Bangkok Post
Section: Business/NATIONAL
Date: Tuesday 7 January 2014
Volume: - No: - Page: B2(Center)
Bangkok Post
Circulation: 70,000
Ad Rate: 1,500
Col.Inch: 43.40 Ad Value: 65,100 PRValue (x3): 195,300 Clip: Full Color
Column: LEADING THE WAY: FREE ZONES: ARE THEY STILL WORTH IT?

FREE ZONES: ARE THEY STILL WORTH IT?

LEADING THE WAY

PwC THAILAND

To attract foreign direct investment and increase the country's international competitiveness in the region, Thailand introduced the Free Zone programme more than a decade ago. The main idea was to attract manufacturing activities and foreign companies to invest in the country.

A Free Zone is treated as an area outside Thailand for customs purposes. It allows companies to import raw materials into the country, and to manufacture and export the finished goods out of Thailand without paying any duties and taxes. Moreover, finished goods manufactured in a Free Zone and sold to the domestic market can qualify for a lower preferential duty rate (typically zero) instead of the normal import duty rate.

Over the past decade, many foreign companies, especially in the automotive industry, have taken advantage of these benefits, in particular the privilege for domestic sales, by establishing their operations in a Free Zone. However, authorities have recently made changes to the Free Zone regulations, particularly the domestic sales aspect, that businesses need to be aware of.

One of the critical issues has been whether products manufactured in a Free Zone met the required 40% local "Thai" content to qualify for the preferential duty rate when sold domestically. Essentially, the relevant regulations state that as long as 40% of the product's ex-factory price is local content, the product should be eligible for the preferential duty rate when sold from the Free Zone to the domestic market. However, the regulations do not clearly define how and exactly what cost elements can be used to calculate this 40% local content.

For example, the regulations allow including "profit" into the "domestic costs of production" but do not give a clear definition of "profit" or any guidance on the acceptable profit level. As a result, the Customs Department could be justified in wanting to know whether the profit level being counted toward the 40% local content calculation is appropriate. If Customs were to deem the profit level inappropriate, it could disqualify the products, deny the Free Zone privilege for domestically sold products and seek retroactive duties and penalties.

In early December, the Customs Department invited stakeholders to a public hearing to provide their input on the proposed amendments related to domestic sales. Although it seems that Customs appreciates that the regulations need clearer definitions and guidance to prevent any "misuse" of Free Zone status, it also transpired from this meeting that Customs is proposing more stringent documentation requirements as well as longer approval processes.

So what can Free Zone companies expect in the near future?

Based on the proposed amendments, it is clear that there will be more scrutiny of Free Zone companies, either at the approval stage or enforcement level. This is likely to lead to lengthier and more burdensome approval processes as well as increased post-clearance activities for Customs enforcement units on the qualification of products.

An issue that may continue to be unclear is the definition of acceptable "profit" that can be included in the 40% local content calculation. It seems this was not discussed during the public hearing.

Another issue that could also affect companies in Free Zones in the near future is the potential for the EU-Thailand Free Trade Agreement to not allow duty exemptions or suspension on imported goods contained in finished exports to the EU. If this provision is included, this could mean that the Free Zone duty exemption can no longer be used for any raw materials used in the production of exports to the EU.

Authorities will be finalising the draft amendments in the next few months. More restrictive interpretations by Customs as well as more stringent documentation requirements are expected, and this could affect companies operating in a Free Zone.

In particular, if Customs decides to impose a cap on the profit level, this could lead to products no longer qualifying and companies no longer being able to use the Free Zone privilege for domestic sales. This may lead some Free Zone companies to reconsider whether it is viable for them to retain their investments in the Free Zone or to move elsewhere — perhaps abroad.

As they work to finalise the proposed amendments, it is hoped the relevant authorities will consider their potential impact and address the concerns and comments from Free Zone stakeholders in order to maintain Thailand's competitiveness, and so as not to go against the grain of what was originally envisaged when the Free Zone programme was established.

By Nu To Van, Director of PwC WMS, Thailand. We welcome your comments at leadingtheway@th.pwc.com