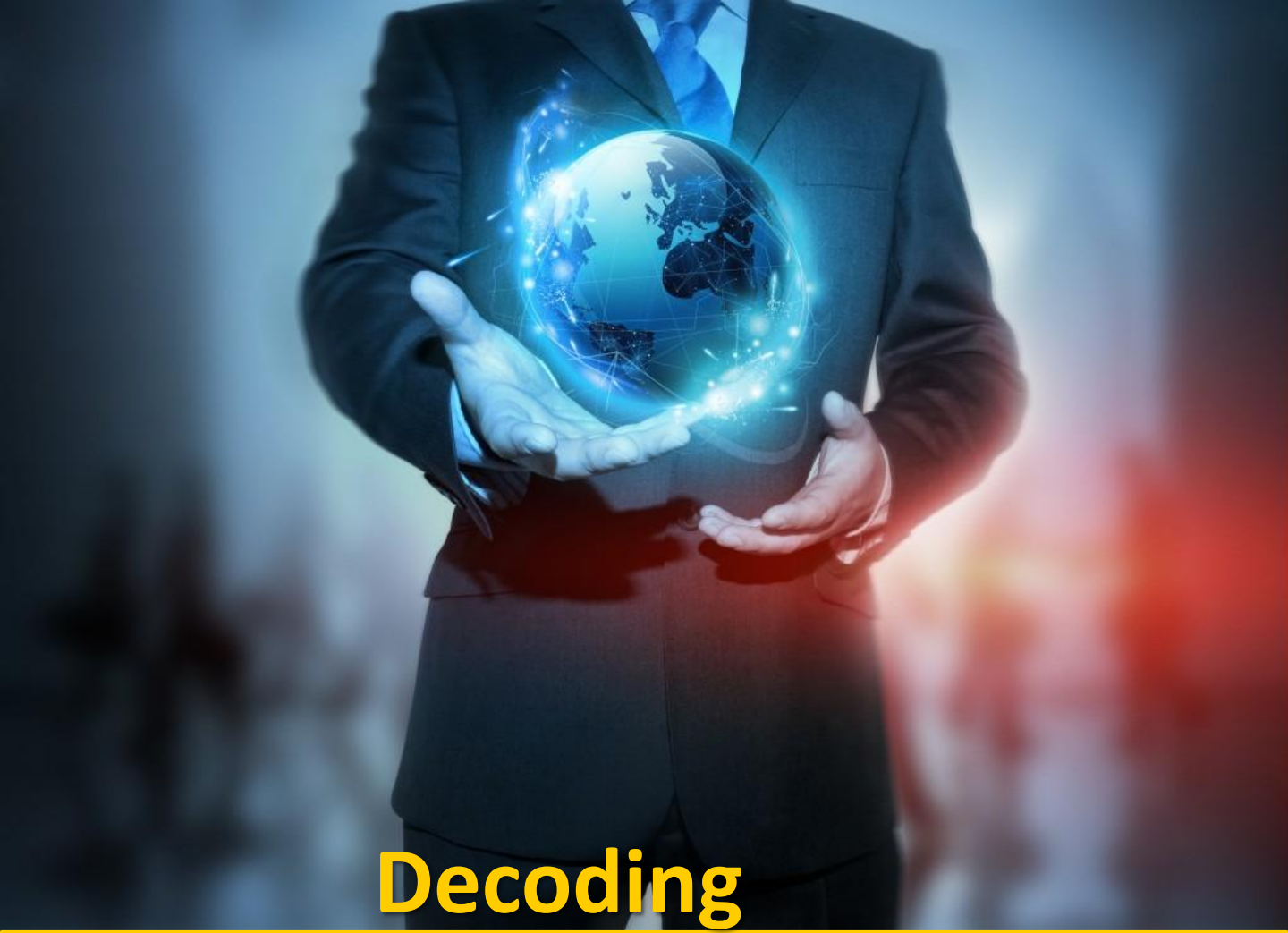

Decoding Expatriate Taxation

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Chartered Accountants

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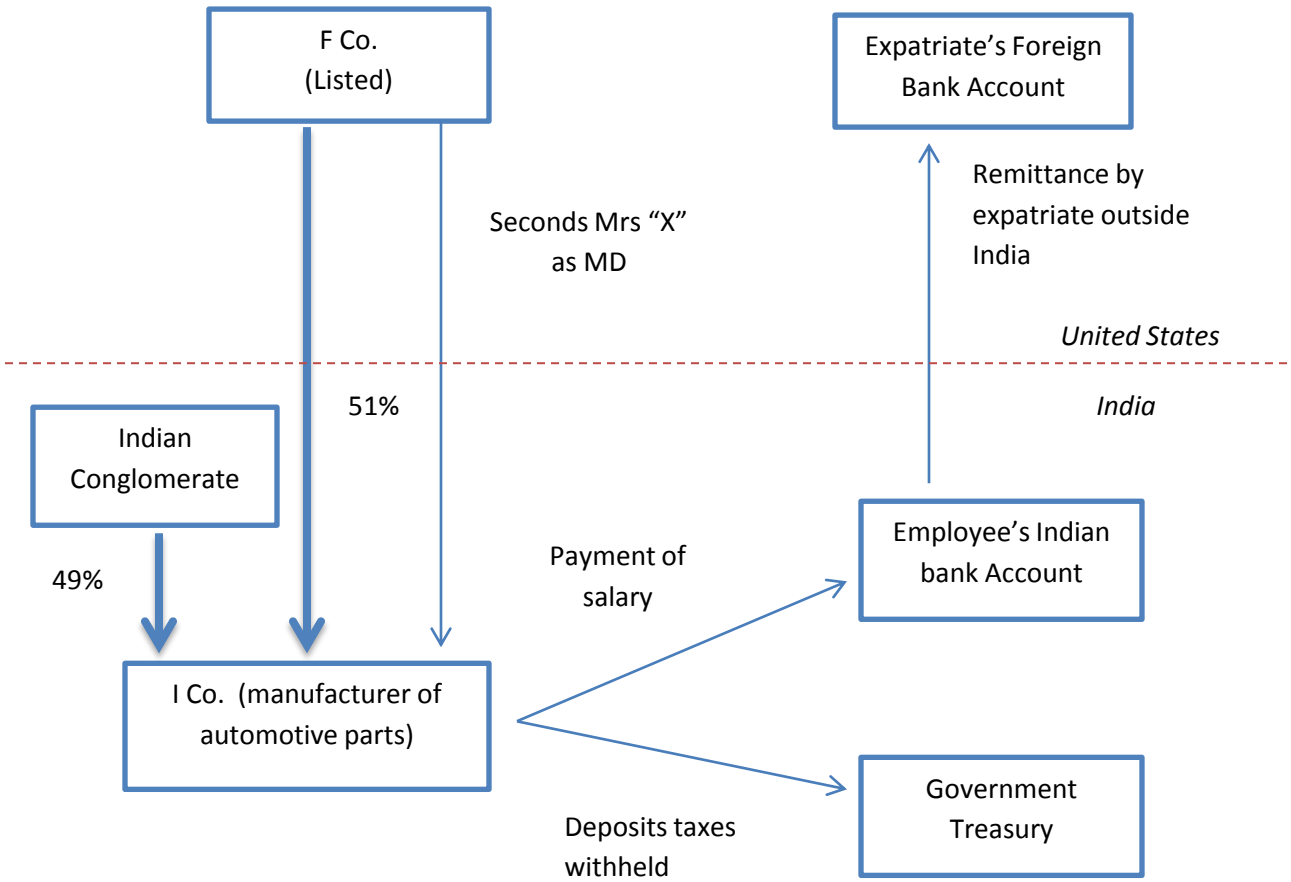
Case Study I: Secondment as "MD" to Indian JV – Scenario 1



Mechanics:

- I Co is a JV between F Co (set up and listed in US) and Indian conglomerate
- I Co is engaged in manufacturing of auto parts
- As per the JV agreement between F Co and I Co, F Co has right to second its employee as MD of I Co. Accordingly, F Co seconds Mrs X to I Co for 3 years
- I Co has obtained Central Government approval for the remuneration payable to Mrs X since the proposed remuneration exceeded the prescribed limits under the Companies Act
- The employment of Mrs X with F Co was temporarily suspended and Mrs X is on the payroll of I Co.
- F Co shall not contribute to the Social Security Benefits of Mrs X
- I Co shall be responsible to pay the salary of Mrs X in India
- Mrs X would remit the funds from India to its foreign bank account

• Indian income tax on salary is paid in India by way of WHT done by I Co
• I Co to deposit the Indian WHT on total salary into the Government Treasury
• I Co shall decide the terms of employment of Mrs X including their salary, increments, bonus, leave, appraisals, etc.
• Mrs X to report and work under the management, supervision, instructions and control of I Co.
• Mrs X would not represent the F Co in India and would work solely for I Co
• I Co. would be responsible for the work of the Mrs X and shall bear all risks in connection with the same
• Employment policies of I Co would be applicable to Mrs X
• I Co has the right to terminate the employment of Mrs X (under certain circumstances)
• Mrs X have the right to recover salary and other dues from I Co and can take legal recourse to recover the same
• Mrs X continues to be part of ESOP plan of F Co
• Mrs X reports to the BOD of I Co but also has certain 'dotted line' reporting independently to the CEO of F Co Group

Questions:

Q1. Which entity should be regarded as the "employer" of Mrs X?
Ans. *I Co. should be regarded as the "employer" of Mrs. X considering the below factors:*
a) Control and supervision and responsibility for work with I Co.
b) Terms and conditions of employment to be regulated by I Co.
c) Legal recourse with Mrs. X for salary dues lies against I Co.
d) Right to terminate services of Mrs. X (i.e., lien on employment) with I Co.
e) Payment of salary and Social security by I Co.

