

The logo for BDO, featuring the letters 'BDO' in a bold, blue, serif font. The letters are set against a white background with a light gray gradient. A thick red horizontal bar is positioned below the letters, and a thick red vertical bar is positioned to the left of the 'B'.

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# Tax planning for optimizing withholding tax credits

**Paul Ashburn**

**Senior Partner**

**BDO Richfield Advisory Limited**

**Tax & Legal Services**

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**BDO Richfield Advisory Limited**  
Tax & Legal Services

# Outline

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- WHT – the basics
- WHT – excess credits
- WHT planning
- Corporate tax rules for foreign income
- Foreign tax credit relief
- Foreign dividend taxation



## WHT basics

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- Withholding taxes are simply a way of collecting income tax in advance at source
- In practice it expands the income base of the Revenue
- Onus on the payer to pay tax rather than recipient
- Cash basis v accrual basis – timing difference
- Typically rates range from 1% - 5%



## WHT – excess amounts

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- Can only be treated as a tax credit in the year in which the tax is deducted.
- Cannot be claimed as an income tax deduction.
- Tax refund is not automatic – must request refund and undergo tax examination.
- Excess tax credits not refunded may trigger tax examination anyway!



## Withholding tax credits - Example for refund

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Profit before tax	<u>500</u>
Corporate income tax @ 30%	150
WHT credit – DR Taw Paw 4	(175)
WHT credit – Section 69 bis	<u>(25)</u>
Tax refundable	<u>(50)</u>



## Excess WHT refunds – time limits

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WHT provision	Time limit
Department Regulation Taw.Paw. 4	3 years from the last day of the year in which the amount was deducted
Section 69 ter	3 years after last date for filing the return (exceptions apply)
Section 69 bis	3 years after last date for filing the return (exceptions apply)

## **WHT tax rates – minimum net profit**

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WHT rate	Min net profit percentage	
	<b>30% tax rate</b>	<b>25% tax rate</b>
5%	16.67%	20%
3%	10%	12%

## WHT Planning Ideas

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WHT planning often seeks to avoid an excess tax credit position at year-end. Such planning may include a review of the following:

1. Timing of income recognition v receipt
2. Income characterisation
3. Income splitting e,g. carve out goods portion
4. Bottom line management



## WHT – timing

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- Revenues recognised on accrual basis
- WHT credits follows cash basis
  - Excess WHT credit expected next year - bring forward the collection of receivables.
  - Excess WHT credit expected this year - defer collection of receivables.



# Excess WHT credits

## - Timing

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	Yr 1	Yr 2	Yr 3	Total
Gross Income	(80) 100	(120) 170	(100) 30	300
<b>Net income</b>	<b>20</b>	<b>34</b>	<b>6</b>	<b>60</b>
Thai tax payable @ 30%	6	10.2	1.8	18
Tax credit	(2.4)	(3.6)	(3)	(9)
<b>Tax payable (refundable)</b>	<b>3.6</b>	<b>6.6</b>	<b>(1.2)</b>	<b>9</b>

# Tax Planning Ideas: Nature of contractual relationship

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- Consider income characterisation as a result of contractual relationship
- Often hire of work contracts with significant materials component are focus of WHT planning
- Split of contracts
  - Split type of contract: sale of goods and provision of service
  - Split the contractual parties: seller and service provider
  - Split of contracts is not prohibited under Thai law whilst the real intention is acceptable



# Tax Planning Ideas: During negotiation and drafting - split of contracts

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*Supreme Court Judgement No. 4450/2542*

- Split of sale price and service fees in one contract concerning the construction of telephone exchange and installation
- The Supreme Court ruled that real intention of contractual parties is acceptable



# Split of hire of work and sale of goods contracts – some points to consider

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1. The intention and the practice of the contractual parties must be considered i.e. whether the contract concentrates on the transfer of ownership of goods or the result of the work performed.
2. A contract for the sale of goods would normally concentrate on the materials used that result in the finished product whereas a hire of work contract concentrates on the result of the work performed.
3. Split of sale price and the fee for hire of work in one contract can be acceptable
4. The terms of payment for materials and equipment should not tie to the completion of hire of work.



