



## **TMI Eye No. 6 Sales of Goods vs. Provision of Service for Tax Purposes**

In this article, we would like to bring to your attention the differentiation between the sales of goods and the provision of services (hire-of-work). TMI has encountered several cases in which taxpayers have misconstrued the type of transactions, thereby leading to tax liabilities. This article aims to provide guidelines for these transactions so that readers can review their own transactions, identify their tax position, and determine whether there are any risks.

### **Comparison of Tax Implications**

The Revenue Code imposes different tax implications for sales of goods and provision of services (or hire-of-works), as set forth below.

	<b>Sales of Goods</b>	<b>Provision of Services</b>
<b>VAT</b>		
• Tax Base	7% of the sale price	7% of remuneration (may include raw materials)
• Tax Point	Generally, upon the delivery of the goods	Generally, upon the receipt of payment
<b>Withholding Tax</b>	NA	3% of remuneration
<b>Stamp Duty</b>	NA	1 Baht for every 1,000 Baht of remuneration (0.1%), upon execution of the agreement

### **How to classify the type of agreement?**

In principle, a sale of goods is a contract whereby the seller transfers ownership of goods to the buyer, and the buyer agrees to pay the price for such goods. On the other hand, a hire-of-work is typically a contract whereby the contractor agrees to accomplish a definite task for the employer, who, in turn, agrees to pay remuneration based on the results of the work.

However, modern-day transactions become more sophisticated, and disagreements can arise between taxpayers and the Revenue Department. Take, for example, a situation where a taxpayer produces a product based on detailed instructions from customers. The complexity increases when the customer provides key raw materials and a secret recipe. In such cases, questions arise as to whether this should be considered

manufacturing for sale, or whether it would more appropriately be classified as a contract manufacturing service for tax purposes.

The criteria for considering the difference between the two types of transactions are as follows:

- 1) Parties' intent.
- 2) Form of the agreement.
- 3) Aim of the transaction, focusing on the result of the work, or the materials.
- 4) Ordinary course of business of the manufacturer.
- 5) Procurement of raw materials, particularly the key materials.
- 6) Owner of the formula, recipe, know-how, or intellectual property.
- 7) Type of products.

Here are some examples.

- **Manufacture:** If a manufacturer sells certain products in its ordinary course of business and receives an order to manufacture the same or similar products, it will be considered a sale of goods, regardless of minor adaptations. However, if the manufacturer does not produce such product in its ordinary course of business, the manufacturing of such product will be considered a hire-of-work. For instance, when the customer supplies most of the materials and formula, the manufacturer would be regarded as providing a hire-for-work service.
- **Construction with the supply of material:** It is generally considered that the purpose of construction is the result of the work. Therefore, even if the payment for the materials and that for the services is separate, it is still regarded as a hire-of-work.
- **Sale of goods with installation:** The sale of goods, such as an elevator, an escalator, or an air-conditioning with installation is, as a whole, considered a sale. However, if the sales and the installation services are separate, and the selling price and service charge are clearly distinguished, it is considered to involve two transactions: i.e., the sale of goods and the hire-of-work. In the latter case, the service portion is subject to withholding tax and stamp duty.
- **Repair service:** A repair service is generally treated as a service, and thus the entire amount of the remuneration (spare parts and labor) is subject to withholding tax.

### **Important Points for Readers**

Readers should exercise caution when classifying the types of contracts. If the transaction is treated as a sale of goods, the seller must issue a tax invoice with a 7% tax rate upon the delivery of such goods, which typically occurs earlier than the provision of services. Please note, however, that sales are not subject to a 3% withholding tax or stamp duty.

However, if the transaction involves the provision of services or a hire-of-work, the customer must deduct a 3% withholding tax from the payment. Additionally, the service provider (e.g., the manufacturing company) is required to pay stamp duty at the rate of 0.1% of the remuneration.

Based on our experience, it is more common for manufacturers to consider themselves as sellers, but they may actually be classified as service providers for tax purposes. In such cases, the manufacturer may inadvertently fail to pay the required stamp duty, while the customer may neglect to deduct the 3% withholding tax. Additionally, there is also a risk of failing to charge 7% VAT and issue tax invoices at the correct time. These oversights could lead to penalties for both the manufacturer (including stamp duty and a surcharge of up to 6 times the duty) and the customer (including 3% withholding tax and a surcharge of up to 100% of the tax).

Therefore, readers should exercise the utmost caution when classifying transactions. Ensuring the correct interpretation of transactions will lead to proper tax treatment. Otherwise, taxpayers may face the risk of being assessed for tax liability by the Revenue Department.

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