

Secondment of Employees



Human resources are the bedrock of any organisation. Over the last two decades, the business environment has expanded the horizon of human resources. Liberalisation and globalisation has made this world into a global village and has opened a whole vista of opportunities for the skilled workforce. Now, global mobility has increasingly become the way of life. It is quite usual today for multinational companies setting up their business in India to send their key management and technical personnel on deputations and secondment to the offices in India. Thus, making deputations and secondment of employees a natural extension of a globalised economy which demands that the right employee with the appropriate skill set is at a particular organisation to fulfill organisational requirements. Companies are increasingly leveraging on the knowledge and experience of their employees both in project execution and business expansion. While today's business environment is becoming borderless, the realities of taxation have not! That's the irony.... Read on to know more.....

Tax Controversies

There has been a lot of tax controversies over the taxation of deputations and secondment arrangements ranging from the constitution of permanent establishment, provision of fees for technical services, withholding taxes, supply of manpower, etc., resulting in a number of different tax rulings on deputation and secondment arrangements for expatriate staff working in India and creating an environment of uncertainty for firms setting up in the country. Let us now look at the tax controversies on deputation and secondment arrangements from a Service Tax perspective.



CA. Sushil Kumar

(The author is a member of the Institute who may be contacted at capsushilkumar@rediffmail.com.)

In recent times, the Indian government has increased its attention towards the expatriate population. This has translated into the changes in various legislations and resulted in increased responsibilities and additional compliance requirements. It is a pity that the revenue wants to tax payments made to the said staff through the parent company considering the service as "supply of manpower" revenue contends there is a transaction of supply of manpower by the group entity to the Indian company.

Analysis of Manpower Supply Companies

Different types of manpower supply companies are:
Type 1: There are a number of companies in India which are specialised in the business of temporary supply of manpower. Typically, these companies would recruit employees in their organisation incur all staff costs including statutory and labour law related levies and these employees would be made available to work in a client location. The company would receive actual re-imbursment of the staff costs as well as service charges.

Type 2: There are many agencies specialised in assisting an organisation in the recruitment of respective employees. Such agencies normally have database of various prospective candidates for employment, which provide details of age group, position currently held by candidates, expected salary, mobility, experience, etc., and the database may be available online in websites like Naukri.com, Monster.com, shine.com, etc., or may be provided offline to the organisations.

Type 3: There are many contractors who are expert in organising labour and supply thereof to various companies. Organisations enter into contract with such contractors for supply of the specified number of persons. The contract specifies the qualification, experience of the person required. These contractors who supply labour not only charge the salary of labour but also their agency commission.

Legal Position under Service Tax Law

Rule 2(g) of Service Tax Rules, 1994 defines supply of manpower:

'Supply of manpower' means supply of manpower, temporarily or otherwise to another person to work under his superintendence or control.

Thus, the essence of service is that the service provider must only be responsible for supply of manpower. The manpower will work under the supervision and control of the service receiver.

The definition of manpower supply and recruitment agency was amended from 16.06.2005 in the erstwhile Section 65(68) to provide taxability on supply of manpower temporarily or otherwise. After the amendment, the CBEC has described the scope of amendment in Para 22 of CBEC circular issued from F. no. B-1/6/2005 –TRU dated 27.07.2005. Sub paras (2), (3) and (4) give the scope of said taxability under supply of manpower, which have been reproduced:

- *A large number of business or industrial organizations engage the services of commercial concerns for temporary supply of manpower which is engaged for a specified period or for completion of particular projects or tasks. Services rendered by commercial concerns for supply of such manpower to clients would be covered within the purview of Service Tax.*
- *In these cases, the individuals are generally contractually employed by the manpower supplier. The supplier agrees for use of the services of an individual employed by him to another*

person for a consideration. The terms of the individual's employment may be laid down in a formal contract or letter of appointment or on a less formal basis. What is relevant is that the staff is not contractually employed by the recipient but come under his direction.

- *Service Tax is to be charged on the full amount of consideration for the supply of manpower, whether full time or part time. The value includes recovery of staff costs from the recipient, e.g. salary and other contributions. Even if the arrangement does not involve the recipient paying these staff costs to the supplier (because the salary is paid directly to the individual or the contributions are paid to the respective authority). These amounts are still part of the consideration and hence form part of the gross amount.*

Position under Positive List

Service of manpower supply was taxable under the category of manpower recruitment/supply agency service. The term manpower recruitment or supply agency was defined under the erstwhile Section 65(68):

"Manpower recruitment or supply agency" means any person engaged in providing any service, directly or indirectly in any manner for recruitment or supply of manpower temporarily or otherwise to any other person.

The taxable service was defined under the erstwhile Section 65(105) (k):

"Taxable service" means any service provided or to be provided – to any person by a manpower recruitment or supply agency in relation to the recruitment or supply of manpower, temporarily or otherwise in any manner.

Explanation – For the removal of doubts, it is hereby declared that for the purposes of this sub clause, recruitment or supply of manpower includes services in relation to pre-recruitment screening, verification of the credentials and antecedents of the candidate and authenticity of the documents submitted by the candidate.

Position under Negative List

With effect from 01.07.2012, the term service is defined under Section 65B (44) to mean any activity carried out by a person for another for a consideration. Thus even after 01.07.2012, the services provided by manpower supply are taxable. The scope of taxability prior to 01.07.2012 and after 01.07.2012 has remained the same except for the

introduction of a new concept of *partial reverse charge* mechanism wherein Service Tax is payable partially by service provider and partially by service receiver for service of manpower supply.

Reverse Charge

Prior to 01.07.2012, Service Tax on services of manpower supply was payable by the provider of services. However from 01.07.2012 as per the notification no.30/2012-ST dated 20.06.2012, Service Tax is payable partially by service provider and partially by service receiver for service of manpower supply.