Q2. What position should I Co/ F Co adopt in India in respect of secondment of Mrs X for:
- Disclosure in accounts?
- Corporate tax/ PE?
- TP documentation/ TP certificate/ TP method?
- FEMA?
- Social security contributions?

Ans. All the above compliances are to be followed by I Co. w.r.t. secondment of Mrs. X. They are as below:

- **Disclosure in accounts:** I Co. (if listed co.)must disclose the details of employee in its Director's report under section 134(3) of Companies Act, 2013, in case annual salary of Mrs. X is 6 million Rupees or more. Further, details of Mrs. X are also to be mentioned in Director's report as she is seconded as "MD" of I Co. Further, salary due to Mrs. X shall also be disclosed by I Co. in accounts as salary cost.

- **Corporate Tax** : As Mrs. X is on the payroll of I Co., salary paid to Mrs. X is booked as an expense in the accounts of I Co. and while calculating the corporate tax it must be taken into account as deductible expense.
- **Permanent Establishment (PE)** : There is no PE in respect of F Co. in this case as Mrs. X is working in India under the control and direction of I Co. and considered as employee of I Co. It cannot be said that F Co. is carrying on business in India through presence of Mrs. X in India. Also for all her salary dues she can take legal recourse against I company.

- **TP documentation/ TP certificate/ TP method**: As Mrs. X is appointed as a " Managing director" of I Co., it will be considered as related party and TP documentation would be mandatory. TP method would be Transactional net margin method (TNMM) or Comparable Uncontrolled Pricing method (CUP). I Co. would have to file Form 3CEB being TP audit report with the tax authorities in respect of salary paid to Mrs. X as it is considered as related party transaction.

- **Foreign Exchange Management Act** : As repatriation of salary is outside India, FEMA guidelines are to be followed by Mrs. X, which allows 100% remittance outside India after payment of taxes as per below circular of RBI:

- **Social security contributions**: India has Social Security Agreements (SSA) with different countries . If as per respective SSA between two countries, contribution is being deposited by the home country (in this case, US), then there is no need of any contribution in other country (i.e., India). At the time of writing this article there is no SSA between India and USA therefore employee deployed in India will have to pay Provident Fund under Employees Provident Fund Act , 1952 of gross salary drawn by her whether in India or in US.

Q3. Is there any risk of F Co creating a PE in India? If yes, why and how can the exposure be minimized?

Ans. While drafting an intercompany agreement and deciding terms of deputation between F Co. and I Co. following points should be taken into consideration which will minimize the risk of F Co. becoming a PE in India:

- Salaries, allowances, perquisites and benefits payable and other terms and conditions of employment of Mrs. X with I Co. would be governed by the Employment Agreement entered into between I Co. and Mrs. X.

- I Co. may at its discretion extend or terminate the Employment Agreement entered into with the Mrs. X. During the period of assignment, Mrs. X shall work solely under the control, direction and supervision of I Co. and shall report to the management of I Co. Further, Mrs. X shall be bound by, and treated in accordance with the applicable rules, policies and regulations established by I Co.

- F Co. shall not be responsible for selection/ identification of Mrs. X to be sent on assignment to I CO. and F Co. will only act as per the written instructions/ consent/ communication received from I Co. from time to time.

- F Co. shall not be responsible to I CO. or any other entity for the work executed by Mrs. X during the period of assignment and all the risks and rewards of the work performed by him shall rest with I CO..

- I CO. shall reserve the right to evaluate and review the performance of Mrs. X in accordance with its standard HR policies and procedures and may also undertake necessary steps to ensure satisfactory performance as per its prescribed standards.

- I CO. will be under an obligation to bear all the salary, perquisites and other benefits payable to Mrs. X for this assignment. However, F Co. may facilitate disbursement of such salary, on behalf of I CO., to the bank account of the Mrs. X in US solely for the purposes of administrative convenience, subject to the Indian exchange control regulations and any other laws in India.

- I CO. shall be responsible for withholding taxes from the total remuneration payable to Mrs. X and deposit the same into the Indian Government treasury in accordance with the tax laws of India.

- During the period of assignment, the payroll of Mrs. X shall be maintained by I Co.

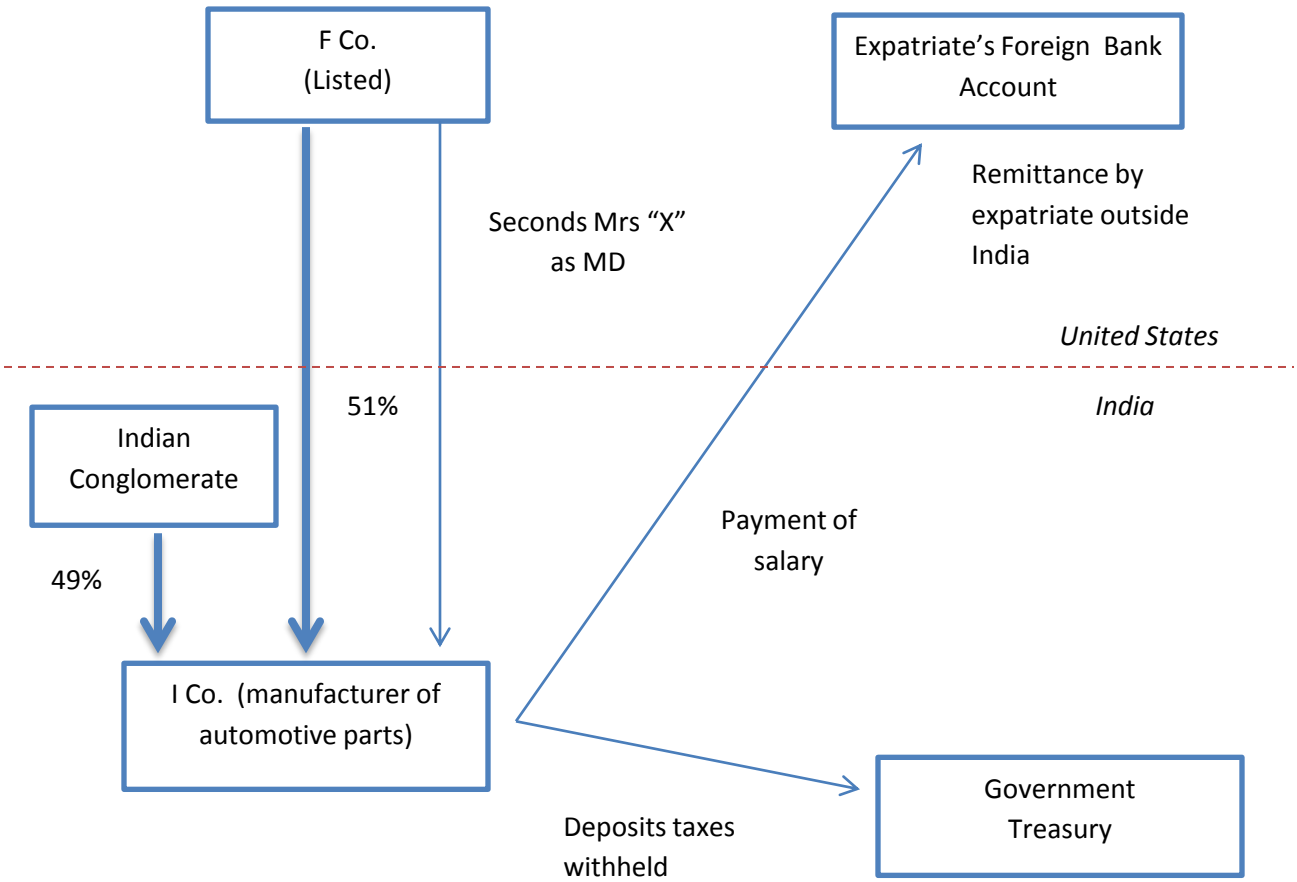
- Mrs. X will be required to comply with the social security rules and regulations, as may be applicable, in accordance with the laws in India and US.

