

**IN THE INCOME TAX APPELLATE TRIBUNAL
“B” BENCH : BANGALORE**

**BEFORE SHRI GEORGE GEORGE K., JUDICIAL MEMBER
AND
Ms. PADMAVATHY S, ACCOUNTANT MEMBER**

IT(TP)A No.254/Bang/2021
Assessment year : 2016-17

Cerner Healthcare Solutions India Private Ltd. [Erstwhile Cerner Healthcare Solutions Pvt. Ltd.], 10 th Floor, Wing B, Block H2, Mountain Ash, Manyata Embassy Business Park, Nagawara, Bangalore. PAN: AAFCC 8750R	Vs.	The Deputy Commissioner of Income Tax, Circle 2(1)(1), Bangalore.
APPELLANT		RESPONDENT

Appellant by	:	Shri Chavali Narayan, CA
Respondent by	:	Dr. Manjunath Karkihalli, CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	12.05.2022
Date of Pronouncement	:	18.05.2022

ORDER

Per Padmavathy S., Accountant Member

This appeal by the assessee is against the order of National e-Assessment Centre Delhi dated 21/04/2021 for the assessment year 2016-17 passed u/s. 143(3) read with section 144C of the Income-tax Act, 1961 [the Act].

2. The assessee has raised 9 grounds and several sub grounds. During the course of hearing, the learned AR submitted that the assessee is withdrawing the grounds relating to transfer pricing (Ground No. 4) as the assessee has entered into an Advance Pricing Agreement (APA). Ground Nos.1 to 3 are general in nature and does not require. Hence Ground Nos.1 to 4 are dismissed.

3. The grounds raised with regard to corporate tax (Ground No. 5 to Ground No. 9), are for the following issues -

- (i) Disallowance of ESOP expenditure amounting to Rs.3,96,91,313 u/s. 37 of the Act (Ground No.5).
- (ii) Disallowance of salary cost paid to be Cerner Corporation amounting to Rs.48,08,011 u/s. 40(a)(i) of the Act (Ground No.6).
- (iii) Disallowance of communication expenses amounting to Rs.2,42,95,765 paid to Cerner Corporation. (Ground No.7).
- (iv) Without prejudice to the above, claim for consequential deduction u/s.10AA of the Act of amount disallowed (Ground No.8).
- (v) Initiation of penalty proceedings u/s. 271(1)(c) of the Act (Ground No.9)

Brief facts of the case

4. The assessee is a company engaged in the business of software development and testing services in healthcare solutions. For the assessment year under consideration the assessee filed the return of

income on 13/07/2017 declaring a total income of Rs.16,40,38,170. The return was processed u/s. 143(1) of the Act and the case was selected for scrutiny. The assessing officer besides the transfer pricing adjustments also made several additions on the corporate tax front which are confirmed by the DRP. The assessee is in appeal against these additions and has raised grounds pertaining to the same.

Disallowance of ESOP expenditure

5. The assessee has claimed employee stock exchange expenses amounting to Rs.3,96,91, 313. The assessing officer (AO) disallowed the expenditure stating :-

- (i) ESOP expenditure should be reflected in the books of the holding company and not in the books of the assessee.
- (ii) The ESOP expenditure is not crystallized on the basis that there is no actual outflow of cash.
- (iii) Cerner Corporation is incentivizing the employees of the assessee and hence any loss incurred should be borne by Cerner Corporation.
- (iv) The differential price in the issue of shares cannot partake the character of the expense incurred in connection with the issue of shares.

6. The DRP against the objections raised by the assessee held that there is no real expenditure incurred as the employee merely gains to the extent of appreciation in share value and that the expenditure is

capital in nature. The DRP confirmed the disallowance made by the AO. The assessee filed an appeal before the Tribunal contending disallowance.

7. The learned AR submitted that the expenses accrued over the vesting period is cross charged by Cerner Corporation to the assessee on a quarterly basis at cost-to-cost which is paid by the assessee and debited to the profit and loss account. The learned AR also submitted that the differential value of the shares representing discount is taxed in the hands of the employees as perquisite. The learned AR further submitted that the discount on ESOP claimed as expense are incurred wholly and exclusively for the purpose of business and hence eligible for deduction u/s.37. The learned AR brought to our attention that this issue is already covered by the decision of the coordinate bench of the Tribunal in assessee's own case in *IT(TP) A No. 279/Bang/2021 dated 30.03.2022* where the issue is decided in favour of the assessee. The learned AR also placed reliance on the decision of coordinate bench of the Tribunal in the case of *Biocon Ltd vs DCIT (2013) 35 Taxmann.com 335*.

