Foreign Direct Investment in Thailand: "Business As Usual"

Thailand is currently in the midst of one of the worst natural disasters in its recent history. The catastrophic 2011 floods have so far claimed more than 500 lives, left tens of thousands homeless, and brought production to a standstill in many large-scale manufacturing plants throughout the country. Unfortunately, however, the floods are merely the latest in a litany of natural disasters and political convulsions that have plagued Thailand for almost a decade.

First, there was the devastating tsunami in 2004 followed by the ousting of democratically elected Prime Minister, Thaksin Shinawatra, by a military coup on September 19, 2006. Since then, Thailand has endured five years of political instability and upheaval, resulting in the week-long occupation of Bangkok's international airport by anti-government protesters in November 2008, the storming of the venue for the ASEAN Summit by protesters leading to the Summit's cancellation in 2009, and culminating in the May 2010 political rallies in Bangkok which ended in street riots and more than 86 fatalities, hundreds of injuries, and an estimated damage bill of over US$1.25 billion.

One might be forgiven for thinking that all of this must have been disastrous for business. Think again. In fact, by all accounts, business in Thailand appears to be booming − particularly in the area of foreign direct investment.

Why Invest in Thailand?

Despite the recent downward revision of Thailand's economic growth forecast by the Ministry of Finance on September 28, 2011, largely as a result of the fiscal difficulties in Europe and the US economic performance, as well as the prolonged flood damage in 26 provinces throughout the country, the Thai economy remains robust.

The Bank of Thailand announced on September 30, 2011 that, for the month of August, exports were up by 28.4% compared to the same period in 2010 and that foreign currency reserves at the end of August 2011 were US$188.3 billion (up US$700 million from the previous month). In addition, foreign direct investment in Thailand is at record levels. The Thai Board of Investment ("BOI") reported that, between January and July 2011, there were 679 investment applications by foreign capitalized companies, with a total aggregate investment of THB 215.4 billion, up 76.4% compared to the same period in 2010. Japan continued to be the most active investment nation, with 361 applications, followed by Singapore, Hong Kong, South Korea, Taiwan, and Malaysia. Japanese companies invested a total of THB 105 billion, an increase of approximately 111% over the same period for 2010. Politics aside, these are impressive by any measure.

So why is it that with all of the instability and upheaval of the last decade, foreign investors continue to flock to Thailand?

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First, the risks associated with the political shenanigans of the last five years have not created a shift in government policy vis-à-vis foreign direct investment, nor did they affect the flow of business transactions or the general ease of doing business in Thailand. In fact, in June 2011, the World Bank ranked Thailand 17th in the world and 3rd in the Asia-Pacific Region in its Ease of Doing Business Index. The Index ranks a total of 183 countries with reference to 10 topics important to foreign investors, namely, starting a business, dealing with construction permits, registering property, getting credit, protecting investors' rights, paying taxes, trading across borders, enforcing contracts, resolving insolvency, and getting electricity. It is also important to note that Thailand ranked 13th in the world in the category of protecting investors' rights − an issue which is of critical importance to foreign investors.

Secondly, and perhaps more importantly, Thailand gets a big tick when it comes to meeting the basic needs of the foreign investment community. Apart from having a strong economy, a legal system that is fully functioning and transparent, and a government that is highly supportive of foreign investment, the investment incentives granted by the BOI are generous, labour is cost-effective, and Thailand's infrastructure is world-class. As the most recent statistics clearly show, the combination of these positive attributes certainly outweighs any perceived risks associated with the political troubles that Thailand has experienced over the last five years.

The Incentives

The BOI oversees almost all tax and non-tax incentives and privileges applicable to foreign investment in Thailand. At present, there are approximately 200 types of business that are eligible for BOI privileges[1]. Some of these businesses include those that would otherwise be restricted to foreigners under Thailand's Foreign Business Act 1999 ("FBA"), the cornerstone piece of legislation relating to non-BOI-approved foreign investment in Thailand. This incentive alone is very attractive to many foreign investors, as it obviates the need to apply for a foreign business licence (see next section) or enter into joint venture arrangements with a Thai partner.

Other incentives offered by BOI to eligible foreign investors include majority shareholding by foreigners, acquisition of land for industrial use by foreign corporations, exemptions from or reductions of import duties on machinery and raw or essential materials, exemptions from or reduction of corporate income tax up to a maximum of 8 years, and financial assistance in the installation of electrical power and water utilities.

In August 2011, the BOI announced that it plans to reduce privileges in certain industries and to focus on offering incentives to only four main business sectors − infrastructure, high technology, service industries based on domestic raw materials, and industries that use Thailand as a production base. The proposed changes will take place gradually over the next five years, and are not anticipated to have any retrospective effect on existing BOI-approved businesses. These changes, together with government's recently announced proposal to cut the corporate tax rate in 2012 from 30% to 23%, are expected to increase Thailand's competitiveness in the region and to encourage new investment.

1 Investors must meet minimum capital investment requirements to become eligible for BOI privileges.

The Dos and Don’ts for Foreigners

Not all foreign investors are eligible for BOI approval. This is usually due to the fact that they do not meet minimum capitalization and investment requirements, or their business is one which is not part of the BOI’s incentive program. Except for US corporations and US nationals that are granted protection under the Thai-US Treaty of Amity and Economic Relations mentioned below (“Thai-US Treaty”) and those foreign investors who have entered into a joint venture arrangement with a Thai partner who owns at least 51% of the shares of the joint venture company, foreigners wishing to invest in Thailand will be subject to the prohibitions and restrictions on foreign investment contained in the FBA.

