

# EY Tax Alert

**CESTAT upholds levy of service tax on payments to employees seconded from foreign affiliates**

## Executive summary

This Tax Alert summarizes a recent ruling<sup>1</sup> of the Customs, Excise and Service Tax Appellate Tribunal, Chennai (CESTAT). The issue involved was whether the salary and other benefits paid to the employees seconded from the foreign affiliate can be considered towards receipt of "manpower recruitment or supply agency" services by the assessee.

The key observations of the CESTAT in this regard are as follows:

- ▶ On perusal of the Secondment Agreement entered by the assessee and its foreign affiliate, it is clear that payment of salaries and other benefits to the secondees is towards the cost for making services available to the assessee.
- ▶ The clauses of the Agreement in the present case are more or less identical to that of the assessee before the SC in case of Northern Operating System<sup>2</sup>. Therefore, assessee cannot escape the service tax liability in respect of such services under reverse charge mechanism.
- ▶ There is no doubt that what is provided by foreign affiliate is nothing but manpower recruitment services.
- ▶ However, since all the activities were within the knowledge of the Revenue in view of the several audits undertaken during the relevant period, there is no scope to allege suppression of facts.

Basis above, CESTAT upheld service tax demand on amounts paid to foreign expatriates towards "manpower recruitment or supply agency" services by the foreign affiliates. However, demand for the extended period of limitation was set aside.

<sup>1</sup> Service Tax Appeal No. 41736 of 2019

<sup>2</sup> 2022 (61) G.S.T.L. 129 (S.C.)

## Background

- Assessee is *inter alia* engaged in providing Business Auxiliary Services.
- During the course of compliance verification, Revenue came across secongment agreements (SA) entered between the assessee and its foreign affiliate for deputation of employees. Further, a separate employment contract was entered with such employees.
- As per the agreements, a part of the salary was directly paid by the assessee. However, the other part was paid by the foreign affiliate in the form of social security obligations and employee's retirement benefit plans. The same was later reimbursed by the assessee.
- Revenue was of the view that deputation of foreign expatriates in the given case would be covered under the definition of "manpower recruitment or supply agency" services under Section 65(68) of the Finance Act, 1994. Therefore, import of such services would be taxable in the hands of the assessee under reverse charge mechanism (RCM).
- Accordingly, Show Cause Notices (SCNs) were issued proposing tax demands for various tax-periods by invoking extended period of limitation.
- After considering assessee's submissions, Revenue passed orders confirming that the amount paid towards salary and perks of the expats is to be considered as part of the consideration for supply of manpower services.
- Aggrieved by the same, assessee filed an appeal before the Customs Excise and Service Tax Appellate Tribunal (CESTAT).

## Assessee's submissions

- The expatriates are treated as employees of the assessee. The employment contract, which is governed by the laws applicable in India, would provide the job title, contract period, department, effective date of their appointment and annual salary in INR along with perks.
- Documents like Employment Visa, Tax Deducted at Source (TDS) certificates in Form 16 under the Income Tax Act, Provident Fund (PF) registration, etc., proved that the expats were on the payroll of the assessee.
- The amounts paid to the expatriates were disclosed under the head "salaries, wages and bonus" and hence, there was no service provider-recipient relationship with the affiliate.
- Although the pre-secongment events such as selection, negotiation of emoluments, etc., was not within the

scope of the assessee, however, during the entire period of secongment, the secondees were under the complete control of the assessee.

- Even if it is accepted that the affiliate retained control over the expatriates, the arrangement would only result in dual employment wherein the cost of such employees would be shared by the joint employers.
- Various audits were conducted by the Revenue from time to time and all the information along with documents were provided to them. Therefore, the entire activities including the alleged manpower of supply service was very much within the knowledge of the Revenue. There was no question of suppression of any facts to justify invoking the extended period of limitation.<sup>3</sup>
- Even if service tax was required to be paid on the salary paid to the secondees, the same was eligible as CENVAT credit. Therefore, the entire issue is revenue neutral for which the demand of tax and interest cannot survive.<sup>4</sup>
- The decision of Supreme Court (SC) in the case of Northern Operating Systems Pvt Ltd<sup>5</sup> (NOS) and International Merchandising Company, LLC<sup>6</sup> is distinguishable. In the present case, there is a clear finding that the expatriates were on payrolls of both, the assessee as well as the affiliate.

