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ITAT concludes LIBOR to be more appropriate for computing interest on outstanding receivables from AEs

Summary

The Chennai Bench of the Income-Tax Appellate Tribunal (ITAT) in the case of Plintron Global Technology Solutions Private Limited[1] ("taxpayer"), has held that LIBOR denominated rates should be adopted for computation of interest on outstanding receivables from associated enterprises (AEs) as against the Indian Rupee denominated Prime Lending Rates (PLR) as considered by the lower authorities. In arriving at its decision, the ITAT relied on the ruling of the Mumbai Bench of the ITAT in the case of Tecnimont ICB House[2] ("Tecnimont ICB").

Facts of the case

- The taxpayer is engaged in the development and maintenance of telecom software solutions and the services are predominantly rendered to AEs. The TPO recommended a transfer pricing adjustment by imputing interest on the amount of outstanding receivable balances from the AEs. For the said purpose, the TPO had adopted PLR based interest rates for computing the transfer pricing adjustment.
- Taxpayer filed its objections before the Disputes Resolution Panel (DRP) against the proposal of the TPO. However, DRP upheld the positions considered in the order of the TPO.
- Taxpayer filed an appeal before the ITAT against the DRP's directions.

Held by the ITAT

The Chennai Bench of the ITAT evaluated the appropriateness of adopting LIBOR denominated rates for imputing interest on outstanding receivable balances from AEs by relying on the following principles laid down by various benches of the ITAT:

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[1] Plintron Global Technology Solutions Private Limited Vs DCIT; TS-238-ITAT-2018(CHNY)-TP
[2] Tecnimont ICB House Vs. DCIT ITA No.487/Mum/2014

- **Mumbai Bench of the ITAT:**
  - LIBOR denominated rates should be adopted for computing the transfer pricing adjustment on outstanding balances as against the SBI PLR rates adopted by the TPO (Tecnimont ICB).
  - Appropriate international rates (LIBOR) be used for the purpose of benchmarking loans denominated in foreign currency. The rate to be used for undertaking a TP adjustment should be LIBOR denominated and not based on the average yield rates as considered by the learned TPO[3].
  - LIBOR is a rate applicable in the transactions entered into between banks and further loans advanced are secured by security and guarantee. The loan advanced by the taxpayer to its AEs are without any security or guarantee and hence LIBOR plus a mark-up should be considered as arm's length interest rate[4].
  - LIBOR denominated rate has to be adopted in the case of a foreign currency loan[5].
  - EURIBOR denominated rate would be appropriate for imputing interest on advances given to AE (based out of European Union/Germany) in foreign currency[6].

- **Hyderabad Bench of the ITAT:**
  - The arm's length interest rate in respect of foreign currency loan in the international market is to be LIBOR denominated and the same is internationally recognised and adopted.[7]

Relying on the above principles, the Chennai Bench of the ITAT directed the TPO to adopt LIBOR denominated rates for the purpose of computing interest on outstanding receivable balances from the AEs.

[3] Everest Kanto Cylinder Ltd Vs ACIT (LTU) (ITA No. 7073 / Mum/ 2012)
[4] PMP Auto Components Private Limited Vs DCIT (ITA No. 1484/Mum/ 2014)
[5] Hinduja Global Solutions Vs Addl CIT (ITA No. 254/Mum/ 2013)
[6] Tata Autocomp Systems Limited Vs ACIT (ITA No. 7354/Mum/ 11)
[7] Four Soft Private Limited Vs ACIT (ITA No. 1903 / HYD /11)

Our comments

The Revenue Authorities have been categorising the outstanding receivable balances from AEs on similar terms as that of a loan for the purpose of benchmarking. In view of the decision rendered by other benches of the ITAT, it seems to be a broadly settled principle that appropriate international rates (LIBOR/EURIBOR) should to be adopted for computing interest on outstanding receivable balance. Also, the Central Board of Direct Taxes has also placed reliance on LIBOR denominated rates for benchmarking foreign currency loan transactions as part of the safe harbour regulations [vide Rule 10TD(2A)], which provides authenticity for usage of LIBOR rates for benchmarking rather than PLR rates as considered by AO/TPOs.