[2023] 151 taxmann.com 148 (Mumbai - Trib.)[13-01-2023]

INTERNATIONAL TAXATION : Where assessee-company had entered into transaction of secondment of its employees with two of its AE's, since transaction between assessee and its Indian AE's was simply in nature of reimbursement of salary cost on actual basis without any markup and, thus, it was not falling in category of FTS/FIS, this payment did not qualify fees for technical or included services within meaning of article 12(4) of India-US tax treaty

INTERNATIONAL TAXATION : Where transaction related to secondment of employees is not falling either in section 9(1)(vii) or article 12(4) of India-US DTAA, same cannot be referred to TPO for benchmarking

[2023] 151 taxmann.com 148 (Mumbai - Trib.)

IN THE ITAT MUMBAI BENCH 'I'

Morgan Stanley International Incorporated

v.

Deputy Director of Income-tax (International Taxation)*

VIKAS AWASTHY, JUDICIAL MEMBER
AND GAGAN GOYAL, ACCOUNTANT MEMBER
IT APPEAL NO. 5985 (MUM.) OF 2012
[ASSESSMENT YEAR 2007-08]
JANUARY 13, 2023

I. Section 9 of the Income-tax Act, 1961, read with article 12 of DTAA between India and USA - Income - Deemed to accrue or arise in India (Royalties/Fee for technical services - Secondment of employees) - Assessment year 2007-08 - Assessee, US company, provided support services to its subsidiaries worldwide including India - Assessee received certain amount on account of secondment of its employees to its subsidiaries - Assessing Officer treated reimbursement of salary cost received by assessee as fees for technical services under provisions of section 9(1)(vii) or fees for included services under article 12 - Whether transaction between assessee and its Indian AE's was simply in nature of reimbursement of salary cost on actual basis without any markup and, thus, it was not falling in category of

FTS/FIS, as this payment did not qualify as fees for technical or included services within meaning of article 12(4) - Held, yes - Whether further this type of transaction was excluded from section 9(1)(vii) by virtue of Explanation 2 because in such transaction salary paid to seconded employees was already taxable as per section 5 and, hence, same could not be taxed again in hands of assessee - Held, yes [Para 6] [In favour of assessee]

II. Section 9, read with section 92C, of the Income-tax Act, 1961 - Income - Deemed to accrue or arise in India (Royalities or fees for technical Services - Secondment of employees) - Assessment year 2007-08 - Assessee, US company provided support services to its subsidiaries worldwide including India - Assessee received amount on account of secondment of its employees from its subsidiaries and received as reimbursement of salary - Assessing Officer treated reimbursement of salary cost received by assessee as fees for technical services under provisions of section 9(1)(vii) and made an addition to total income of assessee while determining arm's length price of international transaction with its Indian associated enterprises - Similar transaction for assessment year 2005-06 referred by Assessing Officer to TPO under section 92CA(1) was accepted in favour of assessee on ground that transaction needed no benchmarking as same was not attracting section 9(1)(vii), Explanation 2 and article 12(4)(b) of India-US tax treaty - Whether on facts, transaction did not fall either in section 9 or article 12(4), and same could not be referred to TPO for benchmarking - Held, yes [Para 7] [In favour of assessee]

CASES REFERRED TO

Morgan Stanley International Incorporated v. *Dy. DIT (International Taxation)* [2015] 53 taxmann.com 457/153 ITD 403 (Mum. - Trib.) (para 8).

Sunil Moti Lala *for the Appellant.* **Soumendu Kumar Dash**, Sr. Dr *for the Respondent.*

ORDER

Gagan Goyal, Accountant Member. - This appeal by assessee is directed against the order of Commissioner of Income Tax(Appeals)-15, Mumbai (for short 'CIT(A)') dated 5-7-2012 under section 143(3) r.w.s. 144C(3) of the Income-tax Act, 1961 (for short 'the Act') for A.Y. 2007-08. The assessee has raised the following grounds of appeal:

> "The following grounds of appeal are independent of, and without prejudice to one another:
>
> 1. On the facts and in the circumstances of the case, the learned Commissioner of Income-tax (Appeals) ["the CIT (A)"] has legally erred in confirming the action of the learned Assessing Officer ("the AO") of holding that the Appellant has rendered services to the Indian Companies *viz.* Morgan Stanley Advantage Services Private Limited and MSIM Global Support and Technology Services Private Limited.

