

## SAP License & Cost Allocation - Royalties Tax Dispute in Thailand

The Supreme Court of Thailand ruled in 2013 on the tax case of withholding tax against Esso (Thailand) Plc ('ETP'), one of the largest oil company listed in the Stock Exchange of Thailand.

In this case, ETP entered into **Master Services Agreement** with its affiliate Belgian company (Esso Coordination Center N.V. - ECC) in 1997. The terms of the agreement included '**Cost Allocation**' relating to the 'Accounting System' used among group companies including ETP in Thailand. In 1999, ETP made payments for the fee of THB 182 million for the cost that ECC allocated to ETP in Thailand and claimed that they mistakenly deducted 15% withholding tax of THB 27 million. The Thai Revenue Department ('TRD') wrongly granted the refund to ETP upon its request.

7 years later, the TRD came back and ordered ETP to return the tax refunded to ETP of THB 27 million to the TRD as the payment should had been considered as royalty which was subject to withholding tax at the rate of 15%. Unsurprisingly, after ETP returned this amount to the TRD, it proceeded to file a lawsuit to the Central Tax Court ('CTC') against the TRD to claim the tax refund back.



The CTC dismissed the claim of the tax refund raised by ETP. ETP then argued the CTC's decision to the high court.

The Supreme Court at the end ruled in favor of the TRD on the following basis:

1. Exxon Mobil Corporation, the parent company in the US, entered into the **License Agreement** with SAP America Limited for the use of a '**Computer Software**' i.e. SAP R/3. This software was aimed to centralize accounting system among Esso Affiliates around the world. With this license, all Esso Affiliates would have access to the SAP R/3 and received maintenance services from SAP's affiliate company including ETP in Thailand. For the use of the software, the cost would be allocated based on the actual usage.

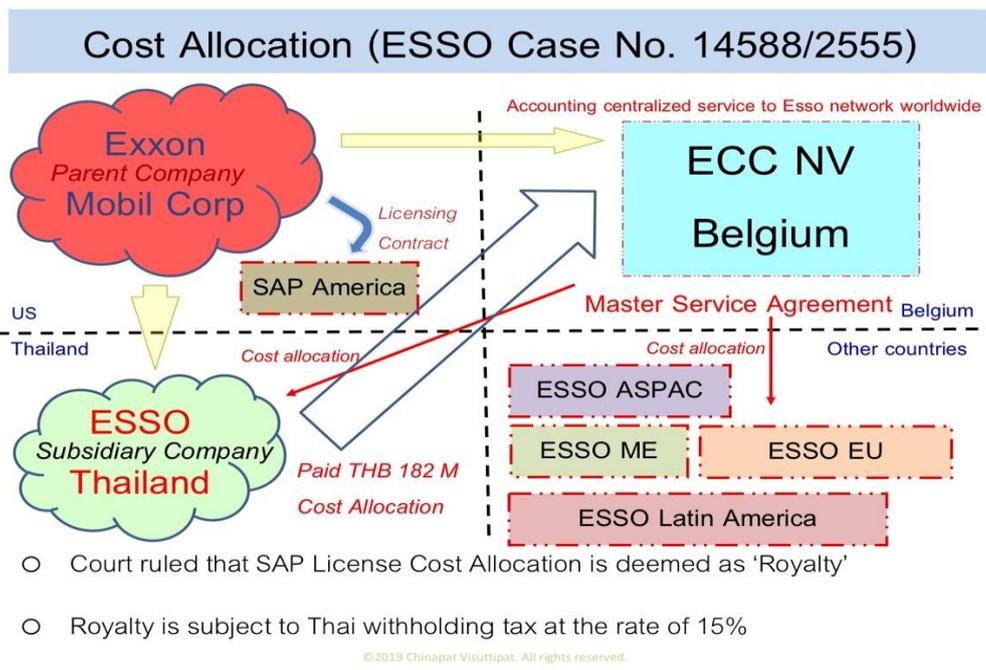
2. ECC in this arrangement would act as the center of gathering accounting information from each Esso Affiliate for the centralized service and maintenance. ECC did not have the ownership over nor the right to sub-license the SAP R/3. As a result, the Supreme Court considered that ECC was not the software service provider to ETP.
  
3. The Supreme Court had their position that regardless of the fact that ECC was not the software service provider, the payment ETP paid for cost allocation should be 'deemed' to be payment of royalties for the right to use the SAP computer software through ECC.

#### ONE Law's Comments

As above, it is understood from the case that a payment for 'cost allocation' should be traced back to its source to investigate the genuine purposes of the payment. The Court would generally adopt the "**Substance Over Form**" concept. Although the agreement terms specify that the payment is for the cost allocation, the court might see it differently as the court would identify the nature of the payment as to whether such payment includes an element of royalties to ensure tax implications and consequences.

There is one thing we found unfortunate of Esso Thailand (ETP) for returning the tax refund to the Thai Revenue Department prior to the final decision of the court.

If Esso Thailand had held the tax refund until the court's final judgement, it would have been the TRD that started the lawsuit to claim over the tax refund. If that was the case, 'burden of proof' and 'court fee' would have been shifted to the TRD and not borne by Esso Thailand. In addition, Esso Thailand would have enjoyed the cash flow of THB 27 million during the court procedure for many years.



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