FTS and Secondment

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FTS – Background (1/2)

- ***Definition under the Act* -** Explanation2 to Section 9(1)(vii) of the Act

  *"means any consideration (including any lump sum consi-deration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel) but **does not** include consideration **for any construction, assembly, mining or like project undertaken by the recipient** or consideration which would be income of the recipient chargeable under the head "Salaries";*

- **Definitions under the DTAA**
  - Make Available – USA, UK, Canada
  - Ancillary and Subsidiary to enjoyment of right/property – US, UK
  - Place of Performance - Finland, China etc
  - No FTS clause – UAE, Philippines etc
  - Exclusive right – Greece and Egypt
  - Secondary Source – US, Iceland, Luxembourg, Mexico etc
- **Interplay with Equalization Levy**

FTS – Background (2/2)

Managerial

- It includes the Act of managing by direction or regulation or superintendence
- R. Dalmia vs CIT (106 ITR 895) (SC)

Technical

- Service requires expertise in technology and involves human intervention
- Bharati Cellular (330 ITR 239) (SC)

Consultancy

- Services constituting provision of advice by someone, such as a professional, who has special qualifications
- OECD Tag Report 2001 – Tax Treaty Characterisation Issues arising from E-Commerce

Construction, Assembly and Mining

Intent of the Legislature – explained in Rio Tinto Technical Services (340 ITR 507 (DEL))

- Not normally regarded as services relating to FTS
- Distinction is made between income earned by way of rendering services vs manufacturing or trading activity
- When interpreted in narrow manner, the activity may not fall under manufacturing or trading, however such narrow interpretation is not warranted
- Exclusion to the aforesaid project is clarificatory
- Project should be undertaken by recipient

- Service provider engaged in supervision or rendering service may not be entitled for exclusion, if they do not carry out the activity of construction/assembly/mining – Clouth Gummiwerke Aktiengesellschaft v CIT (238 ITR 861) (AP); Hotel Scopevista Ltd v CIT (2007) 18 SOT 183 (Del)

- Prospective, Extraction or production of mineral oil; Imparting of training and carrying out drilling – CBDT instruction No 1862 dated 22 October 1990

Secondment – Background and Models

Need for Secondment

- Availability of in-house talent pool
- Sharing of a common pool of resources
- Implementation of best practices amongst the group entities
- Replicating/imparting skill sets across group entities
- Supervising, and executing projects etc.

Meaning

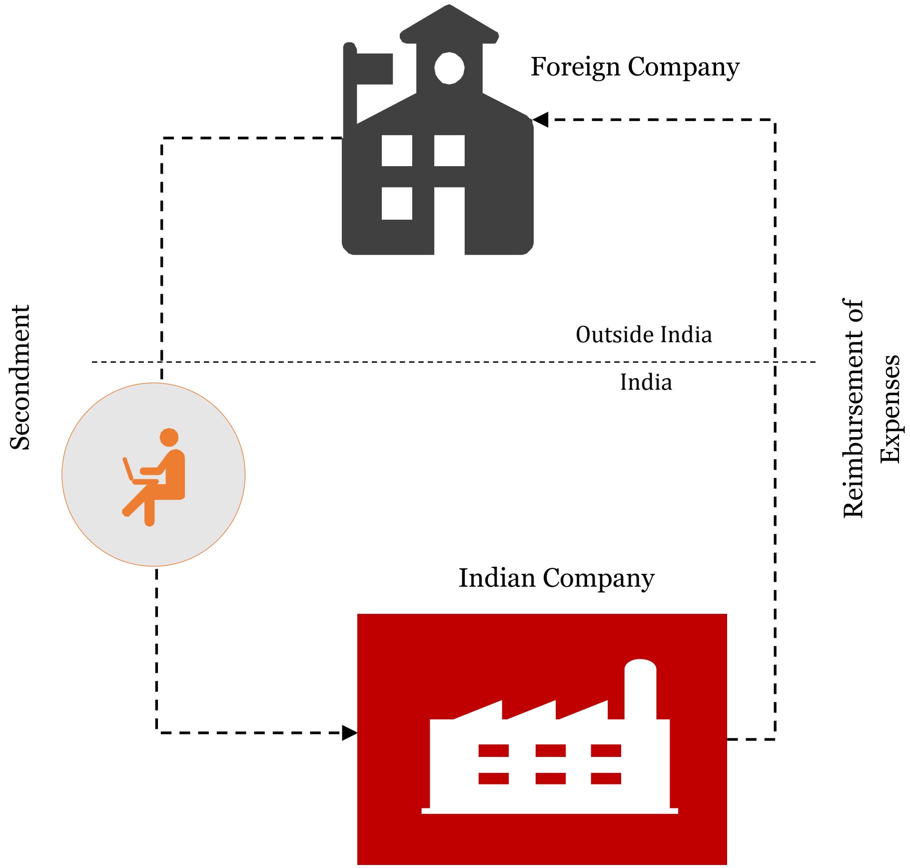
Common terms used are Deputation, secondment, temporary transfer, employee leasing, manpower supply

'Depute' - A person appointed to act in an official capacity or as another official's representative.