2. On the facts and in the circumstances of the case, the learned CIT (A) has legally erred in confirming the action of the learned AO of treating the reimbursement of salary cost received by the Appellant as Fees for Technical Services under the provisions of Section 9(1)(*vii*) of the Income-tax Act, 1961 ("the Act').

3. On the facts and in the circumstances of the case, the learned CIT (A) has legally erred in confirming the action of the learned AO of treating the reimbursement of salary cost received by the Appellant as Fees for Included Services under Article 12 of the Double Tax Avoidance Agreement between India and USA.

4. On the facts and in the circumstances of the case, the learned CIT (A) has erred in confirming the action of the learned AO Transfer Pricing Officer (TPO) in making an addition of Rs. 40,089,133 to the total income of the Appellant while determining arm's length price of international transaction with its Indian Associated Enterprises (AES) relating to Reimbursement of Personnel costs.

5. On the facts and in the circumstances of the case, the learned CIT (A) has erred in confirming the action of the learned AO/TPO in holding that the Appellant had provided 'manpower services" to its Indian AEs as a result of deputing certain employees to the AEs and that it should have recovered a mark-up on the cost of deputed employees.

6. On the facts and in the circumstances of the case, the learned CIT (A) has erred in confirming the action of the learned AO/TPO of using the alleged comparable data relating to Mitsui O.S.K. Lines Maritime (India) Private Limited ('Mitsui India"), which was not available in the public domain.

7. On the facts and in the circumstances of the case, the learned CIT (A) has erred in not appreciating the fact that the learned AO/TPO has erred in providing incomplete/inadequate details relating to Mitsui India, whose net operating margin was used by the TPO as a benchmark details relating to Mitsui India, whose net to determine the arm's length nature of the international transaction relating to reimbursement of personnel costs.

8. On the facts and in the circumstances of the case, the learned CTT (A) has erred in confirming the action of the learned AO/FPO of selection of Mitsui India as a comparable unrelated enterprise to benchmark Appellant's international transaction relating to Reimbursement of Personnel costs, without appreciating the fact that Mitsui India is engaged in business activity entirely different from the business activity undertaken by the Appellant.

9. On the facts and in the circumstances of the case, the learned CIT (A) has erred in rejecting the alternative benchmarking analysis submitted by the Appellant during the course of the appellate proceedings on a without prejudice basis to the Appellant's main contention that no mark up should be added to the costs recovered by it from its AE.

10. On the facts and in the circumstances of the case, the learned CTT (A) has erred in contending that the comparables identified for the alternative benchmarking analysis should have been searched from India and not from the United States of America.

11. On the facts and in the circumstances of the case, the learned CIT (A) has further erred in contending that the comparables identified for the alternative benchmarking should be those which are engaged in the business of staffing where such services are being rendered in India.

12. On the facts and in the circumstances of the case, the learned CTT (A) has erred in confirming the action of the learned AO in not appreciating the fact that the activities performed by the Appellant are not chargeable to tax in India and hence Transfer pricing provisions do not apply.

13. On the facts and in the circumstances of the case, the learned CIT (A) has erred in confirming the action of the learned AO in not appreciating the fact that enhancement of the Appellant's income would result in corresponding increase of Indian AEs' expenses which is against the principles set out in section 92(3) of the Act.

14. On the facts and in the circumstances of the case, the learned CIT (A) has legally erred in confirming the action of the learned AO of levying interest of Rs. 30,30,753/- under section 234B of the Act."