- Purely with a view to subsidize I Co., F Co. may agrees to bear/ pay a certain proportion of the total remuneration payable to each Mrs. X which shall be intimated by F Co. to I Co. from time to time, in writing.

- Further subsidization of the salary as above by F Co. should not be construed as the Mrs. X representing F Co. or any services being received by F Co. from Mrs. X or F Co. exercising any control over Mrs. X or being responsible for any actions or omissions of Mrs. X while employed with I Co.

F Co., for the purposes of administrative convenience, may also perform such acts/ deeds, as may be required, in connection with assignment of Mrs. X which shall be intimated/ communicated by I CO. from time to time.

Case Study I: Secondment as "MD" to Indian JV - Scenario 2



Mechanics:

• Due to personal reasons, Mrs. X prefers receipt of salary from I Co directly into her bank account outside India.

Questions:

Q1. Would your response to any question in case study I (Scenario 1) above change/ vary? If yes, why?

Ans. There will not be any change in the above case study.

The only point to discuss is that I Co. has to follow FEMA guidelines for the purpose of remittance of salary outside India. I Co. has to pay withholding tax on gross salary and then can remit 100% salary outside India, as per RBI circular - A.P. (DIR Series) Circular No.62 dated January 22, 2015.

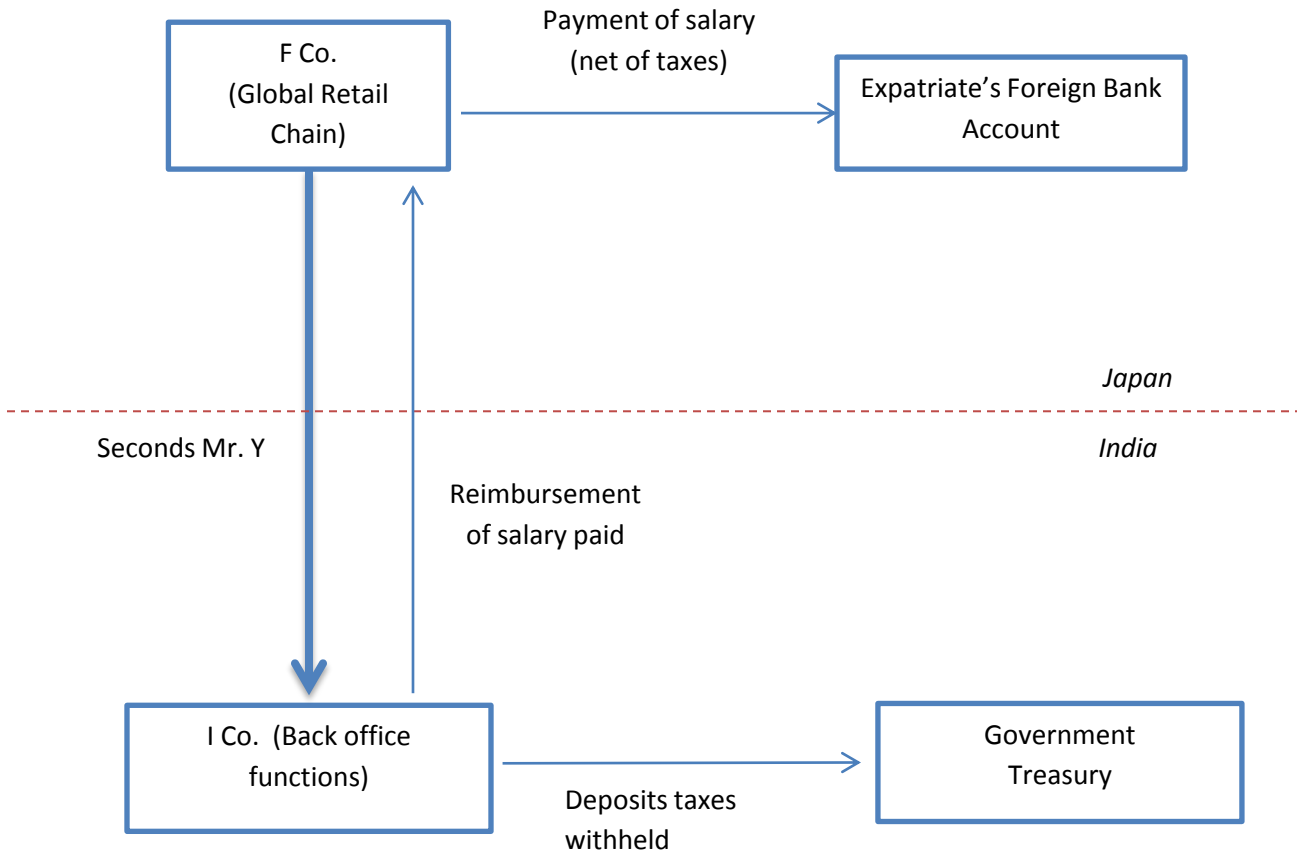
As discussed above, it is allowed as per RBI Circular reproduced below:

RBI has amended Regulation 7(8) of Foreign Exchange Management (Foreign Currency Accounts by a Person Resident in India) Regulations, 2000, (Notification No. FEMA. 10/2000-RB dated 3 May, 2000). This allows a citizen of a foreign State, being an employee of a foreign company, or a citizen of India employed by a foreign company outside India, and in either case on deputation to a group company/ group LLP in India, to open, hold and maintain a foreign currency account with a bank outside India and receive the whole salary payable to him for services rendered to the group company, by credit to such account, provided that income-tax chargeable under the Income-tax Act,1961 (the Act) is paid on the entire salary as accrued in India.

Further, RBI has also permitted a foreign citizen, resident in India being in employment with a LLP incorporated in India to open, hold and maintain a foreign currency account with a bank outside India and to remit the whole salary received in India in Indian Rupees for the services rendered to such LLP, to such account, provided that income-tax chargeable under the Act was paid on the entire salary as accrued in India.

The change is prospective in nature and was made effective from 24 December, 2014.

Case Study II: Back office set up



Mechanics:

- F Co is a global retail chain set up in Japan
- F Co as part of cost reduction exercise decides to set up a 100% subsidiary viz. I Co in India and outsources its group transaction processing and finance process functions and other back office functions to I Co
- I Co to be remunerated on cost plus basis by F Co
- To enable smooth transition and to assist I Co for setting up initial systems, F Co provides guidance and deputes Mr. Y as COO for 2 years to I Co
- Mr. Y has to receive salary from F Co into bank account in Japan to ensure continuity of social security in Japan (assumed) . I Co. will reimburse cost of salary paid in Japan to F Co. and F Co. will not charge any mark up on getting such reimbursement.

Questions:

Q1. You have been approached by F Co and I Co together to advise on appropriate secondment structure from the following perspective:

- Corporate tax/ PE
- FEMA
- WHT
- Service tax
- Tax treaty
- Social security
- TP, etc.

Ans. An appropriate secondment structure would be the one which would ensure minimal exposures under various legislations. Tax complications would be minimized if I Co. is determined as an employer of seconded employee by way of proper Employment visa. I Co. has to satisfy below factors to be the employer of seconded employee:

a) Control and supervision and responsibility for work with I Co.
b) Terms and conditions of employment to be regulated by I Co.
c) Legal recourse with Mr. Y for salary dues lies against I Co.
d) Right to terminate services of Mr. Y (i.e., lien on employment) with I Co.
e) Payment of salary and Social security by I Co.

Various compliances are explained as below:

- **Corporate Tax** : As Mr. Y is on the payroll of I Co., salary paid to Mr. Y is booked as an expense in the accounts of I co. (as the salary paid by F Co. is reimbursed by I Co.) and while calculating the corporate tax it must be taken into account as deductible expense .
- **PE**: Article 5 of DTAA between India and Japan excludes the below from being a fixed place PE for any enterprise:
  "the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a **preparatory or auxiliary character**."
  Mr. Y is working w.r.t. transaction processing, finance process functions and other back office functions in India which are in fact merely the supporting functions. A subsidiary by itself cannot be considered to be a PE of the Principal. It constitutes an independent legal entity for the purpose of taxation. Thus, there is no PE in respect of F Co. in this case under India-Japan tax treaty, as Mr. Y is working in India under the control and direction of I Co. and considered as employee of I Co. Also for all his salary dues he can take legal recourse against I co.

