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Reimbursement of salary costs under secondment agreement not FTS; services rendered by seconded employees do not constitute a Service PE

In brief

- In a recent ruling[1], the Mumbai Bench of the Income-tax Appellate Tribunal (the Tribunal), held that there was no requirement to withhold taxes under section 195 of the Income-tax Act, 1961 (the Act) at the time of reimbursement of salary paid to seconded employees, when taxes have already been withheld under section 192 of the Act.
- Further, the Tribunal held that a Service Permanent Establishment (PE) of the overseas entity would be formed only when it rendered any kind of services in India through its seconded employees. Where the seconded employees were working under the supervision and control of the Indian Company, no Service PE could be said to exist.

Facts

- Temasek Holdings Advisors India Pvt. Ltd. (the assessee) was a wholly owned subsidiary of Temasek Holding Pte. Ltd. (THPL), a Singapore-based investment firm. The assessee rendered investment advisory services to THPL.
- THPL had seconded two employees to the assessee to assist in rendering investment advisory services to THPL. As per the secondment agreement, the employees continued to remain on THPL's payroll. However, they worked under supervision and control of the assessee during the secondment term.

[1] Temasek Holdings Advisors India Pvt. Ltd. *v.* DCIT [2013-TII-163-ITAT-MUM-INTL]

- THPL incurred the salary cost for employees on secondment, on which tax was withheld under section 192 of the Act. In addition to salary costs, THPL incurred other administrative costs related to seconded employees.

- The assessee, in accordance with the terms of the secondment agreement, reimbursed THPL for salary and other administrative costs, and claimed these reimbursements as deductible expenses.

- The Assessing Officer (AO) disallowed the entire payment under section 40(a)(ia) of the Act on the ground that such payments were Fees for Technical Services (FTS) and should be subjected to withholding tax in India.

Issues

- Whether the payments made by the assessee to THPL qualified as FTS and tax were liable to be withheld under section 195 of the Act?

- Whether the secondment of employees to India constituted a Service PE of THPL under the tax treaty?

Assessee's contentions

- On the basis of documents submitted, it could be said that employer-employee relationship existed between the seconded employees and the assessee.

- When services were rendered in India for an Indian Company, tax could only be withheld under section 192 of the Act.

- Once tax had been withheld under section 192 of the Act, there was no requirement to withhold tax under section 195 of the Act.

- As per Explanation 2 to section 9(1)(vii) of the Act, if the consideration was the recipient's income, chargeable under the head 'salaries', it could not be termed as FTS.

Revenue's contentions

- The Revenue contended that there was no employer-employee relationship between the assessee and the seconded employees.

- The payments were in the nature of FTS under section 9(1)(vii) of the Act and Article 12(4) of the tax treaty, as the seconded employees provided advisory and managerial services to the assessee.

- Alternatively, this was an instance of a Service PE as the seconded employees were sent by THPL to work in India with the assessee, and had rendered services on THPL's behalf.

Tribunal ruling

- There could not be double withholding of taxes - once at the time of payment of the salary and again on reimbursement made by the assessee to THPL.

- The two seconded employees worked only for the Indian company and were not rendering services on behalf of THPL. Hence there was no question of rendering managerial or consultancy services by THPL either directly or through the seconded employees. Hence, section 9(1)(vii) of the Act was not attracted.

  Further, the payments made were not covered within the ambit of the 'make available' clause as per Article 12(4)(b) of the tax treaty, as THPL neither rendered any services to the Indian company, nor did they make available any kind of technical knowledge, experience, skill or proceeds to the assessee.

- There was no merit in the Revenue's contention that a Service PE was constituted, as THPL did not render any service in India through the seconded employees.

- Therefore the AO's disallowance under section 40(a)(ia) of the Act was cancelled.

Conclusion

- This decision has agreed with the position taken by the Delhi High Court[2] and various other courts that if the Indian Company has already withheld and remitted employment-related taxes on salaries paid abroad to seconded personnel under section 192 of the Act, any cross-charge of such salary costs by the Indian Company would not attract section 195 of the Act.

[2] DIT *v.* HCL Infosystem Ltd. [2004] 274 ITR 261(Delhi)

- If the seconded employees did not render any services in India on behalf of the overseas entity, a Service PE of the overseas entity was not constituted.

- It may be noted that there are divergent rulings of Courts on the issue of cross-charge of salary costs in case of seconded employees. The applicability of these rulings has to be seen in the context of the facts of each case. The Revenue could appeal against the said decision - we may not have seen the last on this issue.

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