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A Thailand Perspective on BEPS

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Following the release of the OECD BEPS deliverables, evidence suggests that the Thai authorities will respond comprehensively to the initiatives, however, the government is yet to issue a formal announcement as to its policy intentions.

I. Background

International tax avoidance and transfer pricing have recently received an unprecedented high level of attention. High profile examples include technology companies such as Google, Apple and Amazon making the headlines for complex tax structures involving Ireland and Netherlands entities; and Starbucks, which has experienced store boycotts in the U.K. due to its lack of contribution to U.K. tax revenue over several years.

Many of these aggressive tax and transfer pricing structures have been in place since international trade within multinational (MNC) groups increased and double tax agreements were first introduced. So why is it only now considered a critical issue? There is no definitive answer to this but it is most likely a result of the growing significance of intangibles in the value chain of MNCs, given intangibles are very easy to move around for tax advantage; and the ongoing fiscal crisis in Europe and the US in particular creating ongoing pressure for tax revenue.

The OECD has responded in an uncharacteristically prompt, detailed and pragmatic manner through the introduction of a series of action plans designed to address BEPS.

The BEPS Action Plan contains 15 action points addressing the perceived shortcomings in international tax principles as they are currently applied. Broadly, these action points cover a lack of tax information exchange, ineffectiveness of transfer pricing rules and mismatches between tax systems of different countries.

The 15 actions are as follows:

- Action 1: Address the tax challenges of the digital economy;
- Action 2: Neutralize the effects of hybrid mismatch arrangements;
- Action 3: Strengthen CFC rules;
- Action 4: Limit base erosion via interest deductions and other financial payments;
- Action 5: Counter harmful tax practices more effectively, taking into account transparency and substance;
- Action 6: Prevent treaty abuse;
- Action 7: Prevent the artificial avoidance of permanent establishment (PE) status;
- Actions 8, 9, 10: Assure that transfer pricing outcomes are in line with value creation;
- Action 11: Establish methodologies to collect and analyze data on BEPS and the actions to address it;
- Action 12: Require taxpayers to disclose their aggressive tax planning arrangements;
- Action 13: Re-examine transfer pricing documentation;
- Action 14: Make dispute resolution mechanisms more effective; and
- Action 15: Develop a multilateral instrument (to amend bilateral tax treaties).

The timeline for finalizing the BEPS project is ambitious by any standards. Several of the above reports have already been released in draft or final form and the goal is to release the remainder before the end of 2015. The approach has recently been endorsed by the G-20, and various tax authorities in Asia and worldwide have responded quickly and positively to the reports and the pace of reform.

It is noted that the OECD is not a law making body and its initiatives and releases have no direct impact on country tax legislation and enforcement. However, the overwhelming support for these initiatives, as well as Action 15, which, if it is accepted, will allow for the more than 3,000 double taxation agreements (DTAs) globally to be adjusted without the need for each to be separately negotiated, will ensure that BEPS actions

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can be integrated into DTAs and international tax practice within a short time period.

The below is focused particularly on Action 13, as it is a significant evolution of current practice and will deliver the level of transparency and information exchange that is currently lacking in the international system, which will have a direct impact on transfer pricing and tax policy and enforcement in Thailand.

II. Action 13: Transfer Pricing Documentation

Action 13 proposes significant amendments to Chapter 5 of the OECD Guidelines, pertaining to transfer pricing documentation. These proposed amendments will transform Chapter 5 of the OECD Guidelines from broad documentation recommendations to specific, prescriptive documentation and reporting standards. Significantly, however, the OECD has not yet recommended a specific effective date for the changes to Chapter 5 to take place and, from a practical perspective, the actual effective date for the changes will depend on the domestic law of the adopting states.

The OECD has recommended a three-tiered documentation approach that includes:

- A Masterfile to provide a high-level view of a company's business operations and important information on a company's global transfer pricing policies on intra-group services, intangibles, and financing;
- A Country by Country (CbC) reporting template to provide a global financial snapshot of a multinational; and
- Local country files or reports that provide transaction-level transfer pricing and local entity profitability analyses to demonstrate compliance with the arm's length principle by the local country entity.

CbC reporting is a new concept for the international tax world and it represents the biggest change in the revised Chapter 5. The CbC report is a separate and distinct report from the global Masterfile document and is to be prepared in accordance with the template provided by the OECD in the revised Chapter 5.

The current draft of the CbC report template includes eight items that need to be detailed in the CbC report:

(1) Revenues (split between external and related-party revenues);
(2) Profit/(loss) before tax;
(3) Cash income tax paid;
(4) Accrued income tax;
(5) Capital;
(6) Accumulated earnings;
(7) Number of employees; and
(8) Tangible assets.

