

IMPACT OF GST ON BPO/KPO

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Business Process Outsourcing (“BPO”) and Knowledge Process Outsourcing (“KPO”) are engaged in providing back end support to Technology Support and were classifiable under the category of Business Auxiliary Service or Business Support Service upto 30.06.2012 under the selective based taxation regime and effective 01.07.2012 the classification is limited only for the purpose of remittance of service tax. We have in the ensuing paragraphs attempted to provide the impact of GST on BPO / KPO which are primarily service companies.

1. Levy of tax

The implication of GST for a BPO/KPO can be best understood with an illustration wherein a call centre has operation at multiple location as given below

Illustration - ABC Limited operates call centre at Bangalore and Pune. ABC Ltd has a client PQR Limited located in Delhi who has outsourced the customer call support to ABC Limited. The contract is entered by ABC Limited, Pune with PQR Limited and the billing is done from ABC Limited, Pune. The calls from the customer of PQR Limited can be routed to the customer executive located at Bangalore Unit or Pune Unit. The tax implications on the same under GST would be as under:

The entities having operations from more than one State will have to obtain separate registration in each such State where they are operating. Each operating location in different States will be treated as distinct persons and transactions between the two, whether with consideration or without consideration, will be liable to GST. Hence, in the above illustration, to the extent of work executed by Bangalore office towards the assignment, Bangalore Unit will have to raise invoice charging IGST on Pune office. Pune office will raise an invoice on PQR Limited charging IGST. Pune office will be entitled to avail credit of taxes charged by the Bangalore office and set it off against its liability of outward supplies.

Suppose in the above illustration, the customer PQR Limited is located outside India - transaction flow is same as above i.e. Pune raises invoice on the customer and Bangalore raises invoice on Pune. In this case, Bangalore unit will charge IGST on supplies made to Pune unit. The supply of service by Bangalore unit to Pune will be under Valuation Rules where value need to be arrived at (i) open market value, (ii) value of service of like kind or quality or (iii) cost of provision of service +10%. It is to be noted that these options are sequential i.e. one need to establish that determination of value under (i) is not possible before moving to (ii) and so on. To avoid determining open market value in case of revenue neutral transactions where recipient unit (Pune) is entitled to avail the credit, Bangalore may raise invoice valuing the services at its will and value declared in the invoice shall be considered to be open market value.

One should bear in mind that raising of invoice by one unit located in State A to another unit located in State B will not have any impact on the revenue / profitability of a taxable person but these transactions will be reconciliation item between the inward supplies and outwards supplies as per GST returns and expense and revenue as per financial statements.

IGST charged on supply of service by Bangalore to Pune shall be eligible as credit to Pune. Service provided by Pune to overseas client shall be in the nature of zero rated supply i.e. export of service in respect of which it shall have two options for export of service:

- Export on payment of IGST and claim refund of tax paid on export (which may be paid by utilising the ITC availed on input and input service including received from Bangalore)
- Export under bond/letter of undertaking without payment of IGST and claim refund of accumulated input tax credits

It is to be noted that filing and sanction of refund under GST would be easier where 90% of refund amount would be given to claimant within 7 days of filing of claim and balance 10% within 2 months from the date of making complete application, subject to post verification. The refund claim be filed online requiring no interaction with the department officers. The simplified and faster refund process is expected to reduce the accumulation of credits taking place with these industries under existing law.

2. Return filing

Presently service tax assessee are required to file two returns in a year to report the value of services rendered by them and the amount of credit availed / utilised by them. Additionally, they have an option of Centralised registration based on which they are required to file merely 2 returns during one year for all their locations across India. Under GST, service providers will not have an option of Centralised Registration and hence would be required to file monthly returns for each State from where they operate. Additionally each of these units will be assessed separately. Since majority of the BPO / KPO sector is engaged in provision of export services, unadjusted input tax credit would be available at different locations which would mean filing multiple state level refund claims for the same tax period as against under existing law where it can be filed at one centrally registered place.

