

EY Tax Alert

HC rules secondment of employees not taxable under GST

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Executive summary

This Tax Alert summarizes a recent ruling of the Karnataka High Court (HC)¹ regarding taxability under reverse charge on secondment of employees from overseas related entity.

The key observations of the HC are:

- ▶ In *Northern Operating Systems Pvt Ltd*², SC ruled that secondment arrangement was taxable manpower service since the foreign entity in that case retained control and added mark-ups in recovery of costs. It was also clarified that its decision was based on specific facts and should not be treated as a universal precedent for all secondment cases.
- ▶ Businesses must evaluate secondment cases individually, considering factors like control, nature of posting, salary payment method, and whether the secondee returns to the foreign entity.
- ▶ The facts of the present case clearly demonstrate a genuine employer-employee relationship between the petitioner and the seconded personnel, bringing the arrangement within the exclusion under Schedule III to the Central Goods and Services Tax Act, 2017 and outside the scope of taxable supply.
- ▶ Circular No. 210/4/2024-GST clarifies that if a domestic entity eligible for full ITC does not issue an invoice for services received from a foreign affiliate, the value of such services shall be deemed 'Nil' and treated as the open market value under Rule 28(1) of the Central Goods and Services Tax Rules, 2017. Thus, even if the secondment is considered a supply, the deeming provision effectively nullifies any tax liability.

Basis above, HC held that the arrangement in the given case does not give rise to any tax liability and the demand raised by Revenue was liable to be set aside.

¹ TS-647-HC(KAR)-2025-GST

² Civil Appeal Nos.2289-2293 of 2021



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Background

- ▶ The petitioner is engaged in the business of designing, manufacturing, supplying, installing, and commissioning goods pertaining to railway and metro infrastructure projects.
- ▶ For the period July 2017 to March 2023, employees of petitioner's overseas group companies were seconded to work in India for a fixed tenure.
- ▶ During secondment, the secondees were under operational supervision, control, and administration of the petitioner. They are required to comply with all internal rules and policies, including office hours, code of conduct, and statutory obligations under Indian tax laws, particularly the deduction of tax at source (TDS) from their salaries.
- ▶ While the expatriate employees were on petitioner's payroll, the overseas group entities continued to provide social security and related benefits available in their home countries.
- ▶ The same was reimbursed by the petitioner and from November 2020 onwards, it paid integrated tax (IGST) on the same under reverse charge mechanism.
- ▶ An SCN was issued to propose a demand of IGST on the entire value of services, along with interest and penalty on the premise that petitioner was importing "Manpower Supply Service" from its overseas affiliate. The said demand was confirmed vide an order.
- ▶ Aggrieved, the petitioner filed a writ petition before the Karnataka High Court (HC).

Petitioner's Contentions

- ▶ Circular No. 210/4/2024-GST issued by Central Board of Indirect Taxes and Customs (CBIC) clarifies that in cases involving related party transactions where full input tax credit (ITC) is available to the recipient, the value declared in the invoice may be deemed as the open market value under the second proviso to Rule 28 of the Central Goods and Services Tax Rules, 2017 (CGST Rules).
- ▶ Reliance can also be placed on the Delhi HC judgement³ wherein similar show cause notices were quashed in cases where no invoices were raised for alleged manpower supply.

Since no invoices were raised in the present case as well, the open market value must be deemed to be 'Nil'.

- ▶ Without prejudice to the above, as a matter of abundant caution, IGST was already discharged on reimbursed amounts from November 2020 onwards,

even though no invoices were raised for the entire disputed period.

- ▶ Further, the transaction in essence represents a service between employer and employee, which falls squarely within the ambit of Entry 1 of Schedule III to the Central Goods and Services Tax Act, 2017 (CGST Act) and hence does not amount to a taxable supply.

Revenue's Contentions

- ▶ Petitioner's arrangement with its overseas group entities amounts to a taxable supply of service wherein the foreign entity is the supplier and the petitioner is the recipient of such service.
- ▶ By virtue of Notification No. 10/2017 – Integrated Tax (Rate) read with Section 5(3) of the Integrated Goods and Services Tax Act, 2017 (IGST Act), the petitioner was legally obligated to discharge IGST under RCM on the entire value of services provided by the foreign group entities through seconded personnel.

High Court Ruling

- ▶ Under the erstwhile service tax regime, various appellate tribunals consistently held that seconded employees were to be treated as employees of the Indian entity for all practical and legal purposes, and that no taxable manpower supply service was involved.

However, Supreme Court (SC) in the case of Northern Operating Systems Pvt Ltd⁴ marked a significant shift in the legal interpretation of such arrangements.

- ▶ SC observed that despite such arrangements appearing as employer-employee relationships, the foreign entity retained control, paid salaries in foreign currency, and added administrative mark-ups, indicating a service transaction. Thus, such arrangements are liable to tax under RCM.

It clarified that the ruling was fact specific and should not be treated as blanket precedent for all the secondment arrangements.

- ▶ Accordingly, businesses must assess secondment arrangements on a case-by-case basis. Key factors include:
 - ▶ Who bears the economic burden and controls long-term employment?
 - ▶ Whether the posting is task-specific or open-ended?
 - ▶ How salary is paid *i.e.*, directly by the Indian entity or via the foreign company?

- ▶ Whether the secondee is absorbed into the Indian organization or reverts to the foreign entity post-assignment?
- ▶ CBIC also issued an Instruction dated 13 December 2023 directing tax authorities to assess secondment cases individually and to refrain from invoking Section 74 of the CGST Act unless there was clear evidence of fraud or wilful suppression.
- ▶ The facts of the present case establishes the existence of a genuine employer-employee relationship between the petitioner and the seconded personnel, falling squarely within the exclusion under Schedule III of the CGST Act and thereby not constituting a taxable supply.
- ▶ Further, para 3.7 of Circular No. 210/4/2024-GST unequivocally states that if the related domestic entity does not raise an invoice in respect of services received from its foreign affiliate, the value of such services may be deemed to be 'Nil' and such 'Nil' value shall be treated as the open market value in terms of the second proviso to Rule 28(1) of the CGST Rules.

Therefore, even if *arguendo* such secondment arrangement is assumed to be a supply, the deeming fiction under the Circular neutralises any scope for further tax liability.

- ▶ Agreeing with the view of Delhi HC (*supra*), Circular being binding on the authorities, leaves little room for the Revenue to allege a taxable value in the absence of an invoice.
- ▶ Basis above, HC allowed the writ petition by quashing and setting aside the impugned orders.

Comments

- a. HC ruling appears to suggest that, where full ITC is available, Indian component of salary and perquisites paid directly to the employees may not be included in taxable value of consideration, depending on the facts, even if social security of the seconded person is reimbursed to overseas entity and subjected to GST under reverse charge.
- b. HC does not appear to have clearly distinguished in detail the present case from the SC's decision in *Northern Operating Systems*.
- c. This ruling supports the view taken by the Delhi HC that when the recipient can claim full ITC, even a zero value can be used for related party transactions if no invoice is issued.

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