- **Foreign Exchange Management Act**: FEMA guidelines are to be followed by I Co. as it has to reimburse salary payment to F Co. It has to deduct tax on salary of Mr. Y and pay to Government treasury, then it can reimburse to F Co. As I Co. is the employer, it can remit the reimbursement of salary to F Co. provided withholding tax due on salary of Mr. Y is deposited by I Co.

- **Withholding Tax**: The amount of salary being reimbursed by I Co. to F Co. is subject to withholding tax since income of Mr. Y is accrued in India as he is working for I Co. under its control and direction. Thus, I Co. must deduct WHT and deposit with the Indian Government on global salary of Mr. Y paid in Japan .

- **Service tax:** As per section 67 of Finance Act, 1994, service tax can be levied only on gross amount charged for services rendered. In present case, no services are rendered by F Co. to I CO. and it is claiming pure reimbursement from I Co. as no mark up is levied by F Co while asking for reimbursement from I Co. Thus, I Co. shall not pay service tax on reimbursement of salary. Thus, no service tax applies in this case.

- **Tax treaty** : As per Article 23 of DTAA between India and Japan: "Where a resident of Japan derives income from India which may be taxed in India in accordance with the provisions of this Convention, the amount of Indian tax payable in respect of that income shall be allowed as a credit against the Japanese tax imposed on that resident. The amount of credit, however, shall not exceed that part of the Japanese tax which is appropriate to that income." Thus, WHT payable by Mr. Y on salary shall be allowed as credit against Japanese tax.

- **Social security contributions**: India has Social Security Agreements (SSA) with different countries . If as per respective SSA between two countries, contribution is being deposited by the home country (in this case, Japan), then there is no need of any contribution in other country (i.e., India). At the time of writing this article there is no SSA between India and Japan therefore employee deployed in India will have to pay Provident Fund under Employees Provident Fund Act 1952 of gross salary drawn by her whether in India or in Japan.

- **Transfer Pricing**: As I Co. is 100% subsidiary of F Co., it will be considered as Associated Enterprise (enterprise having at least 26% voting power) and TP documentation would be mandatory for I Co.
  TP method would be Transactional net margin method (TNMM) or Comparable Uncontrolled Pricing method (CUP). I Co. would have to file Form 3CEB being TP audit report with the tax authorities in respect of amount reimbursed to F Co. i.r.t. salary cost of Mr. Y, as it is considered as related party transaction.
  However, if the amount remitted by I Co. to F Co. is purely reimbursement in respect of salary of Mr. Y, , I Co. must report the reimbursement of salary cost in form 3CEB.

Q2. You are also requested to provide Indian implications of your recommended structure under the regulations mentioned above. You are also requested to suggest documentation/ agreements to be maintained to support your recommended structure.

Ans. Indian implications have been mentioned above for the respective regulations.
Agreements to be maintained between I Co. and F Co. are:

- **Deputation/ secondment agreement:** This agreement is required for the employee deputed by F Co.in I Co. It must mention all the terms and conditions of secondment which clearly bring out that the intention of parties is not to enter into any service relationship and arrangement is of contract of service.

- **Employment agreement:** This agreement is required between I Co. and Mr. Y to establish employer-employee relationship.

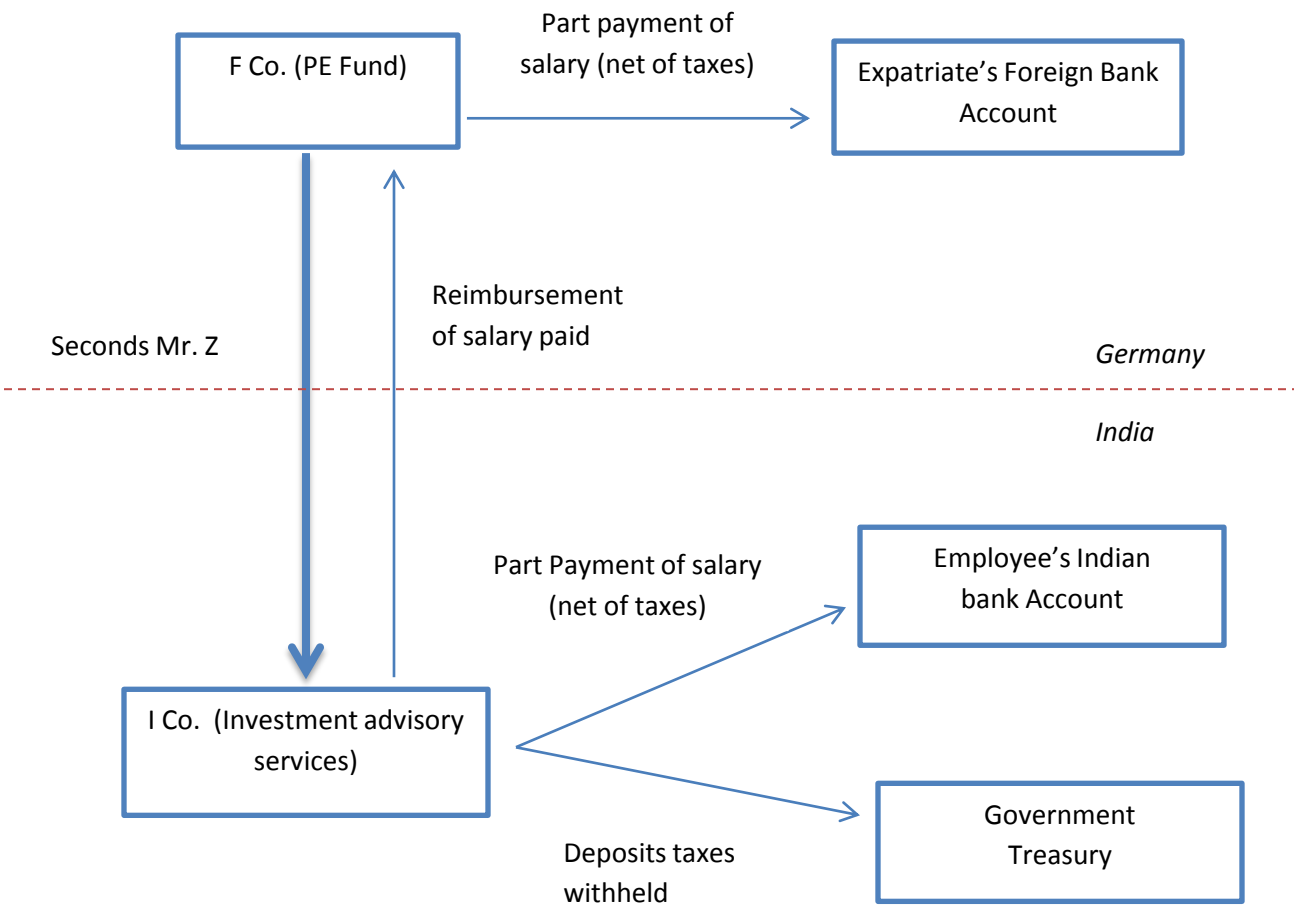
- **Transfer Pricing agreement:** This agreement is required as I Co. is the 100% subsidiary of F co. Further, if salary is reimbursed by I Co. on cost , then also TP agreement is required.

Q3. You are requested to comment on likely profit attribution ,if PE is alleged.
Ans. The activities, which are not undertaken by I Co. and the assets of F Co. outside India cannot be taken into account or attributed for earning/ income of F Co. to be considered as PE in India. In respect of Mr. Y deputed by F Co. to I Co. , F Co. will not become PE because of the following reasons:

a) Control and supervision and responsibility for work with I Co.
b) Terms and conditions of employment to be regulated by I Co.
c) Legal recourse with Mr. Y for salary dues lies against I Co.
d) Right to terminate services of Mr. Y (i.e., lien on employment) with I Co.
e) Reimbursement of salary and Social security by I Co. to F Co. without any mark up.

Q4. Should "costs" for arriving at "cost plus remuneration" for I Co from F Co include salary cost of Mr. Y?
Ans. As Mr. Y is deputed employee of I Co. and salary of Mr. Y is borne by I Co., it is the expense of I Co. and shall be included in the "costs" of I co. for arriving at "cost plus remuneration" charged to F Co.
Moreover, if the arrangement is considered as "services", not only cost of Mr. Y but the 'entire arm's length value of services' may be added to 'costs' of I Co. to arrive at "cost plus remuneration" (using TNM method).

