Reimbursement of exp. to foreign AE was taxable if no nexus was found between services rendered and reimbursement

Summary – The Delhi ITAT in a recent case of BG International Ltd., (the Assessee) held that where assessee-company, a tax resident of UK, had received certain sum from a foreign company which was engaged in exploration and production of oil in oil fields of India and claimed same to be reimbursement of actual cost, but could not establish one to one nexus between services rendered to said company and alleged reimbursement, it would be fair to tax assessee's receipts under section 44BB.

Facts

- The assessee a U.K. based company and was AE of BGEPIL which was incorporated in Cayman Island. BGEPIL was a part of Production Sharing Contract along with ONGC and Reliance Industries Limited, for exploration and production of oil and gas in the oil fields of India. The assessee rendered certain services to BGEPIL.
- The Assessing Officer noticed that assessee had received certain sum from BGEPIL under the heads : Payroll expenses, Management service unit charges, General and Administrative expenses and reimbursement of expenses but, these receipts had not been reflected by assessee in its return of income. The assessee took the plea that they were merely reimbursements and there was no element of profit. The Assessing Officer noted that TPO had observed that no services were actually rendered. He further observed that assessee's claim could not be allowed as the assessee failed to furnish any worthwhile evidence to substantiate its claim of expenses; its accounts were not audited as per section 44AB; and there was no evidence of actual rendering of service as during survey no document requesitioning services by BGEPIL was found.
- The DRP held that since the assessee had not been able to substantiate its claim, it would be taxed in its hands as proposed by the Assessing Officer.
- On appeal :

Held

- The assessee's contention is that in assessment year 2006-07, the Tribunal has considered the same profit sharing contract and under identical circumstances has held that assessee was able to substantiate the entire aspects by producing invoices and no material was brought by the Assessing Officer to doubt the debit note and invoices and, therefore, in this year also the same decision should be applied. This plea of assessee could not be accepted because in assessment year 2006-07, the Commissioner (Appeals) had allowed the claim of the assessee because he held that services had been provided on cost to cost basis. The Tribunal's findings were based on the Commissioner's (Appeals's) observation that assessee had produced invoices and no material was brought by the

Assessing Officer to doubt the debit note and invoices. However, in the present year the assessee has not produced any documents before the Assessing Officer or DRP to justify that it had incurred any expenses (other than pay roll expenses or third party expenses). The decision of the Tribunal for assessment year 2006-07, therefore, cannot be applied, because the principles of *res judicata* do not apply to income-tax proceedings and each year has to be considered on the basis of facts obtaining in each year.

- The assessee also referred to Tribunal's order for assessment years 2003-04, 2004-05 and 2005-06, wherein Tribunal had restored the matter back to the file of the Assessing Officer for factual verification of the assessee's claim. Matter was taken up by the Assessing Officer to give effect to the Tribunal's order for assessment year 2004-05. The assessee clearly stated that since the documents were more than 7 years old, it was extremely difficult to retrieve them from UK. Therefore, on this basis, the Assessing Officer based on his earlier order determined the income under section 44BB.
- The assessee submission that merely because in assessment year 2004-05 the assessee was unable to substantiate its claim on account of elapse of time and offered the income under section 44BB, the same cannot be the basis for arriving at any conclusion that the income should be assessed under section 44BB is to be accepted. In view of above discussions, the decisions given in earlier years have little bearing on the facts as obtaining in the current assessment year.
- The assessee has relied on the DRP's order for assessment year 2009-10 wherein DRP has accepted that the services were rendered by BGEPIL.
- In this regard, the department has submitted that decision of DRP has not been accepted by the department and an appeal has been preferred before Tribunal which is pending adjudication. Therefore, in view of these circumstances, it would not be proper to comment either way on the findings of DRP.
- Now coming to the facts as obtaining in the present assessment year, the first aspect to be considered is the effect of TPO's order relied upon by the assessee.
- The transactions of the assessee, referred in TPO's order are with BGEPIL and these transactions are all receipts by the assessee from BGEPIL. The TPO accepted the receipts as taxable under section 92CA(3). The department has rightly submitted that the issue before the TPO was not to verify the expenses incurred by the assessee.
- The TPO did not propose any adjustment because the TPO was prohibited by section 92C(3) to reduce the transaction price of the receipts which would have resulted in deduction of income. Therefore, the finding of TPO in case of assessee has no bearing on the issue which is with regard to claim of assessee that the receipts are reimbursement of expenses. The department has referred to the DRP's observations with regard to TP order in the case of BGEPIL wherein the TPO has given a finding that BGEPIL was not able to provide any evidence of the services rendered by the BGEPIL and, therefore, the ALP of the transactions was computed at *NIL*. Further, it is noticed that Assessing officer had carried out a survey under section 133A at the premises of BGEPIL and the Assessing

