

Salary paid to directors liable to GST under reverse charge: Rajasthan AAR

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Summary

The Rajasthan Authority for Advance Ruling (AAR) has held that remuneration/salary paid to directors (including a part-time directors) is liable to Goods and Services Tax (GST) under reverse charge mechanism (RCM). In this regard, the AAR stated that:

- The company is the service recipient and directors are service providers.
- The salary paid to the directors is the consideration for services provided by them.
- The directors are not employee of the company. So, their services, for which the consideration is paid by the company under any head, are liable to GST under RCM.

Facts of the case

- The applicant¹ is engaged in manufacturing of bone china crockery, transfer sheet decalcomania, other utensils item and moulds and dies.
- The directors of the applicant are working as employee, for which they receive regular salary and other allowances as per the policy and as per the employment contract. Tax at source is deducted from such salary payment. Applicable Provident Fund (PF) is also deposited.
- The applicant filed an advance ruling before the authority to determine whether the salary/remuneration paid by it to its directors is liable to the GST under RCM².

Applicant's contentions

- The applicant is paying the GST under RCM on **commission** paid to its directors as such the

amount pertains to service provided by them in the capacity of a director.

- Applying legal provisions and on perusal of Memorandum of Association and Articles of Association of the Applicant, it is clear that it is the board that appoint the directors and once it is admitted that there is an appointment, then it is obvious that there exist a relationship of employer and employee between the board of directors and managing director / whole-time director.
- The salary being paid to the directors is being booked under '**income from salary**' by the directors in their income tax returns.
- The services provided by employee to employer are neither treated as supply of goods nor as supply of services³.

¹ M/s Clay Craft India Pvt. Ltd.

² Notification No. 13/2017 – Central Tax (Rate) dated 28 June 2017

³ Clause 1 of Schedule III to CGST Act, 2017

- The directors who are working as whole-time directors are de-facto employees of the applicant and are being treated as an employee at par with other employees. Thus, the payments made to them as salary are not liable to GST under RCM.

Rajasthan AAR observations and order

- **Consideration is against the services provided:** The consideration in form of salary and commission paid to the directors is against the services provided by them to the applicant and the applicant is the service recipient and directors are the service provider.

- **Director is not employee:** The consideration paid to the directors is against the supply of services and are neither covered under the activities nor treated as supply⁴.
- **Salary liable to GST under RCM:** The applicant is located in taxable territory and the director's consideration is paid for supply of services by the directors to the applicant and hence the same is liable to GST under RCM.

Our comments

The provisions under the GST law are quite clear. The services rendered by employee to employer in the course of employment are neither supply of services nor supply of goods. Accordingly, they are outside the purview of the GST. The AAR, in the instant case, has not considered the fact that the directors are offering their incomes to tax as an income from salary. Further, even the company is treating the payout as a salary for the purpose of deducting tax at source. Also, PF laws are applicable to the directors. While the consideration paid as sitting fee/commission to directors may get covered under RCM, the salary component per se is outside GST purview. Thus, the ruling seems to be contrary to the settled legal position and contrary to the intention of the legislature.

It is pertinent to mention here that AAR's decision is applicable only to the applicant, however, there is possibility that department may apply this ruling as an interpretation to issue demand notices in other cases as well. A clarification from the government on this issue will surely be helpful in mitigating future litigation on this account.

⁴ Under Clause 1 of Schedule III to the CGST Act, 2017

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