

# Structural Reform in Thailand

Paper by

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### **Introduction**

Thailand boasts one of the strongest ever track records for long-term economic growth in the developing world. Successful economic development efforts have led to three decades of sustained GDP growth, averaging more than 6% per annum. Moreover, the benefits of this growth have been shared widely across Thai Society, elevating living standards of the lower classes and creating one of Southeast Asia's largest middle classes.

The economic crisis, which started in 1997, however, has cast doubt on the sustainability of Thailand's earlier growth models. The exchange instability and the collapse of the financial sector adversely affected other main economic sectors which in turn resulted in substantial contraction of the overall Thai economy in the late 1990s.

Thailand has explored a variety of strategies for reviving economic growth. These efforts have included fiscal stimulus spending, technical support to SMEs, and trade liberalization. Structural reform has also become a priority in Thailand's development plans to build strong fundamentals within the economy in order to maintain economic stability and to safeguard against the emergence of the so-called bubble economy in the future. The government's work includes efforts to reform the financial sector and also deregulation of state-owned enterprises.

The 1997 economic crisis had renewed our awareness and pointed our attention to the need for legal reforms in Thailand. The impact of the crisis clearly signified the fact that the legal system is neither adequate nor capable of dealing with the economic and social situation of today's world. A number of laws that directly impacted the economy, for example, Bankruptcy and Foreclosure Laws and Foreign Business Acts, have been amended in order to adequately accommodate economic needs and to tackle difficulties and problems arising from changing circumstances.

This paper will attempt to illustrate both past and ongoing efforts in the area of structural and legal reforms, including deregulation in Thailand, that have taken place during the post-crisis period.

#### **a. Financial Sector Reform**

One of the key objectives behind the government's package of recovery measures was to restore confidence in the overall financial structure within Thailand's economy. It was necessary to enhance transparency while providing greater market access to foreign participation in the Thai economic and financial sectors.

The recovery measures began with the forced closure of insolvent institutions in order to pave the way for possible restructuring of the financial sector. At the same time, those institutions and banks considered viable were given a life-line through recapitalization measures to strengthen existing operations past the crisis. It was also important to revise the entire prudential framework, including loan classification, provisioning and adherence to international standards to ensure that appropriate rules

and regulations were in place. As a result, the Financial Institutions Act was passed in parliament to enable a more modern and efficient regulatory framework to be established that would help control financial activity and minimize irregularities within both the financial and banking sectors. In addition, the Bank of Thailand Act was later introduced to strengthen banks independence and accountability and to restore confidence in the banking system. To complete the recovery package, the government set up a special company called the Thai Asset Management Corporation to oversee and resolve bad debts accumulated by discreditable institutions.

Stability within the financial sector paved the way for overall economic recovery that stemmed from implementation of government measures previously mentioned. To ensure a sustained recovery, the Thai government continued to focus their attention on improving the functionality of the financial sector with the goal of achieving future economic development. As a result, "The Financial Sector Master Plan<sup>1</sup>" was introduced in January 2004 as a guideline for the development of the financial sector over the next 5-10 years. The main purpose of the Master Plan is to increase efficiency of the financial system and to institute a more balanced role for the capital market vis-à-vis the financial institutions. Furthermore, the plan aims to broaden general access to high quality services to the underprivileged groups, especially people in rural areas, SMEs and micro enterprises. It also aims to promote fairness and better protection for consumers.

Details of the Financial Sector Master Plan can be viewed from the Annex A.

## **b. The Privatization Master Plan<sup>2</sup>**

The Thai cabinet approved the Master Plan for State Enterprise Reform in September 1998. This plan provides an outline of the objectives and timeframes for the reform programs as well as the privatisation transactions for Thailand's utility and infrastructure sectors (namely, telecommunications, transport, water, and energy) and also privatisation or partial divestiture of additional enterprises in commercial and industrial sectors.

The Privatisation Master Plan, as it has come to be referred, establishes a framework for reform and privatization. The plan defines a total of 59 state-owned enterprises (SOEs) in five sectors:

- Telecommunications;
- Energy;
- Transportation;
- Water, and
- Others (industrial, commercial, agricultural, social and research).

