

Virtual Presence Isn't Tax Presence

In a significant ruling impacting non-resident taxpayers, the Hon'ble High Court of India in the case of **Clifford Chance PTE Ltd v. Commissioner of Income Tax, International**, clarified that a Service PE under a Double Taxation Avoidance Agreement ('DTAA' or 'Treaty') can arise only when services are physically performed and not virtually performed in a contracting state. The definition of a PE cannot be expanded beyond their explicit wording in the treaty.

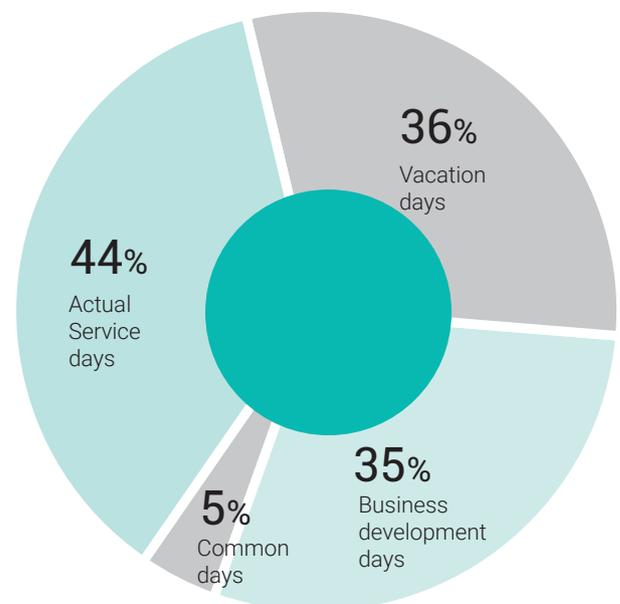
Facts in Brief

Clifford Chance Pte. Ltd., a Singapore-based legal advisory firm, provided legal services to Indian clients.

For this purpose, the employees visited India as follows:

- For AY 2020-21: 2 employees visited India for a total of 120 days break-up of which is provided in the chart.

Break-up of 120 days stay in India in AY 2020-21



- For AY 2021-22: No employees visited India, and services were rendered entirely from outside India.

The Assessing Officer ('AO') alleged the existence of both a Service PE (for AY 2020-21) and a Virtual Service PE (for AY 2021-22) under Article 5(6) of the India-Singapore tax and taxed 100% of revenues earned from Indian clients.

The Assessee, however, maintained that only 44 days involved actual service delivery within India after excluding vacation days, business-development days, and common days, claiming that therefore, no Service PE was constituted.

Issues

The case raised two principal legal questions:

- 1. Whether Clifford Chance constituted a Service PE in India** under Article 5(6)(a) of the India–Singapore DTAA.
- 2. Whether a Virtual Service PE can be read into the DTAA**, thereby taxing offshore services rendered virtually, despite no physical presence in India.

Journey of the case

AO: Held that both a Service PE and Virtual Service PE existed, taxing the entire receipts.

DRP: Upheld AO's view, holding that physical presence was not necessary as long as services continued for over 90 days (including virtual services).

ITAT: Reversed the additions, ruling that actual services rendered in India through physically present employees alone count toward the 90-day threshold, and the DTAA does not recognise virtual PE.

Decision of the High Court:

The High Court made several emphatic determinations:

Physical presence is essential:

The Court held that the wording of Article 5(6)(a) of the India–Singapore DTAA '*furnishes services... within a Contracting State through employees or other personnel*' carries a clear territorial requirement.

- The term 'within India' demands that services must be performed inside India.
- Therefore, absence of physical presence of the employees in India does not lead to creation of Service PE, regardless of the number of days of service rendered remotely.

Only "actual service days" can be counted toward the 90-day Service PE threshold:

The Court upheld the Tribunal's approach that the quality of presence, not merely the number of days an employee is in India, is relevant.

Excluded days include:

- **Vacation days (36 days)** – employees were in India but not rendering services.
- **Business development days (35 days)** – employees were exploring markets, not serving clients.
- **Common days (5 days)** – overlapping days cannot be counted multiple times; man-days cannot be double-counted.

This left only 44 actual service days in AY 2020-21, far below the 90-day threshold.

No concept of "Virtual Service PE" exists under the India–Singapore DTAA:

The Revenue relying on the Apex court ruling in the case of **Hyatt International Southwest Aisa Ltd.** (and several other rulings) held that it is the continuance of services for the threshold limit of 90 days that matters and not the physical presence of the employees. It argued that modern digitisation enables remote services and therefore, a Virtual PE should be recognised.

The Court firmly rejected this on the premise that:

- The DTAA does not mention or contemplate a Virtual Service PE.
- Courts cannot read into the treaty concepts that negotiators deliberately did not include.
- OECD commentary or other jurisdictions' practices cannot override treaty text without express amendment.

The Court noted:

"If something is conspicuous by its absence, the presumption is that it has deliberately been done so."

Treaty law overrides domestic concepts like Significant Economic Presence (SEP):

SEP provisions in the domestic laws cannot override treaty language due to operation of Section 90(2). Until DTAA renegotiation, only physical presence-based PE tests apply.

