Chapter 1

Introduction:

The Past, Present and Future of Thailand's Investment Climate and Its Surrounding Factors

The history of Thailand's economic development from 1950s has shown that Foreign Direct Investment (FDI) has played a crucial role in driving the economic expansion of the country. Thailand has established a regulatory infrastructure to harness the FDI in order to benefit its economy. Theoretically, one of the main legal instruments that the country needs to successfully implement a FDI policy is the FDI controlling measure. This regulatory device is universally accepted as a crucial legal institution that significantly effects the implementation of FDI policy, particularly in the developing country. This research aims to shade some light on the problematic aspects of the Foreign Business Act 1999 of Thailand, the key FDI controlling regulation in the country.

1.1 Background and the Essence of the Research Questions

In the past decades, it is clear that the global trading system has become much more liberalized, and the world economies have become increasingly integrated. It can be argued that this is the result of the successive rounds of trade negotiations under the auspices of the World Trade Organization (WTO), which have resulted in the progressive liberalization of both traditional and new sectors, such as trade in agriculture and services. Inarguably, the establishments of regional trading arrangements and free trade agreements, as well as the increase in international investment agreements around the world have also been conducive to this trend.[1]

[1] Number of BITs concluded, Cumulative and year by year from 1990-2004, UNCTAD (2005), http://www.unctad.org/iia.

I. The Proliferation of FDI in the Global Economy

Foreign direct investment (hereinafter denoted "FDI") has thus been rapidly growing in the global economy as a whole, and has been increasingly seen as an important stimulus to the industrial growth and development for many countries, namely those considered developing. In fact, several studies show that "FDI triggers technology spillovers, assists human capital formation, contributes to international trade integration, helps create a more competitive business environment and enhances enterprise development."[2]

As more and more people have begun recognizing the role of FDI in promoting national development, countries have reacted by creating various incentives designs in order to attract FDI. Granted, the proliferation of FDI has created both its benefits and disadvantages. Nevertheless, the tendency of the last few decades is quite clear: a growing number of countries have evolved or further evolved towards more hospitable FDI climates; i.e., towards more openness for inward FDI. This progressive shift towards more liberal investment regimes has often translated itself in numerous successive legislative and regulatory changes: more protection for foreign investors and their investments, the reduction or elimination of the differences of treatment between foreign and local investors, the reduction of entry and establishment conditions, the liberalization of the foreign exchange regulations and the promotion of FDI by incentives. Thus, trade and investment liberalization has been included into the national development agenda of many countries. The

[2] Baiashvili, Tamar & Luca Gattini, *Impact of FDI on economic growth: The role of country income levels and institutional strength*, EIB Working Papers 2020/02, European Investment Bank (EIB) (2020); OECD, Foreign Direct Investment for Development; Maximizing Benefits, Minimizing Costs, 5 (2002).

adoption of such toward a more increasingly integrated economy is particularly exemplified by developing countries such as Thailand.[3]

II. The Asian Financial Crisis of 1999

A significant turning point in Thailand's economic history was the Asian Financial Crisis of 1997. The crisis caused unpredictable and severely detrimental damages to the Thai economy as a whole. As a result, the government had to seek advice from international financial institutions, namely the International Monetary Fund (IMF) and the World Bank, in order to recover from crisis state to one of economic stability.[4] Since the crisis in 1997, Thailand has been an energetic participant in the world trade arena. The government at that time, led by Former Prime Minister Thaksin Shinawatra, saw trade liberalization as a priority in its economic agenda in order to boost the Thai economy, which suffered substantially from the crisis in 1997. Accordingly, as a strong supporter of free and fair trade, Thailand joined various regional and international forums, such as the Association of Southeast Asian Nations (ASEAN) including the ASEAN Investment Area, the Asia-Europe Meeting (ASEM), the Asia Pacific Economic Cooperation (APEC), the WTO, and is now in the process of considering to join the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). The country is also developing free trade arrangements and closer economic cooperation with countries across the world, especially bilateral trade agreements and foreign trade agreements.[5]

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[3] United Nations Industrial Development Organization (UNIDO), *Foreign Direct Investment in South-East Asia: Experience and Future Policy Implications for Developing Countries*, Report of UNIDO Expert Group Meeting (EGM), Bangkok, Thailand, 21-23, (2005).
[4] Okuda Hidenobu, Comment on "Ten Year After the Financial Crisis in Thailand: What Has Been Learned or Not Learned?", Asian Economic Policy Review, (2007).
[5] Ministry of Commerce, Trade Policy and Strategy Office, Thailand International Trade – January 2020, http://www.tpso.moc.go.th/sites/default/files/3.press_release_eng_inter_trade_jan_2020_final.pdf; Bangkok Post, *The time is Right for Thailand to Join the CPTPP*, 16 February 2021,

The post-consequences of the Asia Financial Crisis in 1997 along with the strong wind of trade liberalization that blew across the Asia region in the last two decades have caused Thailand to liberalize its economy as well as their domestic regulations in order to survive in this era of globalization. The result of the crisis in 1997 was the critical moment in the history that forced the Thai government to find alternative ways to bring back stability to the economy of Thailand. Export-oriented policy has become an importance tool to propel the Thai economy for a positive trajectory.[6] This also highlighted the significant role of FDI in the Thai Economy. As result, the government has implemented the regulatory reform to create more conducive environment towards the FDI regime. This led to the amendment of Foreign Business Act, the main FDI controlling measure of the country.

