Grant Thornton

#GTBharat
SHAPING A VIBRANT INDIA

Secondment of employees by overseas entity tantamount to supply of manpower services – Supreme Court

24 May 2022

Summary

The Supreme Court (SC) held that the assessee (Indian entity) was the recipient of the manpower recruitment service and the supply provided by the overseas entity concerning the employees seconded. The assessee benefited from experts for a limited period and derived economic benefits from such an arrangement. Further, the SC relied on the principle of substance over form and held that the cardinal principles of interpretation of documents implies that the nomenclature of any contract or document is not decisive of its nature but the court must evaluate overall reading of the documents and its effects. The SC noted that the seconded employees remained on the payroll of the overseas entity. Upon expiration of the secondment term, the employees would return to their overseas employer.

Facts of the case

- The assessee[1] entered into agreements with its group companies located outside India to provide general back-office and operational support. To facilitate this, the group entities provided certain technical personnel to the assessee to assist in the business.
- As per the agreement, the seconded employees would continue to be on the payroll of the overseas group entity but shall act under the instructions and directions of the assessee. Accordingly, the seconded employees would receive salary, bonus, social benefits, etc., from overseas group entities and shall be reimbursed from the assessee.
- Proceedings were initiated against the assessee for non-payment of service tax under manpower recruitment or supply agency service regarding the secondment agreements entered with the group companies.
- The assessee submitted that the service received from the group entity did not fall under the manpower recruitment or supply agency service prior to the negative list. Post the negative list, the provision of service by an employee to the employer concerning his employment has been expressly excluded. Thus, the amount paid to the foreign entity as reimbursement of salary cannot be construed as a consideration for the supply of manpower services.
- As a result, the assessee filed an appeal before the Customs, Excise and Service Tax Appellate Tribunal (CESTAT) Bangalore, which set aside the demand and passed an order in favour of the assessee.
- Therefore, the revenue filed appeal against the said order of the CESTAT before the SC.

CESTAT Bangalore observations and ruling[2]:

- **The agreement is for providing certain specialised services:** The group companies are not in the business of supplying manpower. The agreement is specifically for provision of certain specialised services. Further, the employees are seconded to the assessee and the payment of salaries to such employees by group companies is only for further disbursement. Hence, an

[1] Northern Operating Systems Pvt Ltd.

[2] Service Tax Appeal No. 22573 of 2014 order dated 23 December 2020

employer-employee relationship exists and does not fall under the taxable service of manpower recruitment or supply agency.

- **Establishment of a distinct employer-employee relationship:** The agreement does not establish a service provider- recipient relationship. Accordingly, there is a distinct employer-employee relationship between the seconded employee and the assessee. Also, disbursement of salary cannot determine the nature of transaction.
- **No supply of manpower service:** The arrangement is of continuous control and direction of the company to the seconded employees. Thus, such an arrangement is out of the ambit to be called as manpower supply service. Accordingly, the demand is to be set aside.

SC observations and ruling[3]:

- **Operational or functional control over seconded employees:** The assessee is potentially liable for the performance of tasks assigned to seconded employees. The seconded employees were performing the tasks relating to the assessee's activities and not in relation to the overseas employer. Therefore, the assessee had to reimburse the amounts equivalent to salaries of the seconded employees to the overseas entity as the overseas entity was obliged to maintain such employees on its payroll.
- **Overseas company has a pool of highly skilled employees:** The nature of the overseas entity business appears to be to secure contracts, which can be performed by its highly trained and skilled personnel. The role of the assessee is to optimise the economic edge to perform specific tasks given by the overseas employer. Therefore, the overseas entity's highly skilled employees are seconded to the Indian entity to complete such tasks. Upon cessation of the secondment term, they return to the overseas employer and are further deployed. Thus, it is evident that overseas companies have a highly skilled workforce pool.
- **Terms of employment as per the policy of overseas entity:** While the control over the performance of the seconded employees' work and the right to ask them to return if their functioning is not as it is desired, is with the assessee, the fact remains that their overseas employer in relation to its business deploys them to the assessee on secondment and pays them their salaries. Their terms of employment, even during the secondment, are in accordance with the policy of the overseas entity, who is the employer.
- **Assessee is a service recipient of overseas group company:** The assessee derives economic benefit from the overseas group companies, resulting in its revenues. The assessee has the benefits of experts for limited periods. The seconded employees for the duration of their secondment are under the control of the assessee and works under its direction. Thus, the assessee is held to be the service recipient of the overseas entity, which has provided manpower supply service.
- **Invocation of extended period of limitation is untenable:** In the court's considered view, the revenue's argument that the assessee had

[3] Civil Appeal No. 1390 / 2022, order dated 19 May 2022

indulged in wilful suppression is insubstantial. The revenue had discharged two show cause notices (SCNs) to the latter, which evidences that the assessee's view about its liability was neither untenable nor malafide. Thus, the revenue is not justified in invoking the extended period of limitation to fasten liability on the assessee.