'Secondment' - Temporary transfer of official or worker to another position or employment [*Oxford Dictionary of English*, 3rd Edition, 2010]

- **Model 1:** Transfer of employment (Contract of service)
- **Model 2:** Contract for service
- **Model 3:** Dual employment

Secondment – with a Cross Charge



Background

- Employee of F Co seconded to India for a defined period
- A portion of employee salary is paid by F Co in the Home Country Bank Account
- A portion of salary is discharged by I Co in the Host Country Bank Account
- Overseas + Local salaries are considered for withholding taxes under Section 192

Various factors to be kept in mind

- Compensation and Benefits
- Immigration
- Social Security
- Corporate Tax
- Withholding Compliance
- Compliance in Host and Home Country
- Business Case
- Indirect Taxes

Critical elements for consideration

- How the inter-company agreement is executed
- What are the terms of employment?. How it is structured
- Secondment is a Contract of Service vs. Contract for Service
- Supreme Court in Morgan Stanley (292 ITR 416) laid out twin conditions
  - Who is responsible for the work of seconded employees
  - Whether an employee has a lien over the work with F Co
- Legal vs Economic Employer - Factors for consideration
  - OECD Model Convention, 2017 – Art 15 – 8 Factors
  - IRS Factor test
- Legal vs Economic Employment was tested by the Tribunal and Courts
- The jurisprudence is divided as regards taxability of cross chargesis

Potential Issues in Direct Tax

- Fee for service vs. mere reimbursement

- Nature of service
  - Recruitment service
  - Supply service
  - Technical service

- FTS definition in domestic law vs Tax Treaty

  any managerial, technical or consultancy services (***including the provision of services of technical or other personnel***)

- Make available condition in Tax Treaties

  General Motor Overseas Corporation (Mumbai ITAT) - *Technology is made available once employees having requisite knowledge experience and expertise of technology are transferred from one jurisdiction to another*

Potential Issues in Direct Tax

- Service PE
  - Morgan Stanley (SC) - *where the activities of the multinational enterprise entails it **being responsible for the work of deputationists** and the employees continue to be on the payroll of the multinational enterprise or they continue to have their lien on their jobs with the multinational enterprise, a service PE can emerge*

- Fixed Place PE
  - Samsung Electronics (Delhi ITAT) - *If the expats are working under the control of and for the business of Indian company, no fixed place PE was constituted as expatriates were not carrying out business of OGC in India*

- Profit Attribution to PE
  - **Morgan Stanley (SC)** - *Where the Indian entity is remunerated at ALP after proper FAR analysis, then no further profit needs to be attributed to PE*
  - *Indian entity – Captive service provider vs others?*

Potential Issues in Indirect Tax

Valuation of Service

- Salary paid by overseas entity and claimed as reimbursement
- Salary directly paid by Indian entity
- Social security contributions
  - Foreign country
  - India
- Perquisities and other non-monetary benefits
  - Rent free accommodation
  - Car
- Mark up or administration charges charged by foreign entity

Key Issues deliberated in various rulings

- DIT v Abbey Business Services (India) (P.) Ltd (Karnataka)
- IDS Software Solutions India (P) Ltd. vs ITO (2009) 122 TTJ 410
- DIT v. HCL Infosystems Ltd. (2005) 274 ITR 261 (Del)
- United Hotels Ltd v ITO (2 SOT 267)
- AT & T Communication Services (India) P Ltd v DCIT ITA No. 354/Del/2017
- Boeing India Pvt Ltd (TS-790-HC-2022DEL)

Reimbursement

FTS and Make Available

- Centrica India Offshore (P.) Ltd. vs. CIT [2014] 44 taxmann.com 300 (Del),
- Food World Supermarkets Ltd. vs DDIT (International taxation) [2015] 63 taxmann.com 43 (Bangalore - Trib.)
- Verizon Data Services India (P.) Ltd. v AAR (2012) 346 ITR 489 (Mad)
- Flipkart India (Karnataka HC)

- Morgan Stanley & Co vs DIT (Int Tax) [2007] 162 Taxman 165
- Centrica India Offshore Pvt Ltd vs CIT [2014] 51 taxmann.com 386 (HC)
- ADIT Vs E Fund IT Solutions Inc. [2017] 86 taxmann.com 240 (SC)
- Samsung Electronics Company Ltd v. DCIT [2018-TII 91 ITAT DEL INTL]
- GE Energy Parts Inc - 411 ITR 243 (Del)

PE

Critical Observations from the jurisprudence

Centrica Offshore

- There was no employment relationship between Centrica India and the secondees.
- Obligation to pay the salaries rested with the overseas entities and the right of the employee to claim it was only against the F Co.
- The overseas entities had outsourced some of their business functions to India to ensure that the Indian vendors comply with the quality guidelines.
- The seconded personnel were making available their experience and skill in managing and applying the processes

Northern Operating Systems (Service Tax Regime)

- No single factor to determine the contract of services. Substance over form has to be looked at
- Though control is with the Assessee, the secondee remain in the payroll of the F Co
- Secondment was part of Global Policy of the overseas employer
- Salary package were expressed in foreign currency
- Overseas company had a pool of highly skilled employees, post secondment, they may be either return to employer or seconded to other country

Thank You