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LEADING THE WAY

Road BE(M)PS ahead in quest for global tax 'fairness'

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It has been described as "the most significant change to international tax in modern times". Hyperbole perhaps, but BEPS has been a significant theme in the press, especially in the EU. It reportedly even made it to a one-hour prime-time special in Germany!

BEPS is an Organisation for Economic Cooperation and Development initiative for a "fairer" international tax system, called the Base Erosion and Profit Shifting project. What does it mean for us in Thailand?

Thailand's response

The Thai government's only formal published response (to the UN) on the BEPS initiative indicates their main concerns are about the use of limited-risk subsidiaries and the "ineffective" tax collection from cross-border e-commerce.

The digital economy was also flagged as one of the "most important" action points.

e-business on the radar

Currently, most online sales by foreign vendors are not subject to either corporate income tax or value-added tax (VAT) in Thailand.

The reasons vary and include the Thai tax framework, the infrastructure for collections and the traditional test of taxable presence ("PE test") in double tax treaties.

Collection of VAT on cross-border e-commerce is perhaps low-hanging fruit and could be imposed relatively quickly.

The imposition of corporate income tax on foreign vendors without a presence in Thailand is a bigger challenge, one that requires a change in both present Thai tax law and a renegotiation of existing bilateral tax treaties.

Expect new legislation

The government response also made passing reference to transfer pricing, thin capitalisation and controlled foreign corporation (CFC) regulations.

We are familiar with the perils of transfer pricing, as the legislation has been around for some years now. Thailand now has no CFC or thin capitalisation rules, so this could be the first legislative change we can expect.

The effectiveness of the new legislation will depend greatly on how it is drafted. As an outward looking economy, Thailand must walk a thin line between remaining competitive in the AEC-era and defending its tax base.

The Revenue Department will no doubt evaluate and benefit from the experience of other countries before the legislation is drafted. It must consult with representatives from industry and their advisers, to understand the business drivers behind many existing structures.

Well-drafted legislation achieves the objective and encourages compliance, while clarity and context also reduce the possibility of litigation and corruption.

Change is in the air, and as a tax director how do you prepare for the coming storm?

Evaluate legacy structures

As a first step, you should re-examine your firm's legacy tax strategies and structures and assess the effect of BEPS on the business.

Take for example, the introduction
of CFC rules. Thai corporations and individuals traditionally have used a low-tax jurisdiction — tax havens — to route funding to foreign investments. The reasons are not necessarily to evade tax.

CFC rules typically seek to ignore the intermediate holding companies and tax certain "passive" or "tainted" foreign revenue when earned.

A Thai chief financial officer could be in the unhappy position of having to fund and pay Thai taxes on foreign revenue even before the cash is received. CFC planning is then required to be put in place.

New tax focus

The government response also pointedly commented on the mismatch between the "corporate structure" and the "substance of activities".

"Treaty abuse" was listed as one of the "most important" action points. This could mean the Thai tax authorities will like the rest of the world focus on the "substance" of a transaction or foreign recipient. This is generally in the context of applying preferential tax treaty rates in a cross-border transaction.

Could this signal a shift by the tax authorities from their customary reliance on the "legal form" of a transaction? If so, there are multiple transactions that should be re-evaluated, from cross-border payment of equipment rentals and staff secondments to the use of trading structures that result in double non-taxation — and even the taxation of profits and gains.

Stay informed

As a second step, you must purposefully keep informed on fast-moving developments in this area.

Many countries are already moving ahead and introducing new BEPS-ready tax laws before next year's deadline. Belgium, for instance, has introduced both a "fairness tax" and a capital gains tax, while Switzerland has abolished or is phasing out some of its special regimes.

Even without legislative change, some countries are reinterpreting existing regulations in light of the BEPS initiative. These early changes could nudge countries adopting a wait-and-watch approach to start the process.

Regular conversations with your tax advisers to keep abreast of the changes would manage the element of surprise. These changes are so rapid that what worked last year might not work this year or next.

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