

## APPLICABILITY OF GST TO EMPLOYEE PAYMENTS

### 1. INTRODUCTION

The Authority for Advance Ruling (“AAR”) in the case of **Bharat Oman Refineries Limited**<sup>1</sup> (“AAR Ruling”) has held that the following payments / benefits will be subject to Goods and Services Tax (“GST”):

- (A) payments made by employees to employers in lieu of serving the entire notice period;
- (B) insurance premiums recovered at actuals from existing employees for covering non-dependent parents and from retired employees for continuing to avail benefits under group insurance policies; and
- (C) value of canteen facility provided to employees and telephone charges recovered from them.

The AAR also answered specific questions on Input Tax Credit (“ITC”) with respect to the above.

### 2. SUMMARY OF THE RULING

Key aspects of the AAR Ruling are summarised below:

- (1) **Notice period payments.** The AAR held that payments made by employees to employers towards an early exit and in lieu of serving the full notice period specified under contract, will be subject to GST. Such payments will fall within Clause 5 (e) of Schedule II to the Central Goods and Services Tax Act, 2017 (“CGST Act”), i.e., ‘agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act’. The AAR held that by accepting payments in lieu of notice / by accepting a shorter notice period, the employer is tolerating the situation wherein the employee is not serving the agreed notice period. Therefore, such payments will be covered under the scope of supply of services under Section 7 of the CGST Act read with Schedule II of the said Act.

The AAR however did not accept an argument that notice period payments form part and parcel of employment contracts, and therefore should be treated as part of Schedule III (*Item 1 of which states that ‘services by an employee to the employer in the course of or in relation to his employment’ will not be considered supply of services*). The AAR also did not take on record judgments and orders under the earlier service tax regime, wherein similar payments were held not to attract service tax.

- (2) **Recovery of insurance premiums.** The AAR relied on the broad definition of ‘business’ under Section 2 (17) of the CGST Act, which includes the following: (a) any trade, commerce, manufacture ... or any other similar activity, whether or not it is for a pecuniary benefit; (b) any activity or transaction in connection with or incidental or ancillary to sub-clause (a); (c) any activity or transaction in the

<sup>1</sup> M/s Bharat Oman Refineries Limited, AAR (Madhya Pradesh), Order No. 02/2021 dated 07/06/2021

nature of sub-clause (a), whether or not there is volume, frequency, continuity or regularity of such transaction. The AAR held that the company did not extend benefits under group insurance policies to non-dependent parents and to retired employees merely as an agent of the insurance company. Thus, insurance premiums recovered from the employees towards covering non-dependent parents / retired employees at actuals will constitute supply in the course of business (*given the expansive definition of business under the CGST Act*) and subject to GST.

- (3) **Provision of canteen services to employees and recovery of telephone charges from employees.** The AAR once again relied on the broad definition of 'business' under the CGST Act and held that: (a) provision of canteen services by the employer is a statutory obligation under the Factories Act, 1948 and would form part of its business. Therefore, any recovery from employees for canteen facilities provided (even if a nominal sum) will be considered 'outward supply' and subject to GST (*valuation would be as per rules specified for transactions between related parties*). Even if the canteen services were provided free of cost, it still be subject to GST; (b) recovery of telephone charges from employees at actuals will also attract GST.
- (4) **Eligibility to ITC.** The AAR held that other than in respect of canteen services, the employer will be able to avail ITC in respect of recovery of telephone charges and insurance premiums.

### 3. INDUSLAW VIEW

The AAR Ruling follows on the heels of a similar one in the case of **Amneal Pharmaceuticals**<sup>2</sup> wherein payments made by employees in lieu of serving the entire notice period was held to attract GST.

Interestingly, two important issues emerge from this AAR Ruling. Firstly, the AAR Ruling ignores the aspect that the applicable entries under the Service Tax law (tolerating an act) and under the GST are *pari materia*. Therefore, the earlier judgments including that of the Madras High Court<sup>3</sup> and that of the Tribunal<sup>4</sup> will continue to hold fort. Secondly, the Tax Department's view which was put forth by the Jurisdictional Officer was that GST is **not** payable on these activities. The AAR Ruling also does not comment on this aspect. Therefore, the fact that the Tax Department itself holds a view that such recoveries are not chargeable to GST, would be helpful for other assesseees, especially in the State of Madhya Pradesh.

While AAR rulings are typically binding only on the applicant and the jurisdictional officer concerned, they do provide valuable insight on the authority's interpretation of the provisions of the CGST Act. Given that a fair number of employers do permit employees to leave early, this ruling will definitely be useful to examine the GST impact (if any) of such notice period payments made by employees. Also, employers could, while structuring various employee benefits and reimbursements, not only examine their impact from a Wage Code and income tax perspective but also understand in detail, whether any recoveries made from employees would result in liability under the GST regime.

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<sup>2</sup> ADVANCE RULING NO. GUJ/GAAR/R/51/2020 dated July 30, 2020

<sup>3</sup> GE T&D India Limited v. Deputy Commissioner of Central Excise, Chennai 2020 (35) GSTL 89 (Mad.)

<sup>4</sup> HCL Learning Limited v. CCE, Noida 2019 (12) TMI 558 - CESTAT Allahabad

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