6 Improving Thailand's foreign investment regime

This chapter focuses on barriers to entry and operation of foreign investors in Thailand. It explains why reducing barriers and facilitating operations for investors from abroad matter in a world of global value chains and in which Thailand aspires to move into higher value added activities in manufacturing and, particularly, in services. The chapter describes Thailand's regime of FDI regulatory restrictions. It also points to exemption schemes and legal loopholes in the Foreign Business Act, generating uncertainty for investors and potentially affecting Thailand's FDI attractiveness. The chapter identifies a number of policy options for consideration by the authorities.

Summary

It has long been recognised that globalisation offers substantial opportunities for participating countries, but that it also requires an ability for rapid adjustment for them to benefit from these opportunities (OECD, 1999). Possibly no other region has grasped such opportunities as well as Southeast Asia. Thailand was among the first in the region to recognise the powerful role that foreign investors could play in fuelling export-led growth, and was quick in opening up to foreign investment, albeit selectively (mostly in manufacturing as demonstrated below). As with any other policy, there are likely aspects which could have been better designed or implemented, but few today would call those policies into question altogether. There is a broad understanding that such policies and the FDI they subsequently fostered has enabled Thailand to emerge as one of the region's leading manufacturing hubs to the benefit of the Thai economy and its society more broadly.

As in many other emerging economies, there has not been any backtracking from those early FDI liberalisation efforts, but nor has there been much further liberalisation since then. Over time, other ASEAN Member States (AMS) have caught up and even surpassed Thailand in terms of openness to FDI. Partly as a result, Thailand is no longer attracting FDI as it used to, despite the increased appetite of foreign investors in the region (Chapter 4).

Thailand's primary and services sectors remain particularly restrictive to foreign investment according to the OECD FDI Regulatory Restrictiveness Index. Services liberalisation has typically lagged behind that of manufacturing in most countries, and, in this respect, Thailand's experience is no different. Thailand had adopted a rather successful export-oriented FDI strategy relatively early and recently established the 'Thailand 4.0' vision of becoming a high value- added, high income economy by 2037 (Chapter 2). However, various service sectors, considered as a means for achieving this vision, still remain partly off limits to foreign investments. In the modern context of intensified regional and global value chains (GVCs), FDI policies can no longer treat services and goods manufacturing separately.

As argued in Chapter 3, the development of competitive service sectors has great potential to enhance inclusive growth and productivity in Thailand. Besides providing productive job opportunities, services have major implications for the development and upgrading of Thailand's manufacturing industries, notably in a context of GVCs. Modern services can enable more efficient and resilient supply chains and play an increasingly important role as inputs into advanced manufacturing and innovation. The growing 'servicification' of manufacturing activities is reflected in the increasingly significant share of services value added embedded into manufacturing value added. But Thailand's services development still lags behind that of economies with a profile similar to what is aimed for with Thailand 4.0 (Chapter 3). Services account for about 30% of the value added embedded in its manufacturing exports, which is only slightly below the OECD average, but only about half of it is domestically generated (the rest being imported), against about 90% in the case of OECD economies.

It is, therefore, timely for Thailand to reflect on its strategy towards developing such a high-end services and high-tech manufacturing economy envisioned in the 20-Year National Development Strategy and in its Thailand 4.0 initiative. As with its export-oriented manufacturing strategy back in the 1990s, there are likely positive ways in which services FDI liberalisation could be helpful in this context. Although services tradability has increased over time with the rise of digital and communication technologies, they remain naturally more complex to trade than goods. Unlike trade in goods in which factors of production are built into the traded goods themselves, services typically require the actual relocation of capital and labour across borders, often through FDI.

Thailand's current FDI policy concerning services still shares similarities with its policy back in the early 1970s, with the exception of investment incentives (Chapter 5). Back then, faced with a backlash against growing foreign investment in Thailand, the government promulgated the Announcement of the Revolutionary Council No. 281 of 1972 (ARC. 281), which was the first law explicitly governing FDI. The

act introduced strict barriers to entry and operation of majority-foreign investors across all sectors, including manufacturing and services. The objective was overtly to protect indigenous Thai businesses given that Thai technology was not yet competitive, complemented by considerations about national security in a few sectors.

In 1999, the law's incompatibility with the country's attempt to promote foreign investment and international trade and the more open approach adopted in other countries gave rise to the Foreign Business Act (FBA), still in force today. The FBA liberalised FDI in many sectors, mostly in manufacturing, but still kept most of the restrictions pertaining to services. Apart from the FBA, the government exercises similar controls through sector-specific and other legislation, which prevail over the Act. Looking back, the liberalisation embodied in the FBA was circumscribed even in manufacturing where, unusually given the experience worldwide, it kept some restrictions as well. Compared to other economies in the region at the time, Thailand still maintained a relatively more open environment to FDI, but with almost no additional FDI liberalisation in Thailand since then, many other ASEAN Member States have now surpassed Thailand in openness.

While the stipulations of the FBA remains relatively restrictive on paper, foreign investors have explored exemption channels allowed by law or benefited from preferential treatment accorded to them under bilateral treaties. Promoted investors under the Investment Promotion Act and the Industrial Estate Authority of Thailand Act can also benefit from exemptions. Some foreign investors have also found ways into restricted activities through nominee structures, which are not officially permitted in Thailand. Some other foreign investors have recourse to less transparent business structures, such as preferential shares and indirect ownership, to by-pass some of the restrictions in place.

Hence, in practice, Thailand has been more open than a simple reading of the legislation would suggest. But the resulting policy inconsistency of restricting and selectively exempting FDI, as well as the uncertainty associated with some legal loopholes used by investors to by-pass some of the restrictions in the FBA are likely to come at a cost for investors and Thailand. It is difficult to establish how prevalent some of these practices are, but they have caught the attention of the authorities on a few occasions. In 2007, for instance, the Ministry of Commerce prepared a bill to amend the FBA to limit if not end existing legal loopholes, which would render the regime *de facto* more restrictive, but the proposed reform did not go forward in the face of opposition from investors.

Considering all these issues, it seems timely and appropriate for Thailand to undertake an assessment of the impact of the FBA and remaining sectoral restrictions to FDI on the economy. For almost 50 years, various domestic services industries have to a great extent been insulated from foreign competition. To what extent has this policy served its intended public purpose of enabling the development of vibrant local firms and capabilities? Are there activities or sectors that may no longer need insulation from foreign competition? Has this policy indirectly and disproportionately affected other parts of the economy that did not benefit from this treatment?

Available empirical evidence suggests a number of potential costs associated with discriminatory policies against FDI. Not surprisingly, statutory restrictions are found to have a significant negative effect on a country's ability to attract FDI. This is the case even for partial restrictions on FDI, such as foreign equity limitations and discriminatory screening and approval mechanisms (Mistura and Roulet, 2019; Fournier, 2015; Nicoletti et al., 2003). For Thailand, an illustrative simulation exercise using the average elasticity obtained in Mistura and Roulet (2019) suggests that if Thailand were to reduce restrictions to the 50th and 25th percentile levels of OECD FDI Regulatory Restrictiveness Index, inward FDI stocks could be 25% to 80% higher, respectively. But beyond any impact on FDI inflows, there is evidence that consumers and manufacturing sectors are also negatively affected by FDI restrictions in services sectors (OECD, 2019; Spinelli and Rouzet, 2016).

The right of governments to favour some investors over others in order to achieve social, economic or environmental goals is widely accepted, but any policy that discriminates against one group of investors

involves a cost. Discriminatory measures can thus only serve the broader public interest to the extent that their potential costs in terms of forgone investment and potential efficiency gains are compensated by broader social and economic benefits. For this reason, they need to be constantly re-evaluated to determine whether their original motivation remains valid, supported by an evaluation of the costs and benefits, including an assessment of the proportionality of the measure to ensure they are not greater than needed to address specific concerns (OECD, 2015a).

Main policy options for consideration by the authorities

- Undertake a comprehensive regulatory impact assessment of existing restrictions on FDI and publish the results. Include an assessment of potential non-discriminatory measures that could achieve the same objectives as the FBA.
- Reform the institutional setting of the Foreign Business Commission in charge *inter alia* of annually reviewing and proposing amendments to the list of restricted activities for consideration by the Minister, notably to include representatives of Office of the Trade Competition Commission, civil society and academia, as well as from the Joint Foreign Chambers of Commerce of Thailand. Render meeting records and any documentation supporting deliberations associated with non-confidential matters, such as the review of the lists of restricted activities, public.
- Revise the FBA to fully reflect foreign investment restrictions found in other laws, and to codify current practice where feasible, considering the various institutionalised exemptions and legal loopholes permitted by the legislation. Additionally, clarify the scope of application of listed activities by indicating their standard industrial classification code under Thailand's Standard Industrial Classification.
    - Some recent liberalisation announcements and amendments to the FBA are negated because some 'liberalised' activities remain restricted by sector-specific regulations which prevail over the FBA. This undermines one of the positive aspects of the FBA, which is to bring all the restrictions pertaining specifically to foreign investors under one umbrella, as a kind of negative list for foreign investors.
    - Thailand's FDI restrictiveness is attenuated *de facto* through the existence of exemption schemes. Nevertheless, regulatory uncertainty and legal loopholes for foreign investors to by-pass some of the regulatory restrictions on FDI, should also be addressed.
    - The dual-track option between the FBA and the Law on Investment Promotion demonstrate flexibility towards FDI. For better regulatory certainty, it is suggested that authorities could further eliminate any existing policy inconsistency, for instance, with activities which are promoted under the Law on Investment Promotion and at the same time restricted in the FBA, and with activities and sectors where the use of preferential shares and indirect holdings is not covered by the FBA.
- Further liberalise FDI restrictions particularly in services sectors to match levels of openness in other emerging economies and to foster greater convergence towards Thailand 4.0.
    - Many primary and services sectors remain partly off limits to foreign investors, potentially limiting economy-wide productivity gains.
    - Most restrictions date from the 1970s. They were introduced to shield Thai businesses from foreign competition until they were ready to compete on their own. There have been few changes to the regulatory environment since then.
    - In the current context of GVCs and the intensified 'servicification' of manufacturing activities, restrictions on FDI in service sectors also possibly discriminate against Thai manufacturing producers and consumers, who may have to pay relatively higher prices for needed quality-adjusted services inputs.

- Align the general minimum capital requirement for foreign investors to start a business in Thailand with capital requirements for domestic investors.
    - The current minimum capital policy is particularly stringent for investors in less-capital intensive activities, including many high-value added services that could contribute to Thailand's 4.0 strategy.
    - Worldwide, where minimum capital requirements still exist, they are rarely discriminatory – in 2012 only eight countries out of 98 assessed in the World Bank's Investing Across Borders imposed a discriminatory minimum capital requirement – and typically much lower than what is required from foreign investors in Thailand. This is the case even across economies with a level of income per capita much greater than that of Thailand.

