

GST on Employee Transactions

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GST is applicable on “Supplies” of goods and services. The scope of the term “supplies” has been elaborately defined at Section 7 of the Central Goods and Services Tax Act, 2017 (“CGST Act”) which primarily includes transactions made for a consideration. However, in cases referred at Schedule I to the CGST Act, transactions are treated as supplies even if the consideration is absent which includes supplies between related persons when such supplies are made in the course or furtherance of business.

In this context, it would be relevant to note that the explanation appended to Section 15 of the CGST Act provides that employer and employee will be deemed to be “related persons”. Accordingly, supplies by employer to employees would be liable to GST even though these supplies are made without consideration since they are considered as related persons (except gifts upto Rs 50,000 which has been detailed at a later point in time in this document).

However, Schedule III to the CGST Act provides that “*services by employee to the employer in the course of or in relation to his employment*” will not be considered as supply of goods or services and hence GST is not applicable on services rendered by employee to employer provided they are in the course of or in relation to employment.

Hence, transactions which are excluded from the levy of tax for transactions between employee and employer are

1. Supply of services by employee to employer in the course of employment
2. Gifts by Employer to employee not exceeding Rs 50,000 in a Financial Year

Based on the above statutory provisions, we have in the ensuing paragraphs tried to analyse the tax impact on various transactions between the employer and employee

- a. **Providing of certain amenities v Deduction at concessional rate from salary towards amenities provided** – Former is a consideration for services offered by the employee to the employer and hence not liable to GST. Eg – Food provided to all the employees without any charge. Latter is a supply and to be valued at “Open Market” to discharge the tax. Eg – Food provided to employees at concessional rate and the amount is recovered from their salary;

- b. **Allowances v Reimbursements on actuals** – Allowances like Transport Allowance, Uniform Allowance etc. are part of the employment contract. These are considerations for service provided by employee to employer and not supplies by the employer and hence the same will not be liable to GST. With respect to reimbursements, employee has incurred costs which are expected to be reimbursed by the employer since the costs have been incurred on the behalf and at the instance of the employer. The employee will be able to claim reimbursement of the expenses based on the invoices received from the vendors. Different scenario's and possible implications
- Reimbursement of expenses relating to goods / services procured from registered supplier and the GST Number of the employer is quoted on the invoice – Vendor to charge tax (if taxable supplies) and employer entitled to claim credit subject to input tax credit restrictions
 - Reimbursement of expenses relating to goods / services procured from registered supplier and the GST Number of the employer is not quoted on the invoice – Vendor to charge tax (if taxable supplies). Employer not liable to GST under reverse charge since the procurements have been made from registered dealer except that the GST Number of the employer has not been quoted on the invoice
 - Reimbursement of expenses relating to goods / services procured from unregistered supplier (Assuming the Employer is located in State A)

Location of Supplier	Place of Supply	Illustration	Nature of Transaction	Taxability
State B	State B	Hotel Accommodation in State B	Intra State in State B	Not registered in State B and hence not taxable
State B	State A	Commission to Travel Agent in State B	Inter State in State A	Discharge tax under IGST in State A
State A	State A	Hotel Accommodation in State A	Intra State in State A	Discharge tax under CGST +SGST in State A

Based on the requirements of Income Tax Act, 1961, employers are required to collect invoices from employees for the purpose of allowing deduction for income tax computation. These are the cases where the employee has procured the goods / services for self and not for the employer and hence there will be no reverse charge mechanism liability even if the employee procures goods / services from unregistered person.

- c. **Gifts – Option or Compulsory** – Companies have a policy of giving gifts to employees. These could be Gifts on Birthday, Anniversary, Completion of specified period of service, Festivals etc. If these gifts are provided in cash – No tax since payment in cash is not a supply and hence not liable to GST (Income Tax provisions to be referred for cash gifts of Rs 5,000 and above). Non Cash gifts have been analysed below

- Gifts forming part of the Employment Contract – If the company is under an obligation to provide gifts based on the terms mentioned in the employment contract say Rs 5,000 worth gift will be given on Annual Day. The gift is consideration for the services rendered by employee and hence not liable to GST based on Schedule III. The issue which may arise here is – Is it a case of exchange of non-taxable supply by employee for taxable supply by employer?
- Gifts not forming part of the Employment Contract – Gratuitous Act of the employer to provide gifts to employees on the occasion of say company achieving Sales Target - These will be treated as supplies to employees without consideration and attract GST;

Please note that Gifts will be liable to GST only if the value of such taxable gifts exceed Rs 50,000 in a year.

With respect to credit of taxes paid on gifts on which GST is required to be paid, it would be important to note that Section 7 determines the tax levy on outward supplies and Section 17 determines the non-eligibility of credit. If the gift exceeds Rs 50,000 then based on the various provisions connected to Section 7, GST is required to be paid on such supplies. However, credit of GST paid on procurement of such gift will not be eligible merely because it has been used for making an outward supply. Since there exists a specific restriction on availment of credit on such gift, taxes paid on the same will not be eligible for tax credits.

- d. **Notice Pay Recovery** – Employees who resign from their job are expected to serve notice period as mentioned in the employment contract. If the employee does not serve such notice period, the salary of the unserved portion of notice period is retained by the employer. Thus, if the employer were to pay a salary of Rs 50,000 for a month and the unserved notice period is 15 days then the employer will pay only Rs 25,000 as salary to employee.

The payment of Rs 25,000 by the employer consists of two transactions

- Salary payable by the employer Rs 50,000 (Expense in accounting parlance) – Consideration to employee for employment covered under Schedule III and hence not liable to GST;
 - Notice pay recovery of Rs 25,000 (Savings in expense which can be viewed as income to the employer) – Consideration to the employer for “tolerating the act” of the employee to not serve the notice period which was the employee’s contractual obligation. This transaction is liable to GST.
- e. **Disposal or Sale at concessional rate** – Companies might allow employees to retain asset like laptop when he quits the organization or allow the employee to use a company asset for personal purposes. In such cases, the employer will have to pay taxes on the value of such assets irrespective of whether the credit is availed on such assets or not since this transaction will get covered under SI No 2 of Schedule I and not SI No 1 of Schedule I (SI No 1 of Schedule I gets attracted only when the assets on which credit is claimed are disposed off. However, since the transaction in the instant case is with the employee, GST will apply

even if input tax credit has not been claimed by the employer on these assets). Thus, pre GST procured assets provided to the employees free of charge will also be liable to GST.

Organizations offer their products at special price to employees. Eg – Ready Made Garment Trading Company may offer 25% employee discounts for procurements made by employees. In these cases the transaction definitely satisfies all the criteria's to qualify as a supply but since the transaction is between related parties being employee and employer, the valuation would be "open market" value and tax will have to be computed based on the value at which the same product is made available to third party / non employees. Accordingly, amount collected from the employee in this case would be Rs 75 (after Rs 25 discount for every Rs 100) but tax will be calculated on Rs 100.

Based on the above, we can observe that wrt employer employee transactions, there is more than what meets the eye. There are multiple off setting transactions which should not be considered based on the net result but needs to be examined individually to understand that the tax impact as well the credit eligibility. The employee contracts need to be re-worded to ensure that there is no tax loss.

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