2. Brief facts of the case are that assessee is a company incorporated in USA. Assessee is a 100% subsidiary of M/s Morgan Stanley USA and its primary activity is to provide support services to its subsidiaries worldwide including India. In the instant year the assessee has entered into an agreement with M/s Morgan Stanley India Company Pvt Ltd to provide support services the consideration received from this company amounting to Rs. 4,26,38,878/- was offered for tax as FTS. The assessee further received further amount on account of secondment of its employees to M/s Morgan Stanley advantage services Pvt Ltd. (MSASPL) and MSIM global support and technology services Pvt ltd (MGSTSPL) both of which are its subsidiaries. During the year under consideration assessee received Rs. 14, 74, 77,255/- as reimbursement of salary from M/s MSASPL and Rs. 2, 50, 97,573/-from MGSTSPL as reimbursement of salary.

3. Return declaring total income of Rs. 4, 28, 74,257/- was e-filed on 11-10-2007. The case was selected for scrutiny and assessed at Rs. 25, 53, 02,839/-. The income assessed includes the amount of salaries reimbursement received from its two subsidiaries mentioned above and adjustment done u/s 92CA (3) amounting to Rs. 17, 25, 74,828/- and Rs. 4, 00, 89,133/- respectively. Against this order of AO passed u/s 143(3) r.w.s. 144C (3) of the act, assessee preferred an appeal before the Ld. CIT (A)-15, Mumbai. In response to the assessee's appeal Ld. CIT (A) was not agreed with the contentions of the assessee and sustained the order of AO.

4. Against this order of Ld. CIT(A) passed u/s 250 *vide* dated 5-07-2012 assessee preferred this present appeal before ITAT and raised total 14 grounds. Out of this ground no. 1 is general in nature, assessee effectively pressed ground no. 2, 3, 12 and 14 for our consideration. Our adjudication is limited to the ground nos. 2, 3, 12 and 14 only at this stage.

5. We have gone through the order of AO, Order of Ld. CIT (A) and submissions of the assessee along with paper-book relied upon. We observed that the year under consideration, company has entered into the transaction of secondment of its employees with two of its AE's namely MSICPL and MGSTSPL. We found that there is no agreement between the assessee and its AE's w.r.t. secondment of its employees to AE's. Although, the terms of secondment in the form of deputation letter were furnished before the AO and Ld. CIT (A). The terms of deputation are summarised as under:

(*i*) The expatriate employees would be working under the supervision and control of the Indian AE's

(*ii*) Day to day responsibilities of these employees would be managed by the Indian AE's and they would be accountable only to the Indian AE's and shall abide by the Indian companies employee's policies, guidelines and other directions.

(*iii*) The appellant was responsible for the general review of role, discipline, and promotion etc of the expatriate employees. And

(*iv*) The appellant was required to pay salaries to the expatriates on behalf of the Indian companies and in turn will receive reimbursement of salaries post from the Indian companies on actual basis without any mark-up.

6. The above observation is not under challenge by the revenue or assessee. Based on these facts AO referred the matter to the TPO considering the same as FTS for benchmarking of the transaction. We have considered sec 9(1) (*vii*) of the acts along with article 12(4)(*b*) of India-US DTAA. As discussed *supra* the transaction between the assessee and its Indian AE's are simply in the nature of reimbursement of salary cost on actual basis without any mark-up, is not following in the category of FTS/FIS. As, this payment does not qualify as fees for technical or included services within the meaning of article-12(4) of the India-US tax treaty.

7. As observed above that transaction is not following either in Sec. 9 or India -US DTAA article 12(4), the same can't be referred to TPO for benchmarking. It is further noted that assessee doesn't have any PE in India, though few service PE and AE's are registered in India. Company seconded few if its employees to Indian AE's and received reimbursement of expenses on actual basis from the Indian AE's. It is pertinent to mention here that similar transaction for AY 2005-06 referred by AO to the TPO u/s 92CA (1) was accepted in favour of assessee on the ground that the transaction need not bench marking as the same is not attracting sec 9(1)(*vii*) explanation 2 and article 12(4)(*b*) of the India-US tax treaty. We don't see any change in the facts and law of the year under consideration Vis-a vis A.Y. 2005-06. Moreover, the same transaction has been accepted by the revenue for the AY 2004-05, 2005-06 and 2006-07. Based on past history of the matter we don't see any reason for the department to take a different view in this year that is to without bringing anything on record which supports the action of the AO in not following the principle of consistency applicable both to the assessee and revenue.