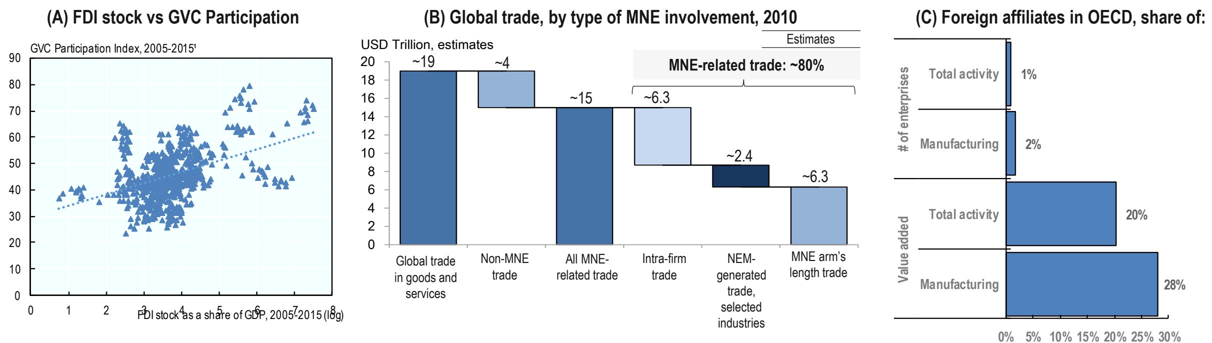
GVCs make barriers to FDI entry and national treatment particularly relevant

GVCs have become an important driver of productivity and economic growth across countries, both in developed and developing countries (OECD, 2015b; World Bank, 2019; Kowalski et al, 2015). The increased international fragmentation of production processes associated with GVCs can be observed in the significant growth in intermediate goods and services trade in past decades. Recently, more than 70% of world service imports were estimated to be intermediate services, and more than 50% of world manufactured imports were intermediate goods (OECD, 2013). Now more than ever firm competitiveness, and consequently that of countries, depends as much on its capacity to import high-quality inputs as on its capacity to export. Firms rely more intensively on access to cheaper or more differentiated and better world-class quality inputs to increase or maintain their productivity – in other words, they import in order to export successfully.

Multinational enterprises (MNEs) play a central role in international production networks, with a large share of cross-border trade taking place within affiliated networks (Figure 6.1). UNCTAD (2013) estimates that MNEs account for about 80% of global trade in goods and services, about 42% of which is intra-firm trade (Figure 6.1, Panel B). Cadestin et al. (2019) estimate a smaller participation but nonetheless important: roughly one-half of international trade. FDI is therefore an important channel through which countries integrate and benefit from GVCs (Figure 6.1, Panel A). MNEs and their foreign affiliates are typically only a small fraction of the enterprise population, but play a much greater role in terms of outcomes, partly because they are typically engaged in more capital- and scale-intensive industries (Figure 6.1, Panel C; OECD, 2013 and 2019). They usually account for a large share of exports and value added, and while part of the value added created may be repatriated, the rest stays in the host country in the form of labour compensation, taxes and reinvestments.

Depending on how strongly they are integrated into domestic economies, MNEs also represent a source of access to international markets and new technologies for their domestic suppliers and buyers, including SMEs, besides contributing to knowledge spillovers for domestic value chains. Every USD 1 of extra sales by foreign affiliates generates, on average, another USD 0.62 for the domestic economy in which they are located (Cadestin et al., 2019). The extent to which countries can provide the necessary conditions for global production networks to operate efficiently is, therefore, a key determinant of their success in linking to and upgrading within GVCs. Multinational firms' location decisions are much influenced by their need to ensure predictable and reliable supply-chains, capable of delivering effectively at each stage of the production chain (Taglioni and Winkler, 2014).

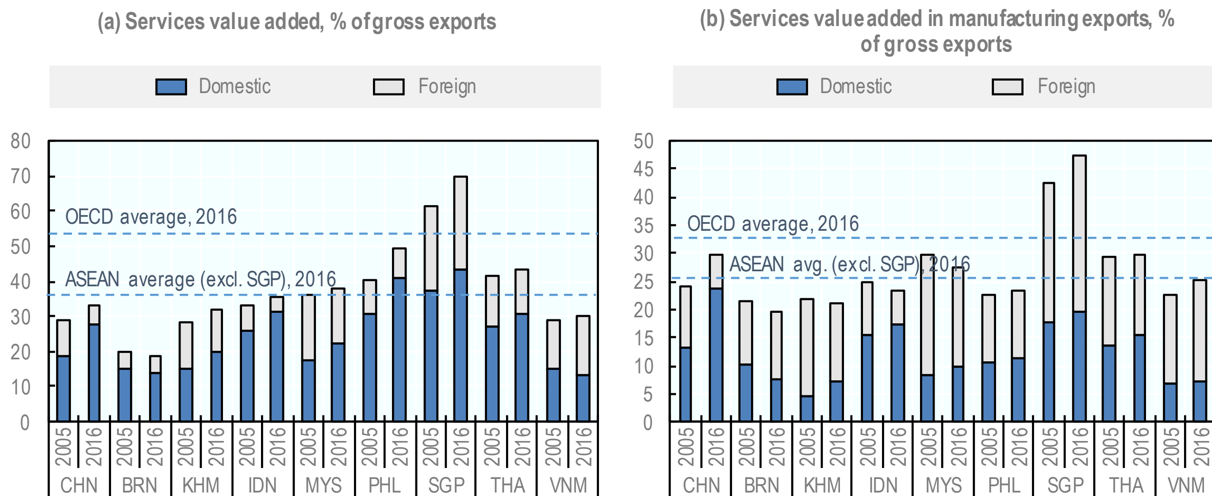
Figure 6.1. The importance of FDI in global value chains



Note: ¹GVC participation index refers to the share of foreign inputs (backward participation) and domestically produced inputs used in third countries' exports (forward participation) in a country's gross exports. See Koopman et al. (2010) for more information. NEM: non-equity modes.
Source: OECD (2014); UNCTAD statistics; UNCTAD (2013) and OECD AMNE Statistics (data for 2014).

The performance of services sectors play an important role in this context. Services are a significant channel for value added generation in the context of GVCs (OECD, 2020). Worldwide, while the share of services in gross exports is relatively limited, service sector activities contribute almost half of the value added inputs to exports (De Backer and Miroudot, 2013). In ASEAN, despite recent improvements, services value added embodied in exports, whether supplied locally or imported, remain subdued (38% excluding Singapore) compared to the OECD average (54%). In Thailand, services valued added share of gross exports stood at 43% in 2016 (Figure 6.2, Panel A), but for over a decade its domestic component has typically grown more slowly than in the other more advanced AMS.

Figure 6.2. Services value added share of exports and of manufacturing exports



Note: Domestic refers to the share of value added produced in the country either by locally-owned services providers or foreign affiliates in the country. Foreign refers to the share of imported value added from service providers located abroad. Service industries include construction, wholesale and retail, hotels and restaurants, transport and communications, finance, real estate and business services as well as public services, i.e. ISIC Rev.4 Divisions 41 to 98.
Source: OECD TiVA database.

In addition, services play an increasingly important role in value added generation in manufacturing activities, either as inputs for production of manufacturing goods or corporate services activities within firms, as well as bundled together with goods sold (Miroudot and Cadestin, 2017). This “servicification” of

manufacturing activities is clearly evidenced when one looks at the decomposition of value added embodied in manufacturing exports (Figure 6.2, Panel B). In OECD economies for instance, services inputs account for about one-third of the value added embedded in manufacturing exports, and adding the in-house provision of services in manufacturing firms, the share of services in manufacturing exports increases to 50% (Miroudot and Cadestin, 2017). In ASEAN and Thailand, the share of services value added embedded in manufacturing exports (excluding in-house services) stands at 26% and 30%, respectively. While most of it is domestically generated in OECD economies (about 90%), in Thailand only about half or less is domestically produced by Thai or foreign-owned companies established in Thailand; the rest is imported.

Barriers to FDI entry and the absence of national treatment in services sectors may, therefore, be an additional deterrent for developing competitive services and downstream manufacturing activities (see discussion further below). Worldwide, FDI activity has been particularly intense in the service sector in the last decade, bringing service sector FDI stocks to more than 60% of total stocks (UNCTAD, 2013). Thailand is no longer attracting FDI as it used to, despite foreign investors' increased appetite for the region in the last decade, and its relatively restrictive environment for FDI in services sectors puts it at a weaker position to capture some of the associated opportunities (OECD, 2019).

Thailand's foreign investment regime could benefit from further liberalisation

Like most other ASEAN economies, Thailand is quite restrictive to FDI according to the OECD FDI Regulatory Restrictiveness Index (Figure 6.3; Box 6.1). Governments all over the world discriminate among investors in one way or another, sometimes deliberately, sometimes unwittingly. The extent of FDI regulatory restrictiveness observed in Thailand, however, is much higher than in most other emerging and developing countries, and is even higher than in some of its direct ASEAN peers, such as Singapore and Viet Nam.

Box 6.1. Calculating the OECD FDI Regulatory Restrictiveness Index

The OECD FDI Regulatory Restrictiveness Index seeks to gauge the restrictiveness of a country's FDI rules. The FDI Index is currently available for almost 80 countries. It is used on a stand-alone basis to assess the restrictiveness of FDI policies in reviews of candidates for OECD accession and in OECD Investment Policy Reviews, including reviews of new adherent countries to the OECD Declaration on International Investment and Multinational Enterprises.

The FDI Index does not provide a full measure of a country's investment climate since it does not score the actual implementation of formal restrictions and does not take into account other aspects of the investment regulatory framework which may also impinge on the FDI climate. Nonetheless, FDI rules are a critical determinant of a country's attractiveness to foreign investors and the Index, used in combination with other indicators measuring various aspects of the FDI climate, contributes to assessing countries' international investment policies and to explaining the varied performance across countries in attracting FDI.

The FDI Index covers 22 sectors, including agriculture, mining, electricity, manufacturing and main services (transport, construction, distribution, communications, real estate, financial and professional services). Restrictions are evaluated on a 0 (open) to 1 (closed) scale. The overall restrictiveness index is a simple average of individual sectoral scores. For a detailed description of the scoring methodology, please refer to the technical working paper by Kalinova et al. (2010).