- **Liable to pay service tax for period covered by SCNs:** The SC set aside the order of the tribunal and held that the assessee is liable to pay service tax for the periods mentioned in the SCNs, excluding any liability for the extended period of limitation.

Our comments:

This is a landmark ruling wherein the secondment of employees by an overseas entity to an Indian entity has been held to be a supply of manpower service and thereby exigible to service tax based on the principle of substance over form. The SC observed that in return of the secondment arrangement, the assessee has the benefit of experts for limited period and is deriving economic benefit from such arrangement.

The ruling will have widespread ramifications on similar secondment arrangements even under the GST regime. Therefore, the businesses must examine their agreements and revisit their tax positions.

However, it is pertinent to note that the SC has observed that the view held by the assessee about its liability was neither untenable nor mala fide. Therefore, the SC turned down revenue's contention of the wilful suppression of facts and held that the extended limitation period was not invokable.

Contact us

To know more, please visit **www.grantthornton.in** or contact any of our offices as mentioned below:

NEW DELHI
National Office,
Outer Circle,
L 41, Connaught Circus,
New Delhi - 110001
T +91 11 4278 7070

NEW DELHI
6th Floor, Worldmark 2,
Aerocity,
New Delhi - 110037
T +91 11 4952 7400

AHMEDABAD
Unit No - 603 B, 6th Floor,
Brigade International
Financial Center,
GIFT City Gandhinagar,
Ahmedabad - 382355
T +91 79 6900 2600

BENGALURU
5th Floor, 65/2, Block A,
Bagmane Tridib,
Bagmane Tech Park,
CV Raman Nagar,
Bengaluru - 560093
T +91 804 243 0700

CHANDIGARH
B-406A, 4th Floor,
L&T Elante Office Building,
Industrial Area Phase I,
Chandigarh - 160002
T +91 172 433 8000

CHENNAI
9th floor, A wing, Prestige
Polygon,471 Anna Salai,
Mylapore Division,Teynampet,
Chennai - 600035
T +91 44 4294 0000

DEHRADUN
Suite No 2211, 2nd Floor,
Building 2000, Michigan Avenue,
Doon Express Business Park,
Subhash Nagar,
Dehradun - 248002
T +91 135 264 6500

GURGAON
21st Floor, DLF Square,
Jacaranda Marg,
DLF Phase II,
Gurgaon - 122002
T +91 124 462 8000

HYDERABAD
Unit No - 1, 10th Floor,
My Home Twitza, APIIC,
Hyderabad Knowledge City,
Hyderabad - 500081
T +91 40 6630 8200

KOCHI
6th Floor, Modayil Centre Point,
Warriam Road Junction,
MG Road
Kochi - 682016
T +91 484 406 4541

KOLKATA
10C Hungerford Street,
5th Floor,
Kolkata - 700017
T +91 33 4050 8000

MUMBAI
11th Floor, Tower II,
One International Center,
SB Marg Prabhadevi (W),
Mumbai - 400013
T +91 22 6626 2600

MUMBAI
Kaledonia, 1st Floor,
C Wing,
(Opposite J&J Office),
Sahar Road, Andheri East,
Mumbai - 400069

NOIDA
Plot No 19A, 2nd Floor,
Sector - 16A,
Noida - 201301
T +91 120 485 5900

PUNE
3rd Floor, Unit No 310-312,
West Wing, Nyati Unitree,
Nagar Road, Yerwada
Pune - 411006
T +91 20 6744 8800

For more information or for any queries, write to us at **GTBharat@in.gt.com**

Follow us @GrantThorntonIN

© 2022 Grant Thornton Bharat LLP. All rights reserved.

"Grant Thornton Bharat" means Grant Thornton Advisory Private Limited, the sole member firm of Grant Thornton International Limited (UK) in India, and those legal entities which are its related parties as defined by the Companies Act, 2013, including Grant Thornton Bharat LLP.

Grant Thornton Bharat LLP, formerly Grant Thornton India LLP, is registered with limited liability with identity number AAA-7677 and has its registered office at L-41 Connaught Circus, New Delhi, 110001. References to Grant Thornton are to Grant Thornton International Ltd. (Grant Thornton International) or its member firms. Grant Thornton International and the member firms are not a worldwide partnership. Services are delivered independently by the member firms.