8. We further refer assessee own case decided by ITAT Mumbai *vide Morgan Stanley International Incorporated* v. *Dy. DIT (International Taxation)* [2015] 53 taxmann.com 457/153

ITD 403 (Mum. - Trib.) adjudicated the similar issue in favour of assessee and held as under :

"9. We have considered the entire gamut of rival submissions and perused the relevant record, placed before us, including the relevant finding of the AO as well as of the ld. CIT (A). The assessee is a tax resident of USA and is providing support services to various Indian companies, who are subsidiaries. The assessee has deputed five of its employees in terms of deputation letter which have been placed on record. These employees were seconded to India to render their services to the Indian companies under supervision and control of the Board of Directors of the Indian companies and their day to day responsibility and activities were managed by the Indian company. However, their salary were paid by the assessee company after deducting TDS u/s 192 of the Act and duly deposited in the Indian Government Treasury. The entire salary paid by the assessee has been reimbursed by the Indian company to the assessee, which is evident from the debit notes appearing in the page 6 of the paper book. The TDS certificates have also been filed giving the details of tax deducted at source. One of the objection of AO as well as ld. CIT(A) was that, in the case of two employees, there has been some discrepancy in the amount shown in the TDS certificate and the amount shown in their income tax return filed in India. From the TDS certificate and the details of amount payable as clarified by the ld. Counsel, we find that, there is no discrepancy so far as the amount of cost which have been reimbursed by the Indian company to the assessee. However, ultimately the amount which has been received by the assessee towards reimbursement of Salary cost has been taxed as FIS which is a subject of dispute. The main issue before us is, whether such a payment received by the assessee on account of reimbursement of cost of salary paid to the Seconded employee, constitutes fees for included services (FIS) within the meaning of Article 12(4) of India-US DTAA, that is, it is taxable in India and hence TDS u/s 195 of the Act was required to be deducted.

10. In the current global scenario the international business entities have extended their business worldwide and they have made their presence by establishing their own subsidiaries or group entities from which they have business arrangement. These overseas entities depute their technical staff and human resources in the other countries, which are growing economies to support their global business functions and to ensure quality and consistency in their operations. Under a classic Secondment agreement, the seconded employees who are under employment of non-resident parent company are deputed or transferred to subsidiary company in the overseas countries to work for special assignment which are more technical and managerial in nature. These seconded employees usually work under direct control and supervision of the subsidiary entities in their country. Since these seconded employees belong to the main parent entity, therefore, they continue to receive their remuneration and salaries with all social security and benefits from the parent entity. The salary cost and remuneration are reimbursed by the subsidiary company to the parent entity. Strictly speaking on paper they remain the employees of the parent entities but they are under direct supervision and control of subsidiary entity, where their day to day activities are managed and governed by them and so much so they can be removed by them. Once the term of secondment is over, they revert back to their parent company entity. In a way subsidiary entity is the economic employer of the seconded employee who ultimately bears the salary cost and exercise control

over their work. Generally it is contended that reimbursement of cost cannot be treated as payment for FTS or FIS, unless there is an explicit agreement between the parties that technical services would be provided through these employees. The deputation of employees is mainly for the benefit of the subsidiary company to smoothly and efficiently conduct the business. However, such a reimbursement of salary cost by the subsidiary entity has been matter of huge controversy, as to what is the nature of such payment, whether it is 'fee for included services' or not. Other related controversy is that, on the basis of duration of the stay of seconded/deputed employees in the host countries, whether the non-resident parent entity constitute the service PE in the host country or not.

11. In the present context the salary paid to the seconded employees by the parent company, the TDS has been already been deducted u/s 192 of the Act, which has been credited to the Government of India account. In case, if it is to be held that reimbursement of salary is nothing but payment for rendering technical services, then TDS has to be deduced u/s 195 of the Act. The Hon'ble Bombay High Court, earlier in the case of Siemens Aktiongesellschaft (*supra*) has held that reimbursement of expenses cannot be regarded as revenue receipt following the decision of the Hon'ble Delhi High Court in the case of *CIT* v. *Industrial Engineering Projects* (1993) 202 ITR 1014 (Delhi) and therefore no TDS is required to be deduced u/s 195. However, this decision is not relied upon as this issue was decided on a different context. We have to examine our case and the issue in hand in the light of Delhi High Court decision.