8. The learned DR supported the decision of the lower authorities.

9. After hearing both the parties we notice that the coordinate bench of the Tribunal in assessee's own case (supra) has dealt with the same issue and held as under:-

“4. After hearing both the parties we find that similar issue came for consideration of the Tribunal in the case of

Novo Nordisk India (P) Ltd. (2014) 63 SOT 242 Bang – Trib.) wherein it was held as under:-

In the present case, there is no dispute that the liability has accrued to the assessee during the previous year. The only question to be decided is as to whether it is the expenditure of the assessee or that of the parent company.

The foreign parent company has a policy of offering ESOP to its employees to attract the best talent as its work force. In pursuance of this policy of the foreign parent company, allowed its subsidiaries/affiliates across the world to issue its shares to the employees.

As far as the assessee in the present case which is an affiliate of the foreign parent company is concerned, the shares were in fact acquired by the assessee from the parent company and there was an actual outflow of cash from the assessee to the foreign parent company.

The price at which shares were issued to the employees was paid by the employee to the Assessee who in turn paid it to the parent company. The difference between the fair market value of the shares of the price at which shares were issued to the employees was met by the Assessee.

This factual position is not disputed at any stage by the revenue. In such circumstances, we do not see any basis on which it could be said that the expenditure in question was a capital expenditure of the foreign parent company.

As far as the assessee is concerned, the difference between the fair market value of the shares of the parent company and the price at which those shares were issued to its employees in India was paid to the employee and was an employee cost which is a

revenue expenditure incurred for the purpose of the business of the company and had to be allowed as deduction.

There is no reason why this expenditure should not be considered as expenditure wholly and exclusively incurred for the purpose of business of the assessee.

23. With regard to the observations of the CIT(Appeals) that the ESOP actually benefits only the parent company, we are of the view that the expenditure in question is wholly and exclusively for the purpose of the business of the assessee and the fact that the parent company is also benefited by reason of a motivated work force would be no ground to deny the claim of the assessee for deduction, which otherwise satisfies all the conditions referred to in section 37(1)

The facts and circumstances of the present case, the expenditure in question was wholly and exclusively for the purpose of the business of the assessee and had to be allowed as deduction as a revenue expenditure.

27. In the result, the appeal of the assessee is allowed.

5. In view of the binding decision of the Coordinate Bench we allow the grounds taken by the assessee.”

10. Respectfully following the above decision of the coordinate bench, we allow the ground in favour of the assessee.

Disallowance of salary cost paid to Cerner Corporation

11. During the course of assessment proceedings the AO noticed that the assessee has made payment of Rs.48,08,011 to Cerner

Corporation in connection with the salary expenses of Mr Archit Saraf without deducting tax at source. Cerner Corporation paid the salaries to the expatriates in his respective bank accounts on behalf of the assessee and later cross charged to the same to the assessee at cost basis. The assessee submitted that salary payments to a non-resident is excluded from the ambit of withholding tax provisions u/s. 195 relating to nonresidents as it is covered separately under provisions for withholding taxes on salary u/s. 192. The assessee further submitted that where taxes are withheld and remitted to the Indian government on the payment of salary to employees such salary cost reimbursement should not again suffered tax withholding. In this regard the assessee relied on the decision of coordinate bench of the Tribunal in the case of *M/s. IDS software solutions (122 TTJ 410)*. The assessing officer did not accept the submissions of the assessee stating that the services provided by the seconded employee is in the nature of fees for technical services (FTS) defined in explanation 2 to section 9(1)(vii) and hence tax need to be deducted at source. The assessing officer relied on the judgment of Hon'ble Delhi High Court in the case of *Syndicate India Offshore Private Limited vs CIT (2014) 364 ITR 336 (Del)*. The assessee raised objections before the DRP, which were rejected by the DRP and confirmed the disallowance made by the assessing officer on the ground that the seconded employees were not under the control/supervision of the assessee as the agreement does not recognize severance of employer-employee relationship between

expatriate and Cerner Corporation. Aggrieved, the assessee is appeal before the Tribunal.

