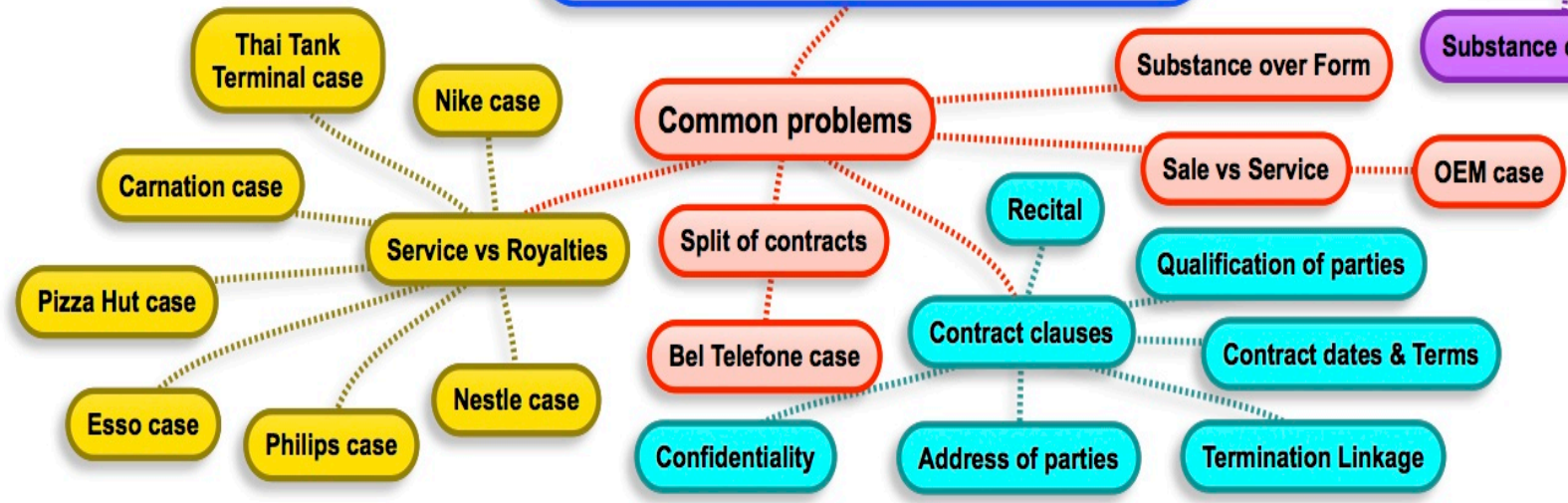
Session 1

Tax considerations on contract drafting & reviewing

Tax Issues: Commercial Contracts



Common problems



Session 2

Basic tax considerations on contracts

Tax considerations on contract drafting & reviewing

6

- **Corporate income tax:** Withholding tax
 - Tax on income / Advance tax payment
 - Net income (tax on tax calculation)
- **Personal income tax**
 - Source income rule / Resident rule (180 days)
- **VAT**
 - Tax on consumption (purchase / use of service)
 - Import of goods / services
 - Export of goods / services

Tax considerations on contract drafting & reviewing

7

- **Specific business tax (SBT)**
 - Financial transactions (Loan, guarantee, FX, etc.)
- **Stamp duty:** Attach to the specified instruments/contracts
- **International tax**
 - Double tax agreement with tax reduction/exemption
- **Property tax (New Land & Building Tax !!!)**
 - Tax on wealth
- **Customs duty:** Tax on import and export of goods

Session 3

Key tax problems in contract practices

1. Tax on real estate lease contract

9

Special consideration beyond normal lease contract (Case No. 5570/2539) สัญญาต่างตอบแทนพิเศษยิ่งกว่าสัญญาเช่าธรรมดา

- Contract without specific form
- Under concept of general contract of the Civil and Commercial Contract (CCC)
 - BTO (Build / Transfer / Operate) = = > Taxes ? VAT ?
 - BOT (Build / Operate / Transfer) = = > Taxes ? CIT ?

