



Global Business Tax Alert

Sharp Insights

¹Kolkata Tax Tribunal says payment received for intra-group services, reimbursement of expenses, not taxable in India. Also holds advisory services as not FTS / FIS.

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¹ The Timken Company [TS-569-ITAT-2017 (Kol.)]

Background / Facts

- Timken Company (TC) entered into an agreement with Timken India Limited (TIL), pursuant to which TC rendered various services to TIL in USA.
- No part of the services were rendered in India. The compensation payable by TIL to TC for the aforesaid services, was on a cost-to-cost basis, without any mark-up / profit. The services were in the nature of administrative, technical and other support services.
- The said services were performed centrally, for all associates of the group. Expenses were identified by cost centers and were allocated to group companies on the basis of allocation keys, on scientific and actual basis.
- TIL approached the AAR, for an advance ruling, on whether or not it was required to deduct tax at source on the aforesaid reimbursements. The AAR held that TIL was liable to deduct tax at source.
- Based on the AAR ruling in TIL's case, the tax authorities held that the aforesaid reimbursement was taxable in the hands of TC, as Fees for Technical Services (FTS) / Fees for Included Services (FIS), in India.
- In addition to the above, TIL also received certain other services from third party vendors. These services were in the nature of legal services, inspection services, travelling expenses, etc.
- These services were billed by the third party vendors to TC, which was in turn reimbursed by TIL, at cost.
- The tax authorities held that the aforesaid reimbursements were also taxable in India as FTS / FIS.

Issue for consideration

The Tax Tribunal [ITAT] examined the issue of whether receipt of reimbursement of expenses of the following nature, by a non-resident, would be taxable in India:

- Advisory services
- Third party reimbursements

Ruling of the ITAT

The ITAT held as follows:

Re.: Reimbursement of expenses, in the nature of advisory services

- On perusal of the agreement between TC and TIL, the ITAT held that the services are in the nature of advisory services.
- The ITAT then relied on Example 7 of the MoU between India and USA, of the India-USA Tax Treaty and held that advisory services cannot be held to be 'made available'.
- Based on the above, the ITAT held that the receipt of reimbursement towards advisory services, was not taxable in India.

Re.: Reimbursement of third party expenses

- On perusal of the details filed by TC, the ITAT held that the services were rendered by third parties directly to TIL.
- The ITAT further held that TC was not involved in rendering any services to TIL. The invoices raised by such third parties were settled by TC, which was in turn reimbursed at cost, by TIL.
- The ITAT also distinguished the cases of CU Inspections², on the basis that the current case was not related to obligation of TIL to deduct tax at source, but was on the taxability of the amount in the hands of TC.
- The ITAT further distinguished the case of Van Ord³, on the basis that the services were rendered by third parties and not by TC.
- Based on the above, the ITAT held that the receipt of reimbursement towards third party expenses, was not taxable in India.

²C.U.Inspections (I) (P.) Ltd. v. DCIT [2013] 34 taxmann.com 75 (Mumbai - Trib.)

³Van Ord ACZ Marine Limited Vs. ADIT ITA No.1733/Mds/2011

Conclusion

The issue of taxability of reimbursement of expenses and the obligation to withhold tax at source, on the person making the payment, has been a matter of considerable debate. Recently, the Bangalore ITAT in Tungabhadra Steel Products Ltd. [TS-485-ITAT-2017(Bang)] and Delhi ITAT in SMS Iron Technology Pvt. Ltd. [TS-555-ITAT-2017(DEL)] rejected the contention that withholding tax is not applicable on reimbursement of expenditure. On the other hand, the Mumbai ITAT, in the case of Pfizer Products India (P.) Ltd. v. ACIT [2017] 87 taxmann.com 243, has upheld the principle of non-applicability of withholding tax on reimbursement of expenses.

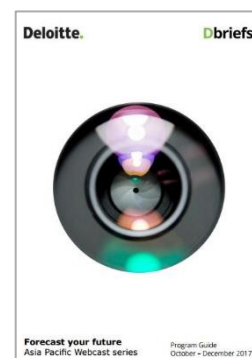
A decision from a higher court would certainly aid in resolving this controversy.

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