Case Study III: Part salary payment



Mechanics:

- F Co is a PE fund set up in Germany
- F Co has a subsidiary in India engaged in providing investment advisory services on a "cost plus" basis to F Co
- There is need in I Co for an economist MBA to explore the Indian markets (targets)
- F Co seconds Mr. Z to I Co for a period of 5 months
- Mr. Z wishes to receive 50% salary from F Co directly into the bank account in Germany and balance 50% from I Co in Indian bank account

Questions:

Q1. Which entity should be regarded as the "employer" of Mr. Z?
Ans. I Co. is the employer of Mr. Z considering the below factors:

1. Control and supervision of I Co. on Mr. Z
2. Responsibility for work of Mr. Z lies with I Co.
3. Right to take disciplinary action by I Co.
4. Terms and conditions of employment to be regulated by I Co.
5. Legal recourse with Mr. Z for salary dues lies against I Co.
6. Right to terminate services of Mr. Z (i.e., lien on employment) with I Co.
7. Payment of salary and Social security by I Co.

Q2. What position should I Co/ F Co adopt in India in respect of secondment of Mr. Z for:

- Disclosure in accounts?
- Corporate tax/ PE?
- TP documentation/ TP certificate/ TP method?
- FEMA?
- Social security contributions?
- WHT?

Ans. Below positions should be adopted by I Co./ F Co. in respect of:

- **Disclosure in accounts**: I Co. must disclose the details of employee in its Director's report under sec 134(3) of Companies Act, 2013, in case annual salary of Mr. Z is 6 million Rupees or more. Also, I Co. must disclose entire salary cost (salary paid by I Co. as well as F Co.) of Mr. Z in its accounts as a deductible expense.

- **Corporate tax**: As Mr. Z is on the payroll of I Co., salary paid to Mr. Z is booked as an expense in the accounts of I co. (as 50% of salary paid by F Co. is also reimbursed by I Co.) and while calculating the corporate tax it must be taken into account as deductible expense . Further, I Co. must also disclose under taxable income the fee received from F Co. for providing investment advisory services. 100% of the salary paid directly or indirectly to Mr. Z would be subject to withholding tax deduction as per Indian Income Tax Act 1961

- **PE exposure**: Article 5 of DTAA between India and Germany excludes the below from being a PE for any enterprise:
  "the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character."
  The outsourcing of activities to the Indian affiliate would not result in either a fixed place or agency PE in India. Deputation of employees of Foreign company to carry out support activities to protect the interests of the F Co. does not result in a service PE in India.

Similarly, employees of the subsidiary who work under the supervision and direction of the Indian affiliate also do not result in a service PE India.
Thus, Mr. Z is working in I Co. i.r.t. investment advisory services which act as support activities for F Co. So, there is **no PE** in respect of F Co. in this case as Mr. Z is working under the control and direction of I Co. and considered as employee of I Co. Also for all his salary dues he can take legal recourse against I company.

- **TP documentation/ TP certificate/ TP method:** As I Co. is subsidiary of F Co., it will be considered as Associated Enterprise (enterprise having at least 26% voting power) and TP documentation would be mandatory for I Co.
  TP method would be Transactional net margin method (TNMM) or Comparable Uncontrolled Pricing method (CUP). I Co. would have to file Form 3CEB being TP audit report with the tax authorities in respect of amount reimbursed to F Co. for salary of Mr. Z, as it is considered as related party transaction.

- **Foreign Exchange Management Act:** FEMA guidelines are to be followed by I Co. as it has to reimburse salary payment to F Co. It has to deduct withholding tax on entire salary of Mr. Z and pay to Government treasury, then it can reimburse the amount to F Co.
  I Co. has to justify the remittance w.r.t. the amount being remitted is purely the amount of salary and no other element of profit is involved in such transaction.
  Further, F Co. can pay salary to seconded employee directly in his foreign bank account, subject to payment of taxes (Withholding Tax) on such salary in India under automatic route.

- **Social security contributions**: India has Social Security Agreements (SSA) with different countries . If as per respective SSA between two countries, contribution is being deposited by the home country (in this case, Germany), then there is no need of any contribution in other country (i.e., India). At the time of writing this article there is no SSA between India and Germany therefore employee deployed in India will have to pay Provident Fund under Employees Provident Fund Act 1952 of gross salary drawn by her whether in India or in Germany .

- **Withholding Tax:** I Co. shall deduct withholding tax on employee's global salary for the duration he is working for I Co.(i.e., salary in India and Germany) and pay to Indian Government since the employee is solely working for I Co. during that period (5 months), and his entire salary (though 50% paid in Germany) is accrued in India. Mr. Z , however, can claim tax relief u/s 90 and 91 of Income Tax Act, 1961 under Double Taxation Avoidance Agreement (DTAA) between India and Germany in respect of tax deducted in India against his German tax. Further, in absence of PE, it can be argued that receipts in the hands of F CO. are not taxable in India. Thus, I Co. should not deduct WHT on payment to F Co. as payments made by I Co. to F Co. are pure reimbursements of salary cost paid by F Co. to Mr. Z.

Q3. Is there any risk of F Co creating a PE in India on account of secondment of Mr Z? If yes, why and how can the exposure be minimized?

Ans. While drafting an intercompany agreement and deciding terms of deputation between F Co. and I Co., following points should be taken into consideration which will minimize the risk of F Co. becoming a PE in India:

a) Salaries, allowances, perquisites and benefits payable and other terms and conditions of employment of the Mr. Z with I Co. would be governed by the Employment Agreement entered into between I Co. and Mr. Z.

b) I Co. may at its discretion extend or terminate the Employment Agreement entered into with the Mr. Z. During the period of assignment, Mr. Z shall work solely under the control, direction and supervision of I Co. and shall report to the management of I Co. Further, Mr. Z shall be bound by, and treated in accordance with the applicable rules, policies and regulations established by I Co.

c) F Co. shall not be responsible for selection/ identification of Mr. Z to be sent on assignment to I Co. and F Co. will only act as per the written instructions/ consent/ communication received from I Co. from time to time.

d) F Co. shall not be responsible to I Co. or any other entity for the work executed by Mr. Z during the period of assignment and all the risks and rewards of the work performed by him shall rest with I Co.

e) I Co. shall reserve the right to evaluate and review the performance of Mr. Z in accordance with its standard HR policies and procedures and may also undertake necessary steps to ensure satisfactory performance as per its prescribed standards.

f) I Co. will be under an obligation to bear all the salary, perquisites and other benefits payable to Mr. Z for this assignment. However, F Co. may facilitate disbursement of such salary, on behalf of I Co., to the bank account of the Mr. Z in Germany solely for the purposes of administrative convenience, subject to the Indian exchange control regulations and any other laws in India.

g) I Co. shall be responsible for withholding taxes from the total remuneration payable to Mr. Z and deposit the same into the Indian Government treasury in accordance with the tax laws of India.

h) During the period of assignment, the payroll of Mr. Z shall be maintained by I Co.

i) Mr. Z will be required to comply with the social security rules and regulations, as may be applicable, in accordance with the laws in India and Germany.

