

## Secondment of employee by group Co. to Indian affiliate for managerial services constitutes its service PE in India

**Summary –** The Delhi ITAT in a recent case of JC Bamford Investments Rochester., (the Assessee) held that where in terms of licence agreement entered into between assessee, a UK based company, and its Indian group concern, certain employees were seconded to Indian company to render services relating to manufacturing of Excavator loader in India, in view of fact that seconded employees furnished services including managerial services for a period of more than 90 days during relevant assessment years, Assessing Officer rightly concluded that service PE of assessee was established in India in terms of article 5(2)(k) of India - UK DTAA.

### Facts

- The assessee company was tax resident of UK.
- There was another group company, JCBE which was also incorporated under the laws of and was tax resident of UK.
- On 5-3-2004, JCBE entered into Technology Transfer Agreement (TTA) with JCBI, an Indian company, to license the know-how and related technical documents consisting of all drawings and designs with an exclusive right to manufacture and market Excavator Loader in the territory of India under the brand name 3DX.
- On 17-12-2007, JCBE, JCBI and the assessee entered into a tripartite Intellectual Property Agreement, pursuant to which JCBE's license of intellectual property, given to JCBI for manufacturing and marketing 3DX in India, was sub-licensed to the assessee company in consideration of the payment of royalty by the assessee to JCBE.
- Under the new agreement, the license was to be commercially exploited by JCBI as was done earlier, but the royalty for such user was to be paid by JCBI to the assessee, who was to pass on 99.5 per cent of the same to JCBE.
- The assessee thus derived income in the nature of royalties/fees for technical services from JCBI which was offered to tax at the rate of 15 per cent in India on gross basis by treating the receipt as 'Royalties and Fees for technical services' covered under Article 13(2) of the India-UK DTAA.
- The Assessing Officer noticed that in the earlier years, viz., Assessment Years 2006-07 and 2007-08, it was held in the case of JCBE that their employees seconded to JCBI on assignment basis in India resulted into constituting service PE of JCBE in India in terms of Article 5(2)(k)(i) of the DTAA.
- The Assessing Officer further noticed in the proceedings for the instant year that JCBE continued to second its employees to JCBI as was done in the earlier years.
- It was undisputed that all the terms and conditions for the use of the license by JCBI were similar to those of the earlier agreement and the only difference in relevant year was that under the new agreement, royalty was first paid by JCBI to the assessee and the assessee, in turn, paid it to JCBE in full less 0.5 per cent.

- After going through various terms of the new agreement in conjunction with the earlier agreement, the Assessing Officer held that the employees of JCBE as seconded to JCBI constituted a service PE of the assessee as they were covered under the expression or other personnel in Article 5(2)(k) of India UK DTAA.
- The question of a service PE of JCBE in India came up for consideration before the Tribunal for assessment years 2006-07 and 2007-08. The Tribunal categorized employees of JCBE on deputation to India on assignment basis in the first category and those doing stewardship activities and inspection and testing in the second category.
- As regards the fees for technical services resulting from the rendering of services by the employees of the second category, the Tribunal held that the same did not fall in para 6 of Article 13 and was, hence, chargeable to tax as per para 2 of the Article 13 of the DTAA.
- As regards the consideration for the employees of the first category, the Tribunal held that the fees for technical services in relation to such employees was covered within para 6 of Article 13 of the DTAA. Accordingly, it was concluded that the consideration for rendering of services by the employees of first category was chargeable to tax under article 7 of the India-UK DTAA.
- The assessee filed instant appeal challenging finding of Assessing Officer that there existed its service PE in India.

#### **Held**

- All the requisite conditions for attracting the mandate of Article 5(2)(k) of India-UK DTAA are satisfied inasmuch as (i) there is furnishing of services including managerial services; (ii) such services are other than those taxable under Article 13 (royalties and fees for technical services); (iii) such services are rendered out of India; (iv) such services are rendered by 'other personnel'; and (v) such activities continued for a period of more than 90 days within 12 months' period. It is thus held that the service PE of the assessee is established in India. The objection raised by assessee is therefore set aside.
- The next major issue raised is against the holding by the AO that the royalty earned by the assessee was effectively connected with the service PE of the assessee in India.
- It is noted that similar issue was there and has been elaborately discussed in the order of the Tribunal for the earlier years. The Tribunal has held that the total amount consisting lump sum licence/know-how fees and also royalty as mentioned in TTA was consideration for the transfer of IP rights simplicitor and also the service rendered by the employees of the second category.
- The Tribunal further held that insofar as the question of royalty representing consideration for the transfer of IP rights simplicitor was concerned, the service PE representing the deputationists had no role to play either creating or making it available to JCB India. That is how the Tribunal came to hold that the same was not effectively connected with the service PE of the assessee in India.
- As the facts for the instant year are admittedly similar to those of the preceding years on this issue, respectfully following the precedent for assessment year 2006-07, the matter is remanded back to the file of Assessing Officer for determining income in consonance with the directions given by Tribunal for the earlier year.

- Further, in cross-objection, revenue raised a contention that since it was JCBE who was the beneficial owner of the royalty received from JCBI and not the assessee, Article 13(2) of the DTAA will cease to apply and resultantly, the assessee should be subjected to tax as provided under the domestic law.
- In this regard, it is opined that the benefit of lower rate as provided under Article 13(2) of the DTAA can be withdrawn if the 'beneficial owner' of the royalty in instant case happens to be not a resident of UK.
- A case has been made out that since the assessee, a resident of UK, is not the beneficial owner of the royalty etc., the benefit of lower rate of taxation would be automatically forfeited.
- This contention is devoid of merits because the requirement for the applicability of Article 13(2) of the DTAA is that the beneficial owner should be the resident of the UK. It is not that if the formal recipient, a resident of UK, is not the beneficial owner, then the benefit is lost, notwithstanding the fact that the beneficial owner is also the resident of UK. Such relief of lower rate of taxation can be denied if the beneficial owner of the royalty is a resident of some third state, neither being India nor UK.
- Despite the fact that the assessee, a resident of UK, is not a beneficial owner as per the standpoint of the Revenue, still the benefit of lower rate of tax cannot be denied because the beneficial owner of the royalty, being JCBE, is admittedly resident of UK.
- As the royalty in the present case has arisen in India, and the beneficial owner of this royalty is resident of UK, it is held that the tax shall be charged at rate of 15% as provided in Article 13(2) of the DTAA.