12. The learned AR reiterated the submissions made before the lower authorities that there is no technical knowledge 'made available' to the assessee on behalf of Cerner Corporation and hence cannot be held to be Fees for Technical Services (FTS) under Article 12 of India USA DTAA. The learned AR submitted that the coordinate bench of the Tribunal in the case of Goldman Sachs services Private Limited vs DCIT (IT(IT)A No.362 to 369 and 338 to 345/Bang/2020). The learned DR on the other hand relied on the contentions of the lower authorities.

13. We heard the rival submissions and perused the materials on record. We notice that the coordinate bench of the Tribunal in the case of *Goldman Sachs services Private Limited, [2022] in IT(IT)A Nos.362 to 369 & 338 to 345/Bang/2020 dated 29.4.2022* has dealt with the same issue and held as under:-

“37. Respectfully following the above views expressed by Hon'ble High Court in *DIT vs. Abbey Business Services India (supra)*, Hon'ble AAR in *Cholamandalam MS General Co. Ltd. (supra)*, Hon'ble Bombay High Court in case of *iris & Spencer Reliance India Pvt.Ltd. vs. DIT (supra)*, Hon'ble Delhi Sit Court in the case of *DIT Vs. HCL Infosystems Ltd. (supra)*, Coordinate bench of this Tribunal in case of *IDS Software Solutions ITO (supra)*, Hon'ble Pune Tribunal in case of *M/s. Faurecia Automative Holding(supra)*, Hon'ble Ahmedabad Tribunal in the case *Burt Hill Designs (P) Ltd. vs. DDIT(IT) (supra)*, we are of the view that the reimbursement made by the assessee in India to overseas

entity. towards the seconded employees cannot be regarded as "Fee For technical Services".

Once there is no violation of provision of section 195, assessee cannot be held to be an assessee in default under section 201(1) of the Act for all the years under consideration. We therefore direct the Id. AO to delete interest levied under section 201(1A) of the Act for all the years under consideration.”

14. Following the binding decision of the coordinate bench of the Tribunal we hold that the reimbursement made by the assessee in India to the overseas entity towards the salary cost of seconded employees cannot be regarded FTS and hence not liable to deduct tax at source u/s. 195 of the Act. Therefore the disallowance made by the AO in this regard on the ground that tax was deducted at source is hereby deleted.

Disallowance of communication expenses paid to Cerner Corporation

15. During the assessment year under consideration the assessee has paid Rs. 2,42,95,765 towards reimbursement of communication charges paid to Cerner Corporation USA. These expenses are in the nature of bandwidth charges paid for utilising the standard facilities and paid to the service provider by Cerner Corporation on behalf of the assessee. The assessee submitted before the assessing officer that these expenses are mere reimbursement of communication charges paid by the assessee to Cerner Corporation and do not constitute income in the hands of the non-resident. The assessee also contended that Cerner

Corporation USA is not rendering any services to the assessee and in fact Cerner Corporation is engaged in the business of software development and testing services to its group companies. Therefore the assessee submitted that there is no basis for treating the reimbursement of expenses payable by the assessee as fees for technical services under the Act.

16. The assessing officer did not accept the contention of the assessee stating that the assessee has made payment in respect of communication expenses for the bandwidth hired by it for transmission of voice and data by accessing the platform provided by non-resident. Right to access would amount to transfer of the right to use the Copyright held by the non-resident and hence the payment made is in the nature of 'Royalty' as defined in article 12 of the DTAA with USA. The assessing officer further stated that the decision of the coordinate bench in assessee's own case in this regard cannot be applied since the revenue has not accepted and is in appeal before the Honourable Karnataka High Court. Against the order of the assessing officer the assessee raised objections before the DRP who confirmed the disallowance u/s.40(a)(i) of the Act.

17. The learned AR submitted that the charges paid by Cerner Corporation on behalf of the assessee is towards bandwidth usage charges and are in the nature of reimbursement of expenses. The learned AO also submitted that these charges are not paid for any services rendered but only as reimbursement without any income

element embedded into such payment in order to be liable for withholding of tax u/s. 195 of the Act. The learned AR submitted that the coordinate bench of the Tribunal in assessee's own case for the AY 2006-07 (ITA No. 627/Bang/2011) where the Tribunal has held that reimbursement payments cannot be liable to tax. The learned DR invited our attention to the decision of the Mumbai Tribunal in the case of *DCIT v. Reliance Jio Infocomm Ltd (2019) 108 taxmann.com 325* where the Tribunal has held that the payments made towards reimbursement of bandwidth services received by the non-resident cannot be brought to tax in India.

