

LEGAL ARTICLE

## DEALING WITH FLOODS FROM LEGAL PERSPECTIVE

By Narit Direkwattanacahai, LLM (Cambridge)



As the year end of 2011 is approaching, Thailand, in particular Bangkok, is facing the worst flooding in decades. Obviously, it is the worst humanitarian crisis as many residents have been trapped in their houses for several weeks without electricity and access to tap water.

Major industrial estates located on the outskirts of Bangkok have been inundated by a large amount of water flowing from the north of Thailand, effectively cutting the critical supply chains. Once again, just-in-time production is called into question. Logistically, distribution centers of many retailers/manufacturers located in the northern suburbs of Bangkok have been cut off from the rest of the world by the flood water.

While the crisis is definitely far from over as of today, the companies facing this crisis may want to take a look at how to remedy the situation from the legal perspectives.

### 1. Force Majeure Clause in Supply/Sale Contract



In case where a seller company cannot deliver goods to a customer because of the flooding situations (either the production base is flooded or the logistic route is unavailable), the force majeure clauses in many of typical supply/sale contracts require the seller to notify the customer in writing of the

occurrence of the force majeure event, otherwise seller's right to raise the force majeure event as an excuse for non-delivery of the goods will be put into jeopardy.

Therefore, whenever flooding makes it impossible for a seller to make the delivery of goods to a buyer within a contract deadline, the seller had better review the force majeure clause in its supply/sale contract to determine whether the seller has any obligation to take any action or not.

As mentioned above, in the circumstance normally a seller is required to notify a customer in writing that the force majeure event occurs. In addition to the notification of occurrence of the force majeure event, in some supply/sale contracts, the force majeure clauses further require the seller to notify the buyer in writing of the course of actions the seller plans to take to remedy the situation so that the delivery of the goods can be made.

Even if the force majeure clause does not impose the written notification requirement, it is still a good idea for a seller to communicate with a buyer in writing about the flooding situation.

## 2. Employees and Suspension of Business Operation

Where a company's premises (i.e. factory or office) are inundated by the flood water, the performance of obligations under employment contracts becomes impossible. Inundation is deemed the force majeure event. In this event, legally speaking the company does not have to pay the wage to employees only to the extent that the suspension of the business operation is attributable to the floods. Basically, once the water reaching company's premises is high, it is legally possible for the company to claim that the force majeure event occurs in order to suspend the payment of wage.

On the other hand, in case the company intends to help its employees during this difficult period, the company is recommended to consider the tax consequences before handing out any flood assistance to it employees.

Besides relying on the force majeure event, the company still has another option, i.e. suspension of business operation. The flood affected company may exercise the right under the Labor Protection Act, B.E. 2541 (1998) to suspend the business operation either entirely or partially and pay employees 75% of the wage during the suspension period. The Labor Protection Act, B.E. 2541 (1998) provides that the company must notify employees and a labor inspector in advance three working days prior to the suspension period.



## 3. Special Assistance to Employees

In this crisis, many companies choose to go an extra mile to retain their talent by offering different forms of the special assistance to their employees. In designing the special assistance (flood assistance), the company has to consider these three tax questions.



**A. Can the company book the special assistance expense as deductible expense in computation of its net profit for the purpose of paying corporate income tax under the Revenue Code?**

Needless to say incurring any nondeductible expense is not tax efficient at all. In order to make certain expenses deductible, the company may have to issue the regulation/notification for the special assistance. It is noted that some forms of assistance may be deemed nondeductible by the revenue official regardless of whether the company issues the regulation/notification or not.

**B. Is the special assistance considered employee's assessable income?**

On the surface, this question may seem irrelevant to the company. But it is relevant to the company. If the special assistance is employee's assessable income under the Revenue Code, then the company has to deduct withholding tax upon giving out the special assistance to each employee. Whether the special assistance is deemed employee's assessable income or not

depends on the form of the special assistance. First, some perks are specifically exempt from income tax by the Revenue Code. Second, other perks are interpreted by the Revenue Department as non-assessable income. Selecting the form of the special assistance carefully may help employees save some tax.

**C. Does the company have to charge, collect and remit VAT on the value of the special assistance to a local revenue office upon handing out the special assistance to employees?**

In handing out certain goods or services to employees, the company may be required to charge, collect and remit VAT on the value of the special assistance (either goods or services) to a local revenue office. To avoid any violation of VAT law, the company should examine the VAT consequence carefully. The answer to this question depends largely on what the special assistance is.

## 4. Insurance

Many companies have insurance coverage. Before filing a claim to an insurer, an insured should review the terms and conditions of the coverage in the policy first. This claim process may involve the negotiation with an insurer. The insured is recommended to take picture of the damage or loss as evidence to substantiate insured's claim. Definitely, insurer's surveyor will have to examine the damage or loss too. When the negotiation with the insurer fails to yield any satisfactory or acceptable result for the insured, the insured may have to bring the case to the courtroom. Company's evidence showing the damage or loss is crucial to strengthen its claim against the insurance company.

Earlier this year the previous administration introduced the tax exemption on the insurance compensation. Under this tax exemption, the compensation amount for the damage caused by flooding that a company (an insured) receives from an insurance company shall be exempt from corporate income tax only for the

amount in excess of the cost of the property after subtracting depreciation and amortization. This exemption is applicable for the year in which the compensation is paid to an insured.

## 5. Tax Treatment of Salvage or Damaged Property

After the water recedes, the company may not book the remaining book value of the property that is damaged to the extent that it can no longer function as deductible expense. But if the company destroys or sells the damaged property, the company can book the remaining book value of the damaged property as expenses.



In case of sale of the damaged property, the proceeds from the sale of the damaged property must be included in the income in computation of the net profit for the purpose of paying corporate income tax.

## 6. Government Support

Apparently, corporate Thailand cannot expect much from the government in terms of the financial support. At this point, this administration has not elaborated in detail on how the government will help companies affected by this crisis.

However, in case a flood affected company happens to receive any compensation amount from the government, the amount shall be exempt from corporate income tax insofar as the company registers with a victim relief center or agency of the government.

## 7. Donation Deduction

A company who makes a donation to the flood victims through a other company or a other juristic partnership or any other juristic person who is a qualified conduit may claim the tax deduction from the amount equal to the amount of donated money or the amount of donated property under the condition that the sum of this donated amount and the donated amount for

other charities does not exceed 2% of its net profit.



To be eligible as a qualified conduit, the conduit must register with a revenue office and issue the receipt of the donated money or the donated property to a company claiming this deduction. A company who is a VAT registrant makes the donation of the goods to the floods victims through a qualified conduit shall be exempt from VAT for the donated goods.

*This legal article was written by Narit Direkwattanachai, a corporate & tax attorney at NARIT & Associates with expertise in corporate tax and commercial dispute. He holds a bachelor of laws (1<sup>st</sup> class honors) from Chulalongkorn University, a master of law from the University of Cambridge, UK and an MBA in finance from the Georgia Institute of Technology, USA. He can be reached at [narit@naritlaw.com](mailto:narit@naritlaw.com)*

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