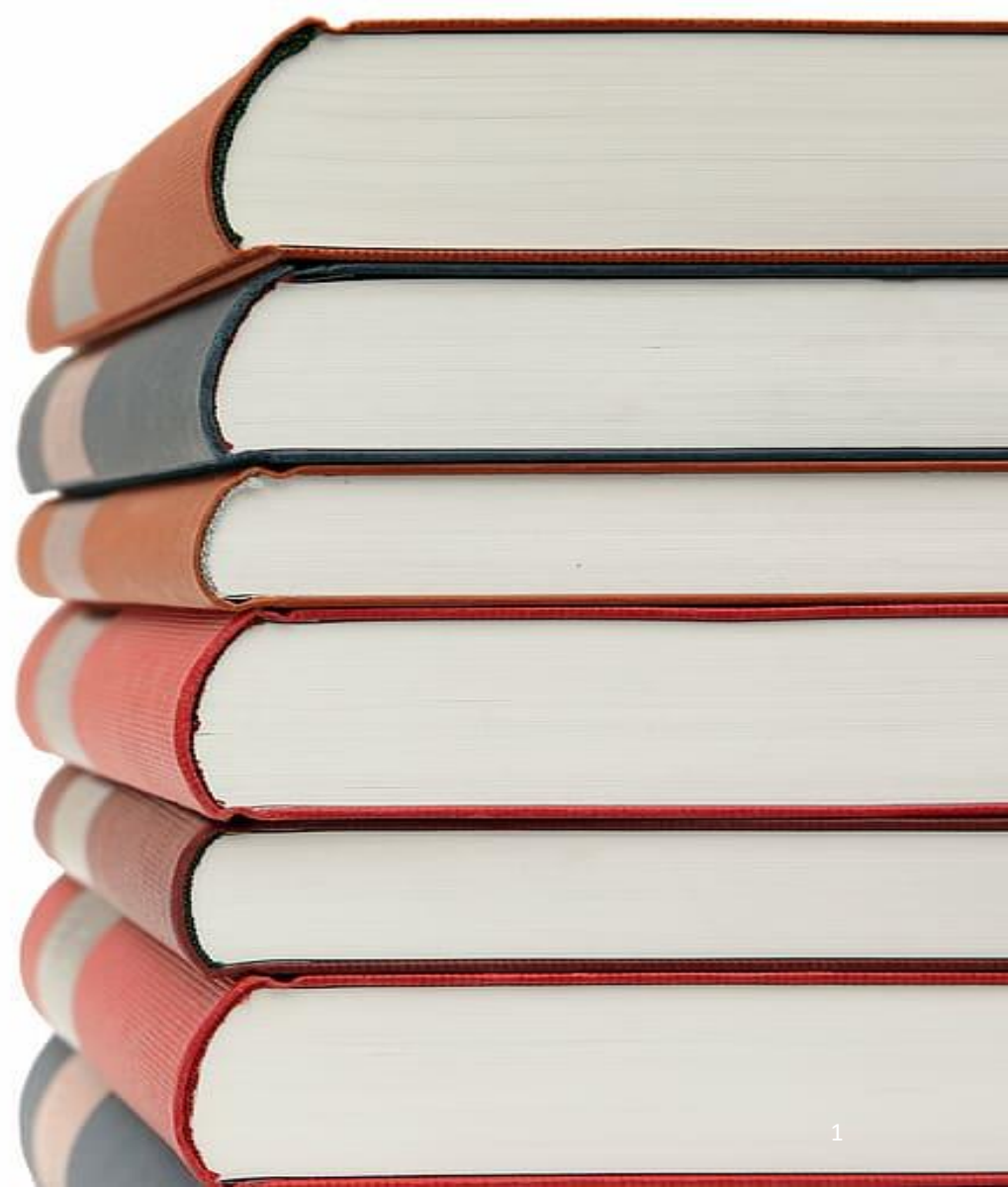


# GST applicable on Directors' Remuneration

April 2020




# No GST on Employer-Employee Relationship

Section 7 provides inclusive definition of Supply;



Sub-section (2) of Section 7 of the Act provides for activities or transactions which would neither be treated as supply of services nor supply of goods as mentioned in Schedule III;



Entry no. 1 of Schedule III specifies 'Services by an employee to the employer in the course of or in relation to his employment';



Accordingly, services of an employee to the employer in the course of or in relation to his employment is out of the ambit of GST;



# Services of Director is covered under RCM


- Services of Director is chargeable to GST and the service recipient making the payment of consideration against such service shall be liable to pay tax under reverse charge mechanism under Entry no. 6 to Notification no. 13/2017-Central Tax (Rates) dated 28-06-2017;

S.No.	Category of supply of services	Supplier of service	Recipient of Service
6	Services supplied by a director of a company or a body corporate to the said company or the body corporate.	A director of a company or a body corporate	The company or a body corporate located in the taxable territory.