Further, the principle laid down in the case of NOS (*supra*) had been complied with by discharging the service tax on the reimbursement of social security charges.

## Revenue's submissions

- Payment made by assessee to the foreign affiliate is for import of manpower services. Further, the salaries paid to the secondees are consideration includable in the gross amount for such services.
- Expats are deputed to assessee on certain terms and conditions, for a specified period and to perform specified tasks. During the secongment period, the expats would remain as employees of the foreign affiliate.
- Such affiliate has the right to replace the secondee or change the secongment period after issuing notice to the assessee. Assessee does not have any power to select the employees. Further, the conditions for employment are determined basis SA and not as per the individual agreement entered with the expatriates.
- Coming to India under Employment Visa does not mean that there is employer-employee relationship between the assessee and the expats.
- The mandatory requirement of PF in India and the provisions of Income Tax Act, considering the income of

<sup>3</sup> 2022 (67) G.S.T.L. 129 (S.C.); 2015 (8) TMI 1053 - Supreme Court

<sup>4</sup> 2015 (320) E.L.T. 22 (S.C.); 2005 (179) E.L.T. 276 (S.C.); 2005 (181) E.L.T. 380 (S.C.); 2008 (231) E.L.T. 195 (S.C.);

2005 (181) E.L.T. 222 (Tri. -Mumbai); 202(3) TMI 847 - CESTAT, Kolkata

<sup>5</sup> 2022 (61) G.S.T.L. 129 (S.C.)

<sup>6</sup> 2022 (67) G.S.T.L. 129 (S.C.)

the expats under the head "salary", do not come in any way of determining the applicability of service tax.

- Accordingly, assessee was liable to service tax on the total amount paid to the foreign affiliates along with the salaries and perks paid to the secondees.
- Revenue heavily relied on the SC decisions in the case of NOS (*supra*) and International Merchandising Company, LLC (*supra*) to support its contentions.

## CESTAT ruling

- On perusal of the SA, it is clear that payment of salaries, bonuses, perks, etc., to the secondees by the assessee is towards the cost for making services available to the assessee.
- The definition of the term "consideration" as provided under Section 67 would include any amount that is payable for the taxable service provided or agreed to be provided. There is no doubt that what is provided by foreign affiliate is nothing but manpower recruitment services.
- The clauses of the SA in the present case are more or less identical to that of the assessee before the SC in the case of NOS. Therefore, ratio of the said ruling would squarely apply to the present case.
- Thus, assessee cannot escape the service tax liability in respect of manpower recruitment or supply agency service under RCM.
- However, the fact remains that all the activities were within the knowledge of the Revenue and hence, there is no scope to allege suppression of facts.
- The issue involved in the present case was of classification and interpretation of taxing statute. For this reason also, suppression of facts could not be alleged.
- Accordingly, CESTAT upheld the demand for service tax for the normal period.

## Comments

- a. While the CESTAT concluded on similarity in facts of present case with the matter in NOS before SC, in the said case, the entire salary and other benefits were paid by the foreign affiliate to the seconded employee which were reimbursed by the Indian company.
- b. Another key parameter of cross-service arrangement between the entities that was present in NOS case before SC is however not there in the present appeal.
- c. Earlier, even the Bangalore CESTAT [2023-TIOL-295-CESTAT-BANG] in case of Dell International upheld the taxability on similar arrangement following the SC ruling in NOS.
- d. It is pertinent to note that similar issue pertaining to taxability of secondment is pending before the SC in two other cases.

