

LEGAL PROBLEMS CONCERNING NOMINEE ARRANGEMENTS IN RELATION TO FOREIGN BUSINESS UNDER THAI LAWS^{*}

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Abstract

This article explores the problems of nominee arrangements under the Foreign Business Act B.E. 2542 (hereinafter the “FBA”), which is caused by the impractical definition of “foreigners” under Section 4 of the FBA, and the unclear criteria relating to what constitutes a “nominee arrangement”, which is prohibited under the relevant laws.

Nominee arrangements are a major problem for foreign business laws in Thailand, as they allow foreigners to circumvent laws which aim to protect the economic interests of Thailand against foreign ownership and control, and protect the interests of Thai businesses in sensitive sectors in which Thai businesses may not yet be ready to compete with multinational corporations looking to expand the scope of their business to Thailand.¹

Despite the laws being effective for over 40 years, the nominee arrangement problem remains a prominent and long standing issue in

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¹ Sakon Harnsuthivarint, ‘Nominee Tue Hoon Tan Khon Tang Dao [Nominee Holding Shares for Foreigners]’ (*Bangkokbiznews*, 8 March 2016) (สกส หานสุทธีวารินทร์, “นอมินี” ถือหุ้นแทนคนต่างด้าว’ (*กรุงเทพธุรกิจ*, 8 มีนาคม 2559)) <<https://www.bangkokbiznews.com/blog/detail/637132>> accessed 24 September 2019.

Thailand, and thus, it is essential to find suitable and practical solutions to fix these problems, with primary focus on revising the definition of “foreigners” and providing a clear criteria to facilitate the identification of a “nominee arrangement” under the FBA respectively. With the implementation of the proposed solutions, nominee arrangements will be eradicated over time, which would result in a more balanced playing field, which will both protect Thai businesses and promote foreign businesses in Thailand.

Keywords: Foreign Businesses, Nominee Arrangement, Foreign Business Laws, Legal Measures, Foreign Direct Investment

1. Introduction

Foreign direct investment plays a huge role in Thailand's development, because multinational companies bring technological advancement into the country, and fund capital investment which help to power Thailand's economic and fiscal development within the global economy. Many countries have tried to promote foreign direct investment by granting both tax and non-tax incentives to foreigners who are looking to establish a permanent legal establishment under its jurisdiction, to enable them to conduct promoted business activities in the country, which the local government believes is essential for the country's economic development. However, other parties harbor a contrary view, and they have sought to restrict foreign direct investment by limiting foreign ownership in certain business sectors, for fear that foreign control in certain business sectors could lead to unfair advantages over their own national businesses, which have fewer resources and are less technologically advanced than larger foreign corporations.²

The types of foreign ownership restrictions imposed in each country is mainly dependent on the degree of economic advancement, and on the internal fiscal and economic policy adopted by each country. For example, developed countries tend to have a relaxed approach and a more welcoming attitude towards foreign ownership (in the form of foreign direct investment) in its own country, while developing and less developed countries tend to adopt a more restrictive and protective approach towards foreign businesses, due to the fear that foreign domination and control in many business sectors could negatively impact the country's long term economic and fiscal development.

Foreign ownership in businesses in Thailand has always been restricted under the relevant laws and regulations, because Thailand is still a developing country, and thus, it is not ready to compete with heavily funded foreign corporations, which are looking to expand their businesses in

² *ibid.*

Thailand. Due to the foreign restrictions under the respective laws, foreigners have attempted to seek alternative solutions in order to conduct business in Thailand, and many risk-tolerant foreigners have tried to find illegal methods to circumvent the foreign ownership restrictions existing under Thai laws.³

2. Development of Foreign Business Laws in Thailand

Under Thai laws, foreigners and Thai nationals have equal rights on all legal matters, unless otherwise stated under the laws. Before 1972, foreigners had the same right to do business in Thailand as Thai nationals. However, in 1972, the Thai government passed the Announcement of the National Executive Council No. 281 (hereinafter referred to as the “**281 Announcement**”), which restricts certain rights of foreigners to invest in and conduct the reserved business activities which are stipulated under the 281 Announcement in Thailand. Under the 281 Announcement, a juristic person is considered an “alien”, based on the number of foreigners and the capital contribution made by the foreigners in the juristic person, which engages in the reserved business activity in Thailand. In addition, foreigners were only allowed to do business in Thailand if they could find a Thai partner to co-invest and co-operate with the juristic person to engage in the reserved business activity with the foreigner(s). However, the Thai partners would hold the majority number of shares or contribute the majority of the capital contribution in the juristic entity, since foreign ownership was restricted to less than the majority amount of capital contributed by the foreigners. As a result, this meant that foreigners would have to give up ownership in the juristic entity in question to the Thai national(s), who would hold the