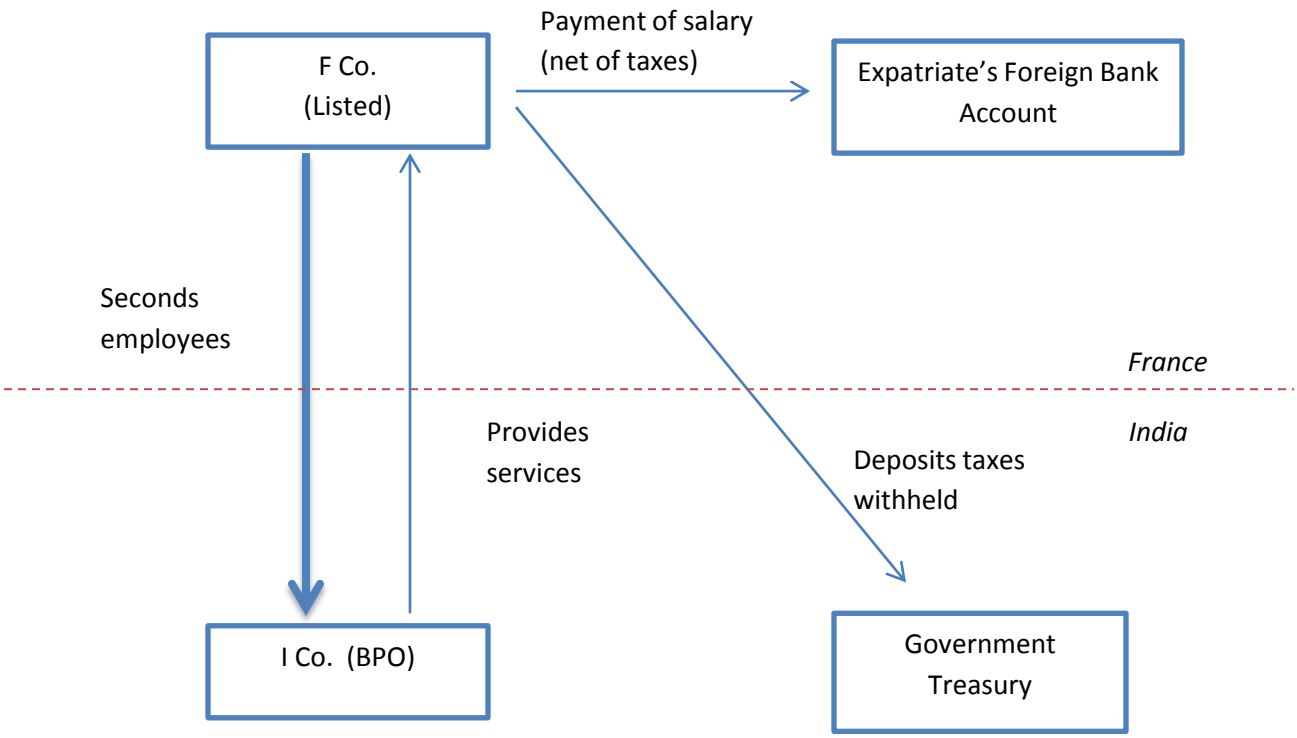
j) Purely with a view to subsidize I Co., F Co. may agree to bear/ pay a certain proportion of the total remuneration payable to Mr. Z which shall be intimated by F Co. to I Co. from time to time, in writing.

k) Further subsidization of the salary as above by F Co. should not be construed as Mr. Z representing F Co. or any services being received by F Co. from Mr. Z or F Co. exercising any control over Mr. Z or being responsible for any actions or omissions of Mr. Z while employed with I Co.

l) Payment of part salary by F Co. as 'disbursement agent' of I Co. only for the purpose of administrative convenience.

F Co., for the purposes of administrative convenience, may also perform such acts/ deeds, as may be required, in connection with assignment of Mr. Z which shall be intimated/ communicated by I Co. from time to time.

Case Study IV: Salary borne by F Co



Mechanics:

- I Co renders certain services (say BPO) to F Co
- I Co charges fees for rendering BPO services on a "cost plus" arm's length basis
- F Co seconds employees to I Co on account of shortage of manpower/ resources in I Co
- Secondees works under direction, supervision and control of I Co
- I Co is responsible for the services of secondees
- Employees retains lien on employment with F Co
- F Co pays the salary to the seconded employees in the home country and does not cross-charge I Co in respect of the same

Questions:

Q1. Who shall be the "employer" of the seconded employees?

Ans. In the given case, control and supervision, and responsibility for work of secondees lies with I Co. However, obligation to pay salary and other employment costs lies with F Co. Further, since employees retain lien on employment with F Co., F Co. is likely to be regarded as the employer. Also, the fact that F Co. pays salary to the seconded employees in home country and does not cross charge to I Co. also leads to the conclusion that F Co. is the legal employer and secondees can take legal recourse against F Co. for their salary dues.

Q2

Q2. Whether there is any PE exposure for F Co in India?
Ans. Considering F Co. is the employer, there is a fixed place PE or service PE exposure for F Co. in India as F Co. is carrying on its business (i.e, outsourced BPO services) through the seconded employees through a fixed place (as per DTAA between India and France, it is for more than 6 months) in India.
Also, for all salary dues, employees can take legal recourse against F co.

Q3. Who shall be responsible for WHT on the salary paid to secondees? Can I Co undertake WHT compliances on behalf of F Co?
Ans. Since F Co. is the employer of seconded employees, F Co. shall be responsible for WHT obligations. However, I Co. can undertake WHT obligations on behalf of F Co. as an agent of F Co.

Q4. Would there be any FEMA implications on payment of salary by F Co?
Ans. Yes, since employees are working under supervision and control of I Co., and salary is paid by F Co., there will be FEMA implications on payment of salary. Tax deduction is mandatory for F Co. before salary payment. F Co. can pay salary to seconded employees directly in their foreign bank accounts, subject to payment of taxes (Withholding Tax) on such salary in India under automatic route.

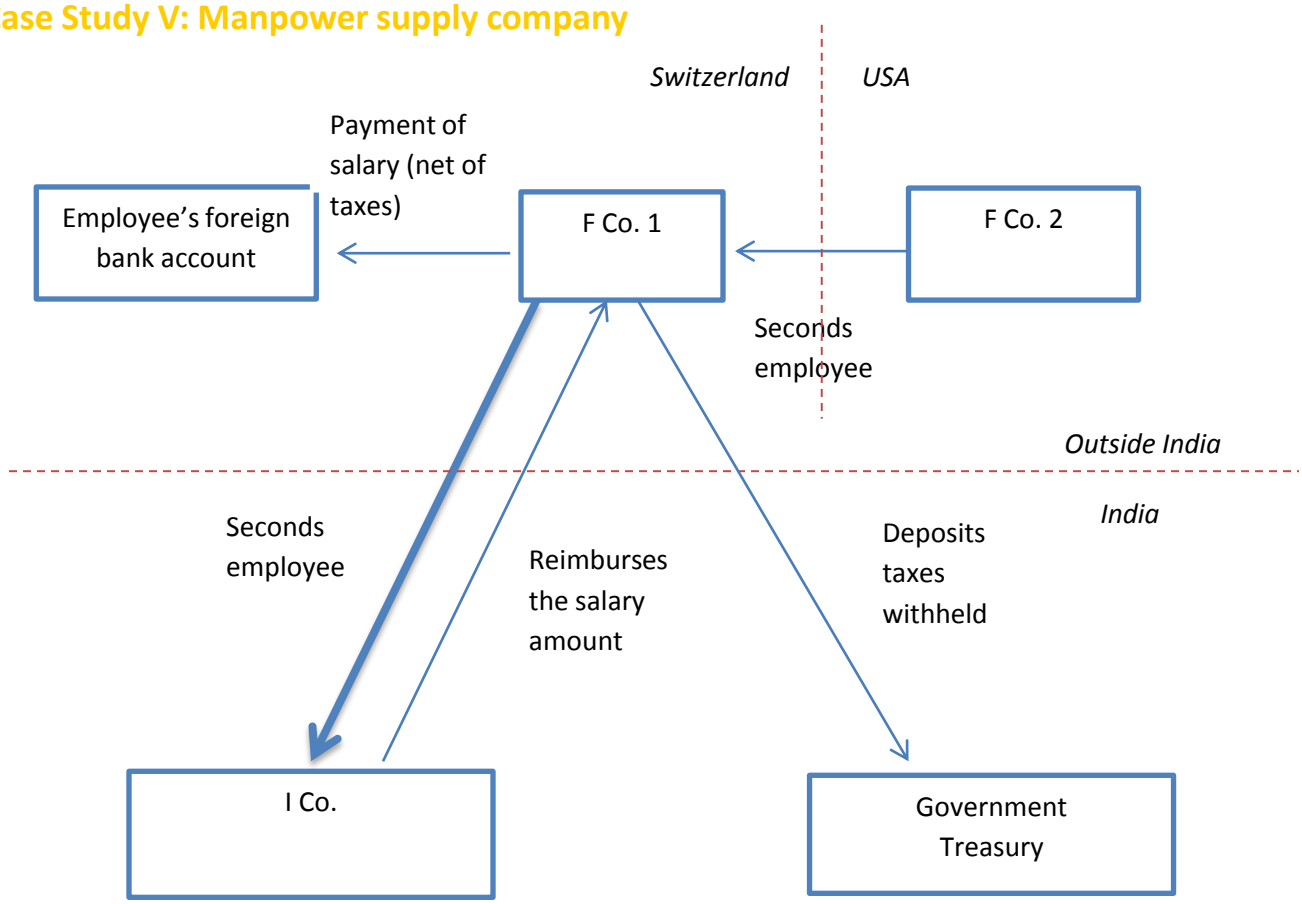
Q5. Whether the deputation of employees by F Co to I Co at no consideration be reported as "international transaction" for TP purposes?
Ans. Yes, this has to be reported under TP as every international transaction must be at arm's length price. As per section 92B of Income tax act, 1961, the term "International Transaction" includes transfer or use of intangible assets (which includes human capital related intangible assets such as trained and organized workforce , employment agreements). Thus, deputation of employees at no consideration may be reported as "international transaction" since it is provision of services to I Co. at no cost which would have a bearing on profits/ losses of I Co. and F Co. both.

