

Sales incentives to employees establish LO promotional activities in India; treated as PE of foreign Co.

Summary – The High Court of Allahabad in a recent case of Brown And Sharpe Inc., (the Assessee) held that Foreign Company established a LO in India - Performance of employees of LO was determined by number of direct orders received by them - Employees were also entitled to sales incentives for these orders - Such incentive plans established that LO was not engaged merely in preparatory or auxiliary activities - Its activities extended to marketing activities as well - Therefore, it would be treated as PE of foreign company and the income attributable to LO activities would be taxable in India

Facts

- (1.) The assessee, a company incorporated in US, established a Liaison Office ('LO') in India. During assessment the Assessing Officer contended that the activities of the LO extended to searching for the prospective buyers and for promoting sales of the assessee in India.
- (2.) The Assessing Officer posed a few queries before the Chief Representative Officer ('CRO') of the assessee which were explained by him.
- (3.) In one of the queries pertaining to the remuneration schemes for the employees, the CRO explained that the employees were entitled to sales incentives to the extent of 25% of their annual remunerations. Further, the performance of the employees was judged by the number of direct orders received by them.
- (4.) The CRO further explained that the incentive plan was a standard term which was inadvertently included in the offer letters given to the employees. In fact, no such incentive was given to any employees during the year.
- (5.) On basis of such an enquiry, the Assessing Officer held that the activities of LO were not limited to preparatory or auxiliary activities in India and they had extended to marketing and promotional activities as well.
- (6.) Accordingly, the income attributable to the LO in India would be taxable in India. The Commissioner (Appeals) and the Tribunal upheld the order of the Assessing Officer.

Held

- (a) Whether or not any incentive was paid to an employee during the year was not material. What was relevant was the nature of the incentive plan.
- (b) Nature of incentives to employees indicated that purpose of LO was not just to advertise products of assessee but extended to activities which traversed the actual marketing of the products of assessee in India
- (c) The explanation that the incentive plan, being a standard language, was inadvertently included in the offer letter was far-fetched, because the assessee carrying over a transnational business

with a range of advisors could not be assumed to have committed an inadvertent mistake on this significant issue.

- (d)* Therefore, LO would be treated as PE of foreign company.
- (e)* However, on the issue of determination of the income attributable to the LO which had to be taxed in India, the High Court restored the matter before the AO.