Officer's letter to assessee stated that 'during the survey operations in case of BGEPIL no documents were produced to substantiate rendering of services.

- The assessee has relied on cost allocation policy and has given a detailed note on the services rendered by BGEPIL, brought nature of services rendered and, benefit derived by BGEPIL. The department has disputed this on the ground that assessee did not submit the details of expenses incurred *i.e.* to whom paid, when paid and where paid along with supporting invoices received. The assessee did not produce any document to substantiate the expenses incurred by it against receipts for which debit notes were raised on BGEPIL. The debit notes did not show as to on what account and where the expenses were incurred by assessee on behalf of BGEPIL. The assessee has to prove that the services rendered by it are regarding federal green recharges. The assessee gave a general note as to what is the nature of these recharges but nowhere it has given any specific detail as to how much were the federal green charges incurred by BGEPIL as a whole and how the expenses relating to BGEPIL were allocated to it for which debit notes were raised.
- The assessee has pointed out that it is not possible to give one to one nexus for each debit note *vis-a-vis* services rendered. However, basic details as pointed out by lower revenue authorities have to be brought on record. Further, the submissions of assessee did not justify the nature of activities specific to India.
- The next services allegedly given by assessee to BGEPIL are in regard to Management and Unit Charges. Debit notes were raised.
- The assessee has relied on the global allocation policy which only provide that those costs which are deemed to benefit the asset are included in the general and administrative overhead cost.
- Once it is accepted that global cost allocation policy exist, then it cannot be denied that the debit notes raised are towards services rendered. The core issue that remains for consideration is whether the whole amount claimed to be reimbursement should be accepted or not. On this count, admittedly the assessee has not been able to establish one to one nexus between the services rendered and alleged reimbursement. There are also no comparable cases which obviously could not be there.
- Thus, in sum and substance the position as it emerges is that inspite of there being a global cost allocation policy, the assessee failed to substantiate its claim regarding allocation of expenses incurred by it for the services rendered to BGEPIL. It has not been able to substantiate its claim as to what common expenses had been incurred; how those were allocated to assessee; and why those needed to be allowed as deduction from Indian operations. It is settled law that unless the assessee is able to substantiate its claim, the deduction cannot be allowed.
- In view of above discussion, keeping in view the entire conspectus of the case, it would be fair to tax the assessee's receipts under section 44BB, as has been done in past also. In this regard the assessee can be agreed that in assessment year 2003-04, the department while preferring appeal before High Court has itself taken a ground that the assessee's receipts are taxable under section 44BB and the Tribunal erred in deciding that the receipts are not taxable under section 44BB.

- Earlier it has been observed that merely because in assessment year 2004-05 assessee agreed for its receipts being taxed under section 44BB, it cannot operate *as estoppel* against it for pleading that the entire receipts were in the nature of reimbursement. However, considering the fact that assessee is not able to substantiate its claim, and the assessee has only given a general write up for the benefits derived by BGEPIL, no fruitful purpose would be served by restoring the matter to the file of the Assessing Officer for examining the assessee's claim again as that would be a futile exercise particularly when assessee has clearly stated that it is not possible to have one to one nexus of the expenses with the services rendered.
- Under such circumstances, the only possible course is to invoke section 44BB because the assessee provide services to BGEPIL, which was engaged in prospecting the mineral oils.