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BEFORE THE AUTHORITY FOR ADVANCE RULINGS
(INCOME TAX) NEW DELHI

27th Day of May, 2011

A.A.R. Nos. 865 of 2010

Present

Mr. Justice P.K.Balasubramanyan (Chairman)
Mr. J. Khosla (Member)
Mr. V.K. Shridhar (Member)

Name & address of of the applicant	Verizon Data Services India Private Limited, Olympia Tech Park, 9th Floor, Altius, Block No.1, Sidco Industrial Estate, Guindy, Chennai-600 032.
Commissioner concerned	Commissioner of Income Tax-III Chennai.
Present for the Applicant	Dr.Anita Sumanth, Advocate
Present for the Department	Mr.K.R.Vasudevan, Addl.DIT(Intl.Tax.)

RULING
(By V. K. Shridhar)

The applicant, Verizon Data Services India Private Limited (VDSI), is a Private Limited company and is incorporated under the provisions of the Indian Companies Act, 1956. It is a wholly owned subsidiary of Verizon Data Services LLC, US (Verizon US). The applicant is engaged in providing services relating to development and maintenance of telecom software solutions and certain information technology enabled services. All services rendered by the applicant are exported from

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India to its parent company Verizon US. The applicant submits that in order to ensure that efficiency is built into the system and the productivity is optimal, the parent company felt that the applicant needs individuals from US. The requirement was met by sending three of the employees of GTE Overseas Corporation, USA (GTE-OC), an affiliate of the parent company and engaged in a business similar to that of the applicant. Pursuant to it, the applicant entered into a Secondment Agreement with GTE-OC on 1st April, 2008. Broadly speaking, the role of the three employees as described in the Secondment Agreement is: that each employee shall function and act exclusively under the direction, control and supervision of the applicant ; that GTE-OC shall not be responsible for the work of any employees nor would undertake any obligation or risk with respect to the quality of the results produced from the work performed by such employees during the term of assignment; that GTE-OC would not be responsible for any claim, liability, etc. arising from the actions of the expatriate employee and that GTE-OC shall pay to the employees for the items which an employee is entitled to receive and the applicant shall reimburse GTE-OC for the items paid or provided to the employees. The responsibility to deduct tax under the Indian tax laws shall be upon the applicant. The first employee has assumed the position in the capacity of the Managing Director of the applicant. The role of the other two employees is to liaise between the applicant and the parent company, to supervise and provide directions on the manner in which the activities of the applicant should be carried out. The applicant submits that

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GTE-OC shall send the bill on the cost of items incurred for payment by the applicant on a month to month basis.

2. The applicant submits that the payments made are in the nature of reimbursement of salary and expenses paid by GTE-OC to the expatriate employees. Nothing is paid over and above the said amount. The tax payable at source on the salary and benefits that accrue to the expatriate employees are paid in India. As the applicant is the economic employer of the seconded employees, the liability to deduct the tax is upon the applicant. No income arises to GTE-OC as it only represents cost to cost reimbursement. As the salary payment and benefits paid to the expatriate employees have suffered tax withholding under section 192 of the Income Tax Act, 1961(Act), the same amount cannot be subjected to tax withholding under section 195 of the Act.

3. The applicant submits that GTE-OC is not rendering any services to the applicant through its expatriate employees. These personnel were deputed at the request of the applicant to work under its control. The reimbursement of salary cost paid by GTE-OC in respect of provision of personnel to the applicant is for administrative convenience and should not qualify as 'Fees for Included Services (FIS)' under India-US DTAA (DTAA). Under Article 12(4)(b), of the DTAA, consideration towards technical knowledge, skill etc. would be considered as FIS only if the technical know-how, skills etc. is made available to the applicant. It would be a case of FIS as there is a transfer of technical knowledge, skills etc. from GTE-OC to the applicant. The expatriate

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employees are engaged in rendering managerial services and not technical services. It is thus the applicant's case that the payments made to GTE-OC are not in the nature of FIS and not liable to tax in India having regard to the provision of the DTAA.

4. The applicant then submits that GTE-OC has no fixed place from where it is carrying on business in India. If it is held that the GTE-OC has a fixed place of business then salary and expenses incurred on expatriate employees would be deductible as an expense from the income earned / amount received from the applicant. The net income would be nil and there will be no requirement to deduct tax at source.

5. The applicant further submits that in case the payment is held to be income in the hands of GTE-OC as Fees for Included Services then it would be subjected to tax at the rate of 10% plus applicable surcharge and education cess on gross income.