³ Pugnatorius, ‘Seven Deadly Sins: The Status Quo of Thailand’s Foreign Business Act’ (Pugnatorius, 16 October 2019) <https://pugnatorius.com/Foreign_Business_Act_B.E.2542/> accessed 25 October 2019.

majority number of shares in the juristic person.⁴ Although, foreigners could apply for permission to conduct certain business activities which were reserved under the 281 Announcement, in order to operate the business activities as a 100% foreign-majority owned entity, such application process proved to be very difficult in practice, and often led to an unfavorable approval outcome. Therefore, many foreigners had to find other ways to carry out business in Thailand.⁵

In 1999, the 281 Announcement and its amendments were repealed and replaced by the Foreign Business Act B.E. 2542 (A.D. 1999), hereinafter referred to as the “FBA”, which adopted almost identical text and provisions from the 281 Announcement. However, under the FBA, the definition of “foreigners” no longer focused on the number of foreign shareholders in the juristic person, but rather, the definition of “foreigners” now placed emphasis on the number of shares held by the foreigners, and/or the amount of capital contribution made by the foreigners in the juristic entity in question.⁶

Similar to the 281 Announcement, the FBA restricted foreign ownership in the juristic person, which engaged in the reserved business activities specified in List Two and List Three annexed to the Act, to less than 50%, in order to encourage foreigners to conduct business activities in the form of a joint business operation with Thai nationals, based on the condition that Thai nationals hold a majority of the shares, and ultimately have more controlling interests in the juristic entity than the foreigners.

⁴ Lorenz & Partners, ‘Rights and Protection of Minority Shareholders in Thailand’ (Lorenz-Partners, May 2017) <https://www.lorenzpartners.com/download/thailand/NL1_8_8_E-Rights-and-Protection-of-Minority-Shareholders-in-Thailand-May1_7_.pdf> accessed 5 May 2019.

⁵ Pugnatorius (n 3).

⁶ Chatchawarl Sornsursardr and Chansilp Laosiriwut, ‘Thai Nominee Shareholders: Aftermath Problem’ (CBSC, 5 August 2010) <<http://www.csbc-law.com/thai-law-insights/thai-nominee-shareholders-aftermath-problem.html>> accessed 24 July 2019.

Furthermore, the FBA also contains provisions, which prohibit Thai nationals from assisting, aiding, abetting, and participating with the intention of holding it out as the Thai national's owned business, or holding shares in the juristic person on behalf of the foreigners with the objective of enabling the foreigners to circumvent the foreign ownership restrictions under the FBA. However, many foreigners still continue to seek out ways to avoid the foreign ownership restrictions under the FBA, since they do not wish to give control or other monetary benefits, such as dividend entitlements from the business operation, derived from the juristic entity to the Thai national(s), and the process of applying for a foreign business license under the FBA appears to be too complex, and often results in the Thai regulatory authorities handing down negative outcomes, which has discouraged many foreigners, who have instead sought to find alternative routes to do business in Thailand.⁷

The lack of a better alternative has driven many foreigners to set up a juristic person with a nominee arrangement, with the sole purpose of avoiding the foreign ownership restrictions imposed under the FBA.⁸

3. Problems of Nominee Arrangements in Thailand

When the 281 Announcement came into effect, it did not take into consideration the legal loopholes which would allow nominee arrangements to be created, since the definition of an "alien" merely focused on the number of foreign shareholders, and the amount of capital contribution made by the foreigners, without any consideration about the voting rights and other indirect control mechanisms, which may be exploited by foreigners seeking to avoid the foreign ownership restrictions established under the respective laws.

Since there are many ways in which a foreigner can legally own and control juristic persons, without having to hold the majority of the shares, or

⁷ Pugnatorius (n 5).