The Master Plan provides a framework to addresses:

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<sup>1</sup> The Bank of Thailand ([www.bot.or.th](http://www.bot.or.th))

<sup>2</sup> The State Enterprises Policy Office ([www.sepo.go.th](http://www.sepo.go.th))

- legal, institutional and regulatory issues;
- new entrants;
- sector liberalisation;
- the introduction of international best practices;
- divestiture;
- performance monitoring and;
- the process for capital market reform.

With respect to the sections on utility/infrastructure, the Master Plan and related policy documents that are being prepared by the Ministry of Finance and various sector Ministries will define the market and the regulatory structure in each sector. The plan calls for a clear separation of policy, regulatory and operational responsibility and the liberalization of markets where possible. Consequently, incumbent State Enterprises will need to be in a position to compete as an operator as well as be prepared for future privatization. The timeframe governing the Privatization Master Plan is eight years (1998 to 2006).

Thailand's privatization program aims to improve the economic efficiency of the economy's infrastructure sectors and relevant enterprises while lowering the costs to consumers and increasing service quality and coverage. Further, the investment burden will be shifted from the government to the private sector.

Integral to the reform of the utility and infrastructure sectors will be the creation of independent economic regulatory authorities that will regulate tariffs for networked industries and where possible promote the introduction of competition and further liberalization.

The focus for the initial stages of the Privatization Master Plan has been on the preparation of market and regulatory policies for the utility and infrastructure sectors. Table 1 describes the key reform initiatives since January 2000.

**Table 1: Key Reform Initiatives**

| Sector            | Key Reform Initiatives   |
|-------------------|--|
| Telecommunication | <ul style="list-style-type: none"> <li>• Creation of independent regulator, National Communications Commission (NCC)</li> <li>• Domestic market liberalisation by October 2000</li> <li>• Corporatisation and privatisation of the dominant SOEs, the Telephone Organisation of Thailand (TOT) and the Communications Authority of Thailand (CAT).</li> <li>• The Cabinet plans to consider and potentially approve the privatisation in 2000.</li> <li>• Full market liberalisation by 2006 in accordance with WTO</li> </ul> |
| Energy            | <ul style="list-style-type: none"> <li>• Power sector restructuring, including:               <ul style="list-style-type: none"> <li>➢ Creation of power pool</li> <li>➢ Formation of independent regulator</li> <li>➢ Privatisation of Electricity Generating Authority of Thailand (EGAT) generating assets beginning with</li> </ul> </li> </ul>  |

|                |   |
|----------------|---|
|                | <ul style="list-style-type: none"> <li>Ratchaburi Power Plant</li> <li>➤ Subsequent privatisation of distribution (Metropolitan Electricity Authority (MEA), Provincial Electricity Authority (PEA)).</li> <li>• Gas</li> <li>➤ Separation of state owned Petroleum Authority of Thailand (PTT)'s gas trading from distribution functions</li> <li>➤ Creation of third party access regime</li> <li>➤ Formation of independent regulator</li> <li>➤ Privatisation of PTT</li> </ul> |
| Transportation | <ul style="list-style-type: none"> <li>• Restructuring of governmental institutions, creation of independent regulators</li> <li>• Privatisation, partial privatisation or restructuring of 14 SOES including, Thai International Airways, Airports Authority of Thailand, Port Authority of Thailand, Bangkok Mass Transit Authority (urban buses), State Railway of Thailand (SRT)</li> </ul>   |
| Water          | <ul style="list-style-type: none"> <li>• Restructuring and privatisation of Metropolitan Water Authority (MWA), Provincial Water Authority (PWA), and Wastewater Management Authority (WMA)</li> <li>• Will establish an independent regulatory body</li> </ul>   |

The need for structural reforms in the key sectors combined with the necessity of establishing a clear regulatory framework prior to privatization means that, with the exception of the enterprises on the 'fast-track' list, most privatization transactions would not occur during the initial stage of the reform program.

Some privatization plans have undergone revisions as they moved through the approval process, which has resulted in some delays in bringing specific transactions to market.

Since 1997, to date there have been a number of key successful privatization activities, as the table below indicates.