III. Understanding the Foreign Business Act (FBA) of 1999

The aftermath of 1997 Crisis has weaken the Thai domestic capital at that time, as most of the Thai investors were negatively affected by the event. The foreign injection through many foreign investment projects was a key element to foster the Thai economy. For reasons such as these, the government decided to liberalize domestic regulations in order to attract more FDI transactions into the Thai domestic market. Thus, many laws related to investment have been revised to facilitate the upcoming trend of foreign investments. As a consequence, the Foreign Business Act (FBA) of B.E. 2542 (1999) was enacted to replace the former Foreign Business Act, the National Executive Council Announcement (NECA) No. 281 of 1972 [*Por Wor* 281], in order to regulate the foreign business conduct in Thailand for the welfare of the Thai economic system.

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https://www.bangkokpost.com/opinion/opinion/2068955/the-time-is-right-for-thailand-to-join-the-cptpp; Sally Razeen Sally, *Thailand's New FTAs and Its Trade Policies Post-Asian Crisis: An Assessment, International Relation Department*, London School of Economics, (2005).

[6] Hidenobu (2007), *supra* note 4.

Following the 1997 financial crisis, a review of the former Foreign Business Act (FBA) of 1972 (NECA No. 281) was conducted under the advice from the World Bank and the IMF with a view of liberalization. Granted, the Act of 1972 had a positive impact to the industrial sectors as it allowed more foreign participation in most manufacturing industries. The Act of 1972 made the rule easier for foreign investors to enter into the domestic industrial market. Yet, the more restrictive nature relative to the former FBA of 1972 with its espousal of protectionism still remained the objective of the FBA of 1999. The protectionist view was adopted and included into the Act (as demonstrated in Annex 1) due to the fact that foreign business interests dominated many sectors of the Thai economy, and it was deemed necessary to provide some protection for Thai owned business entities until they could develop sufficiently, at least with regards to the circumstances at the time. However, the global FDI climate as well as the situation in Thailand have changed significantly in a recent years.[7] According to the Word Investment Report of 2020, the volume of international investment in services sector has considerably increased in recent years despite a dramatic drop of FDI around the world due to the Covid-19 Crisis.[8] Moreover, the digital economy has begun to create new challenges and opportunities for the international investment policy community around the world.[9] Thus, the content of the FBA is now irrelevant to the current international investment environment of Thailand.[10]

The FBA of 1999 has been rendered extraneous in two ways. First, the situation of Thai investor has changed. The domestic investors have become aware of the higher competition in the

[7] Michael V. Gestrin, and Julia Staudt, The digital economy, multinational enterprises and international investment policy, OECD, Paris, (2018), www.oecd.org/investment/the-digital-economy-mnesand-international-investment-policy.htm
[8] UNCTAD, Word Investment Report 2020, *International Production Beyond the Pandemic*, p.6 (2020).
[9] Gestrin & Staudt, *supra* note 7.
[10] The Proposal to Amend the Foreign Business Act (FBA) of B.E. 2542 (1999): Issues of Consideration, Ministry of Commerce, (2007).

domestic market since 1999, and have adapted their business strategies in view of that in order to compete in the current market situation. FDI in service sector has increasingly played an importance role in international investment regime. Also, a digital business transformation of Multinational Enterprises (MNEs) has started to survive in the technology disruption era. Thus, the same protection in the content of the FBA of 1999 should be reconsidered in accordance to the current market situation. Second, currently, the implementation of the FBA have still allowed (a) some very blatant nominee structures employed in order to avoid the law, and (b) some more sophisticated structures, which meet the specific requirements of the law (i.e. majority of shares owned by Thai 's and majority of Thai shareholders) but used preference shares and other legally supportable methods to allow foreign control and major economic interest, utilized in the same manner as before.