Notification no.30/2012-ST dated 20.06.2012 provides that where the service provider is individual, proprietor, partnership, HUF or AOP for services of manpower supplied and the service recipient is business entity registered as body corporate, the Service Tax is payable to the extent of 75% by the business entity registered as body corporate. The payment of Service Tax by business entity registered as body corporate does not have any impact on determining the value of Taxable service.

The value shall be determined as per the provisions of Section 67 which shall be the gross amount charged for the value of taxable service rendered.

Having analysed the legal and practical aspects of *supply of manpower* services, now let us look at the modus operandi or typical arrangement between group companies located outside India and Indian company in a scheme of deputation or secondment.

The Differentiating Factor – Typical Arrangement

Many Indian companies enter into an *Inter-Company Employment Agreement/Expatriate Remuneration Reimbursement Agreement* with their parent overseas company to facilitate employment of personnel from other group companies to assist their business and operations in India. Typically, the main features of the agreement would be:

- o The assigned personnel are relieved by their respective group companies and put at the disposal of the Indian company and function as whole-time employees of the Indian company and work solely under control, direction or supervision of the Indian company in accordance with the policies, rules and guidelines generally applicable

to the Indian company's own employees during the period of such employment.

- o The terms and conditions and place of employment of such assigned employee and their designation will be in accordance with the terms and conditions agreed upon by the Indian company and the group entity.
- o The employment of the assigned employee with the Indian company will be in his personal capacity and not on behalf of the group entity.
- o The Indian company shall have a right to promote/ discipline/ suspend/ terminate the services of such assigned employee in accordance with its policies, without seeking any permission from the group entity.
- o Group entity will not have any obligation or undertake any risk towards the performance of the assigned employee to the Indian company during the period of such assignment.
- o During the period of the assignment, the group entity shall not interfere with the working or the terms and conditions of the assigned employee.
- o The salary including other entitlements shall be the liability of, decided and paid by Indian company. Payment of income-tax would be as per provision of Double Taxation Avoidance Agreement.
- o In case of any default in respect of statutory payments, the group entity shall not be responsible to the assigned employee.
- o If the group entity makes any payment to any third party in the home country of the assigned employee on behalf of the Indian company, the group entity will be reimbursed by the Indian company to such payment.
- o There is no direct or indirect consideration/ charged in cash or otherwise payable to the group entity by the Indian company in this connection.
- o A separate agreement with the assigned employee was entered into by the Indian company.

Now let us look at how revenue authorities view the aforementioned arrangement.

Arguments of Revenue Authorities

- o The Indian company is receiving the services of qualified professionals provided/supplied by the Foreign Service providers for execution of professional work under the agreement.
- o The Indian company pays full salary directly to the assigned employee rather than routing a part through the group entity.

- o The Group entity located outside India deputed certain employees to offices located in India and their salary is paid abroad but shown in the profit and loss account prepared for offices located in India.
- o The assigned employee goes back to the group entity after a period of 3-4 years, and even during the intervening period, the social security liability has been discharged by the group entity in the assigned employees' home country.

Now let us also look at the counter attack of Indian companies on the arguments of revenue authorities.

Counter Arguments of Indian Companies

- o There is no supply of labour or manpower by the group entity to the Indian company.
- o As per the request of the Indian company the parent company facilitates in identifying such foreign employees who are then employed by the Indian company under separate agreement with each assigned employee.
- o The assigned employees work under the control and supervision of the Indian company.
- o Salary for such work done by the global employees is directly paid by the Indian company.
- o The income earned by the assigned employee is subject to Indian income tax. The Indian company also deducts applicable tax at source on salary paid to such assigned employee.
- o A part of the salary of the assigned employee is remitted abroad in their home country and the same was done using the services of the group entity and such amounts would be reimbursed to the Indian company. Routing part payment through parent company by itself may not make it a case of manpower supply.
- o Apart from the reimbursement pertaining to salary, no other amounts were paid to the group entity.
- o Merely because a part of the salary was routed through the group entity, it cannot be said that the group entity was engaged in the supply of manpower.
- o The group entity was not a 'manpower recruitment or supply agency service' as required by the definition under the Finance Act, 1994.
- o Assuming secondment of employees is a service falling under the category of "Manpower recruitment or supply agency for which the appellant is liable to pay tax under Reverse charge mechanism, the same does not have any impact on the revenue as whatever would have been payable would have been available as input credit as the services provided would tantamount to input services, for levying Service Tax there should be two different legal entities involved—one providing service to the other. In view of the agreements and the accompanying facts, the assigned employees working under the Indian company are working as the Indian company's' employees and having an employer-employee relationship.
- o There is no supply of manpower service rendered to the Indian company by the group entity.
- o The method of disbursement of salary cannot determine the nature of transaction.
- o The routing of salary or manner of disbursement of salary cannot determine the nature of transaction.
- o Only their provident fund contribution in foreign exchange was being remitted to holding company as they were earlier working for the holding company - other than provident fund contribution no other payment for the persons, was being made by the appellant to holding company.

Conclusion

Based on various judicial precedents, it is crystal clear that the agreement between the group entity located outside India and the Indian company should be specific and clearly spelt out to the extent that the group entity shall not interfere with the working or the terms and conditions of the assigned employee.

Courts decide the issues based on the specific facts of the each case and hence much would depend on the terms and conditions of the agreement between the group entity located outside India and the Indian entity. Further, there should be proper documentation of the terms of assignment of employees so as to bring out the employer-employee relationship between the assigned employee and the Indian entity.

Once the employer employee relationship is established beyond doubt the manner of disbursement of salary even through the parent company or group entity cannot fasten any liability under the reverse charge with respect to the reimbursements made to the group entity. ■