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Navigating Taxation in Inbound Overseas Secondments through the Labyrinth of Confusion

Inbound secondments to India involve employees of a foreign company (F Co.) working temporarily for an Indian entity (I Co.), typically while remaining on F Co.'s payroll. Tax issues arise around tax on salary, withholding tax obligations, and Permanent Establishment (PE) risk. Courts assess the "real employer" through operational

control, payroll, vested commercial interest of F Co. in operations of I Co., and business conduct, not just formal agreements. Landmark rulings such as Morgan Stanley, Centrica, Northern Operating, Formula One, and Hyatt have progressively refined Service and Fixed Place PE doctrines. Employee short-stay exemptions under Tax Treaties may apply, subject to the foreign employer being considered as the real employer. Strategic planning requires careful scrutiny of functions, assets, risks of I Co. qua F Co., and control thereon by the latter. Further, evolving jurisprudence demands that the facts and arguments are presented holistically and with structure before appellate forums to avoid adverse consequences.

Introduction

Inbound secondments to India usually refer to cases where employees of a foreign entity (parent, group company, or overseas client – hereinafter called F Co.) are temporarily deputed/seconded to work for an Indian entity (hereinafter called I Co.). Generally, F Co. sends skilled employees to I Co. to provide expertise, train local staff, or manage key projects. For global contracts, part of the work may need to be executed in India under the supervision of foreign personnel. The business rationale of secondment lies in I Co. getting direct access to experienced resources while allowing F Co. to maintain oversight and even call the shots. Generally, secondment is not a permanent transfer; the employee remains on the foreign payroll legally or reserves a lien on social security benefits, etc. with the home employer and works for the Indian

company for a limited duration. The employee also receives salary from F Co. into his foreign bank account for administrative convenience. Even if the employee receives salary from I Co. directly in his Indian or overseas bank account, F Co. may continue paying social security benefits to overseas accounts of the employees to ensure continuity after termination of the Indian secondment term/agreement. Generally, the cost in respect of the seconded employee is cross-charged by F Co. to I Co. on a cost-to-cost basis.

A typical secondment arrangement would have three-fold documentation governing the roles, terms and responsibilities between:

- F Co. and I Co. – inter-firm service agreement/secondment agreement
- F Co. and employee – assignment agreement

- I Co. and employee – local employment letter

The following tax controversies may potentially arise in India from this cross-border setup:

1. Taxability of service fees or reimbursement in the hands of F Co.
2. Withholding tax implications on reimbursement
3. Permanent establishment (PE) implications for F Co. through factors like prolonged stay of employee in India, or excessive control over Indian operations, thereby putting the Indian office at their virtual disposal
4. Short-stay exemption in the hands of the employee under the relevant Tax Treaty, if any, and incidental withholding tax implications in India on employee's salary in the hands of I Co.

Issues 1 to 3

These issues rest on one fundamental question i.e., *who the real employer is?*

If the question can be demonstrated in favour of I Co., then it is easy to justify that salary reimbursement to F Co. on a cost-to-cost basis is only for administrative convenience and that once it has carried out TDS on salary under Section 192 of the Income-tax Act 1961 (“the Act”), there is no need for I Co. to examine TDS implications again under Section 195 of the Act on reimbursement of such salary cost to F Co. It is also easy to conclude that if I Co. is the real employer and exercises substantive control on the seconded employee, the latter should not be seen as extended presence of F Co. in India to create a PE in India.

However, if the facts tilt in favour of F Co. as being the “real employer”, authorities may contend that F Co. is receiving service/manpower supply fees in lieu of lending their employees to India which should be taxed in India as fees for technical services (subject to Tax Treaty benefit, if any) in the absence of a PE or business income in the case of constitution of PE in India. F Co., being seen as the real employer of the seconded employee, may symbolise the former having control over the Indian operation or disposal of I Co. premises, thereby posing PE risk to it.

The assessment of parameters defining a master–servant or employer–employee relationship, including directions on ‘what to do’ versus ‘how to do it too,’ and the distinction between a ‘contract of service’ and a ‘contract for service,’ has become more critical than ever in determining the real employer and the degree of control exercised over the employee during and after secondment.