Schedule 3 of the FBA sets out three “lists” of business categories in which the participation of foreigners is either prohibited or restricted. Foreigners are prohibited from participating in the businesses specified in List 1, which includes antiques trading, broadcasting, farming, and forestry. Foreigners are restricted from participating in businesses specified in List 2 unless they obtain a foreign business licence (“FBL”) from the Ministry of Commerce and approval from the Thai Cabinet. List 2 includes activities concerned with national safety, agriculture, arts and culture, and natural resources and environment. Finally, foreigners are restricted from participating in the businesses specified in List 3 unless they obtain an FBL from the Director-General of the Department of Business Development with the approval of the Foreign Business Committee. List 3 contains a total of 21 categories of restricted businesses, including fisheries, forestry, accountancy, engineering, construction (with certain exceptions), retailing and wholesaling (with certain exceptions), advertising, hotel operation (excluding hotel management), tourism, sale of food and beverages, and the catch-all category know simply as “other services”.

A foreign investor who obtains an FBL for any business specified in List 2 or List 3 of the FBA may carry on such business in Thailand on its own without seeking a Thai partner.

For the purpose of the FBA restrictions, a “foreigner” is classified as a foreign individual, a company incorporated outside Thailand, or a company incorporated in Thailand that is majority owned by foreign individuals or foreign companies. As noted above, US corporations that receive protection under the Thai-US Treaty are not subject to the restrictions set out in the FBA. There are, however, certain categories of business that even US companies with Thai-US Treaty protection are unable to carry out − including those involving land, communications, and inland transportation.

The FBA has often been the subject of criticism from the foreign investment community. One of the main criticisms is that List 3 of the FBA is too inclusive in the number of business categories that are subject to restriction, and that some business categories that are included in List 3 are too broadly defined − such as the “other service businesses” category (Item 21 of List 3).

There have been calls over the years to remove certain categories from List 3. Given the fact that the current administration has recently introduced steps to promote and encourage foreign investment, such as the proposed corporate tax cuts, it is not inconceivable that List 3 may be amended in favour of a more liberal environment in the coming years. However, the timing of any such amendments, or whether they will occur remains unknown.

The general perception of the foreign business community appears to be that obtaining an FBL is a time-consuming and uncertain business. The FBA provides a 60-day turnaround time following submission of an application to the Foreign Business Committee, although the clock on the 60-day period does not start to run until the relevant official from the Ministry of Commerce formally accepts the application for review by the Foreign Business Committee. The application will only be formally accepted when the relevant official is satisfied with the supporting documents and information provided by the applicant. It should be noted that the timeframe for the official's review is not specified by the FBA. Typically, therefore, the whole process could take from between 4 to 6 months to receive a final decision from the Foreign Business Committee, depending on the extent to which additional documents and/or information requests are made. There are also no guarantees that the outcome of the application will be favourable. The Foreign Business Committee will take into account many factors when making its decision − including, among others, the benefits the business will provide Thailand in the areas of natural resources, technology transfer, research and development, the size of the enterprise, and the opportunities for employment and training of Thai people. Foreign investors are encouraged to seek professional advice before submitting an FBL application to the Ministry of Commerce so as to maximize their chances of success.

Going Green

Thailand has recently adopted a number of special investment incentives to encourage investment in the green energy sector. This is partly in response to the Thai government's Strategic Plan for Renewable Energy Development − which requires 20 percent of the country's energy production to be from renewable resources by the year 2020.

Solar power now appears to be leading the charge in terms of green energy, outperforming other green energy platforms such as biomass and landfill gas. Thailand is a particularly attractive place for foreign investors in the solar industry due to its consistent solar radiation levels. In addition, solar projects are supported by the BOI, and the government provides additional incentives to investors through the provision of attractive "feed-in" tariffs.

In 2011, a record number of foreign corporations and government agencies, including the Asian Development Bank and International Finance Corporation, were involved in solar power projects in Thailand. Bloomberg's Global Trends In Renewable Energy Investment 2011 reported that renewable energy investment in Thailand rose by 320% over 2010. The vast majority of these investments were in large-scale solar PV projects.

The BOI has also announced the introduction of special tax incentives under its Investment Policy for Sustainable Development Program. The aim of the program is to encourage Thailand's competitiveness in science and technology, and to improve manufacturing quality and reduce the potentially negative environmental impact of manufacturing operations.

Existing manufacturing businesses, including both BOI-promoted and non-BOI-promoted, are eligible for substantial tax and import duty exemptions and reductions, as well as savings in utility costs, if they are able to meet criteria specified by the BOI. Applications under this program are open until December 31, 2012, and it is expected that many existing businesses will take advantage of these additional "green" incentives offered by the BOI.

Looking Ahead

The Thai people have experienced five years of political instability since the military coup of 2006. The current administration, which swept to power following the general election in July 2011, appears determined to mend past political fences and to pursue its goal of national reconciliation. This is a constructive shift in attitude and long overdue. Whether or not, and the extent to which, the government succeeds in this ambitious goal is still a matter of conjecture. However, if past experience is anything to go by, irrespective of Thai politics, it is likely that foreign investors will continue to look at Thailand as an attractive place to invest and do business.

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