6. Advance ruling is sought on the following questions framed by the applicant:-

> *1. On the facts and in the circumstances of the case whether the amounts (representing salary and benefits payable by GTE-OC to Expatriate employees) reimbursed by the Applicant to GTE-OC Overseas Corporation ('GTE-OC') is "income" accruing to GTE-OC and therefore, whether the same is liable to deduction of tax in accordance with the provisions of section 195 of the Indian Income Tax Act, 1961 ('the Act')?*

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2. *If the answer to Question No 1 is in the affirmative, then whether the same is taxable as "Fees for Included Services (FIS)" under the Act read with the India-USA Double Taxation Avoidance Agreement ('DTAA')?*

3. *Is there a Permanent Establishment of GTE-OC in India under the DTAA and if so, is the amount received by GTE-OC from the Applicant in the nature of "business profits" attributable to such Permanent Establishment in India under the DTAA?*

4. *If the answer to Question No 3 is in the affirmative is the amount of taxable income NIL, in as much as the reimbursements are at actual?*

5. *It the answer to Question No 1 is in the affirmative, then what is the rate at which tax is to be deducted at source on the payments made by the Applicant to GTE-OC?*

7. The learned Addl.DIT argued that the Secondment Agreement does not bring to the fore the complete picture of the arrangement among the three entities: the applicant, the parent company and the affiliate of the parent company. When all three are part of Verizon group, the expatriate employees in substance may well represent the parent company and the plea that the applicant is the economic employer of the employees may not hold good. The act of deduction of tax under section 192 of the Act would not confer the status of an employer upon the applicant. The employees of the deputing

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company do not become the employees of the company to which they are deputed as observed in the case of Morgan Stanley, reported in 292 ITR 416.

8. The Revenue submits that the applicant is providing exclusively all its services to its parent company Verizon USA. GTE-OC is not benefited in any way by this Secondment Agreement. While the applicant claims that these seconded employees are on the pay roll of the GTE-OC, the employees show themselves as part of Verizon in as much as that Mr. Rajiv Saxena is shown as Senior V.P. of Verizon in his profile. The website of Verizon also shows him as Group V.P.-Europe.

9. Referring to the Secondment Agreement the Revenue submits that the seconded employees are to perform certain managerial or other services and activities. They are not merely performing managerial services. The payment term is for salary, commission, benefits and other items as per the international assignment policy and not merely for salary. Though it does not appear in the application but the applicant is only responsible for housing, car and drivers of the expatriate employees. GTE-OC can replace the seconded employees. The employees shall remain the employees of GTE-OC who alone has the authority to terminate the employees with or without cause. But the cost of termination is to be borne by the applicant. In the event of dispute reference is to be made to HR of Verizon US for a final decision. If the Secondment Agreement is independent of Verizon US there was no reason to refer the dispute to Verizon US. The arrangement appears to be altruistic and not a commercial arrangement.

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10. The learned Addl.DIT further argued that this Authority in the case of AT&S India, 287 ITR 421, held the view that the payment towards reimbursement of salary cost of the seconded employees is in the nature of FTS and the fact that the taxes are paid under the head 'Salaries' is of no consequence. The seconded employees working under the direct control or supervision did not militate against the compensation paid to AT&S. In the case of Cholamandalam M.S.M. General Insurance, 309 ITR 356, it is held that withholding of tax is not applicable on reimbursement of salary to an overseas entity. The AAR distinguished the case from AT&S on the ground that there was a part reimbursement in Cholamandalam whereas in the present case it is a full reimbursement. The concept of part reimbursement also emanates from mutual benefits.

11. The Revenue then submits that it is not correct to say that the make available clause specified in the DTAA does not apply as the services are managerial. The concept of FIS has been explained in the MOU attached with the convention. The technical personnel have been deployed in India and the applicant's case is covered under example mentioned at sr. no. 3 in the MOU. It is not correct to say that persons occupying managerial position cease to be technical personnel or do not render technical service any more. In fact, they have been given leadership position only to render technical advice/guidance to the team. For these reasons the case of the applicant falls under FIS and is covered under Article 12(4) of the DTAA.