⁸ *ibid.*

providing the majority of the capital investment in the juristic entity, foreigners have used a backdoor channel to circumvent the foreign ownership restrictions under the 281 Announcement and ultimately, the FBA.⁹ They have achieved this by setting up a juristic entity under Thai laws, and thereafter, permitted Thai nationals hold the majority of the shares which possess diluted voting rights (for example, ten (10) shares for one (1) vote), while the foreigners would hold a minority number of the shares which possess more voting rights per share than the preference shares held by the majority Thai shareholders.¹⁰ Such arrangement is commonly known as a “**nominee arrangement**”, which in effect implies a situation whereby a person (known as the “**nominee**”) holds shares, and operates business activities in his or her capacity as the legal shareholder of the company on behalf of another person (known as the “**beneficial owner**”) who is, in fact, the real owner and the beneficiary of the shares held by the nominee(s) for the purpose of protecting and hiding the real identity of the beneficial owner for the purpose of circumventing the foreign ownership restrictions under Thai law.¹¹

A nominee arrangement is possible under Thai law, since under the Civil and Commercial Code of Thailand, companies can be set up with two (2) classes of shares, i.e. ordinary shares and preference shares. Preference shares can be given with different voting rights, and other types of benefits (such as the right to receive a higher dividend rate, or the right to appoint

⁹ *ibid.*

¹⁰ *ibid.*

¹¹ Anupan Kijnichcheeva and Nampon Tonguthaisri, *Karn Hai Kwaam Chuaylheu Leu Sanubsanoon Leu Ruemgun Leu Teu Hoon Tan Kon Tang Daow Tarm Matra 36 Hang Por.Ror.Bor. Karn Prakorb Turakit Kong Kon Tang Daow Por.Sor. 2542* [Assisting, Supporting and Holding Shares on Behalf of Foreigners under Section 36 of the Foreign Business Act B.E. 2542] (Chulalongkorn Law Journal, 28(2) August 2011) (อนุพันธ์ กิจนิจ ชีวะ และ นำพล ทองอุทัยศรี, *การให้ความช่วยเหลือหรือสนับสนุน หรือร่วมกัน หรือถือหุ้นแทนคนต่างด้าวตามมาตรา 36 แห่ง พ.ร.บ. การประกอบธุรกิจของคนต่างด้าว พ.ศ. 2542* (วารสารกฎหมาย คณะนิติศาสตร์ จุฬาลงกรณ์มหาวิทยาลัย, ปีที่ 28 ฉบับที่ 2 สิงหาคม 2554)).

member(s) of the board of directors, etc.).¹² The lack of clear criteria on the characteristics and rights which are allowed to be given to the preference shares under Thai law, means that preference shares can have any rights as desired by the promoters and the shareholders of the company. Consequently, this has led to a situation where foreigners have used the loophole under Thai corporate laws to circumvent the foreign ownership restrictions under Thailand's foreign business laws, i.e. the 281 Announcement and the FBA.

From the perspective of corporate laws, the corporate structure of preference shares with diluted voting rights has been confirmed by the Office of the Council of States to be legally valid on the ground that the determination of rights and conditions associated with preference shares can be determined in accordance with the wills of the promoters of the juristic entity, without legal restrictions, since the determination of different voting rights or any other benefits of the preference shares does not cause any unfair disadvantages to the other shareholders of the company, and nor does the determination of different rights and benefits between the two (2) classes of shares (ordinary shares and preference shares) contradict or contravene the laws, public order, or good morals of the general public. Since the assignment of different rights and benefits to preference shares were deemed to be a private matter, therefore, this could be undertaken without any restrictions under the laws.¹³

In practice, a number of foreign investors have set up a juristic person, with Thai nationals holding the majority of the shares with fewer voting rights than the foreigners, who hold fewer number of shares, in order to ensure that the juristic person in question is regarded as a "Thai" company under the criteria stipulated under the FBA. Therefore, such juristic

¹² Sopon Ratanakorn, *Kum Athibai Pramuan Kodmhai Pang Lae Panich Hoonsuan Borisut [Explanation of the Civil and Commercial Code: Companies]* (11th edn, Nitibannakarn Publishing House 2009) (โสภณ รัตนกร, คำอธิบายประมวลกฎหมายแพ่งและพาณิชย์ หุ้นส่วนบริษัท (พิมพ์ครั้งที่ 11, สำนักพิมพ์นิติบรรณการ พ.ศ. 2552)).