3. Input service credit

BPO / KPO spend a lot of money on employees in the name of “employee experience” which includes free / subsidized food, cab facility, travel etc. A comparative table of ineligible input service credits as per the present CENVAT Rules, 2004 and as per GST Law which are relevant is provide below:

| Nature of Service | Eligibility – CENVAT Provisions | Eligibility – GST Provisions |
|--------------------------|--|---|
| Rent-a-Cab Services | Ineligible | Generally, ineligible. But eligible if : i) obligatory for employer to provide services to employees under any law for time being in force. Eg Cab services to be provided mandatorily for women employees working at night shift ii) The inward supply of said services is used for providing outward taxable supply of same category of services |

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|---|---|---|
| Food and Beverage | Ineligible – Primarily for personal use or consumption of employee (though view exist that when provided to all employees uniformly, not to be treated as primarily for personal use of employee and credit allowed) Eligible – Not primarily for personal use of employee. Eg Food served at Business Conference of Vendor / Customer Meeting | Ineligible |
| Outdoor catering, beauty treatment, health services, cosmetic and plastic surgery | Ineligible – Primarily for personal use or consumption of employee (alternate view as discussed above exists) | Ineligible |
| Membership of a club, health and fitness centre | Ineligible – Primarily for personal use or consumption of employee | Ineligible |
| Life insurance, health insurance | Ineligible – Primarily for personal use or consumption of employee | Generally ineligible. But eligible if: i) obligatory for employer to provide services to employees under any law for time being in force. ii) If the inward supply of said services is used for providing outward taxable supply of same category of services |
| Travel benefits extended to employees on vacation such as Leave or Home Travel Concession | Ineligible | Ineligible |

This indicates that few of the services presently could possibly be claimed as credits but in GST, the restriction has been more stringent and may not be availed as ITC resulting in increased cost of export.

4. Transactions between Related Persons

a. Overseas Parent Company

Supplies between related parties are liable to GST irrespective of whether such supplies are made for a consideration or not. Hence, any support received from the parent company (not being a loan transaction) including visit of Management Team of the Overseas Parent Company to oversee the operations of the local company, assistance in decision making, Central Human Resource Team which interviews candidates to be employed by the local company, extending of corporate guarantee etc. will be liable to GST. A review of these transactions will have to be conducted and a proper valuation mechanism has to be arrived taking into account the valuation rules under GST regime and the transfer pricing laws under Income Tax Laws for recording of these transactions and discharging of GST under reverse charge mechanism on the same.

b. Overseas Subsidiary Company

Inversely, support functions provided by a local company to its overseas subsidiary company would be treated as zero rated supply (viz. export of services) and will have to be accounted based on the valuation principals mentioned above. In the absence of consideration being realised in foreign currency (one of essential conditions of considering supply as export of service), the supply would be liable to IGST.

c. Employer and Employee Cost

Employer and Employee are treated as related persons under GST and hence supplies with or without consideration between employer and employee would also be liable to GST. A specific exclusion has been carved out here to provide that supplies by employee to employer in the course of employment will not be treated as supplies of goods and services and hence the same will not be liable to GST.

Accordingly, salary paid to employees based on the employment contract would not be liable to GST. However, supplies by employer to employee have not been excluded from the ambit of GST and hence the same will attract taxes. Sale of used laptops at nominal value to employees, subsidized food at canteen to employees etc would be liable to GST and since the transaction is between related parties, the fair market value of the supplies will have to be considered for computation of GST.

Gifts upto Rs 50,000 in a year by employer to employee would however not be liable to GST. And cash gifts will not be liable to GST since tax is applicable on goods and services and cash being money, is neither goods nor service. However, there could be Income Tax implications for cash gifts beyond Rs 5,000. Additionally, components of salary appearing under perquisite valuation could also be matter of debate and liable to GST.

5. Common Cost vs. Outward Supplies

There can be variants of transactions between Head office located in State A and Branch Office located in State B.

1. Head office located in a State can provide support services to its branch located in another State. Eg. Head Office maintaining the records of transactions of Branch office.
2. Head office incur expenses which may be common administration expenses for both Head Office and Branch. Eg. Head office outsources the accounting function to a third party.

First Scenario - As discussed supra, head office has to raise an invoice on the branch since both Head office and Branch are distinct persons.

Second Scenario - Head office to transfer credits to the extent it relates to the branch (turnover basis) using Input Service Distributor (ISD) route.

Before parting, it could be said that though there could be some increased compliance burden on the industry but it is expected that the faster disposal of refund would solve cash flow and credit accumulation problem of the industry.

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Acknowledgements

We thank Study Group on Indirect Taxes Bangalore for drafting this article and CA. Ashish Chaudhary for reviewing the same. For any queries, you may connect with CA. CA. Yeshwanth GN at yeshwanth@jcssglobal.com.

- Indirect Taxes Committee