As for the second case, the more sophisticated structures provided in the Articles of Association refer to two kind of shares, namely (1) preference shares (which were held by Thai shareholders giving, a Thai shareholder one vote for each 10 shares held, and (2) ordinary shares (held by foreign shareholders, giving one vote per share held). Thus, a Thai shareholder holding 510 preference shares would have 51 votes, and a foreign shareholder holding 490 shares would have 490 votes. Under the preference shares, the Thai shareholder would get paid, for example, a return of 3-5% on capital invested (capped) as a dividend and all other dividends would go to the foreign shareholder. Therefore, the minority foreign shareholder has 90% of all the votes, and would get all the profit except for an amount of 3-5% on capital investment, which is paid to the Thai preference shareholder.[11]

[11] The Consideration Regarding the Amendment of the FBA of 1999 presented to the Ministry of Commerce, The Investment Policy Committee, The Board of Trade of Thailand, (2006).

Many companies in Thailand have used this mentioned structure with the approval by many registrars at the Business Registration Department, Ministry of Commerce of Thailand. The reason of the approval is that the above-mentioned structure in the memorandum and the article of a company is not in conflict with the Company Law nor does it impact the application of the FBA of 1999. Hence, this structure is seemingly valid under the law of Thailand and foreigners should therefore, be permitted to do so. Furthermore, the evaluation of this structure is very complex and time consuming. Also, it could take several years through the judicial system in Thailand. In consequence, there has not been any published events involving the prosecution of a Thai or a foreigner, or any orders made to close down the businesses, which use "nominees" in order to avoid the law.[12]

As a result of high profile transactions using a preference share structure in a strategic area of business, the government and the public have become aware of the various structures implemented to avoid the FBA of 1999, and their widespread use. For that reason, the Ministry of Commerce of Thailand has submitted a draft bill to amend the FBA of 1999 to the cabinet on the 9th of January 2007, in which it was approved in the principle of the proposal.[13] On May 14, 2007 the proposal to amend the FBA of 1999 was presented to the National Legislative Assembly, and later it was sent back to the Ministry of Commerce for further consideration as many Foreign Chambers of Commerce in Thailand expressed their considerations to the proposal to amend of the Act.[14] Even though the present situation of the amendment of the FBA of 1999 has diminished due to the political uncertainty that overwhelms the country and foreign political resistances, the

[12] *Id.*
[13] The Foreign Business Act Amendment: A Brief Explanation, Ministry of Commerce, Thailand, (2007).
[14] The Official Report Regarding the Concern of Foreign Counterparts to the Proposed Amendment to the FBA of 1999, Department of Trade Negotiations, Ministry of Commerce, (2007).

problematic aspects of the implementation of the FBA of 1999 still remain unsolved, and still are causing damages to the Thai international investment environment. The recent foreign investment scheme should thus be analyzed in accordance with the level of economic development of Thailand. Furthermore, the result of the analysis will help Thailand to create an efficient set of laws and regulations, which will be beneficial to the future of Thailand's economy. Accordingly, the assessment of the problematic aspects of the implementation of the FBA 1999 will be the main focus of this research study. By strengthening the FDI controlling measure in Thailand, it will allow the country to fully achieve the beneficial aspect of FDI that leads to a stable and prosperous economic environment of the country.

1.2 Objectives of the Research

1) To study the theory, concept, and fundamental principle in drafting the law concerning the foreign investment controlling measures
2) To analyze the inherent issues in the implementation of the Foreign Business Act of 1999 as a tool to control foreign investment in Thailand
3) To propose appropriate considerations to strengthen the implementation of the Foreign Business Act of 1999 as a controlling measure for foreign investment in Thailand

1.3 Research Methodology

This research is conducted based on the qualitative research methodology together with in-depth interviews. The study reviews literatures, books, academic articles, reports, research and studies relating to the controlling measures of foreign direct investments (FDI), the application of the law and the enforcement mechanisms regarding the control of FDI in Thailand. The study also includes in-depth interview of scholars, government officials, legal experts and practitioners in the field of international investment law in Thailand as follows;

1. Interview with the Director of Foreign Business Administration Division, Department of Business Development
2. Interview with Law Professor from Thammasat University
3. Interview with the Secretariat of the Minister of Industry
4. Interview with Law Professor from University of Wisconsin, Madison Law School
5. Interview with Partner at C.B. Law Office
6. Interview with former Inspector General of Ministry of Commerce, Thailand

1.4 Research Framework

This research studies theories, structures, strategies, and fundamental elements in legislating the law as a means to enforce and control foreign investment in Thailand. The research utilizes theoretical findings together with in-depth interviews with public and private organizations concerning foreign investment to gauge their views on inherent issues of the Foreign Business Act of 1999 which affect the current state of foreign investment in Thailand, directly linking to the country's economic development.

1.5 The Utility Prospective Outcome of the Project

1) To understand the theory, concept, and fundamental elements in optimally drafting the law to control foreign investment
2) To understand the inherent issues in the implementation of the Foreign Business Act of 1999 as a tool to control foreign investment in Thailand
3) To acquire the appropriate measures to strengthen the implementation of the Foreign Business Act of 1999 as a controlling measure for foreign investment in Thailand