As this forms the focal point of dispute, it has generated a plethora of litigation over time—each case adding

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fresh perspectives and yielding varied conclusions on fact patterns that are similar yet not identical. The result is a labyrinth of complexity, with several principles already settled by the Apex Court. Yet new dimensions remain unexplored, with tax authorities and appellate forums adopting an evolving ambulatory approach, and judicial scrutiny often lifting the veil on contrived arrangements.

In the Morgan Stanley¹ case, the Apex Court got an occasion to deliberate on the following aspects, where it coined the following principles of law:

■ PE in India:

It was held that Morgan Stanley Advantage Services (MSAS), an Indian affiliate, constituted a Service PE of Morgan Stanley US under Article 5(2)(1) of the India–US DTAA.

■ Attribution of Profits:

Once the Indian entity (MSAS) was remunerated at arm’s length

price (ALP) for the services rendered, no further profits could be attributed to the foreign company in respect of the PE.

Thus, transfer pricing and PE profit attribution principles were harmonized.

■ Stewardship vs. Deputation:

A line was drawn between stewardship function and deputation.

Employees sent on “stewardship” functions (oversight, ensuring quality, protecting investor interests) do not create a PE; however, employees seconded and working under the control of I Co. could contribute to PE characterization.

Later, another landmark Delhi High Court judgement in the case of Centrica², dealt with Permanent Establishment (PE) issues in the context of secondment of employees.

Centrica UK and other group entities seconded some employees to its Indian subsidiary, Centrica India Offshore Pvt. Ltd. (CIOP),



¹ Director of Income Tax (International Taxation) v. Morgan Stanley & Co. Inc. (2007) 292 ITR 416 (SC)

² Centrica India Offshore (P.) Ltd. v. CIT (2014) 364 ITR 336 (Del) - SLP dismissed later by the Supreme Court

for managerial and technical functions. It was held that if secondees remain employees of F Co. (contractually, payroll, repatriation rights) and render services in India “on behalf of F Co.”, F Co. may be considered to have a Service PE in India, even if I Co. reimburses costs.

In the Northern Operating Systems³ ruling, the Supreme Court observed that the secondment arrangement was essentially the foreign entity “lending” its employees to the Indian company. Reimbursements of salary cost were consideration for a *taxable supply of manpower services* under indirect tax law. This has triggered a spur of discussion of re-evaluating the fundamentals of the secondment arrangement in the corridors of the income tax office too.

In the Hyatt case⁴, the Supreme Court got the occasion to decide whether Hyatt International had a Fixed Place Permanent Establishment (PE) in India under Article 5(1) of the India-UAE DTAA, through its Strategic Oversight Services Agreement (SOSA) with Indian hotel companies, thereby making its income taxable in India.



The Supreme Court examined the case through a Fixed Place PE lens and affirmed the same, owing to many factors, some of which are:

- Continuous and substantive operational control exercised by Hyatt over hotel operations.
- Exclusive possession of premises is not essential, and stability, productivity and dependence tests form the principle of Disposal and Fixed Place PE test; following its coordinate bench ruling in the case of Formula One⁵.
- Frequent visits coupled with intermittent return by Hyatt's executives collectively established a continuous business presence.
- Revenue-linked service fee arrangement seen as vested interest of F Co. in *controlling* the operations of I Co.
- India PE, assessed as a separate taxable entity and merits profit attribution exercise, regardless of global losses of F Co.

Thus, from 2007 (Morgan Stanley) → 2014 (Centrica) → 2022 (Northern Operating) → 2025 (Hyatt), the controversy regarding taxation of employees sent on secondment has come a long way, showing how Indian courts have progressively refined the PE doctrine and applied strictness on secondments and foreign control in India, moving from examination of Service PE to even Fixed Place PE. Courts are consistently looking at real control, payroll, repatriation rights, and commercial nexus, not just contracts.

Issue 4

Taxability of salary in India (also linked with withholding tax thereon) is founded on the basic principle of where services are rendered or performed, regardless of where it is paid. While a resident as well as non-resident employee is hence taxable in

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respect of salary accrued during the exercise of employment in India, some benefit may be explored under Tax Treaties in respect of a non-resident employee.