1. Tax on real estate lease contract

- Not a specific personal right: No cessation of lease right when the lessee's death (**Different from normal lease contract**) (Supreme Court Case No. 2760/2534), for example:
 - To build a tower and transfer the ownership of tower to the lessor (Case No. 172/2488)
 - To lease out the land and obtain the construction cost from the lessee, ownership of building transfer to the lessor (Case No. 488/2523)

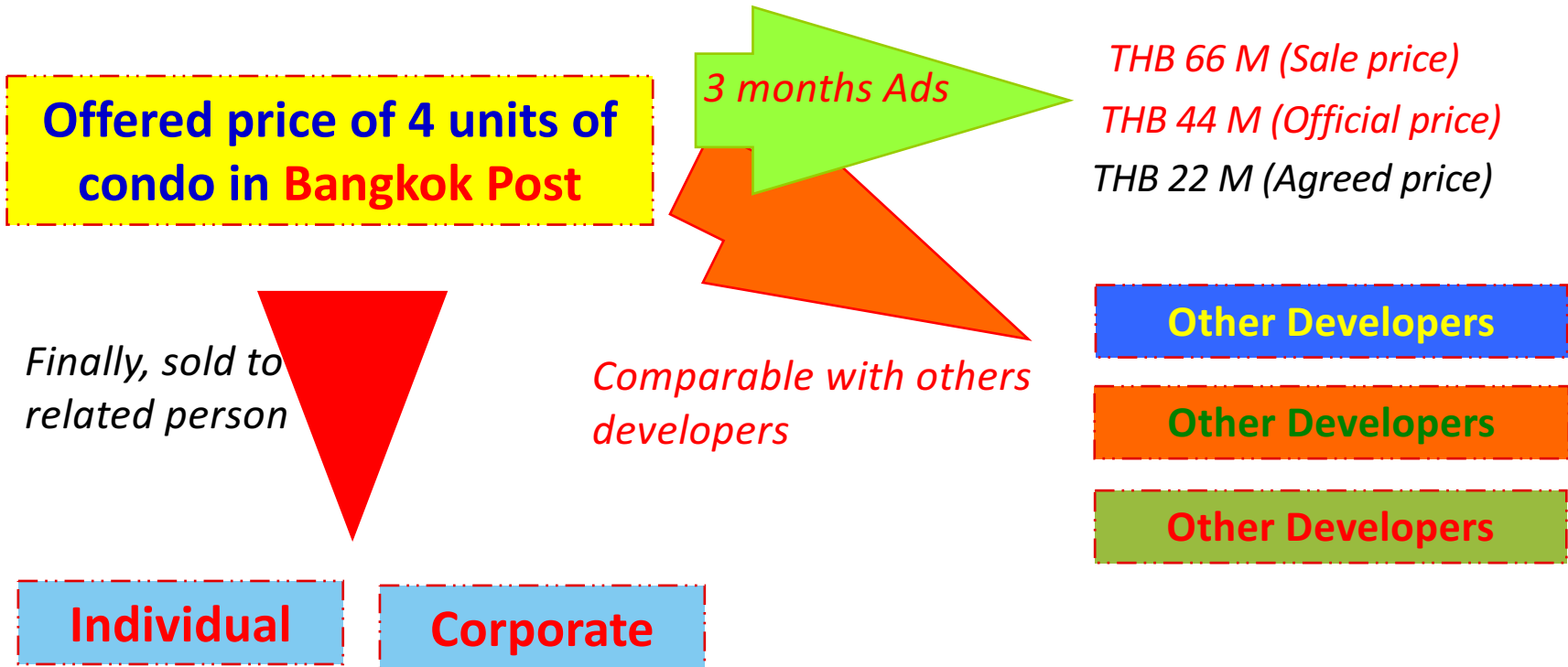
Property Developer Case (Market Price)

11

- Condominium developer with the rest of 4 units (Sukhumvit 26)
- Sale price comparable with others (via Ads)
- Ads via Bangkok Post during 3 months but no buyer during 1997 econ crisis
- 1 unit sold to individual, then 3 unit sold to related companies (but no tax conspiracy)
- Sale price (THB 22 M) lower than 'Official Price' (THB 44 M)
- 'Official Price' is regarded as 'Market Price' ?