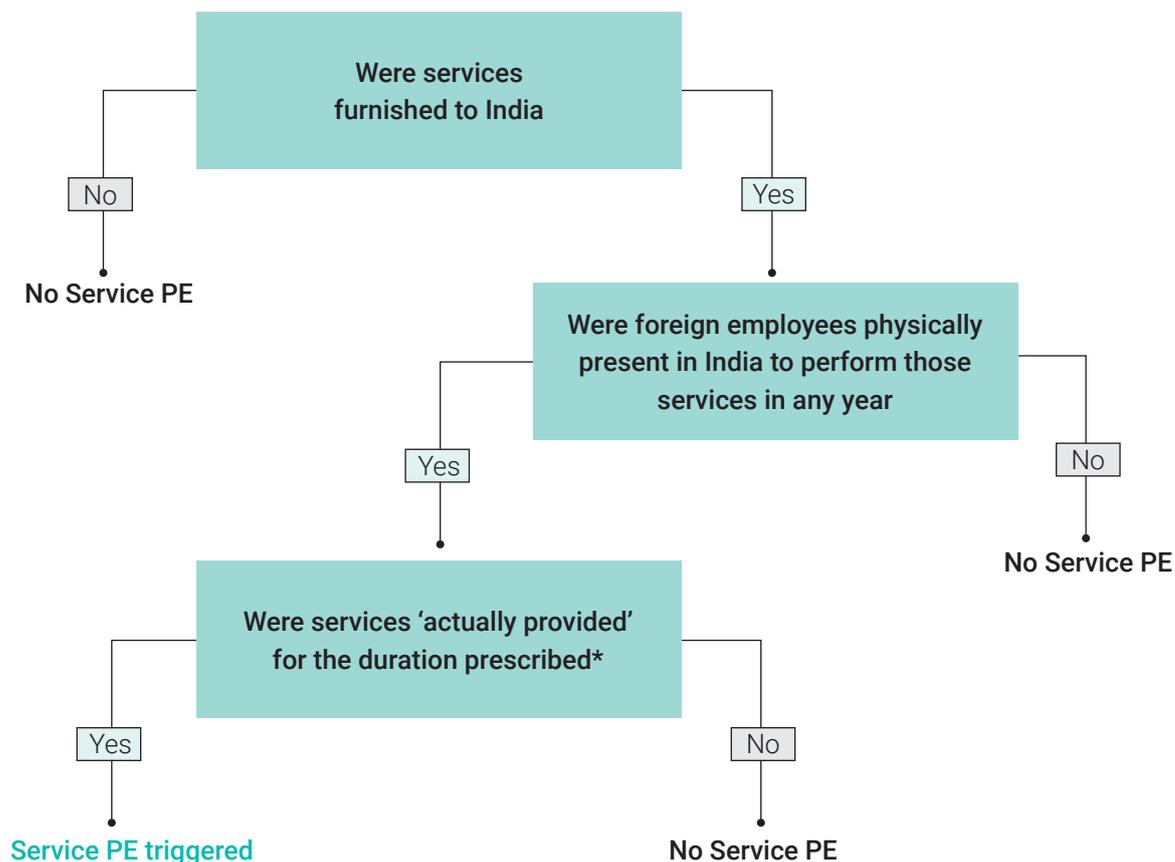
International commentary (OECD, BEPS) is persuasive but not binding:

The 2018 OECD Interim Report reflects emerging views but no treaty amendments have been made. Courts cannot apply OECD interpretations when they conflict with clear treaty text.

Key Takeaways

- **Strict treaty interpretation prevails:** Courts cannot infer virtual PE or digital nexus thresholds unless expressly incorporated in the language of DTAA.
- **Physical presence remains central for Service PE:** Days of actual service performance - not mere presence, not business development - govern PE thresholds.
- **Offshore professional services remain protected:** Cross-border providers in legal, consulting, IT, engineering, and financial services sectors can rely on treaty protection where services are delivered remotely.
- **Revenue cannot rely on OECD commentary or global trends:** Emerging concepts like digital PE/virtual PE/ SEP cannot override treaty text unless renegotiated.
- **Compliance clarity for multinational service providers:** Entities can safely design remote-delivery models without triggering PE in India unless employees or other personnel perform services physically within India over the prescribed duration.

Flow Chart explaining the manner of triggering Service PE as per DTAA in light of the aforesaid judgement:



*Notes:

- **Computation of Service PE Threshold:** For determining whether a Services Permanent Establishment (Service PE) is triggered, only the days on which services are actually rendered in the source country are to be counted. Days that do not involve service delivery—such as vacation days, weekends spent without work, business development or preparatory/liaison meetings, and transit days—are excluded from the threshold calculation under the relevant DTAA.
- **No Concept of Virtual Service PE Under Current DTAA:** At present, no DTAA includes provisions for a virtual or remote Service PE, either for the purpose of triggering a Service PE or determining the continuation of an existing one. Therefore, in the absence of explicit DTAA language, a Service PE cannot be said to arise without the physical presence of foreign personnel in the source jurisdiction.

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