**Table 2 : List of Privatized Companies and Method of Privatization**

| 1997 | Off-Shore Mining Organization         | Agricultural | Dissolution   |
|------|---------------------------------------|--------------|---|
|      | The Provincial Waterworks Authority   | Water        | Set up subsidiary (East Water) to provide water supply in Eastern Seaboard area, then IPO |
|      | The Metropolitan Waterworks Authority | Water        | Set up new company to offer pipeline maintenance services                                 |
| 1998 | The Preserved Foods Organization      | Industrial   | Dissolution   |

|             |   |                       |                                       |
|-------------|---|-----------------------|---------------------------------------|
|             | The Textile Organization                        | Industrial            | Dissolution                           |
|             | PTTEP (PTT'S subsidiary)                        | Energy                | Public Offering                       |
|             | EGCO (EGAT's subsidiary)                        | Energy                | Strategic sale to China Light & Power |
| 1999        | -   | -                     | -                                     |
| 2000        | -   | -                     | -                                     |
| 2001        | PTT   | Energy                | Initial Public Offering               |
| <b>Year</b> | <b>State Enterprise</b>                         | <b>Sector</b>         | <b>Method of Privatisation</b>        |
| 2002        | Airport Authority of Thailand (AOT)             | Transportation        | Corporatizaton                        |
|             | Telecommunication of Thailand (TOT)             | Communication         | Corporatizaton                        |
| 2003        | Communication Authority of Thailand (CAT)       | Communication         | Corporatizaton                        |
|             | Krung thai Bank                                 | Financial Institution | Public Offering                       |
| 2004        | Bangchak Petroleum Public Company (BCP)         | Energy                | Second Public Offering                |
|             | Thai Airways International Co., Ltd.(Thai)      | Transportation        | Second Public Offering                |
|             | AOT   | Transportation        | Initial Public Offering               |
|             | Mass Communication Authority of Thailand (MCOT) | Communication         | Corporatizaton                        |

Source : State Enterprises Policy Office

The results of privatization efforts over the last decade have reduced the number of state enterprises from about 100 to 59 today. This has been accomplished through the liquidation of small-scale enterprises, partial sale of shares, mergers (such as Thai Airlines Co. and Thai Airlines International); and partial divestitures.

### c. The Stock Exchange of Thailand Reform

Even though many of the primary causes of financial crises exist primarily beyond the boundaries covered by corporate governance and securities regulation, there seems to be evidence to support the view that there was sub-optimal performance of these laws. First, the quality of disclosure received by investors in Thailand was extremely poor, considering the fact that the economic meltdown had taken so many investors by surprise. Second, evidence also points to rampant insider trading and outright fraud by

managers during the boom years. Finally, there were no successful prosecutions for securities fraud or insider trading after the meltdown and investors had no viable legal recourse to seek compensation.

In the early years that followed the Asian financial crisis, Thai government officials pursued a strategy of legal reform that was consistent with the Washington Consensus prescriptions. In the realm of securities regulation, the most significant step occurred in 1999 when the SEC and SET moved from a qualitative to a more disclosure-based system of regulation. This had the advantage of being a more efficient means of deployment of the regulators' resources, as investors themselves will have to take responsibility for the outcomes based upon the information available. In the first year of heightened disclosure scrutiny, 38 listed firms were required to revise their financial statements, 79 companies were penalized for late or faulty disclosure and 14 securities companies were fined a total of 15.5 million baht.

The SEC also required listed companies to form independent audit committees by the beginning of 2000 to scrutinize company disclosures and accounting procedures, and called for firms to appoint at least two independent directors to their boards.

In order to ensure that Thai directors were getting the message across about the heightened expectations for their performance during the post-crisis era, the SET, SEC and Bank of Thailand established the Thai Institute of Directors (IOD). The IOD was responsible for organizing a curriculum for directors regarding their duties, the principles of good corporate governance, transparency and their responsibilities to their shareholders, while stressing that good governance is good business.