Property Developer Case (Market Price)

12



Sale and Lease-back: Advantage

- Become to "Asset light (slim) company"
- Restart depreciation of sunk cost
 - Net book value come to end at THB 1
 - Not reflect fair market value (FMV)
 - Rental = Deductible expense
- Utilize tax loss carry forward
 - Sold out of balance sheet at FMV over NBV with Gain
 - 5 years tax loss carry forward

Sale and Lease-back:

Advantage

- Utilize creditable input VAT
 - Output VAT of sale price creditable against input VAT carry forward
 - No limit period of Input VAT carry forward
 - No need VAT refundable in cash
- Resume cash to replace sunk asset
 - Cash replace asset after write-off it from balance sheet
- Improve Debt : Equity Ratio

2. Hire of work (service) vs Hire of service (employment)

Scope of contract

15

“Construction Contractor shall assume care, custody and control of the Imported Equipment at its port of shipment when ownership of the Imported Equipment is transferred to NPC under the Supply Contract. Construction Contractor shall be responsible for insurance of the Imported Equipment with effect from when it assumes care, custody and control thereof. Construction Contractor shall arrange on NPC's behalf customs clearance of Imported Equipment and shall be responsible for bonds, guarantees, warehousing and transportation therefor from Thai port to the Site”

2. Hire of work (service) vs Hire of service (employment)

16

Case No. 1144/2549

Sale of rice machine and installation with design and test-run in the factory / Ownership of machine will transfer to the buyer upon completion of project and personnel training with delivery of completion

Tax highlights

Hire of work (service)

Sale of goods

Description of works
is required

Goods must be specified

Completion of works
is required

Transfer ownership of goods
is required (**When?**)

Written evidence is
not required

Written evidence is required
for civil lawsuit

Tax highlights

Tax Liabilities	Hire of works	Sale of goods
Withholding tax	3%	No (unless immovable property = 1% for CIT)
VAT	7%	7% (unless immovable property)
SBT	No	No (unless immovable property = 3.3%)
Stamp duty	0.1%	No (unless immovable property not paid SBT & share transfer)

Royalties	Non-royalties
<u>Samples</u> : Technical service / Franchise / Trademark license / Customer data / Ancillary services of software	<u>Samples</u> : Management service / Consulting service / Installation / Training / Design/Maintenance / Distribution / Marketing
<u>Confidentiality</u> : Required	<u>Confidentiality</u> : Not required
<u>Yield</u> : License fee / Royalties	<u>Yield</u> : Service fee