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12. The preamble of the Personnel Secondment Agreement states that to perform certain managerial services, the applicant has procured the services of US based personnel who are under the employment of GTE-OC. A team of three employees has been sent by GTE-OC. One of them has assumed the position of the Managing Director of the applicant company. It is a matter of common knowledge that the Managing Director of a company is incharge of the day to day affairs of the company. It is he who runs the company with the team of employees. The Board of Directors holds meetings off and on to take decisions on policy matters of the company. To say that the Managing Director of a company is under the control and supervision of the company is nothing more than use of an expression. The control and superintendence of the company vests with him. In the present case, the three employees together have constituted a team. While these employees are providing services to the applicant, they will remain the employees of GTE-OC. Their employment can only be terminated by GTE-OC. It goes to show that it's GTE-OC who has rendered managerial services to the applicant company. For the items paid or provided to the employees, the applicant is to reimburse GTE-OC on the basis of bills presented by GTE-OC. At the time of remittance, the obligation to withhold taxes is upon the applicant and if any amount is held as taxes the applicant is required to pay GTE-OC an additional amount. In other words, the applicant is required to pay the amount net of taxes. This again is an important aspect of the agreement. Firstly, it is GTE-OC's employees who are to

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perform managerial services in India and secondly, the applicant is liable to bear the taxes on the remittances. There is no argument that the remittances are in consideration for the services rendered. The reason for the applicant to bear the taxes on the impugned payments to GTE-OC lies in the fact that the services rendered by GTE-OC are liable to tax in India. But an issue has been raised that the remittances are in the nature of reimbursements and as the employees are paying taxes on their salary income there is no income which can be said to have accrued to GTE-OC. We are to analyze how far the applicant's contention is acceptable to us.

13. The Personnel Secondment Agreement specifically provides that the seconded employees shall remain the employees of GTE-OC. The payment of their salaries is not dependent on the applicant. These employees will continue to get their salaries from GTE-OC as long as they remain in their employment. It follows that the managerial services performed by them are as employees of GTE-OC and not as employees of the applicant. Without GTE-OC the seconded employees have no *locus standi* vis-à-vis the applicant. It is a trite law that the capacity in which the person receives the amount determines its taxability in his hands. In that view of the matter the sums that are remitted by the applicant accrue and arise to GTE-OC for providing services to the applicant. What accrues and arises to the employees is by virtue of their employment with GTE-OC. The application of the income by GTE-OC while making payment of salaries to its employees has nothing to do with its accrual. The nature of the two

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receipts, one in the hands of GTE-OC for rendering services and the other in the hands of employees by way of salaries spring from different sources and are of different character and represent different species of income. By correlating the two payments/receipts in the Personnel Secondment Agreement, neither the nature nor substance of the transaction would change to give it the character of reimbursement. The name given to the transaction does not decide the nature of the transaction. A receipt is what it is and what it is called. We have noted that the salaries are paid out of the income of GTE-OC. The total income of GTE-OC may be the sum total of receipts under different heads of income, for example: business, royalties, fees for included services, house property, interest, dividends etc. but the expenditure incurred by way of salaries to the employees cannot *ipso facto* determine the nature of the income which is to be brought to tax either under the Act or under the DTAA in the hands of GTE-OC. We are of the view that, amounts paid by the applicant to GTE-OC represent income in the hands of GTE-OC. The reliance placed on the cases cited by the Learned Advocate are not on the issue as per the facts of the applicant.

14. The Learned Advocate submits that as the definition under DTAA is more beneficial the same may be applied to the applicant's case. Referring to Article 12(4) of the DTAA, it is contended that managerial services being consultancy services are not made available to the applicant. No technical knowledge, experience, skill etc. is transmitted to enable the applicant to independently apply the same. The employees are

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engaged in rendering managerial services and not technical services. Other than deputing its employees, GTE-OC has not rendered any services to the applicant through its employees. The payment made do not qualify as "fees for including services" and is not liable to tax having regard to the provision of the DTAA.

15. We agree with the learned advocate that the managerial services rendered are not technical but we do not agree that the consultancy services being managerial services, the requirement under Article 12(4) of the DTAA that these must be made available, ought to be satisfied. We now examine the nature of services rendered by the employees on behalf of GTE-OC.

16. The employees whose services are utilized by the applicant are to perform certain managerial or other services and activities in India as stated in the Personnel Secondment Agreement. Their exact details are not mentioned in the Personnel Secondment Agreement. However, these find place in a summary manner in Annexure II to the application filed before the Authority. It is noted that one of the seconded employees is to perform the function as Managing Director of the applicant and other two are to supervise and provide directions in the manner through which the activities of the applicant are to be carried out and to liaise with the parent company in USA. *In Intertek Services*, this Authority observed that:

> "The adjective "managerial" relates to manager or management. Manager is a person who manages an industry or business or who deals with administration or

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a person who organizes other people's activity. As pointed out by the Supreme Court in R. Dalmia vs. CIT [1977] 106 ITR 895, "management" includes the act of managing by direction, or regulation or superintendence. Thus, managerial service essentially involves controlling, directing or administering the business."