In late 1997, Thailand sought financial assistance from the Asian Development Bank (ADB) under the auspices of the Financial Markets Reform Program. Under this program, Thailand was required to restructure its financial markets in accordance with what is referred to as the "Policy Matrix" as specified by the ADB. The Policy Matrix also requires Thailand to amend the Securities and Exchange (SEC) Act. The major amendments that must be promptly carried out, in accordance with the ADB's request are as follows: (1) restructuring the Securities and Exchange Commission (SEC) and the board of directors of the self-regulatory organization (SRO) to become more independent; (2) empowering the SEC to issue or withdraw securities business licenses; and (3) promoting and developing the role of the SRO to be more independent and efficient.

Accordingly, the Office of Securities and Exchange Commission has compiled studies and reviewed provisions in the SEC Act and has proposed a draft Amendment to the SEC Act aimed at promoting greater efficiency in its regulatory supervision and law enforcement functions as well as good corporate governance, transparency and protection of shareholders and investors. This draft was approved by a committee at the Ministry of Finance and is currently pending consideration by the Committee at the Office of the Council of State.

#### **d. Bankruptcy Laws**

The financial crisis in 1997 also stressed the need for amendment to the Bankruptcy Laws in Thailand in order to regain confidence of lenders, especially foreign lenders, who contribute significantly to investments in Thailand. The amendment was also a condition set down by IMF to qualify for the US\$ 17.2-billion bail-out package.

Therefore, Thailand's House of Representatives and Senate approved and adopted the amendments to Thailand's 1940 Bankruptcy Act on March 4, 1998. The amendments became effective on April 10, 1998 in the form of the Bankruptcy Act Amendment No. 4.

Although the 1998 Amendment remained intact with the old regulations, it was warmly welcomed by both the legal and business communities in Thailand and abroad, by adding a new chapter to the old Act. The new chapter introduced alternative avenues for creditors seeking satisfaction for amounts owed to them with a structure designed to rehabilitate a debtor's business and to render viable a distressed company while protecting the interests of the creditors.

One feature of the new law is that it allows new creditors, such as those putting fresh funds into cash-strapped companies, the option to seek the right of repayment under the reorganization plan by sending a letter to the planner or, by a repayment request with the receiver. This aspect of the new law was commended as it allowed parties to inject new capital into ailing businesses without the fear that they will be denied the opportunity to regain their investment.

Because the 1998 amendment was passed abruptly, the house of Parliament then decided to pass an amendment to the 1998 amendment. The Bankruptcy Act Amendment No. 5, was passed by the house of parliament in March 1999. The purpose of Amendment No. 5 was to refine and strengthen the principles introduced in the 1998 amendment and to address certain issues of contention which were not properly dealt with under the 1998 Amendment. One such issue concerned the exemption of guarantors of debts from bankruptcy suits.

The 1999 amendment also shortened the time period which a person declaring bankruptcy could be discharged, from ten years to three years, on the condition that the bankrupt person was not guilty of any misconduct or fraud contributing to his insolvency. In addition, it introduced a mechanism of classification of creditors in order to resolve issues involving the rights of small creditors. As previously mentioned, many privileges were reserved for creditors who owned a minimum of two thirds of the total outstanding debt. Furthermore, the amendments increased the amount of debt required before a bankruptcy proceeding could be initiated against a debtor from Baht 50,000 to Baht 1,000,000 for a natural person and from Baht 500,000 to Baht 2,000,000 for a juristic entity.

In line with the amendment to the Bankruptcy Act, a special Bankruptcy Court was also established with a rationale that bankruptcy cases are fundamentally different from general civil cases and that the results of bankruptcy cases may have effects on the economy as a whole. Further, it was considered necessary to have judges with specialized experience and training in bankruptcy cases presiding in these cases. With the establishment of the Central Bankruptcy Court, Thailand's debtors and creditors can expect a faster and more efficient disposition of their bankruptcy and debtor rehabilitation cases.

Moreover, new foreclosure laws have also been passed with the aim of shortening the timeframe for foreclosure cases to be completed. The new laws allow most foreclosure cases to be completed within a twelve to eighteen month time frame. It



also means that "non-complicated cases" are to be heard continuously every day until judgment is rendered. This is in contrast to the old law under which cases could be extended for months. Further, the execution process which follows the foreclosure adjudication has also been shortened due to the fact that (a) there can only be one objection to a bid price at an auction and (b) if the price, at the second auction, is close to the one offered at the first auction, the property must be sold. In addition to such new elements to the law, the expansion of the Courts of Appeal will also facilitate a faster process if foreclosure cases are taken to the appeal stage.

