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Chennai ITAT rules that amount received by foreign company from Indian subsidiary towards reimbursement of salary cost of deputed employees, is 'FTS'

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Facts of the case

- Panasonic Corporation (tax payer) is a company incorporated in and resident of Japan.
- The tax payer had entered into an agreement with its Indian subsidiary, M/s Panasonic India Pvt. Ltd (Panasonic India), for deputation of senior and highly skilled employees to Panasonic India for specific support services.
- The tax payer received from Panasonic India, reimbursement of salary cost incurred by it in respect of the deputed employees.
- The tax payer claimed the above receipt in the nature of "reimbursement of expenses" and hence did not offer it to tax in India.
- The Assessing Officer (AO) disallowed the claim of the tax payer on the grounds that the tax payer received a fee in the nature of fees for technical service (FTS).
- From the facts, the department representative alleged that the tax payer had not deducted tax while making salary payment to the deputed employees.
- AO has further observed the following key points:
 - The deputed employees never ceased to be employees of the tax payer (i.e. there was no termination of employment). Therefore, the salary paid was borne out of the inherent obligation of the tax payer as employer.
 - The deputed employees are not free to move anywhere, but are required to go back to the tax payer on expiry of their tenure. Therefore, they retain a lien on their employment with the tax payer.
 - All the employees are senior personnel deputed to Panasonic India to lend their experience as employees of the tax payer.
 - The deputed personnel have come to India to imbibe the culture of the group and ensure application of group policies and other quality standards in Panasonic India. This clearly demonstrates that once the standards are imbibed/retained, there is no need for personnel to come again for technical service and Panasonic India can apply itself. Hence the services have also "made available" the technical knowledge/ skill and experience.
- The Dispute Resolution Panel (DRP) upheld the order of the AO and *inter alia* observed the following additional points:
 - The mere fact that as per the agreement the employees would be performing under the direction and control of Panasonic India, does not change their status of employment with the tax payer, of which they are employees.
 - The above arrangement is a very common method adopted by a service provider and also adopted not only in the private sector but by the government also, on deputation.
 - In absence of reconciliation of receipts by the tax payer, what was reimbursed is a part of the salary and it not social security cost alone.
 - The receipts are to be considered as FTS, irrespective of the fact whether it is received with mark-up or cost-to-cost basis. Reliance was placed on the decisions of Bangalore ITAT in case of Food World Supermarket Ltd. (63 taxmann.com 43) and Delhi High Court in the case of Centrica India Offshore (P.) Ltd. (44 taxmann.300).

Issue under consideration

Whether the receipt on account of reimbursement of salary cost of the employee, deputed to India by the tax payer, from its Indian subsidiary, is covered within the ambit of 'FTS'?

Ruling of ITAT

- The ITAT affirmed the AO and DRP order, with the following observations.
 - The personnel seconded, have to work under the control, direction and supervision of the tax payer, as all are senior technical/managerial position employees, who report to the president and vice president and who in turn are expected to report to the tax payer.
 - Since the employees are rendering highly technical services, they would fall under the ambit of FTS under the Indian Income tax Act, 1961.
 - The ITAT also upheld the finding of AO that technology was made available to the subsidiary company in India and there is no need for the employees to come again.

Conclusion

The taxability of reimbursement of salary cost of deputed employees has been a matter of litigation. On similar arrangements, Delhi High Court held, in the case of DIT v. HCL Infosystems Ltd. [2005] (274 ITR 261), no withholding tax applies on reimbursement of salaries. Further, Bombay High Court in the case of M/s. Marks & Spencer Reliance India Pvt. Ltd. [TS-178-HC-2017 (Bom)], held that reimbursement of salary cost cannot be treated as FTS. The above rulings have not been referred/distinguished in the ITAT order. One important point to note in this ruling is that the ITAT has observed that the tax payer has failed to substantiate with documentary evidence that the payment was on a cost-to-cost basis.

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