MNCs need to be aware of the risk management issues associated with this new reporting regime. Clearly, their transfer pricing positions and business operations will become significantly more transparent and there is a risk that additional commercially sensitive information may need to be disclosed to tax authorities. There are also issues as to the quantity and quality of the information that needs to be collated, analyzed and submitted. These risk management matters have significant corporate governance implications and therefore MNCs will need to give detailed consideration as to their internal compliance and governance policies and procedures.

Most tax authorities will be reviewing the new Chapter 5 and assessing how those proposals can be applied in the context of their local documentation rules (if any) and where amendments may be required. Hopefully, those governments and tax authorities are considering the key issues associated with the need to balance access to information that is useful to tax authorities, the maintenance of commercial confidentiality and ensuring that the compliance requirements are not excessive and disproportionate to the benefits gained by the tax authorities.

III. Implications for Thailand

Although there has been no official pronouncement from the Thai Revenue Department (TRD) in relation to BEPS, there is significant evidence available that points to a prompt and comprehensive approach:

- Responses from the TRD to the United Nations (UN) questionnaire on BEPS indicated they are very conscious of global developments and considering the appropriate actions;
- The Thai corporate tax rate has been cut from 30% to 20%, in addition to reductions in personal tax rates, as well as the undertaking of several large infrastructure projects. These measures have significantly heightened the pressure on tax collection;
- Thailand's ASEAN neighbors, including Vietnam and Indonesia, have significantly tightened up their tax enforcement regimes and introduced mandatory transfer pricing rules and other anti-avoidance measures. In this respect Thailand has some ground to make up in the near future;
- Thailand is highly dependent on small and medium enterprises (SMEs) to drive economic growth and employment. Any tax policy that is perceived to provide an advantage to MNCs over local SMEs is damaging to confidence and growth; and
- Recent political challenges in Thailand have accentuated the need to establish a more stable investment climate, which includes certainty on tax treatment of transactions in line with international norms.

All of the above will create significant impetus for Thailand to support and follow the approaches of the OECD, G-20 and their Asian neighbors with regard to measures to fight BEPS.

IV. Thailand Transfer Pricing Pre- and Post-BEPS

Thailand has had transfer pricing guidelines in place since 2002 (DI Paw 113/2545) and Advance Pricing Agreement (APA) guidelines since 2010. However, the 2002 guidelines do not impose a compulsory documentation requirement and have been enforced in a somewhat ad hoc and unsystematic manner with a focus on the largest taxpayers or specific industry groups only.

It is understood that new transfer pricing regulations and documentation rules will be released next year. There is no reason to think these rules will not be in line with the OECD's guidance in Action 13, i.e. compulsory documentation and detailed reporting on the entire value chain.

To implement these measures consistently and thoroughly, resources at the TRD will need to be enhanced. The encouraging point is that this is happening already. A separate transfer pricing audit team, focused on the largest taxpayers, has been in place for some time and recently this team has been training and developing general tax audit staff across the country. This cooperation, including the escalation of difficult transfer pricing issues to the specialist central team for resolution, is a strong indication of the direction in which the TRD is moving. BEPS will only accelerate this trend.

Thailand has an APA regime in place and has concluded around 20 bilateral APAs to date. APAs will form an important element of the tax regime under BEPS as taxpayers and tax authorities seek to agree on an appropriate and balanced tax outcome. Up to now, APAs have been negotiated by the transfer pricing audit team at the TRD, which sends the wrong signal to taxpayers about the extent of cooperation and confidentiality that can be expected. It is understood that these teams will be separated in future, which is a very welcome development.

Transfer pricing is only one, but critical, aspect of BEPS. As an indication of the policy direction, in response to the UN questionnaire, the TRD highlighted what it considered to be the most common distorting practices: excessive debt pushdown, artificial business restructuring, treaty abuse and avoidance of permanent establishments in the e-commerce sector. Regulations and guidelines to address these issues, coupled with greater exchange of information with treaty partners, will bring these issues into the spotlight together with transfer pricing.

V. Conclusion

Despite the lack of formal policy announcements or regulatory changes at this point, all evidence suggests that Thailand will respond fully and comprehensively to BEPS initiatives, in line with its neighbors and global developments. In particular, transfer pricing and the likelihood of a mandatory documentation rule as well as greater transparency through CbC reporting will have a profound impact on the transfer pricing and compliance and enforcement regime in Thailand.

Other aspects of BEPS are expected to lead to further regulations on thin capitalization, treaty shopping and anti-avoidance in the near future. Increased resources at the TRD and greater global and regional sharing of resources will ensure that the TRD is well placed to deal with these challenges. It is therefore imperative that taxpayers doing business in Thailand rise to the challenges that BEPS will create, ensure their tax and transfer pricing models are robust and supported with the appropriate level of documentation.

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