18. We have heard the rival submissions and perused the materials on record. Cerner Corporation has entered into a global agreement with Sprint communication systems under which service provider provides bandwidth services to Cerner group companies including the assessee. The service provider raises invoice on Cerner Corporation for the services rendered to various companies including the assessee. During the assessment year 2016-17 Cerner Corporation has paid a sum of Rs. 2,42,95,765 towards communication expenses to the service provider on behalf of the assessee and in turn cross charged these expenses to the assessee on cost to cost basis without any profit/element. The assessee had submitted copies of invoices to support this claim before the lower authorities. The important element that needs to be considered here is the amount reimbursed by the assessee to Cerner Corporation is on cost or cost basis and does not contain any element of profit. We notice that a similar issue has been considered by the

Pune bench of the Tribunal in the case of *T-3 Energy Services India Pvt. Ltd vs JCIT (ITA No.826/Pun/2015)* where the Hon'ble Tribunal has held that -

“25. Now, coming to the next aspect of the issue that reimbursement of charges is not subject to tax in India. The basic principle underlying the same is that where reimbursement of expenses do not include any income element, then the same is not subject to tax in India. The assessee before us has filed extensive evidence in this regard i.e. Qwest Communications Inc had raised charges upon T-3, USA and the portion allocable to the assessee was charged on cost to cost basis. Hence, it cannot be said that there was any income element which has arisen in the case and consequently, we hold that where the assessee had reimbursed the expenses having no income element, there is no requirement to withhold tax out of such payments. The case of Revenue in this regard is that it is not case of reimbursement but is a case of payment to third party through its associated enterprise and hence, the need for withholding tax. We have already decided this issue in the paras hereinabove that under the provisions of DTAA, the term 'royalty' is defined and it does not cover any such services availed and payment made and hence, there is no merit in the stand of Revenue in this regard and the same is dismissed. In any case, the privity of contract is between Qwest Communications Inc, the service provider and T-3, USA, who in turn had received bandwidth and passed on the services to various entities of group on cost to cost basis. The assessee as recipient of services had reimbursed the same and in the absence of profit / income element, there is no liability to deduct tax at source. Hence, the assessee cannot be held to be in default.

26. The Assessing Officer had also raised the issue of payment being in the nature of fees for technical services. However, in the final analysis disallowance has been made

in the hands of assessee for non deduction of tax at source on the payments being made in the nature of royalty i.e. amended provisions of the Income-tax Act. We have already decided the said issue in the paras hereinabove and accordingly, we hold that there is no merit in invoking the provisions of section 40(a)(i) of the Act for non withholding of tax on the amount of charges paid for reimbursing associated enterprise for lease line charges.”

19. The determinant factor of reimbursement is, whether there exist an obligation on the part of the person bearing the expenditure to incur such expenditure. Where the ultimate obligation/liability to bear the expenses rests on another person and the payment for the same was made on his behalf the repayment of such expenses could partake the nature of reimbursement. The judicial precedents have upheld the principle that the reimbursements do not constitute income.

20. In view of the above discussion and respectfully following the decision of the Pune bench of the Tribunal, we hold that the bandwidth charges reimbursed by the assessee to Cerner Corporation on the cost or cost basis without any element of profit cannot be treated as Royalty liable to be taxed in India and hence there is no liability to deduct tax at source on such reimbursements. When there is no liability to deduct tax at source the question of disallowance u/s.40(a)(i) does not arise. This ground of the appeal is allowed in favour of the assessee.

21. During the course of hearing, the learned AR submitted that if the appeal is allowed in favour of the assessee, then Ground Nos.8 and 9 which are consequential in nature will not be pressed. Since we have allowed the grounds raised by the assessee in ground Nos. 5 to 7 in

favour of the assessee, there is no requirement to adjudicate ground No. 8 and 9 which are consequential in nature and hence dismissed.

22. In result the appeal is allowed in favour of the assessee.

Pronounced in the open court on this 18th day of May, 2022..

Sd/-

(GEORGE GEORGE K.)
JUDICIAL MEMBER

Sd/-

(PADMAVATHY S.)
ACCOUNTANT MEMBER

Bangalore,
Dated, the 18th May, 2022.

/Desai S Murthy /

Copy to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore.

By order

Assistant Registrar
ITAT, Bangalore.