Q6. Can the Tax Authorities include the cost of such employees while computing the cost of services rendered to AE and apply arm's length mark up on the same?
Ans. Yes, tax authorities can include cost of such employees while computing cost of services rendered to AE and apply arm's length mark-up on the same because no consideration is not justified between two AE's w .r.t. arm's length price. Further, F Co. is already paying fee on "cost plus arm's length basis" to I Co. for BPO services.

Q7. Can I Co justify non-payment of consideration for the seconded employees citing section 92(3) of the Act?

Ans. Section 92(3) says that if determination of any cost or expense has the effect of reducing the income chargeable to tax or increasing the loss, computed on the basis of book entries, provisions of sec. 92 (i.e., arm's length price) shall apply. In present cost of seconded employee should be have been added to total cost incurred by I Co. to arrive at total cost . Since salary cost of seconded employee is not included therefore mark up which has to be calculated on cost plus mark up has been reduced. Therefore exclusion of cost of seconded employee while calculating mark up is not justifiable as per Indian transfer pricing regulations.

Case Study V: Manpower supply company



Mechanics:

- F Co1 is a group manpower supplying company for seconding employees worldwide within the group
- I Co is in need of Mrs. X and request F Co1 to provide manpower with specific qualification/ expertise
- F Co2 has employee with the said qualification/ expertise and is fine with seconding employee
- F Co2 seconds employee to F Co1 for 6 months who in return seconds to I Co for 6 months
- F Co1 pays salary, etc. of the employee which is reimbursed by I Co to F Co1 without any mark-up
- F Co1 is paid specific fee (2 months' salary cost) by I Co for recruitment of employee
- Employee works under the supervision and control of I Co.

Questions:

Q1. Which entity should be regarded as the "employer" of seconded employee?
Ans. In the given facts of the case, I co. shall be the employer of seconded employee as he works under its supervision and control and also, salary is being borne by I Co. and employee can take legal recourse against I Co. for his salary dues.

Q2. Whether there is any PE exposure for F Co 1 and F Co 2?
Ans. PE Exposure for F Co. 1: Service PE shall not be attracted as per India-Switzerland DTAA as the manpower supply services are not considered under "technical services". Further services rendered by employee works under the control and supervision of I Co. and not under the control of F Co. 1 or FC0 2.

PE Exposure for F Co. 2: Tax authorities may contend that F Co. 2 could have directly seconded employees to I Co. rather than through F Co. 1. It may be deliberately arranged to avoid service PE exposure to F Co. 1. However, based on the facts if it could be demonstrated that F Co. 1 renders manpower supply services to group companies, tax authorities may hold a different opinion. Further, if secondment periods and terms of secondment are different for F Co.1 and F Co.2, then it may be established that F Co. 2 has no PE exposure in India.

Q3. What position should I Co/ F Co adopt in respect of secondment of seconded employee for:
- Disclosure in accounts?
- Corporate tax/ PE?
- TP documentation/ TP certificate/ TP method?
- FEMA?
- Social security contributions?
- WHT?

Ans. I Co. / F Co. should adopt below positions:

- **Disclosure in accounts:** I Co. must disclose the details of employee in its Director's report under sec 134(3) of Companies Act, 2013, in case annual salary of seconded employee is 6 million Rupees or more. Further, salary expense shall be disclosed in accounts by I Co.

- **Corporate tax**: As seconded employee is on the payroll of I Co., salary paid to secondee is booked as an expense in the accounts of I co. (as salary paid By F Co. 1 directly is reimbursed by I Co.) and while calculating the corporate tax it must be taken into account as deductible expense . Further, I Co. shall also disclose in accounts as an expense the service fee paid to F Co.1 for manpower supply. F Co. 1 shall disclose taxable income as received from manpower supply service provided to I Co.

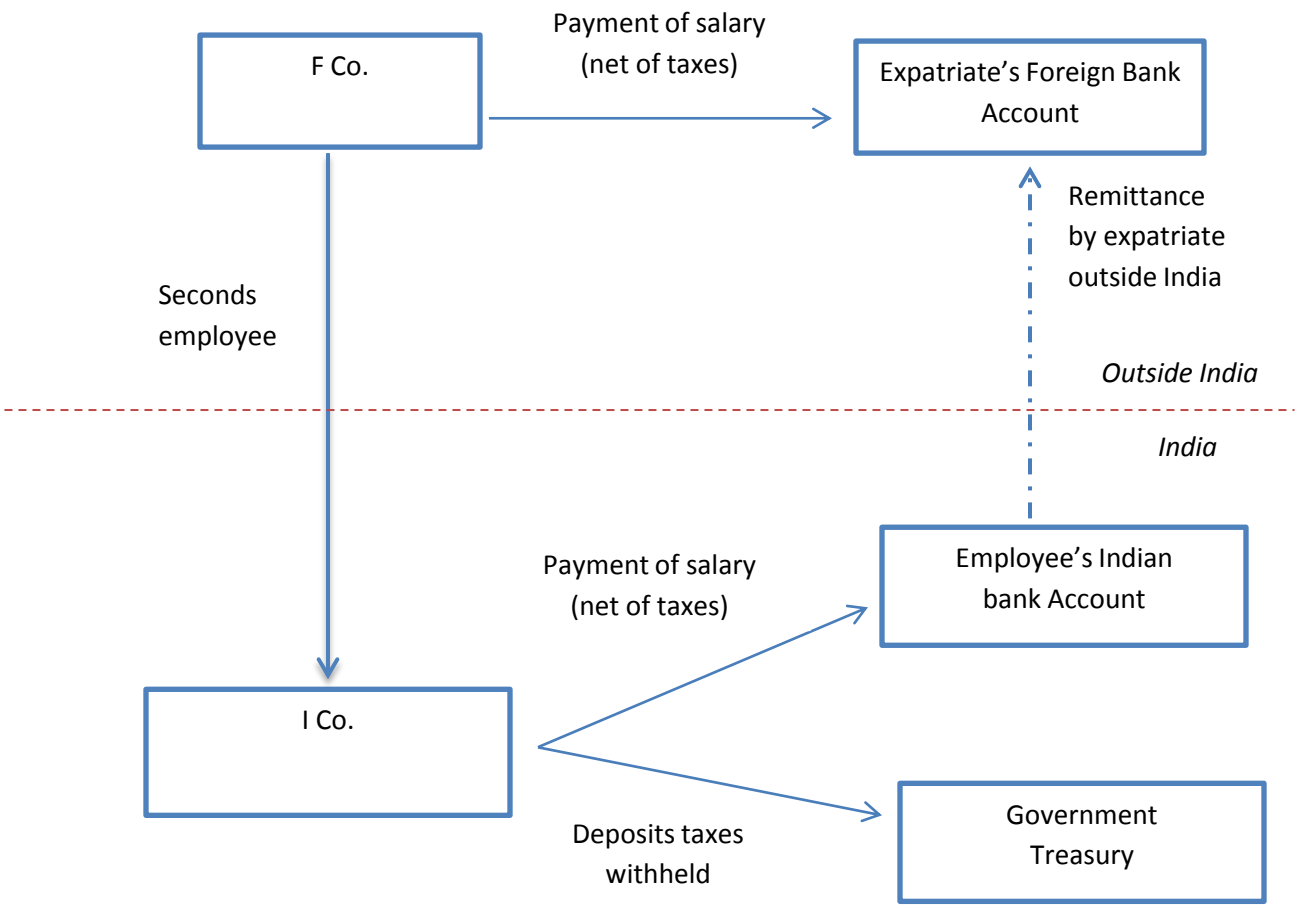
- **TP documentation/ TP certificate/ TP method**: TP documentation would be mandatory in this case. TP method would be Transactional net margin method (TNMM) or Comparable Uncontrolled Pricing method (CUP). I Co. would have to file Form 3CEB being TP audit report with the tax authorities in respect of amount paid to F Co.1 i.r.t. manpower supply fee charged by F Co.1.