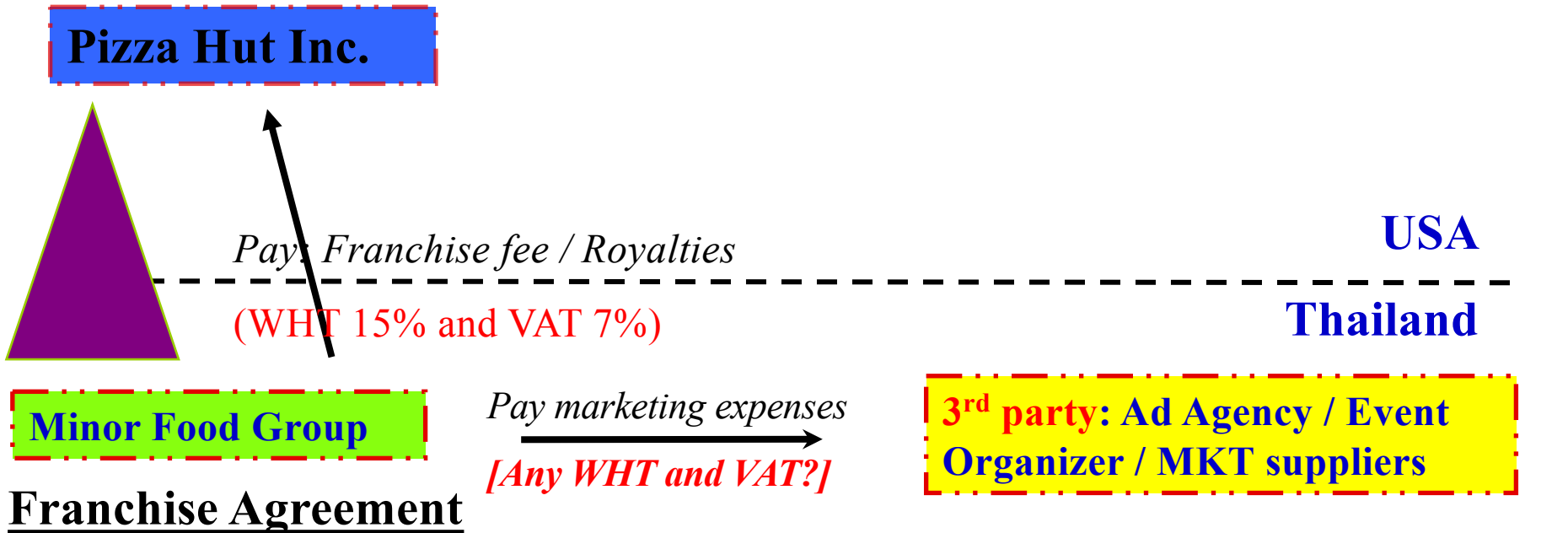
Tax highlights

20

Tax Liabilities	Royalties	Non-royalties
Withholding tax	3% (local) 15% (offshore)	3% (local) 15% (offshore) No (DTA)
VAT	7%	7%
SBT	N/A	N/A
Stamp duty	N/A	0.1% (Hire of work)

Pizza Hut Case

21



- Franchise fee / Monthly royalties (WHT & VAT)
- Marketing expense not less than 3% of gross sale
- Marketing activities and collateral under control and consent of Pizza Hut

3. Franchise & License agreements

22

- Precedent case study (Pizza Hut)

- MKT expenses under Franchising Agreement (Food) paid by the franchisee under control of the franchisor
- MKT expense shall be certain percentage of gross sale
- MKT expense paid to the independent PR supplier
- No MKT expense paid to the franchisor
- MKT expense shall be a part of franchise fee and is regarded as royalties
- WHT and VAT shall be applied by the franchisee

How to revise the franchise contract?

License agreement

23

Case No. 665/2537 (Nestle)

Engineering and advisory services on production of goods with separation of contracts (Engineering / Trademark License) including:

- (1) confidentiality condition (non-disclosure)
- (2) all documents shall be returned to the service provider at the termination of contract
- (3) Not allow to copy
- (4) Termination linkage (Engineering and License)