¹³ *ibid.*

persons with nominee arrangements would fall outside the scope of a “foreigner” as defined under the FBA, and thus, such entity can freely engage in any business activity which is reserved under the laws, and which are intended to be operated exclusively by Thai nationals only. The use of nominee arrangements, coupled with a preference shareholding structure with diluted voting rights, thereby creates a perfect legal loophole for foreigners to skirt the boundaries of the laws of Thailand.

In addition, although both the 281 Announcement and the FBA contain provisions which prohibit nominee arrangements, however, the lack of a clear definition as to what constitutes a “nominee arrangement”, or the factors which should be taken into consideration when contemplating what constitutes a “nominee arrangement” under the laws, has created problems with both the interpretation and the enforcement of the foreign business laws in Thailand, which has negatively impacted the credibility and reliability of the Thai legal system in the eyes of foreign investors who are seeking to invest in Thailand, as the foreigners view the legal system of Thailand as being unclear, unpredictable, and full of gray areas.

Furthermore, although the laws have established a regulatory authority to investigate and prosecute nominee arrangements in Thailand, however, in reality, only a few formal investigations have been conducted by the regulatory authority each year in a few selected industries, such as tourisms, bars and restaurants and property etc., most of which are small-sized business operations which do not cause any significant economic impact when compared to nominee arrangements existing in other sensitive business sectors, such as the telecommunication sectors, land transportation, air transportation, and agriculture, etc.

Therefore, the use of nominee arrangements is still widely practiced in Thailand, due to weak enforcement by the regulatory authority, and the complications in proving the true intentions between the Thai nominees and the foreign shareholders in respect to setting up such nominee arrangement. The lack of clear objective criteria for determining a nominee arrangement has compounded the problem as this renders it extremely

difficult for the regulatory authority to prosecute any wrongdoer for violations under the relevant laws.¹⁴

This is why a deeper analysis of the legal loopholes under the current foreign business laws of Thailand is important, in order to facilitate greater understanding of how these particular laws are failing at both ends of the spectrum i.e. both in terms of offering protection to real Thai businesses, and promoting foreigners to conduct business in Thailand.

4. Conclusion

The main objective of the FBA is to regulate how foreigners conduct business activities in Thailand, and to encourage foreigners to do business with Thai partners by setting up a Thai company together, which will result in the transfer of technology and knowledge, and a sharing of resources, with Thai persons. However, in reality, there are many foreigners, both natural persons and juristic entities, who/which have exploited the loopholes under Thai corporate laws, by setting up a business entity in Thailand and engaging a Thai national to hold shares on its behalf, in the form of a nominee arrangement, for the sole purpose of circumventing the foreign ownership restrictions under Thai laws.¹⁵

This is because the FBA focuses only on the foreign shareholding percentage and the amount of capital contributions made by the foreigners, without considering the voting powers and/or other indirect control mechanisms, which the foreigners may use to directly, or indirectly control the juristic person in question.

¹⁴ Athuek Asawanont, *Kodmhai Karn Prakorb Turakij Kong Kon Tang Daow Gub Nuk Kodmhai* [Conducting Businesses by Foreigners and Foreign Lawyers] (New Law Articles, 2007) (อธี อัสวานนท์, กฎหมายการประกอบธุรกิจของคนต่างด้าว กับนักกฎหมายต่างด้าว (วารสารข่าวกฎหมายใหม่, 2550)).

¹⁵ Chatchawarl Sornsursard and Chansilp Laosiriwut, 'Thai Nominee Shareholders: Aftermath Problem' (CBSC, 5 August 2010) <<http://www.csbc-law.com/thai-law-insights/thai-nominee-shareholders-aftermath-problem.html>> accessed 24 July 2019.

In addition, although Section 36 of the FBA prohibits nominee arrangements, by stating that a Thai national who assists, aids, and abets, or participates, in the operation of a foreigner's business, which is specified in the Lists under the Act, or who operates a business in a manner which holds it out as the Thai national's sole business, or who hold shares on behalf of the foreigners, will be found to be in breach of the Act. However, in reality, very few parties have been prosecuted for these violations due to the difficulties relating to proving the factors that would exactly constitute a nominee arrangement and the limitations on the interpretation of the laws by the regulatory authority.