- The important question is whether all services provided by Directors are covered under Reverse Charge Mechanism (RCM);

# Advance Ruling-RCM applicable on Director Remuneration

As per the recent GST Advance rulings of Karnataka and Rajasthan Authority of Advance Rulings, GST under reverse charge mechanism shall be applicable on payment of Directors' remuneration as per Entry no. 6 to Notification 13/2017-Central Tax (Rates);



In the ruling, Hon'ble authority has mentioned that Directors are not the employees of the companies therefore the payment of remuneration shall not be covered under Entry no. 1 to Schedule III. However, no reasoning has been provided in the ruling;



The ruling has not considered the facts that directors are appointed through an employment agreement with roles and responsibilities, given equal benefits and emoluments as per the employee policy, PF and TDS compliance as employee, issuing salary slips, etc.

# Judiciary - Director is an Employee

- As per below judgement of Hon'ble Supreme Court, it was held that **'Directors are employees under the provisions of ESI Act, 1948'**:
  - ESI Corporation vs Venus Alloy Pvt Ltd. (Civil Appeal No. 1464 of 2019 decided on 05<sup>th</sup> February 2019) – **Held that Director shall be covered under the definition of Employee under ESI Act.**
  - ESI Corporation vs Apex Engineering (1998) 1 SCC 86– **Held that 'Managing Director' is covered under the definition of Employee under ESI Act.**



# Requisites of Employer-Employee Relationship

- Concept of employment involves 3 ingredients:
  - (1) employer (2) employee and (3) the contract of employment.
- **Control and Supervision** by the Employer over Employee;
- Appointment through an **Employment contract agreed to both Employer and Employee;**
- Payment of **Salary on Regular Basis** and **Treatment of Payments under Tax and Other Regulatory Statutes;**

The above illustrative factors are essential features of Employer-Employee Relationship.



# RCM on Director's Remuneration (Pre-GST Regime)

- In the Pre-GST regime, this question was also litigative. However, CBEC<sup>1</sup> had clarified that **Managing Director performs management functions and does not provides consultancy services separately.**
- Also, MCA<sup>2</sup> in the year 2012 had clarified that **Non-Whole Time Director are not covered under the exemption hence payment of sitting fees/commission them are taxable under service tax.**
- Further, in various **judgements of Hon'ble CESTAT**, it has been held that where a director is providing services in the capacity of Employer-Employee capacity i.e. appointment of director is on **same terms as with other same designed employees, Salary structure, treatment of Salary in their personal income tax returns, working whole time with the company, Payment on regular basis**, etc., then the service tax was not leviable.

1. Circular no. 115/09/2209-ST dated 31-07-2009

2. Circular no. 24/2012 dated 09-08-2012



# Director under Companies Act, 2013

- **'Director'** defined under the Act as person appointed as Director.
- However, appointment of Director may or may not serve as Full time to the Company.
- A Director may be appointed for different purposes under Companies Act, 2013.

## Executive Director

Rule 2(1)(k) -Companies (Specification of definitions details) Rules, 2014

- Whole-Time Director
- Managing Director

## Non-Executive Director

Non Defined under Companies Act, 2013

- Independent Director
- Ordinary Director
- Other/Part-time Director



# Director under Companies Act, 2013

## Executive Director

Rule 2(1)(k) of the Companies (Specification of definitions details) Rules, 2014 “Executive Director” means a *Whole Time Director* as defined in clause (94) of section 2 of the Act”

## Whole Time Director

As per Clause 2(94) of Companies Act, 2013 ““whole-time director” includes a Director in the **whole-time employment** of the company.

## Managing Director

Clause 2(54) of Companies Act, 2013 defines “managing director” as director who, by virtue of the articles of a company or an agreement with the company or a resolution passed in its general meeting, or by its Board of Directors, is entrusted with substantial powers of management of the affairs of the company and includes a director occupying the position of managing director, by whatever name called.



# Factors\* to Decide Director is an Employee

Director appointed through an Appointment letter;

Roles, Responsibility and Remuneration should be part of Appointment letter;

Directors should be covered and regulated under Employee policy of the Company;

Any specific benefit to Directors should be supported by a reasonable basis;

Termination clause should be applicable as per Employee policy;

Any payment arise other than employer-employee relationship should be treated other than Salary;

TDS compliance and other Statutory compliance should be done accordingly by the company;

These are suggestive factors. We suggest to get the arrangement vetted from your Indirect Tax Consultants and if required, modify the arrangements accordingly;

# GST applicability on Various Directors

## Whole Time Director(WTD)/Managing Director (MD)

- WTD/MD is in whole time employment of the company;
- Provided other criteria is fulfilled;
- Payment of salary shall not be taxable under GST law;

## Independent Director/Ordinary Director

- Shall not be treated as employee as they are not employed by the company under employment contract;
- Any amount paid to them shall be taxable under GST under Reverse Charge Mechanism;

## Part-Time Director

- **Two School of Thoughts:**
  - If the company enters into employment agreement with them and makes the payment proportionate to other WTD, then the contract may qualify as employment contract. The GST authorities may still challenge this arrangement treating this as Consultancy services provided by the Part-Time Director to the Company;
  - The company comply with GST provision on payments made to the Part-Time Director;

# Questions?

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