License agreement

24

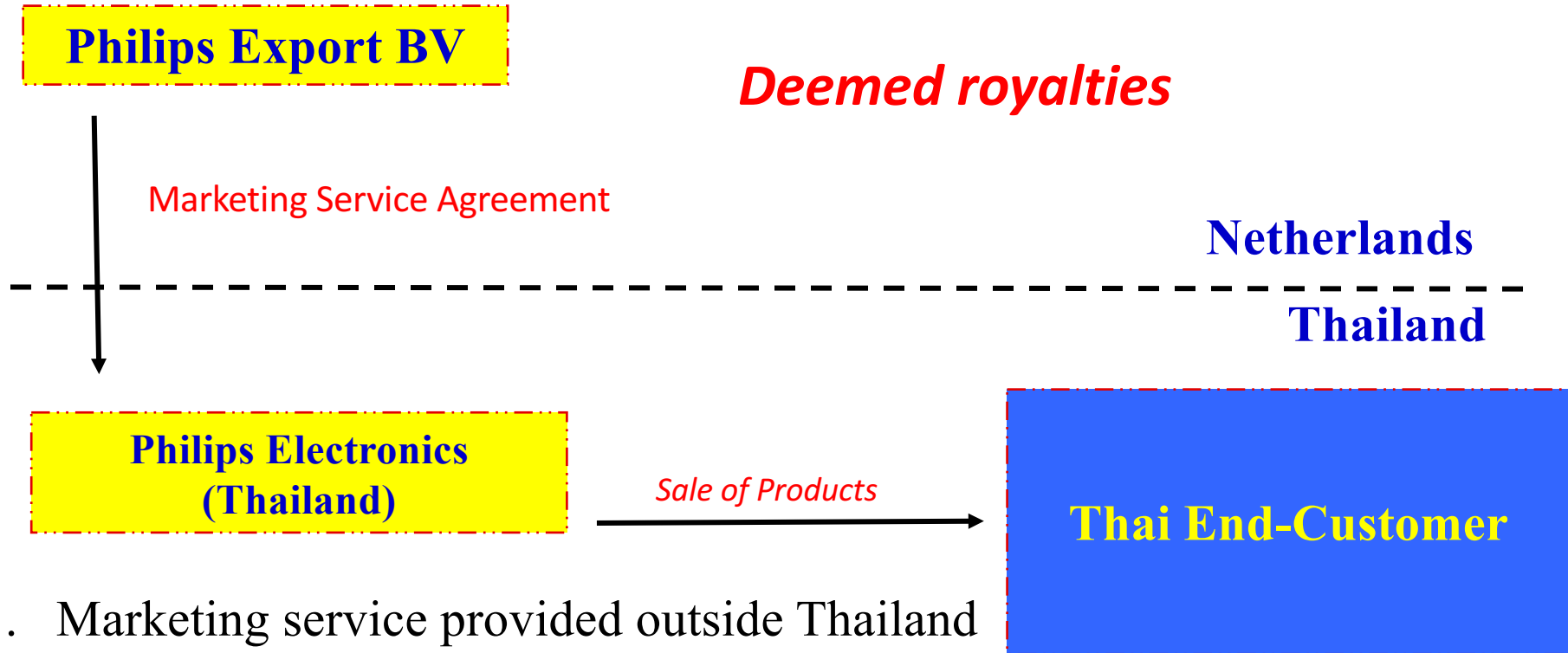
Case No. 2642/2538 (Carnation)

Engineering advisory contract and Trademark license contract with separate contractual parties BUT:

- (1) Offshore parties - same address
- (2) Both contracts – same contract period
- (3) Termination linkage of both contracts

Philips Electronics: Marketing Fee

25



1. Marketing service provided outside Thailand
2. Trade secret is to support marketing service
3. Confidentiality is required / **Then, it is regarded a royalty**

Nike Case: No. 962/2554

26



Trademark License and Sole Distributorship Agreement

- For trademark usage of NIKE products in Thailand
- OEM pricing for golf ball in Thailand and US are not different (per unit)

Not royalties

4. OEM agreement

27

Case No. **5827/2545: OEM / copper wire**

- Melting service of copper to be copper wire
- Loss from manufacturing process
- No commitment to absorb such loss
- Who will be responsible for such loss?
- Any term and condition under OEM contract to handle with such loss?
- **Deductible expense for corporate tax purpose?**
- **Output VAT from shortfall inventory?**