It is fairly clear that the functions performed by these seconded employees are purely managerial in nature. The applicant's contention is that these managerial services are consultancy services and are covered under Article 12 (4) of the DTAA. The Article12 (4) reads as under:

" 4. For the purposes of this Article, "fees for included services" means payments of any kind to any person in consideration for the rendering of any technical or consultancy services (including through the provision of services of technical or other personnel) if such services:

(a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment, described in paragraph 3 is received; or

(b) make available technical knowledge, experience, skill, know-how, or processes, or consist of the development and transfer of a technical plan or technical design."

The applicant contends that as the managerial services are not made available to the applicant, the services rendered by the seconded employees are not covered under Art 12(4)(b) of the DTAA. In this connection we may refer to the memorandum of

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understanding of the DTAA which explains the meaning of "fees for included services" as under:

> "Article 12 includes only certain technical and consultancy services. By technical services we mean in this context services requiring expertise in a technology. By consultancy services, we mean in this context advisory services. The categories of technical and consultancy services are to some extent overlapping because a consultancy service could also be a technical service. However, the category of consultancy services also includes an advisory service, whether or not expertise in a technology is required to perform it.
>
> Under paragraph 4, technical and consultancy services are considered included services only to the following extent; (1) as described in paragraph 4(a), if they are ancillary and subsidiary to the application or enjoyment of a right, property or information for which a royalty payment is made; or (2) as described in paragraph 4(b), if they make available technical knowledge, experience, skill, know-how, or processes, or consist of the development and transfer of a technical plan or technical design. Thus, under paragraph 4(b), consultancy services which are not of a technical nature cannot be included services."

The phrase technical or consultancy services appearing in Article 12(4)(b) of the DTAA, is further explained in the MOU as under:

> "Paragraph 4(b) of Article 12 refers to technical or consultancy services that make available to the person acquiring the service technical knowledge, experience,

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skill, know-how, or processes, or consist of the development and transfer of a technical plan or technical design to such person. (For this purpose, the person acquiring the service shall be deemed to include an agent, nominee, or transferee of such person.) This category is narrower than the category described in paragraph 4(a) because it excludes any service that does not make technology available to the person acquiring the service. Generally speaking, technology will be considered "made available" when the person acquiring the service is enabled to apply the technology. The fact that the provision of the service may require technical input by the person providing the service does not per se mean that technical knowledge, skills, etc. are made available to the person purchasing the service, within the meaning of paragraph 4(b). Similarly, the use of a product which embodies technology shall not per se be considered to make the technology available."

17. From the memorandum of understanding of the DTAA it is clear that the services which are not in the nature of technical services, the make available clause would not apply. As the services provided by GTE-OC are in the nature of managerial services, the payments made by the applicant are covered under "fees for included services" under Art.12 (4) of the DTAA. As the services are managerial in nature, the payments are also covered under "fees for technical services" as defined under Explanation 2 to section 9(1)(vii) of the Act.

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18. In view of the foregoing discussion, the questions raised by the applicant are answered as follows:

Question no.1:

The amounts reimbursed by the applicant represent income accruing to GTE-OC and accordingly charged to tax within the provision of section 195 of the Act.

Question is answered in the affirmative.

Question no.2:

The amounts reimbursed by the applicant are taxable as "Fees for Included Services (FIS)" under the DTAA and also under the Act.

Question is answered in the affirmative.

Question no.3 &4:

As we have held that the amount reimbursed by the applicant is taxable as FIS, the answers to these questions are academic.

Question no.5:

"Fees for Included Services (FIS)" is taxable at the rate of 20% as provided under Article 12 (4)(b) of the DTAA.

Accordingly ruling is given and pronounced on **27th** Day of **May, 2011.**

Sd/-	Sd/-	Sd/-
(J. Khosla)	**(P.K.Balasubramanyan)**	**(V.K.Shridhar)**
Member	**Chairman**	**Member**

F.No. A.A.R. No. 865 of 2010 Dated ….

(A) This copy is certified to be a true copy of the advance ruling and is sent to:

1. The applicant.
2. The Commissioner of Income-tax-III, Chennai..

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3. The Joint Secretary (FT&TR-I), M/Finance, CBDT,Bhikaji Cama Place, New Delhi.
4. The Joint Secretary (FT&TR-II), M/Finance, CBDT,Bhikaji Cama Place, New Delhi
5. Guard file.

(B) In view of the provisions contained in Section 245S of the Act, this ruling should not be given for publication without obtaining prior permission of the Authority.

(Nidhi Srivastava)
Addl. Commissioner of Income-tax(AAR-IT)