# Our offices

## Ahmedabad

22nd Floor, B Wing, Privilon  
Ambli BRT Road, Behind Iskcon  
Temple, Off SG Highway  
Ahmedabad - 380 059  
Tel: + 91 79 6608 3800

## Bengaluru

12th & 13th floor  
"UB City", Canberra Block  
No. 24, Vittal Mallya Road  
Bengaluru - 560 001  
Tel: + 91 80 6727 5000

## Ground Floor, 'A' wing

Divyasree Chambers  
# 11, O'Shaughnessy Road  
Langford Gardens  
Bengaluru - 560 025  
Tel: + 91 80 6727 5000

## Chandigarh

Elante offices, Unit No. B-613 & 614  
6th Floor, Plot No- 178-178A  
Industrial & Business Park, Phase-I  
Chandigarh - 160 002  
Tel: + 91 172 6717800

## Chennai

Tidel Park, 6th & 7th Floor  
A Block, No.4, Rajiv Gandhi Salai  
Taramani, Chennai - 600 113  
Tel: + 91 44 6654 8100

## Delhi NCR

Golf View Corporate Tower B  
Sector 42, Sector Road  
Gurugram - 122 002  
Tel: + 91 124 443 4000

## 3rd & 6th Floor, Worldmark-1

IGI Airport Hospitality District

Aerocity, New Delhi - 110 037

Tel: + 91 11 4731 8000

## 4th & 5th Floor, Plot No 2B

Tower 2, Sector 126

Gautam Budh Nagar, U.P.

Noida - 201 304

Tel: + 91 120 671 7000

## Hyderabad

THE SKYVIEW 10  
18th Floor, "SOUTH LOBBY"  
Survey No 83/1, Raidurgam  
Hyderabad - 500 032  
Tel: + 91 40 6736 2000

## Jamshedpur

1st Floor, Shantiniketan Building,  
Holding No. 1  
SB Shop Area, Bistupur  
Jamshedpur - 831 001  
Tel: + 91 657 663 1000

## Kochi

9th Floor, ABAD Nucleus  
NH-49, Maradu PO  
Kochi - 682 304  
Tel: + 91 484 433 4000

## Kolkata

22 Camac Street  
3rd Floor, Block 'C'  
Kolkata - 700 016  
Tel: + 91 33 6615 3400

## Mumbai

14th Floor, The Ruby  
29 Senapati Bapat Marg  
Dadar (W), Mumbai - 400 028  
Tel: + 91 22 6192 0000

## 5th Floor, Block B-2

Nirlon Knowledge Park  
Off. Western Express Highway  
Goregaon (E)  
Mumbai - 400 063  
Tel: + 91 22 6192 0000

## Pune

C-401, 4th floor  
Panchshil Tech Park, Yerwada  
(Near Don Bosco School)  
Pune - 411 006  
Tel: + 91 20 4912 6000

## Ernst & Young LLP

EY | Building a better working world

## About EY

EY exists to build a better working world, helping to create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Information about how EY collects and uses personal data and a description of the rights individuals have under data protection legislation are available via [ey.com/privacy](http://ey.com/privacy). EYG member firms do not practice law where prohibited by local laws. For more information about our organization, please visit [ey.com](http://ey.com).

Ernst & Young LLP is one of the Indian client serving member firms of EYGM Limited. For more information about our organization, please visit [www.ey.com/en\\_in](http://www.ey.com/en_in).

Ernst & Young LLP is a Limited Liability Partnership, registered under the Limited Liability Partnership Act, 2008 in India, having its registered office at 9th Floor, Golf View Corporate Tower B, Sector 42, Golf Course Road, Gurugram, Haryana - 122 002.

© 2023 Ernst & Young LLP. Published in India.  
All Rights Reserved.

This publication contains information in summary form and is therefore intended for general guidance only. It is not intended to be a substitute for detailed research or the exercise of professional judgment. Neither EYGM Limited nor any other member of the global Ernst & Young organization can accept any responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication. On any specific



Download the EY India Tax Insights App

[ey.com/en\\_in](http://ey.com/en_in)

@EY\_India EY EY India EY Careers India @ey\_indiacareers