#### **e. The Foreign Business Act**

Prior to 1999, the most important law governing alien-controlled businesses in Thailand was the Alien Business Law 1972 (National Executive Council Announcement No. 281). In 1999, a new Act, entitled The Foreign Business Act, B.E. 2542 (1999), was then introduced to replace the Alien Business Law. One important feature of the new Act is that it divides the various types of businesses into three main categories - each category subjected to different limitations with respect to foreign ownership.

Activities that fall under List 1 are strictly prohibited to aliens.

Businesses that are covered under List 2 are prohibited to aliens unless specific permission is granted by the Commerce Ministry, and with approval by the Cabinet. Alien juristic entities allowed to engage in List 2 activities must meet the following two conditions:

- At least 40 percent of all shares must be held by Thai persons or non-alien juristic entities (This may be reduced to 25 percent on a case-by-case basis)
- Two-fifths of the members of the Board of Directors must be of Thai nationality.

Activities in List 3 are prohibited to aliens unless permission is granted by the Director-General of the Department of Business Development, Ministry of Commerce, and with the approval of the Foreign Business Board.

The List of businesses under each category can be viewed under Annex B

#### **f. Thai Trade Competition Act**

The Trade Competition Act of 1999 has been enacted since April 1999, along with the Price of Goods and Services Act of 1999. These two laws replaced the former Price Fixing and Anti-Monopoly Act of 1979. The 1979 Act consists of two parts - pricing and anti-monopoly. The section on anti-monopoly in the 1979 Act is aimed at promoting fair competition. It empowers the Central Committee to look after business structures that may create a monopoly and engage in restrictive business practices. However, since this law created problems in enforcement, the Department of Internal Trade (the agency in charged of the Act) amended the Act by separating it into 2 Acts, namely, The Price of Goods and Services Act and the Competition Act.

The objective of these Acts is to promote fair and free trade under a competitive environment and to control anti-competitive practices. This is based on the view that competitive markets are the best way to promote economic efficiency, and thus

maximize total economic welfare. Finally, consumers will benefit through more efficient pricing and increased choice of products and services.

The scope of the Act applies to all types of business operations except:

- central, provincial, or local administration;
- state enterprises under the law on budgetary procedure;
- groups of farmers, cooperative or cooperative societies; and
- businesses prescribed under the Ministerial Regulation.

The Trade Competition law is enforced by the authorized government body namely, the "Trade Competition Commission" with the Minister of Commerce as the Chairman, the Permanent-Secretary for Ministry of Commerce as the Vice-Chairman, the Permanent-Secretary for the Ministry of Finance and not less than 8 but not more than 12 qualified persons in the field of law, economics, commerce, business administration or public administration as members, and the Director-General of the Department of Internal Trade as the Secretariat. The commission shall have the powers and duties to consider complaints, prescribe rules for dominant position, consider applications seeking permission to merge businesses, or to initiate joint reduction in competition. They also have the powers to suspend, cease, correct, or vary the activities undertaken by business operations.

To date, progress of work under Trade Competition Act can be concluded as follows:

1. The Trade Competition Commission has established 7 Sub-Committees responsible for:
  - 1.1 The cable television monopoly case and restrictions on video movies production businesses
  - 1.2 Restriction on whisky and beer
  - 1.3 Criteria and guidelines for mergers
  - 1.4 Unfair trade practices
  - 1.5 Wholesales / retail businesses
  - 1.6 Restrictions in the motorcycle industry
  - 1.7 Criteria for dominant position
2. Approved forms, rules and procedures, applications for permission of any concerted agreement amounting to monopoly, reduction of competition or restriction of competition according to Article 27 (5)-(10). They were published in the Government Gazette on February 25,2000.
3. Approved criteria for dominant enterprise in 2 sectors.
  - 3.1 Wholesales and retail businesses
    - Single enterprise has market share 20% or more and last year sales volume above 27,000 million Baht
    - Top 3 enterprises having a combined market share of 33.33% or more and combined sales volume above 45,000 million Baht