# Tax effects from the split of entities

## Entity selling materials

## Entity providing labor

Recognition of income upon sale of goods	Recognition of income according to completed work
There is no WHT on cost of goods sold.	The labor cost shall be subject to WHT.
Materials and goods report is required under VAT purposes.	Materials and goods report is not required.
Tax point for VAT arises upon the delivery of goods.	Tax point for VAT arises upon the receipt of the payments.
There is no stamp duty on the written contract.	Value of labor shall be subject to stamp duty if it is made in writing.



## Hire of work & transport contracts

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<b>Tax Liabilities</b>	<b>Hire of work</b>	<b>Transport</b>
<b>Withholding tax</b>	3%	Domestic= 1%
<b>VAT</b>	7%	Domestic= exempt Air and marine International= 0%
<b>SBT</b>	No	No
<b>Stamp duty</b>	0.1%	No

## Space rental & service contracts

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<b>Tax Liabilities</b>	<b>Services</b>	<b>Space rental</b>
<b>Withholding tax</b>	3%	5%
<b>VAT</b>	7%	Exempt
<b>SBT</b>	No	No
<b>Stamp duty</b>	0.1%	0.1%

## Hire purchase v Leasing

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Hire purchase	Leasing
Hire of asset with <b>CONDITION</b> to purchase	Lease of asset with <b>OPTION</b> to purchase
Ownership will transfer at the end of installments	Ownership may or may not transfer at the end of installments
Void if agreement is not concluded in writing	Written evidence is required for civil lawsuit

## Hire purchase & leasing contracts

<b>Tax Liabilities</b>	<b>Hire purchase</b>	<b>Leasing</b>
<b>Withholding tax</b>	No	5% (nil if meet requirements of DRTawPaw. 4/2528)
<b>VAT</b>	7%	7%
<b>SBT</b>	No	No
<b>Stamp duty</b>	0.1%	No



## Possible exposures

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1. Shortfall of withholding tax amount
2. Surcharges 1.5% per month of withholding tax remittable or fraction thereof (maximum equal to withholding tax remittable)
3. Possible liability to stamp duty depending on the contract and surcharges maximum 5-6 times of shortfall (with scope for reduction).

# Taxation of income

## - Thai income tax calculation

	Scenario 1	Scenario 2
Net profit before bonus	200	200
<b>Less: bonus</b>	<b>100</b>	<b>-</b>
Net profit	100	200
<b>Tax payable (30%)</b>	<b>30</b>	<b>60</b>
Less: WHT credits	40	40
Net tax payable/refundable	(10)	20



# Taxation of income

## - Thai income tax calculation

	Scenario1/ Bonus	Scenario 2/ Dividends
Bonus/dividend	100	78
Less: tax	30	8
<b>Net bonus/dividend</b>	<b>70</b>	<b>70</b>
<b>Total tax paid</b>		
Corporate income tax	40	60
Personal income tax	30	8
<b>Total tax</b>	<b>70</b>	<b>68</b>



## WHT –branch offices

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- 5% WHT rate applies to payments for hire of work to a foreign co carrying on business in Thailand without a permanent branch office.
- 3% WHT if a permanent branch office. Must either
  - Own its place of business.
  - Engage in other business besides hire of work.
  - Have a provident fund set up for employees.