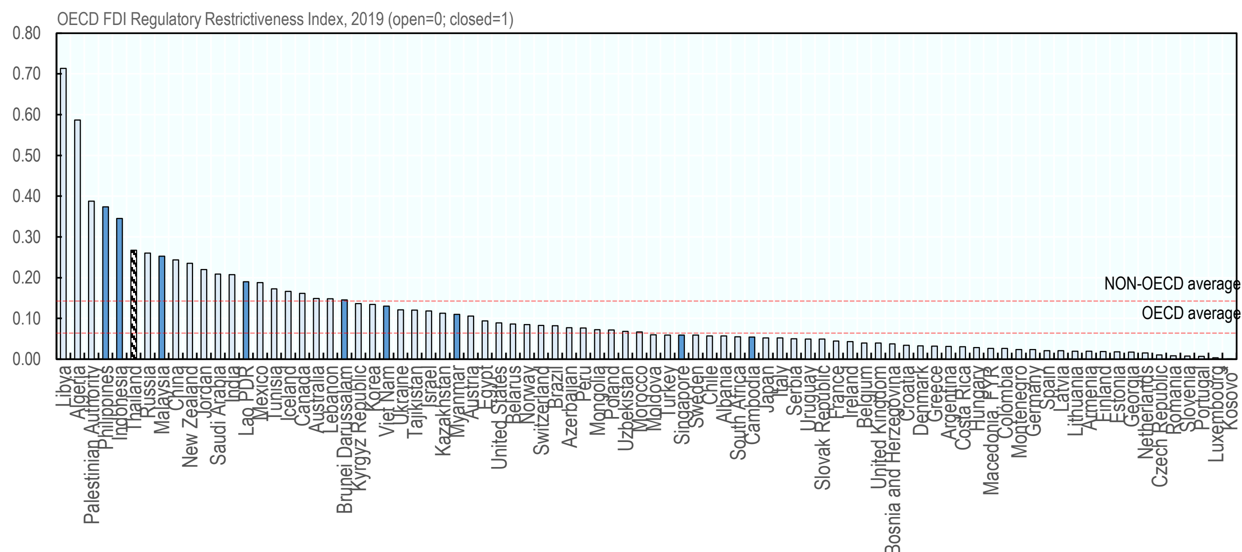
For each sector, the scoring is based on the following elements:

- the level of foreign equity ownership permitted,
- the screening/approval procedures applied to inward foreign direct investment;
- restrictions on key foreign personnel; and
- other restrictions, e.g. on land ownership, corporate organisation (branching).

The measures taken into account by the Index are limited to statutory restrictions on FDI typically reflected in official OECD instruments on investment or identified in OECD Investment Policy Reviews and yearly monitoring reports. The discriminatory nature of measures, *i.e.* when they apply to foreign investors only, is the central criterion for scoring a measure. State ownership and state monopolies, to the extent they are not discriminatory towards foreigners, are not scored. Preferential treatment for special-economic zones and export-oriented investors is also not factored into the FDI Index score, nor is the more favourable treatment of one group of investors as a result of preferential treatment under international agreements.

Thailand's current FDI regime can trace its origin back to its first regulation on FDI established in 1972. At the time, concerned with the growing number of foreigners investing and operating in Thailand, the government promulgated the Announcement of the Revolutionary Council No. 281 of 1972 (ARC 281). Seeking to protect Thai businesses from foreign competition, in addition to some considerations about national security in a few sectors, the ARC introduced strict barriers to entry and operation of foreign investors across the board, including in manufacturing and services sectors.

Figure 6.3. OECD FDI Regulatory Restrictiveness Index, 2019

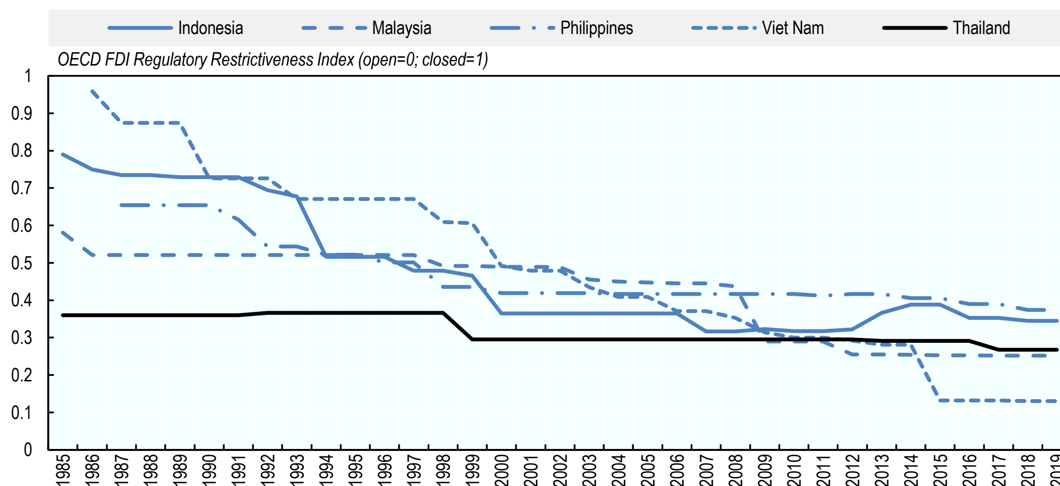


Note: The OECD FDI Regulatory Restrictiveness Index covers only statutory measures discriminating against foreign investors (e.g. foreign equity limits, screening & approval procedures, restriction on key foreign personnel, and other operational measures). Other important aspects of an investment climate (e.g. the implementation of regulations and state monopolies, preferential treatment for export-oriented investors and SEZ regimes among other) are not considered. Data reflect regulatory restrictions as of end-December 2019. Please refer to Kalinova et al. (2010) for further information on the methodology.

Source: OECD FDI Regulatory Restrictiveness Index database, http://www.oecd.org/investment/fdiindex.htm; See also the ASEAN FDI Regulatory Restrictions Database for information on the underlying measures captured in the Index, https://qdd.oecd.org/subject.aspx?Subject=ASEAN_INDEX.

While other AMS continued to liberalise their investment regimes over time, there have been only a few revisions to Thailand's FDI regime since the 1970s (Figure 6.4). The most important was the enactment of the Foreign Business Act in 1999, which repealed the ARC and reduced to a great extent (albeit not entirely) FDI restrictions mainly in manufacturing. The FBA is not the only legislation governing the participation of foreign investors in the Thai economy. Some restrictions also exist in sector-specific legislation, which prevails over the FBA. As such, over time Thailand has slowly lost much of that relative competitive edge it had in terms of friendliness to foreign investors which had helped to position it among the main recipients of FDI in the region in the 1990s.

Figure 6.4. OECD FDI Regulatory Restrictiveness Index: an historical perspective, 1985-2019



Note: See note to Figure 6.3 above.
Source: Author's elaboration based on the OECD FDI Regulatory Restrictiveness Index methodology.

More recently, a few amendments to the FBA have narrowed the list of activities in which Thai businesses are not yet ready to compete with foreigners and in which foreign majority shareholding is only allowed subject to approval by the Director-General of the Department of Business Development and the Foreign Business Council. However, some of these changes have had only a limited effect *de facto*, because many of the activities removed from the list remain restricted in sector-specific regulations.

The government nevertheless continues to contemplate further services FDI liberalisation. In 2019, the Foreign Business Commission reviewed the list of restrictive business categories under the FBA and identified four additional activities to be removed from the list, namely: i) telecommunications business (type 1 licence) in accordance with the Telecommunications Business Act; ii) treasury centres in accordance with the Exchange Control Act; iii) certain aircraft maintenance; iv) high value-added software development activities. Proposed changes are not yet in force, awaiting needed ministerial regulations for becoming effective, but they denote a welcoming step towards modernising Thailand's foreign investment regime. Foreign investments in these activities would then be dispensed from obtaining a foreign business licence under the FBA (see below). The proposed changes are justified *inter alia* on the basis of the importance of such business categories for supporting the development of Thailand's 'New S-curve' digital industries (see Chapter 3 and 5), as well as on the need to reduce duplication of government oversight as these businesses are governed by specific laws. Another 18 business categories are proposed to remain restricted until further study is undertaken by the Foreign Business Commission (FBC, 2019).

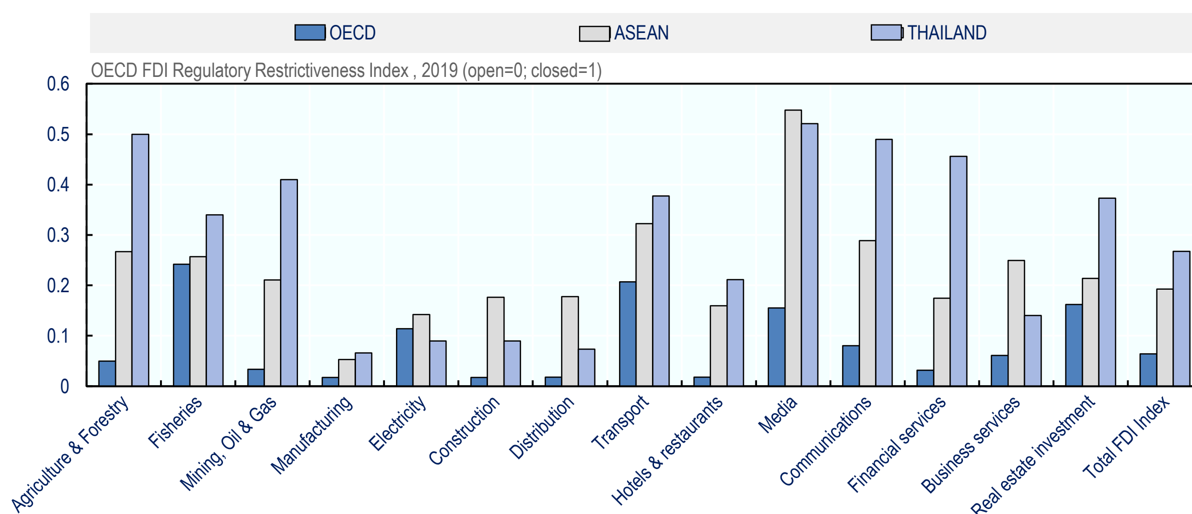
Domestic manufacturers and consumers would benefit from services liberalisation

Many primary and services sectors remain partly off limits to foreign investors, often to an extent that exceeds considerably the ASEAN average (Figure 6.5). Services liberalisation has particularly lagged behind that of manufacturing almost everywhere, including in OECD countries, finding strong resistance in powerful domestic interest groups. But having shielded domestic service providers from foreign competition for half a century –since the ARC first introduced most of the restrictions – Thailand has not only been treating foreign investors differently, but has also implicitly favoured Thai services providers over domestic consumers and manufacturers. Barriers to establishment enable incumbent services firms shielded from foreign competition to raise their prices, affecting downstream activities and end-consumers (see discussion below on the implications of FDI restrictions).

The development of efficient services depends as much as on policies that eliminate discrimination and barriers to entry and allow for greater competition and contestability pressures, as on policies that promote an efficient regulatory environment behind the borders to all firms in the sector, including in relation to competition policy (see Chapter 7 for a discussion on Thailand's competition framework). A more granular analysis of the domestic regulatory regime in services is beyond the scope of this review, as service sectors are quite diverse and would require a more industry-specific approach. Market access barriers, on the other hand, share commonalities across service sectors and allow for a more general discussion within this chapter.

