SATURDAY INTERNATIONAL TAX GYAN !!!
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Rieter Machine Works Limited v. ACIT (International Taxation), Circle-2, Pune [1]

Reimbursement of software expenses will be liable to tax as FTS/Royalty, where such software was bundled with other IT services of the company.

Facts:

- Assessee, a Switzerland based non-resident rendered IT services of Rs. 20.04 cores to RIPL its group company and paid tax of 10 per cent, pursuant to Master Services Agreement with RIPL.
- Assessee claimed an amount of Rs. 3.89 crores as reimbursement of IT licence cost incurred towards centrally purchasing software licenses on which no tax was paid.

Assessee's contention:

- Assessee submitted that the amount paid was claimed as reimbursement of IT license costs incurred towards centrally purchasing software licenses and use by RIPL (Indian entity) as no markup was applied on cost paid by asseseee.

Revenue's contention:

- Assessing Officer held that amount of Rs. 3.89 crore claimed as reimbursement, was no different from receipt of Rs. 20.04 crore from IT services rendered under Agreement, which was offered to tax and hence would be chargeable to tax in India as Fees for Technical Services/Royalty under article 12 of DTAA.

Ruling:

- In the judgment it was held that for claiming any amount as reimbursement of expense it should fulfill twin conditions:
  - **Undiluted benefit flowing from the incurring of the expenditure is passed on, as such, to the other and**
  - **The amount incurred is recovered as it is from the other without any plus or minus to that**.

[1] 134 taxmann.com 326 (Pune - Trib.)

- If the costs incurred go in a common pool which are then shared by several persons on certain allocation keys, even if the amount so allocated and recovered may be without any mark up, but it may not necessarily constitute reimbursement in the strict sense qua each participant independently. Hence, service could not be considered as reimbursement.
- Further in the current case assessee was not providing the software directly to its Indian Company rather it was integrating the software in assessee's master software and then was providing the same software as a service. Since assessee did not have authority to resell the software as per its agreement with the software vendor this cannot be considered as sale of software royalty.
- Also, the agreement for service Rs. 20.04 crore on which assessee was paying tax and Rs. 3.89 crores which was claimed as reimbursement were similar and hence the tribunal is of the opinion that since assessee was providing similar service and there was no undiluted benefit flown from assessee to Indian company and thus the amount claimed by assessee was liable to tax as Fees for technical service/ royalty.

Our comments:

- Many times, it is seen that various contracts are entered at group level for a better deal and single point of contact. However, in such cases it also needs to be seen that such services are transferred to group entities on an as is basis and all the related benefits should also be passed to group entities without any modification to qualify as reimbursement of expense.
- From the above judgement we can say that for any payment to be considered as reimbursement, it should fulfill **twin conditions** and if one of the conditions is not fulfilled it will not be considered as reimbursement and could be liable to tax.
- Even if any services are offered on cost-to-cost basis to the group entities, still same could be considered as Income liable to tax in India, if the condition of reimbursement is not fulfilled.

Section	**Section 9, Article 12**
DTAA/Country	**India-Switzerland**
Court	**Pune Tribunal**
Date of Decision	**21.10.2021**

Note: Case law name in Red- in favour of the Revenue, Green- In favour of the Assessee, Orange = Partial.

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Thank you