

# INDIA LEGAL UPDATE

September 19, 2023

## GST on Secondment of Expatriates

### What does it mean for Japanese Companies in India?

**Court:**

Supreme Court of India

**Case:**

C.C.C.E.&S.T., Bangalore v.  
M/s Northern Operating  
Systems Pvt. Ltd.

**Judgement Date:**

May 19, 2022

**Weblink:**

[C.C.C.E.&S.T., Bangalore v.](#)

[M/s Northern Operating](#)

[Systems Pvt. Ltd.](#)

**SUMMARY:**

- The decision may not be applicable to all the companies having expatriates in India.
- GST on expatriate salary may not be applicable on the following companies:
  - If expatriates perform tasks for Indian entity and for Indian business
  - If expatriates manage the business operations in India
  - If the terms of employment with expatriates are based on Indian entity
- GST on expatriate salary may be applicable on the following companies in India:
  - If expatriates support back-office operations in India for foreign entity
  - If expatriates support initial business set up in India
  - If expatriates work for foreign entity
  - If the terms of employment with expatriates are based on foreign entity

**HLS Opinion** - In our considered opinion, the Supreme Court decision on NOS India is applicable only to fact specific situations where Indian entity provides back-end services to the foreign entity and the term of employment is as per foreign entity only. Accordingly, this decision may not be applicable on most of the companies operating in India as the facts would required to be matched with the facts of NOS India.

## How Japanese companies can manage the ongoing dispute with GST authorities?

- First line of defense – Review documentation and assess GST and PE risks.
- Second line of defense – Make a strategy for past and future.
- Cooperate with tax authorities.
- Payment of GST (without protest) may lead to acceptance of salary to expatriates as fee for technical services which may result in withholding tax liability @ 10% or 20%, as applicable, along with interest and penalty. This may also result in exposure of risk of permanent establishment (PE) whereby the foreign entity may be asked to pay the corporate tax @ 40%.
- Pay GST (under protest), avoid interest and penalty, take the input tax credit and appeal to higher tax authorities and courts.

### A. INTRODUCTION:

1. The background of this dispute is the Supreme Court ruling / order in the case of Northern Operating Systems Pvt. Ltd (NOS India).
2. The Supreme Court analyzed that India subsidiary is not the employer of the expatriates. The expatriates were providing the services in India on behalf of foreign entity. Hence, the services are covered under the definition of manpower supply services. Accordingly, on such services, NOS India is liable to pay service tax.
3. The Supreme Court specifies that it's a **fact-based specific ruling**. This means that this ruling is not applicable to all companies.
4. This ruling is applicable to those companies whose situation matches with the facts discussed and analyzed by the Supreme Court.
5. The Supreme Court mentioned that 'Direction and Control' test is not the sole criteria to determine employment. There are other factors to be considered and tested in determining the employer and employee relationship.
6. The Supreme Court mentioned that these expatriates came to do the work for foreign entity even though they were physically placed in Indian entity.
7. The Supreme Court also mentioned that the terms of employment during secondment were as per the foreign entity.
8. Recently, there has been another similar case of a back-office operations in India of Dell International where it was held by the Tribunal that Dell International is liable to pay service tax under the reverse charge mechanism.

## What is the dispute going on regarding the GST on salary paid to expatriates?

- The dispute arises because the Supreme Court did not clarify in detail what are the determinative tests to identify whether secondment arrangement will be treated as employment or services.
- No clarifications have been issued by the Government of India through Central Board of Indirect Taxes and Customs (CBIC) regarding the criteria to be satisfied by companies to prove that whether the expatriate qualify as an employee or not.

## B. IMPACT ON JAPANESE COMPANIES IN INDIA

### 1. What is the action from tax office?

i. The Directorate General of GST Intelligence (DGGI) has started the investigations and issuing Show Cause Notices (SCNs) demanding GST from Indian companies having expatriates.

ii. What are the last dates of issuing (SCNs)?

Financial Year	Last Date to Issue SCN	Last Date to Issue Order
2017-18	30-Sep-23	31-Dec-23
2018-19	31-Dec-23	31-Mar-24
2019-20	31-Mar-24	30-Jun-24
2020-21	28-Nov-24	28-Feb-25
2021-22	30-Sep-25	31-Dec-25
2022-23	30-Sep-26	31-Dec-26

iii. The DGGI has started asking for documentation and evidence to check whether expatriates employed with Indian entity are having employment with foreign entity or Indian entity.

iv. Following documents and evidence are being required by DGGI:

- o Directors' report
- o Board minutes
- o Secondment contracts
- o Employment contracts
- o Details of salary and perquisites
- o Form 16
- o Employment proofs in foreign country
- o Social security details in foreign country
- o Transfer Pricing studies and audit report in Form 3CEB.