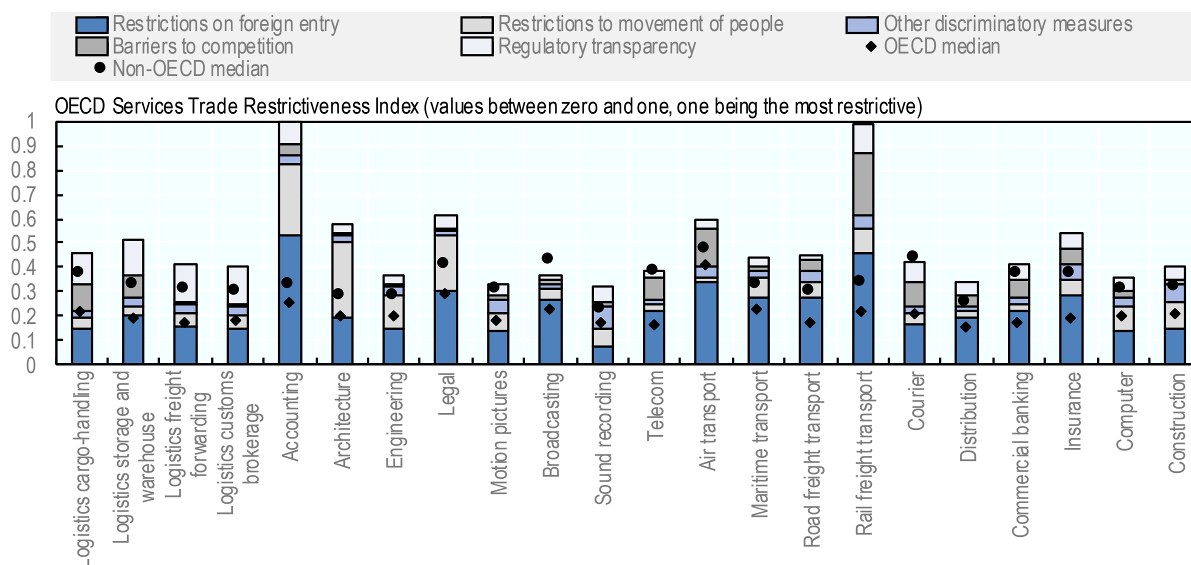
Nonetheless, it is important to note that Thailand also maintains a fairly stringent regulatory regime in respect to a number of other policy dimensions important for services development beyond restrictions on foreign entry, such as measures related to the movement of people, barriers to competition (see Chapter 7), regulatory transparency and other discriminatory measures that affect the ease of doing business as captured in the OECD *Services Trade Restrictiveness Index* (Figure 6.6). In almost all 22 services sectors assessed by the indicator, Thailand appears as more restrictive than the average of OECD and non-OECD economies covered. And while restrictions on foreign entry are particularly important, the level of restrictiveness observed in the other policy dimensions assessed is also considerable.

Figure 6.5. OECD FDI Regulatory Restrictiveness Index, by sector: Thailand vs. ASEAN vs. OECD, 2019



Note: See note to Figure 6.3 above.
Source: *OECD* FDI Regulatory Restrictiveness Index database, http://www.oecd.org/investment/fdiindex.htm; See also the ASEAN FDI Regulatory Restrictions Database for information on the underlying measures captured in the Index, https://qdd.oecd.org/subject.aspx?Subject=ASEAN_INDEX.

Figure 6.6. OECD Services Trade Restrictiveness Index, by sector and policy area, 2019



Note: The STRI indices take values between zero and one, one being the most restrictive. They are calculated on the basis of the STRI regulatory database which contains information on regulation for the 36 OECD Members, Brazil, China, Colombia, Costa Rica India, Indonesia, Malaysia, Russia, South Africa, and Thailand. The STRI database records measures on a Most Favoured Nations basis. Preferential trade agreements are not taken into account. Air transport and road freight cover only commercial establishment (with accompanying movement of people).
Source: OECD Services Trade Restrictiveness Index, http://oe.cd/stri.

Foreign equity restrictions dominate barriers to FDI worldwide, but FDI screening and other operational measures are much more prevalent in Thailand

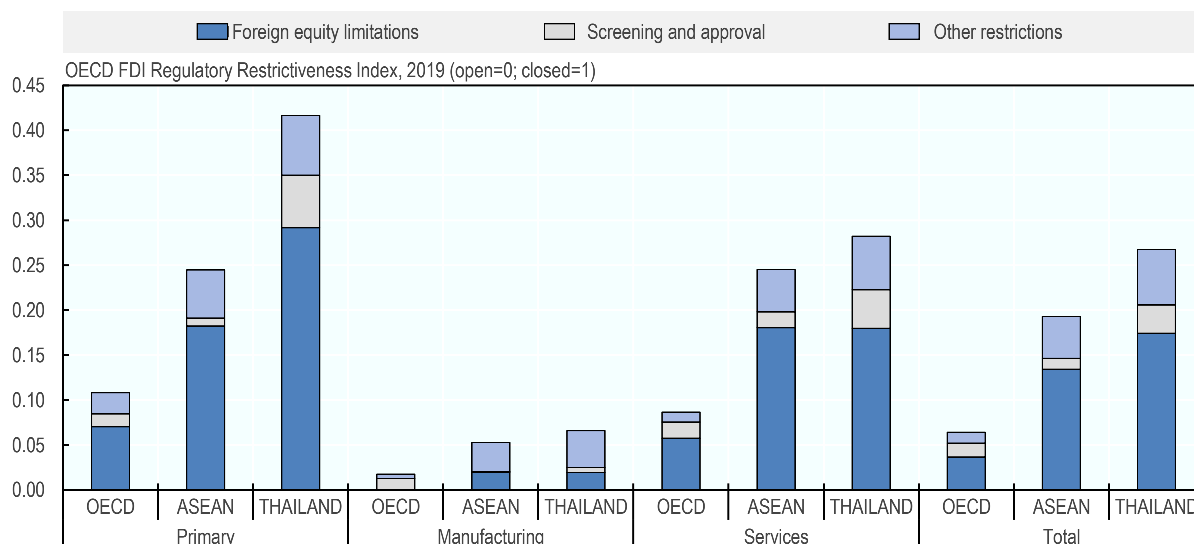
Foreign shareholding restrictions are considered a more important barrier to FDI in the OECD FDI Regulatory Restrictiveness Index than are other restrictions covered by the indicator, such as foreign investment approval mechanisms, restrictions on the employment of key foreign personnel and other operational restrictions. Hence, their weight is greater in the *Index* methodology (see Kalinova *et al.*, 2010).

This partly explains why foreign equity restrictions dominate in terms of barriers to FDI in Thailand and elsewhere. However, the extent to which this is the case in the aggregate, is largely driven by their scope of application, both across and within sectors. In the former case, this is determined by how prevalent foreign equity restrictions are in the 22 sectors covered in the *Index;* in the latter, by how stringent these restrictions are. The *Index* methodology distinguishes three thresholds in this respect: if foreign investors are fully prohibited from investing in the sector, if they are allowed to hold only a minority participation in companies operating in the sector, or if they are only restricted from establishing a wholly-owned operation.

As seen in Figure 6.7, Thailand's FDI regime is relatively more stringent in terms of foreign equity limitations in primary sectors than elsewhere. In manufacturing and services, the incidence of foreign equity restrictions is on average on a par with the average ASEAN economy, although it is still much higher than observed in OECD economies. The result is reflective of foreign equity limitations contemplated in both the FBA and other sector-specific legislation (see Annex 5.A and Table 6.1 below).

The prevalence of foreign investment approvals across almost all service sectors as per the FBA is a somewhat more distinctive feature of Thailand's FDI regime, as is the incidence of Thai nationality requirements for corporate board members in a number of sectors. This explains to a large extent the result in Figure 6.7.

Figure 6.7. OECD FDI Regulatory Restrictiveness Index, by type of restriction, 2019



Note: See note to Figure 6.3 above. Other restrictions groups together restrictions on key foreign personnel and other operational measures.
Source: *OECD* FDI Regulatory Restrictiveness Index database, http://www.oecd.org/investment/fdiindex.htm; See also the ASEAN FDI Regulatory Restrictions Database for information on the underlying measures captured in the Index, https://qdd.oecd.org/subject.aspx?Subject=ASEAN_INDEX.

The FBA requires foreign investors to obtain approval from the Council of Ministers to hold absolute majority shareholding stakes, limited to a maximum of 75%, in businesses in List Two (see Annex 5.A). Foreign investors are equally required to obtain an approval from the Foreign Business Commission (FBC) to hold absolute majority shareholding stakes without limitation in businesses in List Three, which includes most service activities, except for domestic transport services covered under List Two and some financial activities, which are typically restricted to foreign investors through sectoral regulation (see Annex 5.A). Until early 2019, even intra-group services provided to affiliates in Thailand, such as consultation on management, marketing, human resources and information technology, as well as lending money and renting out office space to affiliated and group companies in Thailand, were captured by List Three.[1]

Table 6.1. FDI Restrictions under sector-specific or horizontal legislation

Scope of application (sectoral or horizontal)	**Brief description of the measure**	**Legal authority / official source**
Horizontal	Foreign investors (foreign shareholding above 50%) are prohibited from holding ownership titles to land but may obtain land on a leasehold basis. An exception may be granted to foreigners who bring in capital in excess of THB 40 million. Such investors may be authorised to buy up to 400sqm of land within designated areas, notably Bangkok, the city of Pattaya and defined residential areas.	Act Promulgating the Land Code B.E. 2497 (1954), as amended Urban Planning Act B.E. 2562 (2019)
Real Estate Investment	Ownership by majority-foreign owned investors (above 50% of voting capital) of commercial or residential real estate is limited to 49% of the total area of all units in the condominium.	Condominium Act B.E. 2522 (1979), as amended
Media - radio and TV broadcasting	Foreign investment in radio & TV broadcasting is limited to 25% of the total voting capital and three-fourths of the board of directors must be Thai citizens.	Broadcasting and Television Businesses Act, B.E. 2551 (2008), as amended
Media - printed media	Foreign investment in printed media (press) is limited to 30% of the total voting capital, and three-fourths of the board of directors must be Thai citizens.	Printing Recordation Act, B.E. 2550 (2007), as amended

Scope of application (sectoral or horizontal)	Brief description of the measure	Legal authority / official source
Air transport	Foreign investment in scheduled and non-scheduled air services, as well as other air commercial services, is limited to 49% of the total voting capital, and two-thirds of the board of directors and the manager or the person having the power to manage must be Thai citizens.	Notification of Ministry of Transport Re: Rules and Conditions on Granting the Permission to Operate Trading Business in Air Navigation B.E. 2559 (2016)
Tourism	Foreign investment in tourism business (essentially travel agencies and tour operator services) are limited to up to 49% of voting capital, and more than 50% of directors must be Thai.	Tourism Business and Guide Act, B.E. 2551 (2008), as amended
Financial Institutions	Foreign shareholding in commercial banking, finance business and credit foncier business is limited up to 49% of the total voting capital, but can be higher if necessary for strengthening the stability of a financial institution or the stability of the financial institution system. The majority of the board of directors must be Thai citizens.	Financial Institutions Business Act B.E. 2551 (2008), as amended
Insurance	Foreign shareholding in insurance activities is limited up to 25% of total voting capital and not less than three-fourths of the total number of its directors must be Thai nationals. Foreign shareholding in excess of the limitations established by law is possible on an exceptional basis subject to authorisation from the Ministry of Finance.	Life Insurance Act, B.E. 2535 (1992), as amended Non-Life Insurance Act, B.E. 2535 (1992), as amended
Financial securities	Foreign investment in securities business is subject to local incorporation	Securities and Exchange Act B.E.2535 (1992) as amended
Telecom	Foreign investment in telecommunication business, with the exception of Type 1 licensed business - which includes essentially service-based telecommunications providers, such as internet access service, audio text service, resale of public switched telecommunications service, store-and-retrieve value-added service and international calling card service - is limited to 49% of the voting capital.	Telecommunications Act, B.E. 2544 (2001), as amended

In granting permission to foreigners for the operation of businesses under the FBA, the FBC and the Council of Ministers shall consider advantageous and disadvantageous effects on national safety and security, economic and social development of the country, public order or good morals, national values in arts, culture, traditions and customs, natural resources conservation, energy, environmental preservation, consumer protection, sizes of undertakings, employment, technology transfer and research and development.