- **Foreign Exchange Management Act:** I Co. has to follow FEMA guidelines to remit funds outside India w.r.t. salary payment by F Co.1 . It must ensure taxes are duly paid by F Co. i.r.t. salary. Further, F Co. can pay salary to seconded employee directly in his foreign bank account, subject to payment of taxes (Withholding Tax) on such salary in India under automatic route.

- **Social security contributions**: India has Social Security Agreements (SSA) with different countries . If as per respective SSA between two countries, contribution is being deposited by the home country (in this case, Switzerland), then there is no need of any contribution in other country (i.e, India). At the time of writing this article there is SSA between India and Switzerland therefore employee deployed in India will not have to pay Provident Fund under Employees Provident Fund Act 1952 of gross salary drawn by her whether in India or in Switzerland.

- **Withholding Tax:** since employee is working under control of I Co. and I Co. is considered as the employer, it is liable for payment of taxes to Indian Government. In this case, it must ensure due payment of taxes on salary of seconded employee while remitting funds to F Co 1. Further, in respect of manpower supply fee charged by F Co. 1 from I Co., I Co. must deduct WHT on such payment and also, F Co.1 shall be liable to pay 10% (plus surcharge and education cess) on net basis on such income. DTAA between India and Switzerland has to be referred in this case.

Case Study VI: Dual employment



Mechanics:

- F Co to second employee to I Co based on specific request from I Co
- I Co to select the employee and employ it on its payroll
- The employment of the seconded employee would not terminate with F Co and the employee shall be on the payroll of I Co as well as F Co
- The seconded employee would work solely for I Co when he stays in India (say 8 months) and would work solely for F Co when he stays in the home country (say 4 months)
- Respective entity viz. I Co/ F Co shall be responsible to pay the salary of seconded employee in India/ home country respectively

• Seconded employee would remit the funds from India to its foreign bank account
• I Co shall decide the terms of employment of the seconded employees including its salary, increments, bonus, leave, appraisals, etc. for the work to be done in India.
• The seconded employees to report and work under the management, supervision, instructions and control of I Co for India related work
• Respective entities shall be responsible for the work of the seconded employees and shall bear all risks in connection with the same

Questions:

Q1. Which entity should be regarded as the "employer" of seconded employee?
Ans. Considering the facts of the given case (i.e., control and supervision, responsibility for work, legal recourse, obligation to pay salary, regulation of terms and conditions of employment, payroll, bearing of risk lies with both I Co and F Co. for the respective duration of work) prima-facie the employee is on dual employment. Both I Co. and F Co. shall be regarded as employers for the specified duration of stay (8 months and 4 months respectively)of the seconded employee.
However, tax authorities may contend that F Co. is the employer as 'lien on employment' lies with F Co. as employment would not terminate with F Co.

Q2. What position should I Co/ F Co adopt in respect of secondment of seconded employee for:
• Disclosure in accounts?
• Corporate tax/ PE?
• TP documentation/ TP certificate/ TP method?
• FEMA?
• Social security contributions?
• WHT?

Ans. I Co./ F Co. must adopt position as below:

- **Disclosure in accounts**: I Co. must disclose the details of employee in its Director's report under sec 134(3) of Companies Act, 2013, in case annual salary of employee is 6 million Rupees or more. Further, salary cost shall also be disclosed as expense by I Co. and F Co. in their accounts.

- **Corporate tax** : As seconded employee is on the payroll of I Co. and F Co., salary paid to secondee is booked as an expense in the accounts of I co. and F Co. and while calculating the corporate tax it must be taken into account as deductible expense for the respective period of each employer.

PE Exposure : No PE exposure is there if business of F Co. and I Co. is not carried out in India and outside respectively since the seconded employee would work solely for I Co when he stays in India (8 months) and would work solely for F Co when he stays in the home country (4 months).

• **TP documentation/ TP certificate/ TP method**: No TP documentation would be required as the entities are not associated enterprises and there is no international transaction involved. The given case does not mention the fee, if any charged by F Co. for secondment of employee. But, if there is any cost sharing agreement between I Co. and F Co. to share the salary cost of seconded employee, then TP documentation would be mandatory. Then, it has to be reported in form 3CEB and method would be TNMM or CUP.

• **Foreign Exchange Management Act**: Seconded employee has to follow FEMA guidelines for repatriation of salary outside India. He must ensure that WHT has been deducted on salary being remitted.

• **Social security contributions**: I Co. must ensure social security contribution is deposited w.r.t. the salary accrued in India. As the employee has separate employment agreement with both I Co. and F Co., both are responsible for the contributions depending on their respective laws of the countries in case of dual employment. But, if F Co. is the employer, then F Co. shall be responsible.
Further, SSA agreement between the two countries has to be referred in particular case.

• **Withholding Tax**: Tax shall be deducted on income sourced or received in India. Thus, salary paid in India for work done for I Co. has to be net of withholding tax. There is no WHT obligation by F Co. on salary paid by F Co. for work done abroad since salary is neither sourced nor received in India.

Case Study I – Eligibility for employment visa

Facts:

The salary structure of Mr. Peter is as under:

Components	Amount (USD)
Base salary	18,000
Taxable value of rent free accommodation	2,700
Tax gross up (approximately)	9,300
Total salary	30,000

Question:

Q1. Is Peter eligible to obtain an Employment visa?

Ans. No, Peter is not eligible to obtain employment visa because salary must exceed USD 25,000 (or its equivalent) per annum to obtain employment visa. However, this limit shall not apply to Ethnic cooks, language teachers/ translators and staff working for concerned Embassy/ High Commission in India.

Case Study II – For the purpose of employment

Facts:

- XYZ India sent its employee on a secondment to China. Part salary paid in India and part abroad. However, entire cost was borne by the foreign company
- Terms and conditions under which he was seconded were in line with the terms and conditions of the employees of the Indian company working in India
- The employee spent 98 days in India during the tax year
- The employee filed a non-resident return contending that he left the country for the purpose of employment and hence he could use the benefit under explanation to Section 6(1)

Question:

Q1. Can the employee claim the benefit of the explanation which provides for 'for the purpose of employment outside India'?

Ans. As per explanation to section 6(1)(c), a citizen of India who leaves India for the purpose of employment outside India shall be considered as 'non-resident' if his period of stay in India is less than 365 days within 4 years preceding the tax year and less than 182 days in the tax year.

Under the given case, the employee spent only 98 days in India during the tax year. Thus, he is a non-resident and can claim the benefit under this section.

Case Study III– Residential Status as per Tax Treaty

Facts:

- Mr. Joseph is a citizen of England.
- He is deputed to India to see I Co's Indian operations.
- He has houses in the US and India.
- The US house is rented out to a third party, while the Indian house is occupied by his wife and children.

Question:

Q1. Assume, Mr. Joseph is a tax resident of India and England, how would you determine his residential status as per the tie breaker rule?

Ans. The tax residency in a particular country is determined by rules that include physical presence, domicile and citizenship as may be prescribed under the domestic tax laws of different countries.

The individual who travels frequently and works in cross-border locations may sometime face a situation of 'dual tax residency'. Dual tax residency means acquiring tax residency of two countries simultaneously in a particular tax year by satisfying the specified conditions of domestic tax laws of both the countries.

Most of the tax treaties have stipulated 'tie breaker' rules for resolving the conflict of dual residency between two countries:

a) he shall be deemed to be a resident only of the country in which he has a **permanent home** available to him; if he has a permanent home available to him in both countries, he shall be deemed to be a resident only of the country with which his personal and economic relations are closer (**centre of vital interests**);
b) if the country in which he has his centre of vital interests cannot be determined, or if he has not a permanent home available to him in either country, he shall be deemed to be a resident only of the country in which he has an **habitual abode**;
c) if he has an habitual abode in both countries or in neither of them, he shall be deemed to be a resident only of the country of which he is a **national**;
d) if he is a national of both countries or of neither of them, the competent authorities of both the countries shall settle the question by **mutual agreement**.

Thus, in the given case, since India house of Mr. Joseph is occupied by his wife and children, his centre of vital interest would be India. So, he is tax resident of India.

Case Study IV– Eligibility of short stay exemption

Facts:

- An I Co wishes to hire international workers/foreign citizens resident for a period less than 183 days
- I Co does not directly hire the workers but through a intermediary set-up abroad
- Legally, the workers are employees of the intermediary company and not I Co

Question:

Q1. Whether the employees would be eligible to claim short stay exemption in India?
Ans. In case of employees on short-term assignments in India, short stay exemption may be claimed in respect of India taxes subject to fulfillment of the prescribed conditions in the relevant Double Taxation Avoidance Agreement/ Domestic tax law.

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