### 2. How much GST is to be paid and how ITC will be availed?

i. In case GST is to be paid by the Indian entity, then it will be levied on the following amounts:

- o Amount paid to expatriates by Indian entity.
- o Amount paid to foreign entity.
- o Amount spent on perquisites for expatriate employees.

ii. The companies can avail ITC of GST paid on expatriate salaries by generating self-invoice, it can pay the tax and claim ITC.

iii. A self-invoice for the said transaction may be issued with the current date. The timelines for availment of credit u/s 16(4) must be considered basis the self-invoice in case of reverse charge transactions. For example, if the date of self-invoice is 15 April 2023, input tax credit can be availed by 30 November 2024 or date of actual filing of annual return.

iv. **Situations where benefit of Input tax credit is available:**

- Section 73 – Cases other than Fraud or any willful-misstatement or suppression of facts

Input tax credit will be available to companies where the demand is raised in terms of Section 73 of the CGST Act, 2017.

**v. Situations where benefit of Input tax credit is not available:**

- Section 74 – Fraud or any wilful-misstatement or suppression of facts
- Section 129 – Detention of goods in case of non-compliances in transportation of goods
- Section 130 – Confiscation of goods and levy of penalty.

Input tax credit will not be available to companies where tax demand under show cause notice (SCN) demand is raised and paid in terms of Section 74 of the CGST Act, 2017.

**vi. What is the liability towards interest component?**

Interest liability is more likely to arise than not. Such interest liability would be calculated from the due date of payment up to the date of payment of tax. Practically, once the tax is paid, the amount of interest liability freezes.

### **3. What are the legal protections available to employment of Japanese expatriates in Indian subsidiaries?**

i. **Service Tax:** Under the Finance Act, 1994 (Service Tax law), there is a Negative List which provides that services provided by employees to employers are not chargeable under service tax.

ii. **GST:** Under the Central Goods and Services Tax Act, 2017 (GST law), Schedule III provides that services by an employee to the employer are outside the purview of GST.

iii. **Favourable Court Decisions on Service Tax / GST:** Several court decisions are in favour of the Indian companies. Additionally, below are the favourable cases which are pending before the Supreme Court:

- Nortel Networks India (CESTAT)
- Komatsu India (CESTAT)

iv. **Director's Remuneration:** CBIC issued a Circular on 10 June 2020 which clarifies that:

- a. Whole time director is an employee.
- b. He may function in dual capacity
- c. If payment is made as salary and withholding tax is deducted under the head salary, then the remuneration is considered as salary otherwise professional fees

v. **Favorable Court Decisions on Income Tax** – Analysis of court cases provides clarity on employer and employee relationship of expatriates working for India entity. If the purpose of expatriate is to work for Indian entity in accordance with terms of employment of Indian entity and Indian entity does not provide services of back-office support to foreign entity or Indian entity is not in the phase of initial business set-up, in such situations, the courts have concluded that expatriates are employees of Indian entity.

vi. **Consistency from the Government** - GST / Service tax department and Income tax department are different branches of Government of India. They cannot provide different views. For example, if the Income tax department says that withholding tax is required to be deducted in salary payment to expatriates then service tax / GST department cannot say that it is not a salary. (CESTAT on Rent Works India)

## vii. What is the demand towards penalty component?

- The tax authorities may issue a Show Cause Notice demanding GST on such transaction under Section 73 of the CGST Act, 2017. A penalty maximum upto 10% of the computed tax may be levied. However, in case payment is made within 30 days of issuance of the notice, no penalty would be applicable.
- Further, in case a notice is issued under Section 74 of the CGST Act, 2017, in addition to tax and interest, the Department may also demand penalty of up to 25% (increase upto 50%-100%) of tax. In this case, penalty (as determined by the officer) will be required to be discharged even if complete payment is made within 30 days of issuance of notice.
- Where GST liability is discharged pursuant to issuance of SCN under Section 74, companies would not be able to claim credit of GST so paid due to specific restriction provided under the GST law.

## What companies are doing in India?

Based on our experience, in most of the situations, the facts are not similar to the facts discussed in Supreme Court decision, hence, the Supreme Court's decision may not be applicable on several companies operating in India. Therefore, generally, the companies have been taking following actions:

- Reviewing the risk of GST as every company is having different facts and situations.
- Aligning the position of GST with Income Tax to avoid PE risk or risk of default in payment of withholding tax on fee for technical services.
- Improving documentation such as contracts and gathering evidence.

## Past GST Liability

- For the past GST liability, as the GST is not a cost for the companies, several companies have paid GST (under protest) and have taken input tax credit (ITC).
- Written an application to the tax office and explained that the Supreme Court decision is not applicable to them.
- Tax offices have been issuing show cause notices (SCN) and demand letters.
- For GST, Interest and Penalty, generally, companies are preferring to appeal once an order / result is obtained from the tax offices.

## Future GST Liability

- To avoid the interest liability, generally, several companies are making monthly GST payment (under protest) and taking input tax credit.
- Payment of GST (without protest) may lead to acceptance of salary payments to expatriates as 'Fee for Technical Services' which may result in withholding tax liability @ 10% or 20%, as applicable, along with interest and penalty.
- This may also result in exposure of risk of PE whereby the foreign entity may be asked to pay the corporate tax @ 40%.

## How HLS Global can support you?

- Review of existing documentation and evidence.
- Advisory on the strategy for the past and future GST liability and PE risks.
- Drafting of contracts based on the facts applicable to the companies and guidance available based on latest ruling by the Supreme Court and other judicial precedents.
- Representation before tax office and appellate bodies on behalf of companies.

## Queries?

If you have any queries about this article, please reach out to our experts:



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