The practice of screening foreign investment based on economic development matters was once common, including in OECD countries, but is now the exception to the rule and often circumscribed in scope (e.g. applying only to strategic industries for instance). While 30 years ago, about 70% of the OECD countries screened FDI projects, now fewer than one in six still do (Mistura and Thomsen, 2017). Screening measures which are exclusively for considerations of public order and essential national security are not considered in the OECD FDI Regulatory Restrictiveness Index.

It is hard to measure how much FDI screening policies act as a deterrent to FDI, because policy design and implementation aspects vary greatly across countries using such policies, but FDI screening measures as captured by the OECD FDI Regulatory Restrictiveness Index are found to significantly deter FDI on average (Mistura and Roulet, 2019).

In Thailand, the FBA endows the Minister of Commerce with ample powers to impose conditions for granting Foreign Business Licences to majority-owned foreign investments in List Two and Three (see Annex 5.A), including for instance in relation to (1) the ratio of the capital to loans for the operation of permitted businesses; (2) the number of foreign directors who must have a domicile or residence in the Kingdom; (3) the amount of, and the period of time for maintaining, the minimum capital in the country; (4) technology or property; (5) other necessary conditions.

Various criteria are used to consider the impact of the proposed business operation, such as the advantages and disadvantages to the nation's safety and security, economic and social development, size

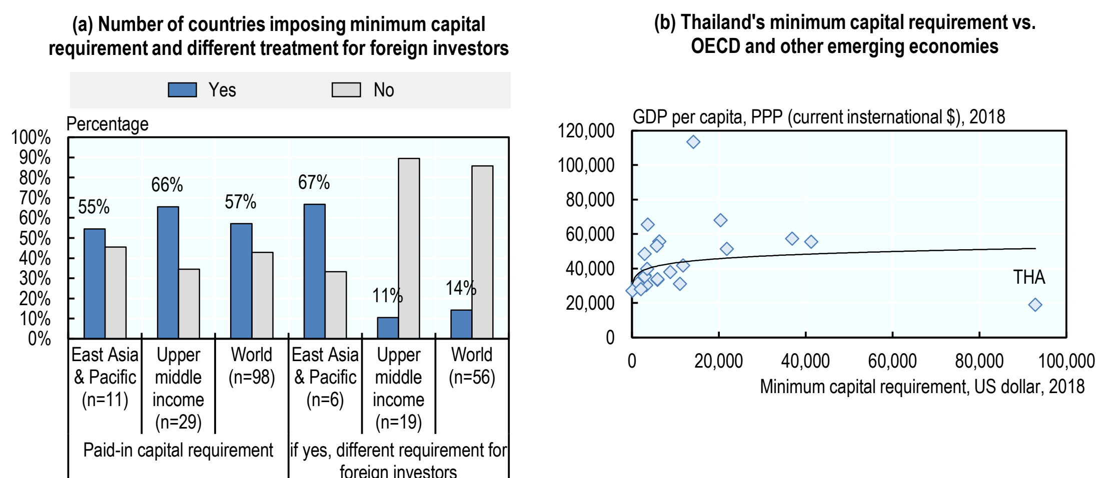
of the enterprise, local employment, etc. Approval of a business license application is more likely when the authorities view the business as providing significantly more benefits and protect and promote Thai interests. Thus, for some investors, “The Foreign Business License application is a complicated long process.” (Siam-legal, 2019).

The FBA also imposes Thai nationality requirements for boards of directors of companies operating in sectors included in its List Two. Restrictions on the employment of foreign persons for key managerial positions and boards of directors are rarely used by other countries covered in the *Index*. Somewhat more frequent is the use of residency requirements when addressing governments’ aspirations of facilitating local learning and securing jobs for local skilled workers. Residency requirements are not considered a restriction under the OECD FDI Regulatory Restrictiveness Index.

Also unusual is the different level of minimum capital required for foreign and domestic investors to start a general business in Thailand. Only a few countries discriminate between domestic and foreign investors in this respect (Figure 6.8a). According to the World Bank’s Investing across Borders database, across all regions only eight countries (out of the 98 covered) discriminate between foreign and domestic investors in this regard, four of which are in the East Asia and Pacific region. In fact, the use of minimum capital requirements for general business activities[2], whether or not discriminatory, has declined considerably over the past decade. According to the World Bank (2014), 39 economies eliminated capital requirements in the preceding seven years, and many others never had them in the first place. Despite this, minimum capital requirements remain a reality in many countries. Out of 190 economies included in the World Bank’s Doing Business 2020, 56 economies still required a minimum amount of capital to be paid-in by investors to register a business (World Bank, 2020).

Where minimum capital requirements still exist, the amount required is typically much lower than what is required for foreign investors in Thailand. This is the case even across economies with a level of income per capita much greater than that of Thailand (Figure 6.8b). The minimum capital requirement of not less than THB 2 million for a foreigner to be allowed to establish operations in Thailand, or not less than THB 3 million in the case of activities under List Two of Three of the FBA, clearly puts Thailand as an outlier in this respect. The comparison is based on minimum capital required for limited liability companies, but it would also hold true in relation to capital required from public stock companies in the observed countries.

Figure 6.8. Thailand’s minimum capital requirement policy in international comparison



Note: Data in Figure 6.7b refer to minimum capital requirement for limited liability companies and was converted at the 2018 yearly average exchange rate. In addition to Thailand, the figure covers another 25 OECD and large emerging economies applying minimum capital requirements for the establishment of limited liability companies as reported in the OECD Services Trade Restrictiveness database.
Source: World Bank's Investing Across Borders database (Panel a); OECD Services Trade Restrictiveness database, IMF International Financial Statistics and World Bank’s World Development Indicators (Panel b).

Thailand could also improve access to land and public procurement for foreign investors. With few exceptions, foreign majority-owned investors are prohibited from holding ownership title to land in Thailand. They are only entitled to lease land up to 50 years, renewable for another 50 years. While this is not unusual elsewhere, the regime in Thailand is somewhat more stringent than typically the case. Most often, discriminatory measures concerning foreign ownership of land, if applied, tend to circumscribed to legal entities established abroad. Locally incorporated companies, regardless of their foreign ownership levels, are often accorded national treatment, especially if the land is required for business purposes.

Unlike most countries, Thailand also gives preferential treatment to majority Thai-owned companies meeting the criteria for entering the "Thai Innovation List", a list of novel products and services invented by majority Thai-owned companies. The eligible firms benefit from simplified procurement procedures under special procurement method and a market reservation policy which requires all government agencies to source up to 30% of their demand for goods and services featuring in the list from the listed firms.

Regulatory reviews are frequently conducted but could be improved with an adequate structure and technical support

The right of governments to favour some investors over others in order to achieve social, economic or environmental goals is widely accepted, but any policy that favours some firms over others may involve costs in terms of less competition and hence lower firm-level efficiency. Discriminatory measures will therefore only serve the broader public interest to the extent that their potential costs are compensated by broader economic and social benefits. For this reason, they need to be constantly re-evaluated to determine whether their original motivation remains valid, supported by an evaluation of the costs and benefits, including an assessment of the proportionality of the measure to ensure they are not greater than needed to address specific concerns (OECD, 2015a).

The FBA appropriately provides for regular revisions of its lists of restricted activities by the Foreign Business Commission (FBC), which is composed by representatives of various ministries and government bodies, including from the Office of the National Economic and Social Development Council, the Board of Investment and Consumer Protection Board among other government agencies. The three Thai chambers of commerce, namely the Thai Chamber of Commerce, the Federation of Thai Industries and the Thai Bankers' Association, are also represented.

The current institutional setting, however, would benefit from a more balanced representation of interest groups. For instance, the participation of consumers (e.g. through the Office of the Trade Competition Commission, see Chapter 7 for a discussion on Thailand's competition framework), academia and civil society, could be contemplated, although the Minister of Commerce may appoint another five qualified persons to be members of the commission. Foreign Chambers of Commerce are also not represented. A more balanced representation could help to broaden the information-base supporting discussions and deliberations and provide some counterbalance to positions held by well represented domestic business groups.

The FBC deliberates on matters related to its annual mandate by assessing the impact on competitiveness of national investors and proposing revisions to the lists of restricted activities for foreign investors with regard to the impact of liberalisation. The Department of Business Development of the Ministry of Commerce is responsible, under the auspices of the commission, for conducting such a revision at least once annually. The revision must take into account the readiness of Thai businesses to compete with foreigners, comments from concerned line authorities, and overall advantages or disadvantages of removing activities from the lists of restricted businesses under the FBA. The extent to which technical assessments are prepared to support deliberations, for example, is not clear, nor if any policy externalities are considered beyond impact on Thai businesses. If there have been studies, these have not been publicly disclosed. In contrast, the Commission has a much more structured process for making recommendations concerning specific projects requiring approval under FBA. A positive note in this regard is that the FBC

acknowledged in its 2018 Annual Report the need for a more structured approach for issuing recommendations concerning revisions of business categories which remain listed in the FBA (FBC, 2019).

The government may also wish to ensure that announcements of liberalisation measures through changes to the FBA are codified in the underlying sector-specific regulations where restrictions sometimes remain unchanged. These regulations prevail over the FBA. Beyond the frustration that such discrepancies might generate in the business community, they also contribute to undermining one of the most positive aspects of the FBA, which is to bring all the restrictions pertaining specifically to foreign investors under one umbrella, as a kind of negative list for foreign investors. For legibility purposes, and to avoid further regulatory fragmentation, the government could consider revising the FBA to reflect better the restrictions found in other legislation.