Most Tax Treaties with India provide an 183-day or 90-day exemption rule under Article 15/16 dealing with Taxability of Dependent Personal Services. The same, popularly called ‘Short stay exemption,’ signifies that salary will not be taxed in India for an employee who is not a resident in India if all 3 conditions are met (taking the example of a typical tax treaty):

- Stay in India ≤ 183 days in the relevant fiscal year or 12-month period, as the case may be;
- Salary is paid by, or on behalf of, a non-resident employer; and
- Salary cost is not borne by a PE or fixed base of such an employer in India.

³ C.C., C.E. & S.T. – Bangalore (Adj.) v. Northern Operating Systems Pvt. Ltd. (2022) 141 taxmann.com 289 (SC)

⁴ Hyatt International Southwest Asia Ltd. v. Additional Director of Income Tax (2025) 176 Taxmann 783 (SC)

⁵ Formula One World Championship Ltd. v. Commissioner of Income Tax, International Taxation, Delhi (2017) 394 ITR 80 (SC)



If any of these conditions fail, salary remains taxable in India. However, if all three conditions are satisfied in a short-term secondment case, salary may come out of the contours of Indian taxability.

But if the I Co. bears the cost or controls the secondee, Indian tax authorities may treat I Co. as the “real employer,” making salary taxable in India even for short secondments.

Thus, the following potential scenarios typically emanate from an Indian non-resident secondee perspective:

1. **Salary paid abroad by F Co., no recharge to I Co., stay < 183 days**
→ Likely exempt under Tax Treaty.
2. **Salary paid in India by I Co.**
→ Taxable in India, regardless of stay period.
3. **Salary split-pay (part abroad, part in India)**
→ Entire salary relating to services in India taxable.
4. Non-resident employee may have to factor foreign tax credit admissibility in his country of residence in respect of taxes suffered in India on income, if any, taxed in both countries.

Thus, the real employer test can have a bearing on employee tax also. Interestingly, it runs contrary to the findings on Issues 1 to 3. In other words, if F Co. is determined to be the real employer, issues 1 to 3 are likely to result in adverse consequences for the assessee in terms of taxability and PE in the hands of F Co. and additional withholding tax obligations, if any, on I Co. qua F Co.

Conclusion

Overall, while standardised contracts may be in place, the operational reality, shaped by the actual conduct of business, the foreign company’s direct commercial interest in the profitability or revenue of the Indian entity, and insights from employee interviews during tax surveys on ‘who truly exercises control,’ now forms the centre-stage of judicial evaluation of case-specific facts. This means strategic tax advice based on ‘one size fits all’ will no longer suffice. Functions, assets and risks of I Co. qua F Co. will have to be closely scrutinised by applying different perspectives from different judgements. The need is to exercise caution at the representation as well as planning stage.

Representations in ongoing or past cases

Evolving jurisprudence demands that the facts and arguments are presented holistically and with structure before appellate forums. This is essential to prevent restrictive readings of findings, confusion from overlapping agreements, overlooked arguments, omission of relevant precedents, or leaving appellate forums with incomplete issues to adjudicate. Incomplete facts or partially addressed questions may prejudice not only the assessee’s case but also mislead future reliance on the decision as binding precedent.

Planning for the future

When designing cross-border arrangements, it’s important to ensure that F Co. exercises only the level of control over I Co. that is necessary for

its role, whether as a service provider, franchisor, licensor, or the founder of a project office or capability center in India. Keeping the control limited in this way is essential for maintaining tax neutrality over time. Any level of control which crosses this *line of control* may be seen as extended arms of F Co. in India, long enough to be pulled to pay tax in India.

Further, if at the planning stage, F Co. is confident of satisfying the real employer test, I Co. can use the same to explore the benefit of short-stay exemption for the purpose of employee withholding tax under the Tax Treaty, if any. Where the burden of incremental tax in India quo the host country falls on I Co./F Co., this line of analysis may create potential tax savings for the taxpayer group, also saving the non-resident employee from the hassle of seeking foreign tax credit in his country of residence.



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