4. OEM agreement

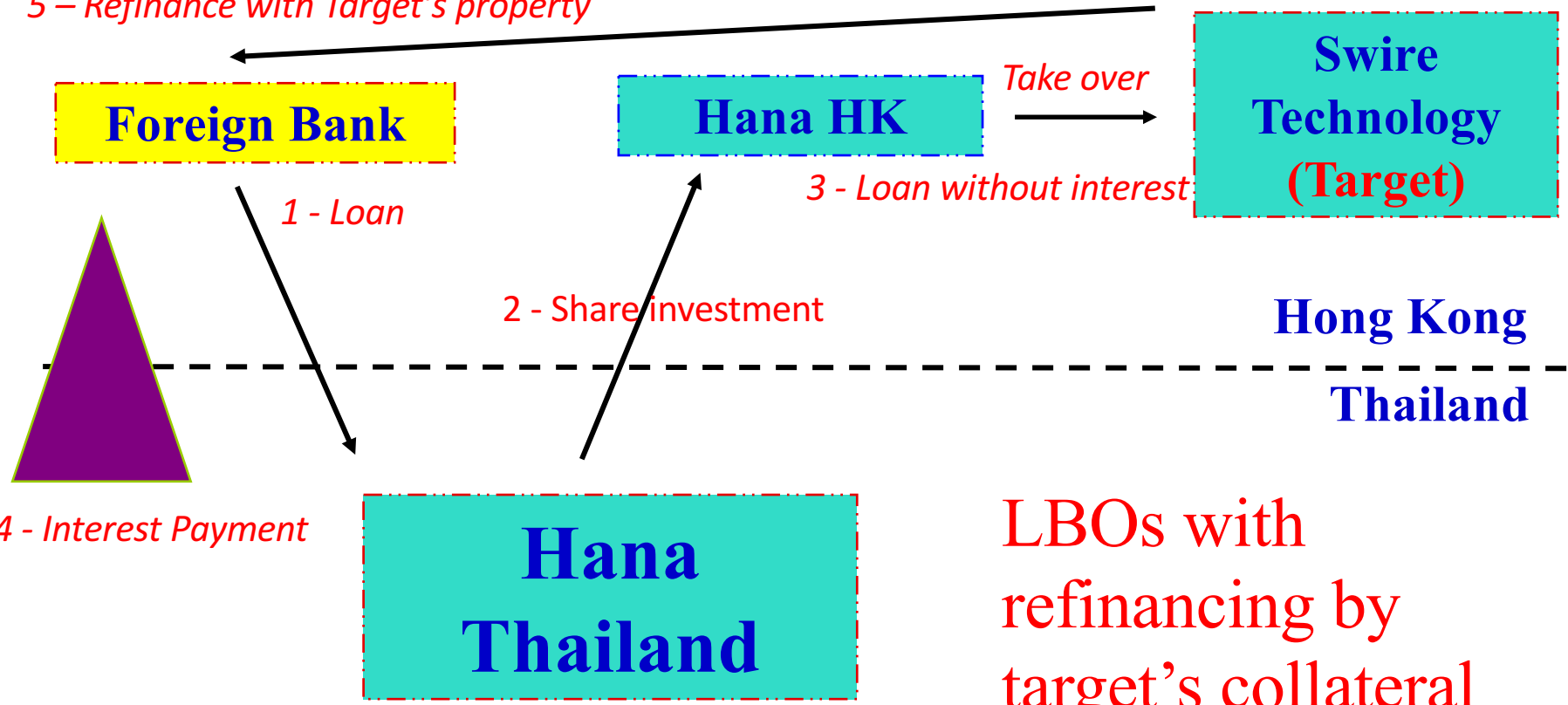
28

Case No. **163/2541: OEM / WHT**

- OEM operator: No factory
- Receive P/O with Specification of products from offshore customer to manufacture in Thailand
- Sample of products and design owned by offshore customer
- **Sale of goods contract OR Hire of work contract?**
- **WHT / VAT / Stamp duty?**