Further clarity with regards to the scope of application of activities listed in the FBA would also be useful. The current list makes no reference to any standard industrial classification, which renders the coverage of listed business activities somewhat uncertain. In this respect, the government may want to adopt a standard classification for listing or excluding industries and business activities from the FBA. This could be done by making explicit reference to Thailand's Standard Industrial Classification which has the advantage of conforming to the International Standard Industrial Classification (ISIC Rev 4).

Exemption schemes and legal loopholes under the Foreign Business Act

Thailand has been in practice more open than suggested by its statutory regime due to exemption schemes offering flexibility for foreign investors vis-à-vis restrictive activities under the FBA. The policy flexibility achieved with the exemption schemes is praised by the Department of Business Development as the authority judges them appropriate for adapting the FDI policy to evolving social and economic circumstances. But the regulatory uncertainty associated with some of the available channels used by investors is likely to come with costs since some foreign investors could explore legal loopholes into restrictive activities and sometimes by illegal means (discussed further below).

Exemption scheme for promoted activities

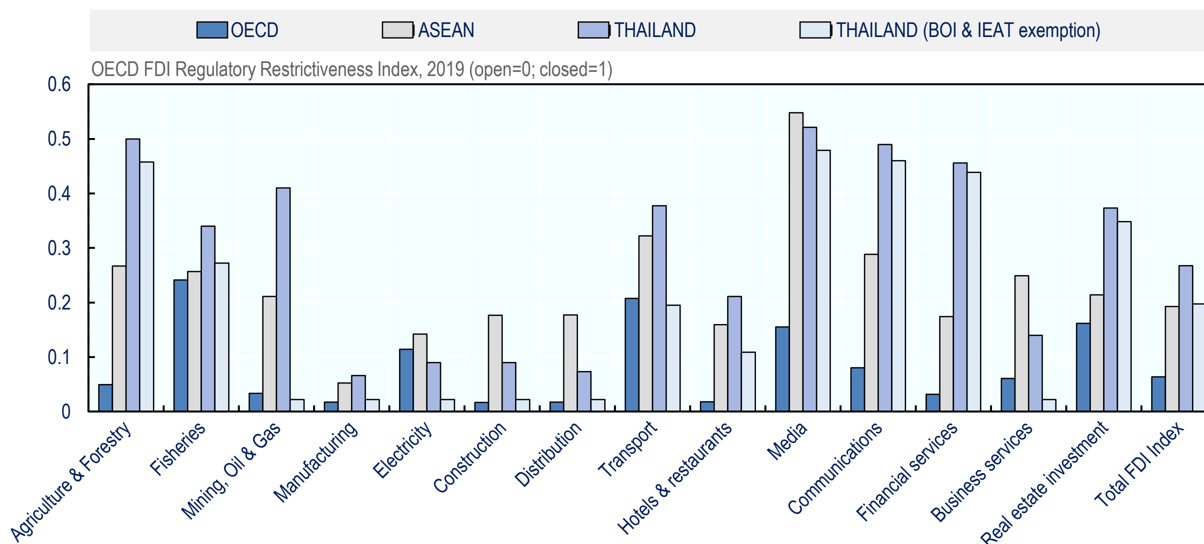
The FBA provides some flexibility for the authorities to selectively exempt some investments from the application of its provisions restricting foreign investment in businesses included in Lists Two and Three of the act. This is typically the case for promoted investors under the Law on Investment Promotion or those granted written permission for carrying out industrial or export-oriented activities under the Law on the Industrial Estate Authority of Thailand or under other laws.

In such cases, foreign investors can be exempted from the approval requirement and equity limitation for businesses under List Two and the approval requirement for businesses in List Three. The promotion exemption scheme relates only to provisions of the FBA and does not give investors the right to by-pass any restriction stipulated in other legislation (Table 6.1). Another loophole of the FBA discussed further below – the possible use of preferential shares or indirect structures to circumvent restrictions – is also not an option for by-passing foreign equity restrictions stipulated elsewhere because these legislations typically limit the share of voting capital that can be held by foreigners.

If, for instance, the exemptions allowed under the promotion exemption schemes were fully taken into consideration by the OECD FDI Regulatory Restrictiveness Index, Thailand's level of FDI restrictiveness would be equivalent to that of Lao PDR. In many sectors, restrictions would be drastically reduced to levels much below that observed in the average ASEAN economy, but the overall level of restrictiveness incorporated in legislation taking precedence over the FBA and in the List One of the FBA which cannot be circumvented remains, nonetheless, considerable (Figure 6.9). This is the case, for instance, in the media sector where the sectoral legislation imposes a 25% foreign shareholding limitation in TV and radio

broadcasting companies. In such cases, any difference in scores is due to changes in the scores of horizontal measures impinging on all sectors and which can be modified under the exemption scheme (e.g. the minimum capital requirement).

Figure 6.9. OECD FDI Regulatory Restrictiveness Index, by sector, 2019: simulating BOI and IEAT exemptions



Note: See note to Figure 6.3 above. The ASEAN average does not reflect Thailand's simulated score considering the investment promotion exemptions schemes under the FBA.
Source: OECD FDI Regulatory Restrictiveness Index database, http://www.oecd.org/investment/fdiindex.htm; See also the ASEAN FDI Regulatory Restrictions Database for information on the underlying measures captured in the Index, https://qdd.oecd.org/subject.aspx?Subject=ASEAN_INDEX..

In 2018 alone, out of 846 foreign projects applying for business permissions under the FBA (including Foreign Business Licences and Certificates altogether), 468 (55%) were exempted from FBA approvals (licensing system) through the investment promotion exemption scheme (FBC, 2019). Exempted investors are issued an automatic Foreign Business Certificate instead. Between March 2000 and end-November 2019, 4 639 certificates were issued under the investment promotion exemption scheme, compared to 5 548 licences (Table 6.2).

The "dual track" approach provides investors the choice of gaining approval either via the FBA or the Investment Promotion Act. This could give rise to questions about the coherence and appropriateness of related policies. Maintaining a dual approach could be perceived as a mixed, if not negative, signal to investors and could undermine the effectiveness of promotion activities (see Chapter 5 for a discussion on promotion policies).

Table 6.2. Number of Foreign Business Licences and Certificates issued under the FBA 1999 (30 March 2000 – 30 November 2019)

	(A) Licences Issued under FBA 1999	(B) Foreign Business Certificate Issued under FBA 1999	Exemption Schemes[3]			
			Treaty of Amity and Economic Relations (Thailand & USA)	Thailand - Australia FTA	Japan-Thailand EPA	Promoted under the Investment Promotion Law (BOI & IEAT)[4]
Service Business[1]	2642	3434	668	1	3	2762
Representative Office / Regional Office	1481	n/a	n/a	n/a	n/a	n/a
Engineering Service and Construction	609	599	72	0	0	527
Broker or Agent Business, Retailing and Wholesaling Business	581	2045	821	0	0	1224
Accounting Service Business and Legal Service Business	176	78	72	0	0	6
Other Businesses[2]	59	340	220	0	0	120
Total	**5548**	**6496**	**1853**	**1**	**3**	**4639**
Share in Total (A+B)	46%	54%				

Notes: Foreign Business Licences are issued to foreign investors approved by the relevant authorities under the FBA procedures to carry out business in Lists Two and Three of the act. A Foreign Business Certificate is the automatic permission issued to a foreigner exempted from FBA restrictions as per the exemption schemes provided for in the FBA.
1. Other service businesses under List 3(21) of FBA e.g. lending to affiliate, rental service, leasing, hire purchasing, repair of products in particular brand, made-to-order service of mold & auto parts.
2. Other businesses e.g. auctioning, advertising business, architecture service business, hotel business, guided tour, selling food or beverages.
3. Data on Foreign business Certificates related to regional operating headquarters (ROH) is included under 'service business'.
4. BOI and IEAT refer to the Board of Investment and the Industrial Estate Authority of Thailand, respectively.
Source: Department of Business Development, Foreign Business Operation Statistics: https://www.dbd.go.th/more_news.php?cid=197.

As mentioned above, there were 468 Foreign Business Certificates issued under the investment promotion exemption scheme in 2018, of which 441 were privileged under the Law on Investment Promotion and 27 were granted by the operation of the Law on the Industrial Estate Authority of Thailand. In the same period, the Board of Investments (BOI) approved a total of 914 projects with foreign participation, hence roughly half of them in sectors restricted under the FBA. The share of BOI promoted projects exempted from FBA restrictions has varied considerably in the past but has generally been very high (Table 6.3).

Table 6.3. Proportion of BOI-promoted projects with foreign participation and FBA exemptions through the promotion channel

	(A) Total number of projects granted a Foreign Business Certificate through the investment promotion exemption scheme of the FBA (only BOI)	(B) Total number of projects with foreign participation promoted by the BOI	Share (A/B)
2018	441	914	48%
2017	437	730	60%
2016	536	625	86%
2015	319	1151	28%

Source: Foreign Business Commission (2019, 2018, 2017 and 2016) and BOI statistics (see Chapter 5).

The large number of exemptions also raises the question of whether the FBA has been considered excessively restrictive by the authorities themselves. The observed practice can be seen as an endorsement of the view that the FBA is too restrictive in the current economic context. Certainly, the exemption channel offers the authorities more flexibility to selectively admit foreign investors and negotiate the conditions under which they are allowed (FBA Licence negotiations are still bound by limits established in the law, such as the maximum foreign shareholding of up to 75% for business activities in List Two), but this may come at a cost to the economy (see discussion of unintended consequences of FDI restrictions below).

Exemption scheme for investments under treaties or international agreements

Foreigners operating businesses specified in the Lists One, Two and Three of the FBA may be exempted from the associated restrictions as a result of preferential treatment accorded to them under treaties to which Thailand is a party. This exemption scheme, for instance, was used 1 857 times over the period from March 2000 to end-November 2019, corresponding to 15% of all Foreign Business Licences and Certificates issued under the FBA in the period (Table 6.2).

The Treaty of Amity and Economic Relations between Thailand and the United States concluded in 1966 is the most relevant one in this respect because it comprehensively exempts US investors from all applicable restrictions since the treaty first entered into force, except in telecommunications, transport, banking, natural resources extraction, business which takes care of property for the benefit of others and domestic local agricultural products trading. Investors from only two other countries, Japan and Australia, have reportedly used privileged conditions under treaties with Thailand to avoid FBA restrictions.

Legal loopholes associated with the use of preferential shares and indirect holdings

The alternative of investing under a minority foreign shareholding to qualify as a Thai company and avoid having to obtain an FBA licence may not be acceptable to some investors, especially if they cannot find a suitable local partner with adequate expertise and capacity. For some, the challenge may be more related to having to relinquish a majority controlling stake in the venture rather than sharing the rents with Thai shareholders. Some foreign investors may be reluctant, for instance, to share internal company documents and discussions with the Thai shareholders.