Despite the fact that there are many alternative ways for foreigners to correctly and legally conduct reserved business activities in Thailand, a significant number of foreign investors still elect to use a nominee arrangement due to its simplicity, cost effectiveness, and the low risk of enforcement by the Thai government authorities for violations of the FBA.

The author believes that foreign business laws in Thailand are in need of a major reform. Before doing so, the Thai government must firmly decide what is more important: (i) the promotion of foreign direct investment; or (ii) the protection of Thai business interests.

It has clearly been evidenced from past experience that sitting on both sides of the fence, and trying to have it both ways, is a policy that is clearly not in the best interests of Thailand, since Thai laws are neither protecting the interests of Thai businesses, and nor are they attracting foreign investors to do business in Thailand.¹⁶ Therefore, in order to improve the efficiency of foreign business laws in Thailand, and their enforcement in respect to real world practices, the author would like to propose the following recommendations to resolve the problems relating to the use of nominee arrangements in Thailand, as follows:

¹⁶ Anupan Kijnichcheeva and Nampon Tonguthaisri (n 11).

4.1 Revisions to the Definition of “Foreigners”

This solution involves a revision to the definition provided for a “foreigner”, as stipulated under the FBA, so that it also includes both the direct and indirect controlling interests (in the form of voting rights and other indirect controlling mechanisms) of foreigners in the juristic person in question. The proposed revision to the definition of a “foreigner” under the FBA would greatly help to close the legal loopholes, which are currently prevalent under the existing foreign business laws of Thailand.

4.2 Revisions to the Criteria for a “Nominee Arrangement”

The proposed revision includes the relevant factors, which are taken into consideration by the regulatory authority, for determining a nominee arrangement, which shall include the following factors:

- (a) Wealth and income of the Thai shareholder(s);
- (b) Source of financing for the purchase of the shares, or for the initial capital contribution by the Thai shareholder;
- (c) The voting rights and the dividend rights of the Thai shareholder(s) in the juristic person in questions, and its correlation to his/her proportion of the shareholding, or the capital contribution made in the juristic person in question;
- (d) The history of attendance at the shareholders’ meetings of the juristic person by the Thai shareholder(s);
- (e) The power to nominate and/or remove members of the Board of Directors by the Thai shareholder(s);
- (f) The level of participation in the management of the juristic person in question by the Thai shareholder(s); and
- (g) The binding signatory powers, and the bank signatory powers of the director(s) of the juristic person in question.

The provision which prohibits nominee arrangements shall also clearly state the types of activities, or arrangements, which should be prohibited under the laws based on the grounds of a nominee arrangement, For example, execution of agreements or relevant documents between a

Thai national(s) and foreigners which involve giving, temporarily or permanently, legal ownerships and controlling interests in the shares, which are held by the Thai national, to the foreigners.

4.3 Update the Lists of Reserved Business Activities under the Act

The lists of reserved business activities, which are stipulated under the lists annexed to the FBA, must be updated with restrictions on foreign ownership in areas where there is an absolute necessity for such restrictions, i.e. restrictions on the grounds of national safety and national interests.

Alternatively, control mechanisms must be imposed on foreigners who are seeking to conduct business in Thailand, which will benefit the country, such as impositions on the amount of minimum capital requirement for foreign-majority owned entities, and requirements for the employment of Thai employees, and compulsory transfer of technology requirements, etc.

4.4 Simplification of the Foreign Business License Process

The application process for a foreign business license should be streamlined, so that it is clearer and faster, with consistent criteria on the information and the lists of documents required to be provided by the applicant, and the criteria adopted by the decision-making authority in granting approval. A simpler and more straightforward application procedure would encourage foreigners, who wish to operate reserved business activities in Thailand, to apply for a foreign business license, rather than pursuing the much cheaper, but illegal, nominee arrangement solution. Additionally, the application process should be available in English, since the majority of the applicants will be foreigners.

In this way, the foreigners can apply for the process by themselves, and it does not need to be processed via a third-party service provider, such as a law firm or an accounting firm.

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