# Corporate taxation of foreign income

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- General principle is that a Thai company is taxed on its worldwide income - overseas income such as branch profits/dividends are taxable
- Accruals basis applies for recognising most forms of income (Section 65; Revenue Department Regulation No.Taw.Paw 1/2528)
- Foreign capital gains are taxable as ordinary income
- Unrealised foreign exchange gains and losses are taxable



# Corporate taxation of foreign income

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- Market value rules for international transactions – transfer pricing rules to consider for transactions with related parties
- Generally, expenses incurred for the purpose of acquiring profits or for conducting business overseas are deductible
- No quarantining of foreign tax losses
- Regional operating headquarters have special tax privileges for certain classes of foreign income



# Foreign tax credits

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## Royal Decree No.300 under the Revenue Code

- Foreign tax credit (“FTC”) is available for tax paid on income in a foreign country.
- Separate income from a business carried on overseas e.g. an overseas branch and income paid from overseas e.g. a service fee
- Separate income on a country per country basis



## Foreign tax credits

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- Compare FTC per country with Thai tax payable on the foreign income
- FTC cannot exceed the Thai tax payable
- Detailed rules, procedures and conditions for claiming FTC can be found in Notification of the Director General of Revenue on Income Taxes No 65.
- A double tax agreement may provide greater scope for foreign tax credits



# Foreign tax credits

## - Example for branch profits

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	Foreign country A (35% tax rate)	Foreign country B (20% tax rate)
Branch profit before tax	<u>500</u>	<u>500</u>
Thai corporate income tax @ 30%	150	150
Foreign tax credit	<u>(175)</u>	<u>(100)</u>
Thai tax payable (foreign tax credit excess)	<u>(25)</u>	<u>50</u>



# Thai Taxation of Foreign Dividends - old rules

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- Generally
  - Foreign source dividends are subject to Thai tax
  - A foreign tax credit (“FTC”) is available for tax paid on the dividend in the foreign country
  - Where a DTA permits, the FTC available can include the tax paid by the dividend paying company, in its home jurisdiction, on the profits out of which the dividend is paid (“Underlying Tax”)



# Thai Taxation of Foreign Dividends - new rules

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- Royal Decree No 442 under the Revenue Code
  - Provides for foreign source dividends to be exempt from Thai tax where:
    - Thai shareholding company holds at least 25% of the voting shares of the foreign dividend paying company; and
    - the shares on which the dividend is paid were held by the Thai shareholding company for at least 6 months prior to the receipt of the dividend; and



# Thai Taxation of Foreign Dividends

## - new rules

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- the dividend must be paid out of net profits which were subject to income tax in the home jurisdiction of the dividend paying company at a rate of not less than 15%, regardless of whether or not the law in the foreign country allows for reduction or exemption from tax on net profits.
- Applies to qualifying dividends received on or after 24 November 2005.



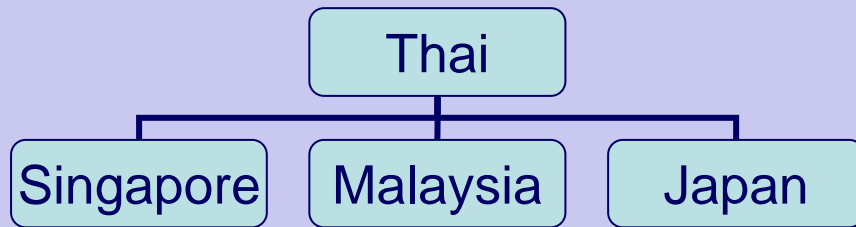
# Thai Taxation of Foreign Dividends - new rules

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- The 25% minimum shareholding rule is similar to some DTAs that allow underlying tax credits
- Some DTAs with Thailand provide minimum shareholding rule of 10% or 15% only in order to access underlying foreign tax credits
  - A DTA may therefore still be beneficial for shareholdings less than 25%



# Proposed investment structure



Wholly owned subsidiaries

**1. All three foreign countries have income tax rate >15%**

**2. Dividend WHT rates**

Singapore	NIL
Malaysia	NIL
Japan	20%

# Taxation of Foreign Dividends

## - Thai income tax calculation (old rules)

	Japan	Singapore	Malaysia	Total
Dividend	100	100	100	300
<b>Foreign WHT payable</b>	<b>20</b>	-	-	<b>20</b>
Thai tax payable @ 25%	25	25	25	75
Foreign Tax credit	(20)	-	-	(20)
Underlying tax credit	-	-	(25)	(25)
<b>Tax payable in Thailand</b>	<b>5</b>	<b>25</b>	-	<b>30</b>
Net dividend after tax	75	75	100	250