In such situations, some investors have explored existing legal loopholes to circumvent the restrictions in the FBA. A common strategy has been to use preferential share structures in order to qualify as a Thai company and avoid FBA restrictions. As in many countries, Thailand's corporate legislation allows a private limited company to issue shares with differential rights. Typically in this case, the Thai shareholders will hold 'preference shares' which entitle them to a fixed dividend and priority over 'ordinary' foreign shareholders in the payment of dividends and upon liquidation. In turn, preferential Thai shareholders have no or reduced voting rights.

Since the definition of 'foreigner' under the FBA only takes into consideration the investors' capital contribution and not their level of control and managerial influence[3], the use of preference shares allow foreign investors to have control over a company while maintaining the status of a Thai company and complying with the FBA. The Thai shareholder needs only to contribute not less than 51% of the capital of the company, but it does not need to hold profit rights and voting power in the same proportion. This can be done, for instance, by entitling foreign common shareholders with voting rights in the proportion of 10 votes per unit of share in the company, against one vote per unit of share for Thai preferential shareholders. Although some may consider that this practice goes against the underlying principle of the FBA, it has not been judicially challenged so far.

Another common strategy used by foreign investors to by-pass the FBA is to explore indirect ownership structures. The FBA takes into account only direct holdings to determine the nationality of a company. As

such, foreigners can make use of indirect holding structures to obtain control over a Thai company. For instance, a foreign investor may acquire a minority participation in a Thai holding company and a minority participation in one of its investees, all qualified as Thai companies under the FBA because direct foreign shareholding does not excess the legal threshold. Indirectly, however, the foreign shareholder may hold a majority controlling stake in the Thai investee company. Indirect holding is said to be a common practice in business services. To ensure transparency of ownership structures and thus lower or eliminate the risk of by-passing the FBA, listed companies in Thailand are required to disclose ultimate shareholders under the Securities and Exchange Act. These rules apply for companies applying for Initial Public Offering ("potential issuers") and companies already listed on Thailand's stock exchange ("listed companies").

The use of nominee structures, albeit explicitly illegal and subject to criminal charges, have also sometimes been used by foreign investors to circumvent the FBA as it is rather simple and less expensive. In its most obvious form, it consists of having a Thai shareholder holding shares on behalf of a foreigner, for instance through share transfer or share pledge agreements, although various other instruments can also be potentially used for such purposes.

The prevalence of nominee structures is difficult to ascertain because of the challenges in identifying them, but a recent government investigation on the practice of illegal nominee shareholding to circumvent the FBA in three target sectors – tourism and tourism-related business, land and immovable property trading, and agricultural business – have pointed to a limited use of such structures. According to the reported information, out of 6 380 Thai juristic entities with foreign shareholding of less than 50% investigated, about 98% of them showed no suspicious conduct of nominee shareholding. In most of the remaining cases (2%), the entities failed to provide the required information to the authorities within the imposed timeframe (FBC, 2019). The applied methodology used was not reported, but the results seem to contrast sharply with businesses' general perception about the prevalence of such structures and some recent government statements and initiatives in this respect.[4]

The government is vigilant and committed to monitoring the recourse to such illegal practices, despite the difficulties in implementation, and the investigation process is said to be transparent and non-discriminatory. In addition to the monitoring exercise carried out by the Department of Business Development of the Ministry of Commerce referred to above, the Ministry of Tourism and Sports has also reviewed the issue of nominees in the tourist industry. The committee created for such purposes has been dissolved following the completion of the exercise. The Securities and Exchange Commission also requires listed companies to disclose the list of top 10 shareholders in their annual reports, which limits considerably the use of nominee structures in listed companies.

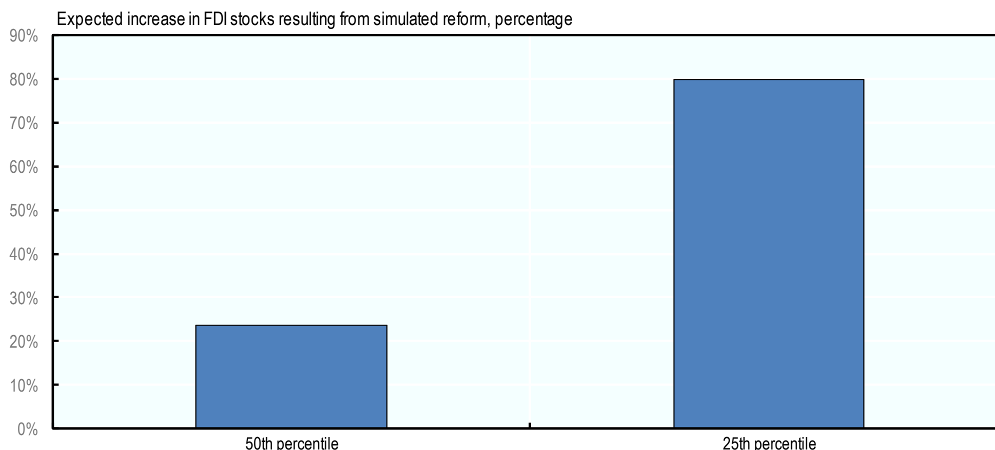
Potential implications of FDI restrictions

The empirical literature suggests a number of potential costs associated with discriminatory policies against FDI. The most obvious is that statutory restrictions are found to have a significant negative effect on a country's ability to attract FDI. While it is evident that when foreign investment is prohibited an economy is expected to receive no such investment, the evidence suggests that even partial restrictions, such as foreign equity limitations and discriminatory screening and approval mechanisms, can have a significant impact on FDI (Mistura and Roulet, 2019; Fournier, 2015; Nicoletti et al., 2003).

In this respect, recent OECD research estimated that the introduction of reforms leading to a 10% reduction in the level of FDI restrictiveness, as measured by the OECD FDI Regulatory Restrictiveness Index, could increase bilateral FDI inward stocks by around 2.1% on average across countries (Mistura and Roulet, 2019). The effect is larger for FDI in services sectors, reflecting the greater incidence of restrictions in these sectors. But even FDI into manufacturing sectors, which are mostly open to FDI, is also negatively affected by an economy's overall restrictiveness level, despite it being typically driven by restrictions in services activities.

For Thailand, an illustrative simulation exercise using the average elasticity obtained in Mistura and Roulet (2019) suggests that if Thailand were to reduce restrictions to the 50th and 25th percentile levels of OECD FDI Regulatory Restrictiveness Index, inward FDI stocks could be 25% to 80% higher, respectively (Figure 6.10).

Figure 6.10. Simulated effects of FDI liberalisation: reducing Thailand's restrictions to the 50th and 25th percentile levels of OECD FDI Regulatory Restrictiveness Index



Note: The simulation is based on the direct partial elasticity of FDI to restrictions (as measured by the OECD FDI Regulatory Restrictiveness Index), estimated using an augmented gravity model of bilateral inward FDI positions using a poisson pseudo-maximum likelihood estimator. Typical gravity variables and a series of other policy and non-policy factors are included (distance, contiguity, the existence of a common language, colonial ties, market size, economic growth, real exchange rates, similarity in size and factor resource endowments, trade openness, natural resource endowments, institutional maturity, FDI restrictions, participation in free trade areas, corporate tax), as well as host and home country and time-fixed effects. The regressions cover bilateral FDI relationships between 60 countries over the 1997-2012 period. Simulated effects assume the average elasticity effect applies.
Source: author's elaboration based on Mistura and Roulet's (2019) baseline estimations.

More importantly, restrictive services regulations typically enable services providers to charge higher mark-ups in a majority of service sectors, affecting downstream activities and end-consumers (Rouzet and Spinelli, 2016). This has economy-wide productivity implications given the increased importance of services as inputs for downstream manufacturing industries (Box 6.2). Previous OECD (2019) work, for instance, demonstrates that ASEAN manufacturing firms in industries relying extensively on services, such as in machinery and transport equipment industries, would greatly benefit from further services liberalisation. Likewise, SMEs have relatively more to gain from such measures than large firms. This is equally true for domestic firms as opposed to foreign-owned firms and for firms that do not export compared to exporters.

Service sector reforms could also translate into significant economic gains in the long-run. The IMF (2018) estimates that Thailand's potential long-term real GDP gain from reducing trade and FDI restrictions to the global average amount to roughly 17% in the medium-to-long term. Nearly 5 percentage points is attributable to FDI liberalisation in the estimation.

Overall, even if restrictions may not deter some investments altogether, they might affect the very nature of the FDI coming to Thailand, possibly towards a more capital light type of investment in order to conform with some of the potential drawbacks of investing jointly with local equity partners (e.g. lack of suitable partners in terms of capital and expertise, technology leakage etc.) or towards a less transparent type of investment that may be more tolerant of using riskier business structures to by-pass the legislation as discussed above.

Box 6.2. Services reforms raise manufacturing productivity

Recent empirical literature has identified a clear association between services reforms and productivity growth in the economy as a whole; as well as specifically in manufacturing (Low, 2016). A study of 15 OECD countries illustrates that anti-competitive upstream regulations in services and other non-manufacturing sectors curbed multi-factor productivity growth in downstream sectors between 1985 and 2007 (Bourlès et al., 2010). A recent study of Lao PDR confirms that services liberalisation benefits economic development across economic sectors, not just in services (Isono and Ishido, 2016).

Focusing on manufacturing, Duggan et al. (2013) employ the OECD FDI Index to assess the effects of FDI restrictions in services on the manufacturing productivity of Indonesian firms and find that service sector FDI liberalisation accounted for 8% of the observed increase in Indonesian manufacturers' total factor productivity (TFP) from 1997 to 2009. Shepotylo and Vakhitov (2015) analyse the impact of services liberalisation on manufacturing productivity in Ukraine over 2001-07 and find that a one standard deviation in liberalisation in services is associated with a 9% increase in the TFP of manufacturing firms. The authors also find that the effect of services liberalisation is stronger for domestic and small firms. Arnold et al. (2012) find that India's policy reforms in banking, telecommunications, insurance and transport services all had significant and positive effects on the productivity of Indian manufacturing firms from 1993 to 2005. Both foreign and domestic firms benefited from services reforms, but the effects were stronger for foreign-owned firms. A one standard deviation increase in services liberalisation resulted in a productivity increase of approximately 12% and 13% for domestic and foreign manufacturing firms, respectively. Relatedly, Berulava (2011) finds that liberalisation in telecommunications, electric power, transport, water distribution and banking stimulated the expansion of export activities of manufacturers in 29 transition economies from 2002 to 2009.

These findings are qualified by a recent study that argues that the effect of restrictions in upstream services is conditional on institutional quality (Beverelli et al., 2015). Using sector-level data in a panel dataset of 58 countries spanning all stages of economic development, the study finds that countries with better economic governance benefit more from open services policies. That is, higher quality institutions attract more productive service providers and support higher levels of services performance, which then affect downstream manufacturing sectors.