Hana Semi-conductor Case

5 – Refinance with Target's property

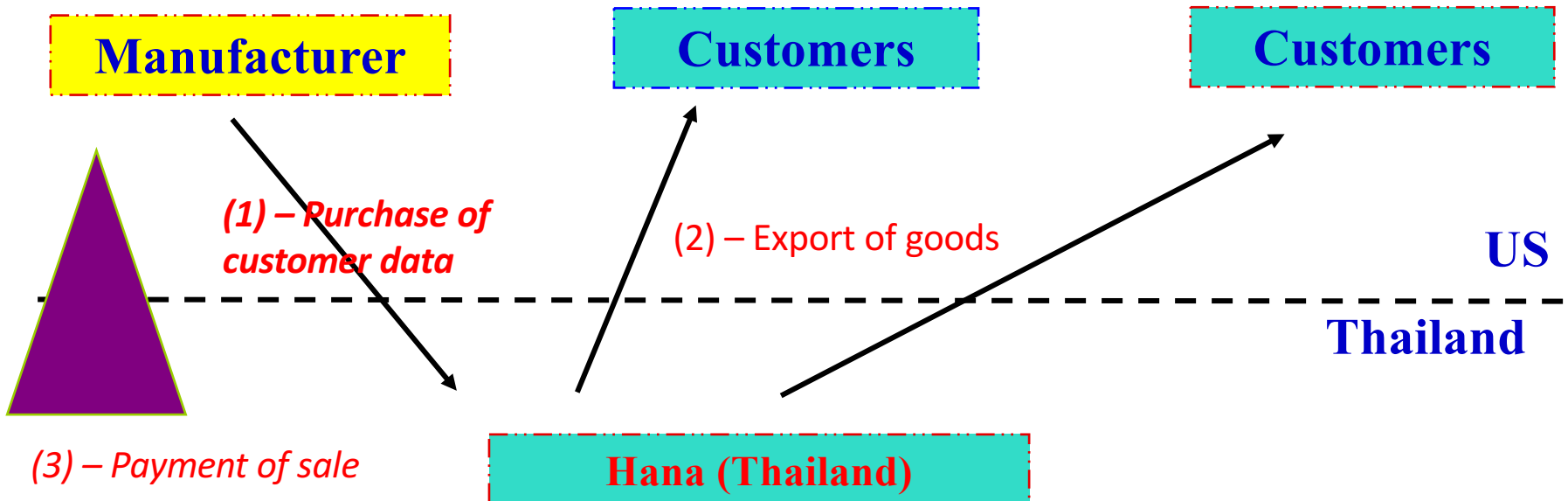


LBOs with
refinancing by
target's collateral

Hana Semi-conductor Case

30

Deemed royalties



1. Customer data = Trade secret ?
2. Trade secret = Royalties ?

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1. ประสบการณ์มากกว่า 25 ปีในงานให้คำปรึกษากฎหมาย ด้านภาษีอากร / IPO / M&A ตลอดจนสัญญาทางธุรกิจ รวมถึง Offshore Incorporation / Family Business
2. ให้คำปรึกษาแก่ลูกค้าทั้งในไทยและต่างประเทศร่วมกับ Partner อีก 13 คนและที่ปรึกษากฎหมายอีกกว่า 120 คนผ่านสำนักงานของ SCL ในไทย เมียนมาร์ / สเปน. ลาว / กัมพูชา
3. วิทยากรบรรยายเรื่องสัญญาธุรกิจและภาษีในงานสัมมนาและฝึกอบรม ตลอดเวลากว่า 15 ปี เป็น “อาจารย์พิเศษด้านภาษีอากร” และ กฎหมายธุรกิจใน หลักสูตรปริญญาตรี/โท ม. รามฯ / ม. ธรรมศาสตร์ / ม. แม่ฟ้าหลวง / ม. ศรีปทุม / ม. หอการค้าไทย / วิทยาลัยดุสิตธานี / จุฬาลงกรณ์มหาวิทยาลัย / ม. กรุงเทพ
4. วิทยากรประจำให้แก่ สถาบันกรรมการไทย (IOD) สมาคมบริษัทจัดการลงทุน (AIMC) ตลาดหลักทรัพย์แห่งประเทศไทย ธนาคารฯ และ สมาคมธุรกิจต่างๆ
5. “คณะกรรมการภาษี” ของสภาหอการค้าแห่งประเทศไทย และ “ผู้ไกล่เกลี่ยคดีภาษี” ประจำศาลภาษีอากรกลาง
6. “กรรมการตรวจสอบ” (Audit Committee) บริษัทจดทะเบียนในตลาดหลักทรัพย์ฯ

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