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Reimbursement of expenditure to member of AOP does not constitute 'share income from AOP'

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Facts of the case

- ITD Cem India JV (the assessee), an 'Association of Persons' (AOP) was formed under a joint venture agreement between ITD Cementation India Ltd. (ITDCL) [an Indian company] and Thai Development Public Company Ltd. [an Italian company]. The assessee was in the business of development of highway projects.
- In the return of income, the assessee, inter alia, claimed deduction of salary paid to employees of one of its members, ITDCL. The assessee claimed that employees of ITDCL were deputed to AOP and the payment was actually made to ITDCL as reimbursement of expenses. The assessee deducted tax at source from the above said payments, by treating the same as contract payments.
- However, the Assessing Officer (AO) considered the payments to be in the nature of salary and disallowed the same on account of non-deduction of tax at source. The AO further held that the payments in nature of salary, interest or bonus paid to its member, are non-deductible expenses as per the provisions of the Income-tax Act (the Act).
- The CIT(A) upheld the disallowance on both counts. The Mumbai Income-tax Appellate Tribunal (Tribunal) deleted the disallowances. The High Court (HC) upheld the order of the Tribunal in deleting disallowance on account of non-deduction of tax at source. However, the HC also expressed the view that the Tribunal has not considered the issue regarding the payments in nature of salary, interest or bonus paid to a member of an AOP and hence, restored the matter back to the Tribunal to consider it afresh.

Issue under consideration

Whether the disallowance of expense for payments made to a member shall prevail only in the case where such payment constitutes share of income from AOP in the hands of the member?

Ruling of the Tribunal

- The Tribunal explained that the disallowance of expenses for payments made to a member of an AOP for the purpose of calculating profits of an AOP inter-alia, include payments of salary and other related expenses. Simultaneously, such payments shall also constitute share income from AOP in the hands of the member.
- The Tribunal observed that the provisions of the Act pertaining to payments made to the members of an AOP inter alia, include interest, salary, bonus, commission or remuneration, etc. and in the instant case, issue under consideration is 'salary and other related expenses' and not 'payments of interest or commission'.
- The Tribunal observed that the payments in nature of salary, bonus or remuneration are usually made for services which are personal in nature, which

can only be provided by individuals. In the instant case, members of the assessee were corporate bodies and hence the question of providing personal services would not arise.

- The Tribunal further held that payments made by the AOP to ITDCL did not constitute "share income from AOP" in the hands of ITDCL. The payment merely offset the expenditure incurred by the member, i.e., the money had been paid to ITDCL towards reimbursement of expenses incurred by it on its employees on behalf of the AOP.
- The Tribunal further noted that ITDCL had duly deducted tax at source on salary payments made by it to its employees who were deputed to the AOP. The Tribunal held that ITDCL had not received the payments from the assessee on its own account. Hence, the same shall not acquire the character of 'share income from AOP' in the hands of ITDCL.
- In view of the same, the claim of deduction of the assessee in respect of reimbursement of salary expenses made to ITDCL was held to be allowed.

Conclusion

This ruling clearly lays down the fact that the disallowance of expense for payments made to a member shall prevail only in the case where such payments constitute share of income from AOP in the hands of the member.

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