

Reimbursement to parent company on cost-to-cost basis not taxable

January 18, 2018

In brief

In a recent decision¹, the Delhi Bench of the Income-tax Appellate Tribunal (Tribunal) held that in the absence of any income element, taxes would not be withheld on actual cost of purchase reimbursed to the parent company.

In detail

Facts

- The taxpayer was an Indian subsidiary of a US based company (parent company). The taxpayer was a reseller of silicon products. It imported computer hardware and software from its parent company to sell them to its customers in India. The taxpayer also provided warranty and post-warranty maintenance services for products of the parent company sold in India.
- The taxpayer entered into a purchase agreement with its parent company for purchase of spare parts required for executing repairs and annual maintenance contract services to its customers in India.
- As per this agreement between the taxpayer and its parent company, the spare parts were obtained by the taxpayer on a cost-to-cost basis without any mark-up being charged by the parent company.
- Since, the payment was in nature of reimbursement for purchase/ sale transaction undertaken with the parent company and the parent company did not have a permanent establishment (PE) in India, the taxpayer did not withhold tax on payment to the parent company.
- Supporting documents like agreement copy with the parent company, payment details, vouchers and sample contracts with customers were furnished by the taxpayer.
- The tax officer (TO) disallowed the taxpayer's claim of expenses pertaining to purchase of spare parts on the grounds that the taxpayer had not supported the claim with proper documents and also could not clarify whether taxpayer complied with the provision of withholding tax. Accordingly, TO observed that the taxpayer was required to withhold tax on the reimbursement made to its parent company relying on CBDT Circular No.7 of 2009.
- On appeal, the Commissioner of Income-tax (Appeals) [CIT(A)] held that there was no provision for withholding tax on purchases, and in the absence of any services being provided by the parent company, no taxes needs to be withheld on the payments made by the taxpayer to the parent company.
- Aggrieved by the CIT(A)'s order, Revenue appealed before the Tribunal.

Issue before the Tribunal

Whether the taxpayer was required to withhold tax on payments made to the parent company towards reimbursement of actual cost of spare parts imported by the taxpayer.

¹ TS-621-ITAT-2017(Delhi)

Revenue's contention

The Revenue contended that the taxpayer could not produce the supporting vouchers and bills for reimbursement of spare cost. In addition, the taxpayer had not furnished the details of parties to whom it rendered the repair services, and in the absence of such details, the addition made by the TO was justified.

Taxpayer's contentions

- The taxpayer contended that as per the agreement submitted before the TO, the payment made by the taxpayer to its parent company was towards reimbursement of actual cost of spare parts, and no additional mark-up was paid thereon.
- As regards the allegation that the taxpayer could not produce the details of parties to whom it rendered repair services, the taxpayer highlighted that it had filed various contracts with the parties in India on a sample basis.
- The taxpayer relied upon the

High Court decision in the case of Van Oord ACZ India (P) Limited², wherein it was held that liability to withhold tax does not arise on a mere reimbursement to a non-resident. The taxpayer also relied on the Supreme Court's decision in the case of GE India Technology Centre (P) Limited³, wherein it was held that liability to withhold tax arose only when the remittance was chargeable to tax in the hands of a non-resident and not otherwise.

Tribunal's decision

- The Tribunal noted that the Revenue had not contended that there was any element of mark-up or margin on the cost-to-cost reimbursement of purchases made by the taxpayer from its parent company.
- The Tribunal held that once it was established that said payments were pure reimbursement of the actual cost of purchase, then ostensibly there was no

requirement of withholding tax while making payment to the non-resident, which was not in the nature of income to the non-resident.

- The Tribunal also observed that the taxpayer supplied relevant details of purchase and parties to whom it rendered repair services.
- Thus, the Tribunal confirmed the order of CIT(A) and deleted the addition made by the TO.

The takeaways

Purchase transactions from outside India are generally not taxable in India unless the non-resident seller entity constitutes a PE in India. The Tribunal has reaffirmed the position that no taxes would be withheld on payments made for reimbursement of cost on purchase/ sale transaction.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact your local PwC advisor

² Van Oord ACZ India (P.) Limited v. CIT [2010] 323 ITR 130 (Delhi)

³ GE India Technology Cen. (P.) Limited v. CIT 327 ITR 456 (SC)

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