What do we "EXPECT" from the Board?

"Where do Board members work?
(Continued from the last issue)

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In a "Board Resolution" of one public company, mistake had been made before the directors "cast their votes" – even before "setting the agenda". It emerged that the authority of the Board was not validated and the "objectives of the company" do not technically allow the company to conduct the actions the Board is taking on its behalf.

Following the resolution being passed, the Board granted approval for the parent company (which is also a public company) to provide loan guarantee for its "affiliate" with commercial banks, a move beyond the parent company's authority (Ultra Vires). The issue got worse as the action undertaken could not obtain ratification from a shareholders meeting because the "company objectives" do not allow so.

Whose responsibility to monitor and prevent the mistake to happen (Preventive Approach Adoption)?

To be exact, the "Corporate Secretary" has the duty to "ensure" full compliance with laws and regulations under securities law. Putting aside the Corporate Secretary's duty, the Chairman of the Board should also "scrutinize" the meeting agenda, content, and meeting documents prior to the issuance of the notice of the Board of Directors meeting (Authorization Check).

Separate but related, you may also give thought to an "intracompany loan" concerning "interest rate" and "special business tax".

In the case that a "parent company" relends bank loan to its "affiliated company", how should the interest rate be charged to clear the issues on "Related Party Transactions" and Transfer Pricing? The answer to this question is the "Market Price". Still, the Revenue Department has a number of tax rulings indicating that the rate should be based on the "cost of funds" and appropriate "cost plus" pricing. Therefore, when the "parent company" borrows money from banks and relends to affiliated company, the parent company must charge interest at the rate not less than the rate charged by the bank. For example, if the parent company borrows money from bank at MRR-xxx, it should add xxx% of profit when relending the bank loan to its associated company. The Revenue Department did not specify clearly how to determine the pricing. A prudent solution is recommended that the "parent company" conduct a benchmarking analysis from the interest rates commonly charged in the industry. The analysis shall also be documented as it is the backbone of transfer pricing documentation. The basis of charging the interest could possibly be questioned in the future.

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Besides the "interest rate", "specific business tax" and "stamp duty" should also be taken into account when it comes to intracompany loan in order to comply with applicable law.

Does the Board Know Related Party Transaction is also Transfer Pricing Issue?

Intracompany lending, either in the form of intracompany loan or cash pooling arrangement, is considered as "business with regular transactions similar to commercial banks" and subject to 3.3% specific business tax.

However, if the following conditions are met, "specific business tax" shall be exempt (refer Royal Decree No. 571):

Associated companies or juristic partnerships (exempted from specific business tax)

"Associated companies or juristic partnerships" means at least two companies or juristic partnerships that one company or juristic partnership ***holds shares or partners in other company or juristic partnership from 25% of the total shares with voting rights for no less than six months prior to the borrowing date.*** *The six-month requirement also covers the period of shares held by companies that have undergone an amalgamation or an entire-business transfer.*

From the above, "associated companies" are determined by "shareholding test", not "control test" nor "economic test". In a way, it is safe to say that this tax legislation does not consider the "substance over form" basis which is commonly found in accounting standard or securities law. In addition, a "time test" must be met in order to be exempt from specific business tax according to this provision. It is understood that the associated company status must endure a certain period, significant enough to be legally eligible for intracompany lending benefit. This type of transaction is not to be conducted in the case of sudden shareholding without certainty. It should also be noted that the six-month shareholding requirement is meant to prevent "tax evasion". Without such additional "condition", this "channel" of short-term "shareholding" may be used for abusive tax planning to exploit undue specific tax exemption.

Does the Board know about taxes for the business? What are other taxes imposed from intracompany lending besides income tax and specific business tax?

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Stamp duty is another tax that "lender" is obliged to pay to the Revenue Department for executing a "loan agreement". The stamp duty is payable on a loan agreement at 0.5% of the contract value but not exceeding Baht 10,000.

According to the law, a "loan agreement" requires signatures from both lender and borrower while only a signature of the borrower is required in an "evidence for the loan" to enable the "lender" to take legal action against the borrower. The Supreme Court has ruled several precedent cases in alignment with law. One notable point is made that the "evidence for the loan" does not require stamp duty because it is not considered as instrument subject to stamp duty.

When consideration is given to other intracompany financing alternatives other than intracompany loan...can the Board approve it?

A number of companies "chose" debt instruments such as bills of exchange (B/E) or promissory notes (P/N) instead of intracompany. These bills require a fixed amount of stamp duty at Bath 3 per bill regardless of the contract value specified on the bills.

Pursuant to the law, a bill is an "evidence of rights over debt". In accounting practice, bills are booked as liabilities in the financial statements of issuers while they are booked as "receivables" in the asset side of holders' (creditor) balance sheets.

Is "Evidence for Loan" or "Bills" considered "tax evasion" scheme (specifically Stamp Duty)?

The answer would be based on "corporate policy" and "practices" of each company that establishes "Treasury Policy & Practice" within its group considering business purposes and corporate structure. The choice of treasury management should reflect economic substance, not sham transaction and tax should not be the key concern when establishing such policy.

Moreover, using bill as a tool to replace intracompany loan agreement is legally accepted by external auditors and the Revenue Department. Listed companies in Thailand and a great deal of multi-national corporations also recognize and widely accept the practice. Therefore, it could be said that the risk of tax evasion is extremely low.

Back to the first question, "Where do Board members work?" reaches a conclusion that the "Board" is capable to work anywhere. The directors' performance reflects through the minutes of the Board of Directors meeting where the Board members work under an official framework as a committee collectively contribute their parts in the Board's meeting.

In the next article, I will continue to talk about "Fiduciary Duty...what are the duties of the Board?"