12. The Hon'ble Delhi High Court in the case of *Centrica India Offshore (P.) Ltd.*(*supra*) had the occasion to deal with the similar issue of taxability of reimbursement of salary cost of the seconded employees, in a Writ Petition against the AAR ruling, wherein their Lordships have analyzed this issue in detail and held that such reimbursement of costs or re-payment, is 'fees for technical services'. Now, we have to analyze, whether this decision would be applicable for the purpose of adjudication of the issue in hand in the present case. The brief facts of the case of Centrica India was that, Centrica India was an Indian company, a wholly owned subsidiary of Centrica Plc, incorporated in the United Kingdom ("UK") which is UK based company. These overseas entities were in the business of supplying gas and electricity to consumers across the U.K and Canada. They outsourced their back office support functions like debt collections, consumers' billings, monthly jobs to third party vendors in India etc. . The Centrica India's principle object was to provide local interface between UK and the Indian vendors so as to ensure that Indian vendors comply with the quality guidelines. For this purpose, the Centrica India had entered into a service agreement with the overseas entities for providing management and quality assurance service for which it was compensated at cost plus 15% mark-up. The Centrica India had also entered into a seconded agreement with overseas entities for secondment of certain employees to India for rendering service and technical services for running its operation at initial stages. Such seconded employees continued to remain on pay roll of the overseas entities and received salary from them. Centrica India reimbursed such salary cost to the overseas employees on cost to cost basis. The AAR held that, since seconded employees continued to be employees of the overseas entity and the seconded employees are rendering their services for their employer in

India by working for specified period, this will give rise to service PE within the meaning of Article 5.2 (*k*) of Indian-UK DTAA and therefore such a payment would be income accruing to the overseas entity and would be taxable in India and TDS has to be deducted u/s 195 of the Act. In the Writ Petition before the Hon'ble Delhi High Court, the major issues for adjudication before their Lordships was, firstly, whether by way of Secondment of employees the overseas entity had rendered any technical services in terms of Article 12 of India - Canada DTAA and Article 13 of India -UK DTAA and secondly, whether the overseas entities establish any Service PE in India. Under these treaties the concept of Service PE has been embodied. The Hon'ble Court after analyzing the definition of 'technical services' and ' FIS' as appearing in the India-UK treaty and India-Canada treaty, concluded that overseas entities are providing technical services to Centrica India through the seconded employees under India-UK treaty and FIS under India-Canada treaty. Regarding the issue, whether overseas entity through their seconded employees have constituted Service PE in India, the Hon'ble High Court has referred and relied upon the decision of the Hon'ble Supreme Court in the case of Morgan Stanley & Co. (2007) 292 ITR 416 (SC) and also examined the terms and condition of the employment of seconded employees, whether they are employees of overseas entity or of Centrica India. The Hon'ble High Court came to the conclusion that the overseas entities were not only legal employer but also real employer of the seconded employees to India. After referring to the relevant potion of the decision of the Hon'ble Supreme Court, the Hon'ble Court held that the seconded employees will constitute a Service PE of the overseas entity in India. It was further observed that, even if there is no mark-up on the cost of seconded employees, it does not change the nature of service and will not affect the taxability in India. Thus, finally the Hon'ble High Court concluded that seconded employees rendering the service on behalf of the overseas employer and accordingly they have established Service PE in India and also they are rendering technical services, which is to be taxed in India.

