

Reimbursement of salary and related costs under secondment arrangement constitutes FTS: Chennai ITAT

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Summary

The Chennai bench of the Income Tax Appellate Tribunal (ITAT), in a recent decision¹, has held that reimbursement of salary paid by a foreign company to its employees seconded to an Indian entity is in the nature of fees for technical services (FTS) under the provisions of the Income-tax Act, 1961 (the Act). Further, it held that reimbursement of other expenses, ie airfare, food expenses, local conveyance, etc., was an essential element of the services rendered and hence bears a clear nexus with the technical services rendered.

Facts of the case

- The taxpayer had entered into a secondment arrangement under which certain employees of its foreign group company visited India to exchange experience and skill.
- The foreign company continued to be the employer of the seconded employees and the employees were to return to the original employer on completion of the secondment period.
- The taxpayer reimbursed the salary cost of the seconded employees and other costs representing airfare, food expenses, local conveyance, etc., to the foreign company. Tax was deducted at source² on the salary payments to the employees.

¹ M/s. Nippon Paint (India) Pvt. Ltd. v The Deputy Commissioner of Income Tax, International Taxation-2(2), Chennai [TS-171-ITAT-2019(CHNY)]

² Under Section 192 of the Act

However, no deduction was made on remittance of salary and other costs to the foreign company treating the same as 'reimbursement of expenses'.

- The tax officer held that since the expense is a technical assistance fee for providing support, training and accompanying activities, it is classifiable as FTS and tax is required to be deducted³ under the Act on the entire reimbursement.
- The first appellate authority⁴ upheld the order of the tax officer. The taxpayer then filed an appeal before the ITAT.

Arguments by the taxpayer

- The taxpayer, relying on a Mumbai ITAT decision⁵, argued that salary could not be treated as FTS. Further, it contended that since the salary has already been subject to tax deduction at source, no tax was required to be deducted under other provision⁶ of the Act.
- As regards reimbursement of other costs, it contended that it was merely a reimbursement with no profit element and hence should not partake the character of income.

ITAT's observation and ruling

- The ITAT observed that the seconded employees continue to remain in the foreign organisation's employment and once the secondment term is over, they will return to their original employer. Thus, the ITAT held that as the taxpayer has not become the employer of the seconded employees, the remittance would be income of the foreign organisation and not be in the nature of reimbursement of salary.
- As regards reimbursement of other expenses, the ITAT concurred with the Tax Department's argument and observed that the deputed personnel's visits were an essential element of the services proposed to be rendered. Further, it observed

³ Under Section 195 on both the remittances

⁴ Commission of Income tax (Appeals)

⁵ Saipem SA v DDIT (2012) 54 SOT 111 (Mumbai)

⁶ Under Section 195

that the expenses had been incurred in connection with the technical service agreement and hence bear a clear nexus with the technical services rendered.

- Therefore, the salary and other costs reimbursed were held to be the service provider's cost and not that of the taxpayer.
- The ITAT also observed that the first appellate authority has clearly recoded its findings and applied the law laid down by courts and AAR/Tribunals⁷. As the taxpayer had not laid any material to dislodge those findings, the ITAT refused to interfere with the first appellate authority' order.

Our comments

Taxation of a secondment arrangement has been a subject matter of extensive litigation, as taxpayers argue that it is a mere manpower-sharing arrangement between group companies, while the tax authorities argue it to be a service arrangement. In the instant case, the appellate authorities have merely followed the ratio laid down in Centrica Offshore. However, relevant aspects of a secondment arrangement, ie nature of relationships, lien of the taxpayer over the seconded employees during the secondment term, responsibility of work performed in India by the employees, etc., have not been discussed. It is necessary to analyse these aspects to take a holistic view of the taxability of a secondment arrangement.

⁷ Reimbursement of salary: Centrica India Offshore (P) Ltd [2014] 364 ITR 336 (Delhi); Target Corporation India (P) Ltd [2012] 348 ITR 61 (AAR). Reimbursement of other expenses: Ashok Leyland Ltd v DCIT (2009) 120 ITD 14 (Chennai); CSC Technology Singapore v. DCIT (2012) 50 SOT 399 (Delhi)

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NEW DELHI National Office Outer Circle L 41 Connaught Circus, New Delhi 110001 T +91 11 4278 7070	NEW DELHI 6th floor, Worldmark Aerocity, New Delhi – 110037 T +91 11 4952 7400	AHMEDABAD 7th Floor, Heritage Chambers, Nr. Azad Society, Nehru Nagar, Ahmedabad - 380015	BENGALURU 5th Floor, 65/2, Block A, Bagmane Tridib, Bagmane Tech Park, C V Raman Nagar, Bengaluru – 560093 T+91 80 4243 0700	CHANDIGARH B-406A, 4th Floor, L&T Elante office Industrial area, Phase-I Chandigarh 160002 T +91 172 4338 000
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KOLKATA 10C Hungerford Street 5th Floor, Kolkata 700017 T +91 33 4050 8000	MUMBAI 16th Floor, Tower II Indiabulls Finance Centre SB Marg, Elphinstone (W) Mumbai 400013 T +91 22 6626 2600	MUMBAI 9th Floor, Classic Pentagon, Nr Bisleri, Western Express Highway, Andheri (E) Mumbai 400099 T +91 22 6176 7800	NOIDA Plot No. 19A, 7th Floor Sector – 16A, Noida 201301 T +91 120 4855 900	PUNE 3rd Floor, Unit No 309 to 312, West Wing, Nyati Unitree Nagar Road, Yerwada Pune- 411006 T +91 20 6744 8800

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