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Global Business Tax Alert
Sharp Insights

The Supreme Court in the case of Director of Income-tax (IT) vs. A.P. Moller Maersk A S, held that cost reimbursed by Indian agents for utilizing global telecommunication facility cannot be treated as fees for technical services and therefore not taxable.

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Background

- The taxpayer, a tax resident of Denmark, was engaged in the business of shipping, chartering and related business.
- The taxpayer appointed agents in various countries including India for certain services. For the sake of convenience of all the agents and to avoid unnecessary cost, a centralised IT system (global telecommunication facility) was maintained by the taxpayer, which enabled the agents to access information like tracking of cargo, transportation schedule, customer information, documentation system and several other information. The IT system also comprised of booking and communication software, hardware and a data communications network.
- The agents reimbursed cost for the said system to the taxpayer on a pro-rate basis.
- The Assessing Officer ('AO') held these payments to be taxable as fees for technical services ('FTS') under the India-Denmark Tax Treaty ('Tax Treaty').
- The Commissioner of Income-tax (Appeals) ['CIT(A)'] upheld the order of the AO. The Income Tax Appellate Tribunal ('Tribunal') decided the issue in favour of the taxpayer following the decisions of the High Court in Skycell Communications Ltd (251 ITR 53) (Madras) and Bharti Cellular Ltd (319 ITR 139) (Delhi).
- The Bombay High Court ('HC') dismissed the Department's appeal holding that IT system was an automated software based communication system which did not require taxpayer to render any technical services. It was a cost sharing agreement to conduct the shipping business more efficiently. The HC specifically observed that there is no finding by AO or CIT(A) there is any profit element involved in the payments received by the taxpayer from Indian agents.
- The Department, aggrieved by the order of the HC, filed an appeal with the Hon'ble Supreme Court ('SC').

Ruling of the Supreme Court

- No technical services are provided by the taxpayer to the agents. The payment is in the nature of reimbursement of cost whereby the proportionate share of expenditure incurred on the system and maintenance is borne by all agents.
- The SC reemphasized that neither the AO nor the CIT(A) has stated that there was any profit element embedded in the payments received by the taxpayer.
- Further, the Transfer Pricing Officer had also accepted that the payments were in the nature of reimbursement and was at arm's length. Once it is found to be in the nature of reimbursement of expenses, it cannot be considered as income chargeable to tax.
- The SC observed that once it is accepted that IT system is an integral part of shipping business and business cannot be conducted without the same, it is only a facility that was allowed to be shared by the agents. Accordingly, the same cannot be treated as technical services.
- The SC has relied on its decision in the case of Kotak Securities Ltd.(383 ITR 1), where it was held that use of facility does not amount to technical services, as technical services denote services catering to special needs of the person using them and not a facility provided to all.

- The Department filed additional written submission after the conclusion of the arguments claiming the payments to be in the nature of royalty. However, the SC dismissed the same considering it as a "desperate attempt" of the Department as the claim was not made before the appellate authorities or the High Court and considering the fact that even this issue was not raised in appeal filed before the SC.

Conclusion

The Hon'ble Supreme Court held that payments received by taxpayer towards reimbursement of costs incurred for global telecommunication facility provided to the Indian agents could not be termed as fees for technical services and accordingly, not taxable under the Tax Treaty.

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