13. If we have to apply the ratio laid down by the Hon'ble Delhi High Court in the present case, then it has to be seen, whether overseas entity *i.e.* the assessee is the real economic employer of the seconded employees *i.e.* the employees are maintaining their lien on employment with the original overseas and whether the assessee remains responsible for the work of seconded employees in India or not. The case of the assessee before us has been that, seconded employees were under direct control and supervision of Indian entity who were managing their activities on day to day basis and the assessee was only paying their salary for the employees convenience and benefit. Whether this fact will lead to any deviation from the ratio laid down by the Hon'ble Delhi High Court, we are not entering into semantics of overall terms of employment of the seconded employees, whether the assessee is the real or legal employer or the Indian entity is the employer. We are proceeding on the premise that the seconded employees are the real employees of the assessee who have come to India to render services and once they are rendering services on behalf of assessee in India then, they constitute Service PE in India. Such an establishment of PE under these circumstances have been dealt by the Hon'ble Supreme Court in the case of *Morgan Stanley & Co* (*supra*). The Hon'ble Supreme Court held that the employee of overseas entities to the Indian entity constitutes service PE in India. The relevant finding of the Hon'ble Supreme Court in this

regard is as under:

"15. As regards the question of deputation, we are of the view that an employee of MSCo when deputed to MSAS does not become an employee of MSAS. A deputationist has a lien on his employment with MSCo. As long as the lien remains with the MSCo the said company retains control over the deputationist's terms and employment. The concept of a service PE finds place in the U.N. Convention. It is constituted if the multinational enterprise renders services through its employees in India provided the services are rendered for a specified period. In this case, it extends to two years on the request of MSAS. It is important to note that where the activities of the multinational enterprise entails it being responsible for the work of deputationists and the employees continue to be on the payroll of "the multinational enterprise or they continue to have their lien on their jobs with the multinational enterprise, a service PE can emerge. Applying the above tests to the facts of this case we find that on request/requisition from MSAS the applicant deputes its staff. The request comes from MSAS depending upon its requirement. Generally, occasions do arise when MSAS needs the expertise of the staff of MSCo. In such circumstances, generally, MSAS makes a request to MSCo. A deputationist under such circumstances is expected to be experienced in banking and finance. On completion of his tenure he is repatriated to his parent job. He retains his lien when he comes to India. He lends his experience to MSAS in India as an employee of MSCo as he retains his lien and in that sense there is a service PE (MSAS) under Article 5(2}(1). We find no infirmity in the ruling of the ARR on this aspect. In the above situation, MSCo is rendering services through its employees to MSAS. Therefore, the Department is right in its contention that under the above situation there exists a Service PE in India (MSAS). Accordingly, the civil appeal filed by the Department stands partly allowed." Thus, from the aforesaid decision it is amply clear that such deputed employees if continued to be on pay rolls of overseas entities or they continue to have their lien with jobs with overseas entities and are rendering their services in India, Service PE will emerge. This concept and the ratio has been strongly upheld by the Hon'ble Delhi High Court also. We therefore, hold that the seconded employees or deputationist working in India for the Indian entity will constitute a Service PE in India. 14. If we accept this concept that, by virtue of deputing seconded employees in India, the assessee has established a Service PE, then whether such a payment made by Indian entity to the assessee, (even though it is reimbursement of salary cost), would be taxable under Article 12(4) of India - US DTAA. Relevant Article 12 of the treaty reads as under:

Article 12 ROYALTIES AND FEES FOR INCLUDED SERVICES 1. Royalties and fees for included services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such royalties and fees for included services may also be taxed in the Contracting State in which they arise and according to the laws of that State; but if the beneficial owner of the royalties or fees for included services is a resident of the other Contracting State, the tax so charged shall not exceed: XXXX *a*. XXXXX *i.* XXXXX A. XXXXX B. XXXX *ii.* XXXX *b.* XXXXX

3. xxxxxxxxx *b.* XXXXX. 4. For 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. a. XXXXX *b.* XXXXXX *c.* XXXXX *d.* XXXXXX *e.* XXXX

6. The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the royalties or fees for included services, being a resident of a Contracting State, carries on business in the other Contracting State, in which the royalties or fees for included services arise, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the royalties or fees for included services are attributable to such permanent establishment or fixed base. In such case the provisions of article 7 (business profits) or article 15 (Independent Personal Services), as the case may be, shall apply.