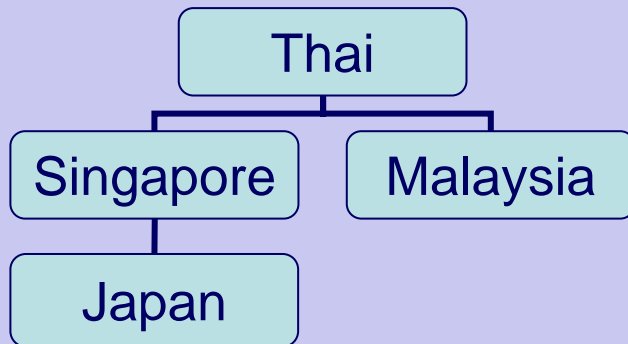
# Taxation of Foreign Dividends

## - Thai income tax calculation (new rules)

	Japan	Singapore	Malaysia	Total
Dividend	100	100	100	300
<b>Foreign WHT payable</b>	<b>20</b>	-	-	<b>20</b>
Thai tax payable @ 25% (exempt)	-	-	-	-
<b>Tax payable in Thailand</b>	-	-	-	-
Net dividend after tax	80	100	100	280



## Alternative investment structure



Japanese subsidiary is a wholly owned subsidiary of Singapore

Under Singapore-Japan DTA the dividend WHT rate is 5%.

The main condition is that Singapore owns at least 25 per cent of the voting shares of Japan during the period of six months immediately before the end of the accounting period for which the distribution of the profits takes place.

# Singapore

## Foreign dividend tax treatment

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- A foreign source dividend, being a dividend paid by a company that is not a tax resident of Singapore, may be exempt from Singapore tax.
- The 5% withholding tax cannot be utilized as a tax credit in Singapore.
- If paid as a dividend to Thailand, then should not qualify for tax exemption under Royal Decree No 442 i.e. not paid out of profits subject to income tax in Singapore.



# Singapore

## Foreign dividend tax treatment

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- A Singapore company can elect out of the tax exemption and include foreign dividends as taxable income and claim foreign tax credits instead.
- The 5% withholding tax can be utilized as a tax credit in Singapore.
- Singapore – Japan DTA allows an underlying tax credit in Singapore for tax paid in Japan on the profits out of which the dividend is paid.
- The result? No further tax payable in Singapore and dividend qualifies for tax exemption in Thailand



# Taxation of Foreign Dividends

## - Thai income tax calculation

	Singapore	Malaysia	Total
Dividend	195	100	295
<b>Foreign WHT payable</b>	-	-	-
Thai tax payable @ 25% (exempt)	-	-	-
<b>Tax payable in Thailand</b>	-	-	-
Net dividend after tax	195	100	295



# Questions from the floor



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## Presenter profile

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<b>Name</b>	Paul Ashburn
<b>Position</b>	Partner, Tax & Legal Services
<b>Expertise</b>	Tax planning for foreign investment, international taxation, mergers & acquisitions
<b>Contact details</b>	Tel: +66 2 260 7290 Fax: +66 2 260 7297 E-mail: <a href="mailto:paul.ashburn@bdo-thai.com">paul.ashburn@bdo-thai.com</a>



## **BDO profile**

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BDO Richfield Advisory Limited specialises in providing tax and legal services to multinationals operating in Thailand and the Asia Pacific region.

BDO Richfield Limited, the Thailand member firm of BDO international, is one of the largest accounting and advisory firms in Thailand.



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# **BDO Richfield Advisory Limited**

## **Tax & Legal Services**

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28th Floor, CTI Tower

191/16 New Ratchadapisek Road

Klongtoey, Bangkok 10110

Thailand

Telephone: +66 2 260 7290

Fax: +66 2 260 7297

Website: [www.bdo-thai.com](http://www.bdo-thai.com)



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