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# Secondment Costs reimbursed to Overseas Group Entities are liable for Service Tax - Indian Supreme Court ruling

## Background

Supreme Court of India recently passed a judgement[1] where the question before the court was whether the overseas group companies, with whom the taxpayer had entered into agreements, provided it manpower supply services, for the discharge of its functions through seconded employees and is liable to Service Tax.

In this alert we have discuss the outcome of this judgement.

## Fact of the case

Northern Operating Systems Pvt. Ltd., India ("NOS India") had contracted with its overseas group entities for secondment of expatriate employees. The seconded employees worked under the directions and control of NOS India. However, the salary, bonus/incentives, social security, and welfare benefits of the seconded employees were paid by the overseas entities and subsequently reimbursed by NOS India on cost-to-cost basis.

The liability to pay service tax on such reimbursements by NOS India was the question before the apex court.

## Judgement

The apex court observed that the issue is the taxability of the cross charge, which is primarily based on who should be reckoned as an employer of the secondees. If the Indian company is treated as an employer, the payment would in effect be reimbursement and

[1] C.C.,C.E & S.T.- Bangalore Vs Northern Operating Systems Private Limited [Civil Appeal No. 2289-2293 of 2021].

not chargeable to tax in the hands of the overseas entity. However, in the event the overseas entity is treated as the employer, the arrangement would be treated as service by the overseas entity and taxed.

The apex court after reviewing all facts, analysing various case laws and adopting a "substance over form" approach concluded that NOS India is the service recipient, and the overseas entity can be said to have provided manpower supply service to NOS India. Though there is not one single determinative factor, the Hon'ble court made the following major observations influencing the judgement:

- The nature of business of overseas entities is to provide certain specialized services (back office, IT, bank related, inventories etc.) to its customers, which it gets done through its group companies for taking locational and economic advantages. As part of this arrangement, a secondment contract is entered into, whereby the overseas entities' employees possessing specific skill sets are deployed for the duration of secondment. The Secondment is "in relation to the business" of overseas entities.

- Though the seconded employees are under the control of NOS India and work under its direction, yet they remain on the payroll of the overseas entities. Their terms of employment, even during secondment, are in accord with the policy of overseas entities, who is their employer.

- On the cessation of secondment period, they have to be repatriated back.

- The other way of looking at the arrangement is the economic benefit derived by NOS India, which also secures jobs or assignments, from the overseas entities, which results in its revenue. The *quid pro quo* for the secondment agreement, where NOS India has the benefit of experts for limited period, is implicit in the overall scheme of things.

Accordingly, it was held that NOS India was liable to pay service tax under Reverse Charge Mechanism ("RCM") under the service tax law on the secondment costs cross charged by overseas entities.

## Our Comments

It may be noted that the said judgement is passed under the service tax law; accordingly, it is applicable till June 30, 2017 only. However, this judgement of Supreme Court may also apply under the present Goods & Service Tax ("GST") law (w.e.f July 1, 2017). In this judgement overseas entities were held to be providing manpower supply services to the Indian entity. Under the GST law since there is no separate definition of manpower supply services, this ruling may form the basis for the revenue authorities to allege that the ratio of this ruling should apply under GST law as well because service tax got subsumed in GST

law w.e.f. July 1, 2017. So, unless the facts are different, this ruling will pose a challenge for businesses having seconded employees. Further, this ruling could have implications under the income-tax laws.

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