7. *a.* Royalties and fees for included services shall be deemed to arise in a Contracting State when the payer is that State itself, a political sub-division, a local authority, or a resident of that State. Where, however, the person paying the royalties or fees for included services, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment or a fixed base in connection with which the liability to pay the royalties or fees for included services was incurred, and such royalties or fees for included services are borne by such permanent establishment or fixed base, then such royalties or fees for included services shall be deemed to arise in the Contracting State in which the permanent establishment or fixed base is situated. b. Where under sub-paragraph (*a*) royalties or fees for included services do not arise in one of the Contracting States, and the royalties relate to the use of, or the right to use, the right or property, or the fees for included services relate to services performed, in one of the Contracting States, the royalties or fees for included services shall be deemed to arise in that Contracting State.

8. XXXXXXX" Para 6 of Article 12 makes it amply clear that taxability of 'royalty' and 'fees for included services' shall not apply, if the resident of the contracting state (USA) carries on the business in other contracting states (India) in which FIS arises through PE situated therein, then in such case the provisions of Article 7 i.e "Business Profits" shall apply. In other words, if there is a PE, then Royalty or FIS cannot be taxed under Article 12, albeit only under Article 7 of the DTAA. It is an undisputed fact in this case, that DTAA benefit has been availed by the assessee and therefore, treaty benefit has to be given to the assessee for granting relief. Now, if the taxability of such payment has to be examined and determined on the basis of computation of business profit under Article 7, then the salary paid by the assessee would amount to cost to the assessee, which is to be allowed as deduction while

computing the business profit of the PE in India. In our opinion, if logical conclusion of the decision of the Hon'ble Supreme Court in the case of *Morgan Stanley & Co* (*supra*) and the decision of Hon'ble Delhi High Court in the case of *Centrica India Offshore (P.) Ltd.* (*supra*) is to be arrived at, then the seconded employees will constitute Service PE of the assessee in India and in that case any payment received on account of rendering of service of such employees will have to be governed under Article 7 as per unequivocal terms of para 6 of Article 12. Thus, the ratio laid down in the decision of Hon'ble Delhi High Court, will not help the case of the revenue, in any manner because under the concept of PE, FIS cannot be taxed under Article 12, but only as a business profit under Article 7. It is very interesting to note that, similar provision is also embodied in the India-Canada DTAA in para 6 of Article 12, but this issue was neither raised or brought to the notice before the Hon'ble Delhi High Court nor it was contested by either parties. There is inherent contradiction in this concept, as in most of the treaties, exclusionary clause like Article 12(6) has been embodied, which makes the issue of taxability of FTS of FIS in such cases as non applicable and have to be viewed from the angle of Article 7. Thus, the decision of the Hon'ble Delhi High Court and all other decisions relied upon by the revenue will not apply in the case of the assessee, as nowhere the concept of para 6 of Article 12 have been taken into account for determining the taxability of such a payment under the provisions of treaty. Thus, in our conclusion, the payment made by the Indian entity to the assessee on account of reimbursement of salary cost of the seconded employees will have to be seen and examined under Article 7 only, that is, while computing the profits under Article 7, payment received by the assessee is to be treated as revenue receipt and any cost incurred has to be allowed as deduction because salary is a cost to the assessee which is to be allowed. Accordingly, the AO is directed to compute the payment strictly under terms of Article 7 and not under Article 12 of the DTAA. In view of the aforesaid finding, the grounds raised by the assessee are treated as allowed."

9. We further observed that taxes on the salary of the seconded employees are already been paid to Indian exchequer and notwithstanding the contention of the revenue it will tantamount to double tax if the same is again made taxable in the hands of the assessee. Here the relevance of explanation -2 to sec 9(1) (*vii*) comes into picture.

10. Now one can understand that categorically this types of transaction are excluded from Sec. 9(1)(*vii*) by virtue of explanation -2 because in such transaction the salary paid to the seconded employees are already taxable as per Sec. 5 hence, same cannot be taxed again in the hands of assessee. In these terms ground no. 2, 3 and 12 are allowed in favour of assessee and the transaction is held not to be in the nature FTS/FIS. AO is directed to delete the additions made on this account. Ground no. 14 is consequential in nature hence no separate adjudication is required.

11. In the result, appeal filed by the assessee is allowed.

POOJA

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*In favour of assessee.