A number of studies also show a positive association between FDI in services and manufacturing productivity. Arnold et al. (2011) illustrate that increased foreign participation in services improved manufacturing productivity in the Czech Republic from 1998 to 2003. A one standard deviation in foreign presence in services is associated with an approximately 8% increase in the productivity of Czech manufacturing firms relying on services inputs. Fernandes and Paunov (2012) conduct a similar study on the effects of FDI in services sectors on the productivity of Chilean manufacturing firms between 1995 and 2004. A one standard deviation increase in service FDI would increase Chilean firms' TFP by 3%, and forward linkages from FDI in services explain 7% of the observed increase in the TFP of Chile's manufacturing firms during the period. Forlani (2012) finds that increased competition in network services in France improves the productivity of manufacturing firms.

Source: reproduced from OECD (2019)

This does not mean that FDI restrictions should necessarily be discarded entirely, as they may be appropriate in some circumstances. Many countries still find them useful to address concerns of national security, for instance. Instead, the evidence above reinforces the importance of weighing their benefits against their costs on a regular basis and in light of the country context and circumstances to derive a conclusion of whether they remain beneficial to society at large.

For Thailand, such an exercise seems particularly timely and appropriate considering its ambition to become a high-end services and high-tech manufacturing economy as envisioned in the 20-Year National Development Strategy and in the Thailand 4.0 initiative. As indicated previously, for almost 50 years Thai services providers have largely been insulated from foreign competition and indirectly privileged over domestic manufacturers and consumers. Yet, it is questionable whether this policy has paid off (see Chapter 3) or is appropriate for delivering on Thailand's development goals going forward.

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Annex 6.A. Lists of restricted activities under the Foreign Business Act, B.E. 2542 (1999)

List One	
BUSINESSES STRICTO SENSU NOT PERMISSIBLE TO FOREIGNERS BY SPECIAL REASON	
(1) The Press, radio broadcasting station or radio and television station business (2) Rice farming, plantation or crop growing (3) Livestock farming (4) Forestry and timber processing from a natural forest (5) Fishery, only in respect of the catchment of aquatic animals in Thai waters and specific economic zones of Thailand (6) Extraction of Thai medicinal herbs (7) Trading and auction sale of antique objects of Thailand or objects of historical value of the country (8) Making or casting Buddha Images and monk alms-bowls (9) Land trading	
List Two	
BUSINESSES RELATED TO NATIONAL SAFETY OR SECURITY OR HAVING IMPACTS ON ARTS, CULTURE, TRADITIONS, CUSTOMS AND FOLKLORE HANDICRAFTS OR NATURAL RESOURCES AND THE ENVIRONMENT	
Chapter 1: Businesses related to National Safety or Security	
(1) Production, distribution and maintenance of:	
	(a) firearms, ammunition, gun powders and explosives; (b) components of firearms, ammunition and explosives; (c) armaments, ships, aircraft or vehicles for military use; (d) equipment or components of all types of war materials
(2) Domestic transportation by land, water or air, including domestic aviation	
Chapter 2: Businesses Having Impacts on Arts, Culture, Traditions, Customs and Folklore Handicrafts	
(1) Trading of antiques or artistic objects that are artistic works or handicrafts of Thailand (2) Production of wood carvings (3) Silkworm raising, production of Thai silk yarn, weaving of Thai silk or printing of Thai silk patterns (4) Production of Thai musical instruments (5) Production of goldware, silverware, nielloware, bronzeware or lacquerware (6) Production of crockery or porcelains representing Thai arts and culture	
Chapter 3: Businesses Having Impacts on Natural Resources or the Environment	
(1) Production of sugar from sugar cane (2) Salt farming, including non-sea salt farming (3) Production of rock salt (4) Mining, including rock blasting or rock crushing (5) Timber processing for production of furniture and utensils	
List Three	
BUSINESSES IN RESPECT OF WHICH THAI NATIONALS ARE NOT READY TO COMPETE WITH FOREIGNERS	
(1) Rice milling and production of flour from rice and economic plants (2) Fishery only in respect of the hatching and raising of aquatic animals (3) Forestry from a grown forest (4) Production of plywood, veneer wood, chipboards or hardboards (5) Production of lime (6) Provision of accounting services (7) Provision of legal services (8) Provision of architectural services (9) Provision of engineering services	

<table>
<tr><td colspan="2">(10) Construction, with the exception of:</td></tr>
<tr><td></td><td>(a) Construction of structures for delivery of infrastructure public services in the sphere of public utilities or transportation requiring the use of special apparatuses, machines, technology or expertise, with the minimum capital of five hundred million Baht or upwards from foreigners;
(b) Construction of other types as prescribed in the Ministerial Regulation</td></tr>
<tr><td colspan="2">(11) Brokerage or agency businesses, with the exception of:</td></tr>
<tr><td></td><td>(a) being a broker or an agent in the sale or purchase of securities or in services related to futures trading of agricultural commodities or financing instruments or securities;
(b) being a broker or an agent in the sale, purchase or procurement of goods or services necessary for the production or the provision of services amongst affiliated enterprises;
(c) being a broker or an agent in the sale or purchase, procurement, distribution or acquisition of domestic and foreign markets for the distribution of domestically manufactured or imported goods, which is in character the operation of international trade, with the minimum capital of one hundred million Baht or upwards from foreigners
(d) being a broker or an agent of other types as prescribed in the Ministerial Regulation</td></tr>
<tr><td colspan="2">(12) Sale by auction, with the exception of:</td></tr>
<tr><td></td><td>(a) a sale by auction which, in character, involves international bidding of items other than antiques, objects of antiquity or artistic objects that are artistic works or handicrafts or objects of antiquity of Thailand or of historical value of the country;
(b) sales by auction of other types as prescribed in the Ministerial Regulation</td></tr>
<tr><td colspan="2">(13) Internal trade related to traditional agricultural products or produce not yet prohibited by law, except agricultural futures trading in the Agricultural Futures Exchange of Thailand without delivery or taking delivery of agricultural commodities within the country [as amended by Royal Decree, B.E. 2556 (2013)]
(14) Retail sale of goods of all types with the total minimum capital in the amount lower than one hundred million Baht or with the minimum capital of each store in the amount lower than twenty million Baht
(15) Wholesale of all types with the minimum capital of each store in the amount lower than one hundred million Baht
(16) Advertising business
(17) Hotel business, with the exception of the hotel management service
(18) Guided touring
(19) Sale of food and beverages
(20) Cultivation, propagation or development of plant varieties</td></tr>
<tr><td colspan="2">(21) Other service businesses, with the exception of service businesses as prescribed in the Ministerial Regulation [as amended by Ministerial Regulation, B.E. 2556 (2013); Ministerial Regulation No. 2, B.E. 2559 (2016); Ministerial Regulation No. 3, B.E. 2560 (2017); Ministerial Regulation No. 4, B.E. 2562 (2019)</td></tr>
<tr><td></td><td>(1) Securities business and other businesses under the law on securities and securities exchange:
(a) securities trading;
(b) serving as an investment consultant;
(c) securities underwriting;
(d) borrowing and lending securities;
(e) mutual fund management;
(f) private fund management;
(g) venture capital management;
(h) granting loans for securities business;
(i) serving as a financial consultant;
(j) serving as a securities registrar;
(k) trusteeship of assets of securities companies' or derivatives traders' customers;
(l) serving as a private fund custodian;
(m) serving as a mutual fund supervisor; and
(n) serving as a debenture holders' representative;</td></tr>
<tr><td></td><td>(2) Derivatives business under the law on derivatives:
(a) serving as a derivatives dealer;
(b) serving as a derivatives advisor; and
(c) serving as a derivatives fund manager;</td></tr>
<tr><td></td><td>(3) Serving as a trustee under the law on trust for transactions in capital market.</td></tr>
<tr><td></td><td>(4) financial institution business, businesses incidental to or necessary for the operation of a financial institution business and the businesses of companies in the financial group of a financial institution pursuant to the law on financial institutions:
(a) commercial banking business;
(b) bank representative office service business;
(c) Shariah financial service;
(d) financial institution agent;
(e) cash deposit services under terms of withdrawal on demand by a customer and custodian services;
(f) private sector repurchase;</td></tr>
</table>

	(g) agent to receive applications and collect insurance premiums or service fees for export insurance and credit insurance for customers; (h) services relating to financial businesses offered to financial institutions, companies within the financial group, the Bank of Thailand and government agencies; (i) leasing of immovable property; (j) purchase or assignment of loan debts; (k) financing service; (l) documentation relating to customer's businesses; (m) debt collection or application receiving agent; (n) hire purchase and leasing.
	(5) life insurance business under the law on life insurance;
	(6) Insurance business under the law on insurance.
	(7) asset management business under the law on asset management company; (8) representative office of foreign juristic person in international trade service pursuant to the Rules of the Prime Minister's Office on Establishment of Visa and Work Permit Service Center B.E. 2540 (1997); (9) regional office of foreign juristic person in international trade service pursuant to the Rules of the Prime Minister's Office on Establishment of Visa and Work Permit Service Center B.E. 2540 (1997); (10) service business to which a government agency under the law on budgetary procedures is a party; (11) service business to which a state enterprise under the law on budgetary procedures is a party
	(12) Services provided to affiliates and subsidiary companies, namely (a) Provision of loans; (b) Leasing office space with utilities; and (c) Consulting services on specific issues: management, marketing, human resources, or information technology.

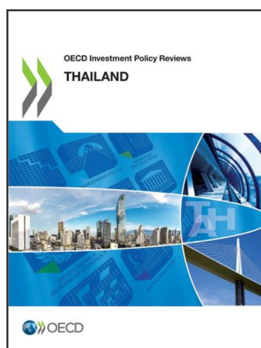
Notes

[1] See Ministerial Regulation No. 4 Determining Service Businesses which Are Not Required to Apply for Permission for a Foreign Business License B.E. 2562 (2019).

[2] "What is a minimum capital requirement? It is the share capital that must be deposited by shareholders before starting business operations. For the Doing Business starting a business indicator the paid-in minimum capital is usually the amount that an entrepreneur needs to deposit in a commercial bank or with a notary when, or shortly after, incorporating a business, even if the deposited amount can be withdrawn soon after a company is created" (World Bank, 2014).

[3] The FBA defines foreigners as: (1) a natural person not of Thai nationality; (2) a juridical person not registered in Thailand; (3) a juridical person registered in Thailand in which (1) or (2) hold no less than 50% of the total capital shares or, in the case of a limited partnership or registered ordinary partnership, the managing partner or the manager of which is natural person not of Thai nationality; (4) a juridical person registered in Thailand in which (1), (2), or (3) hold no less than 50% of the total capital shares.

[4] See, for instance, Bangkok Post (2018) and the recent announcement of a government programme developed by the Department of Special Investigation in collaboration with the Department of Business Development, the Provincial Administration Department, the Revenue Department and the Immigration Bureau in order to analyse and track down offenders who run afoul of the Foreign Business Act (Bangkok Post, 2019).



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