

GST ON DIRECTORS' REMUNERATION

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This Article analyses various AARs to understand the applicability of GST on remuneration paid to directors

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❖ Introduction

The purpose of introduction of GST was to eliminate most of the issues/concerns faced in the erstwhile laws and to provide for a non-litigative platform to businesses. The GST Law has seen its initial teething troubles in the form of GST portal issues but now with the law being almost three years old, it is time to expect legal issues of the GST Law.

In this article, we wish to highlight the controversy of applicability of GST on Director Remuneration which is a result of entry no 6 in Notification No 13/2017 - Central Tax (Rate) dated 28.06.2017. The said entry aims at applying the provisions of Reverse Charge Mechanism on services supplied by a director of a company or a body corporate to the said company or the body corporate, where GST has to be paid by the Company or Body Corporate who has received services from the Director. In order to understand the applicability of such provision, it is necessary for us to understand the types of directors in a company, nature of service they provide (whether as an employee or as an independent consultant), nature of fees charged (whether as a salary or professional fees).

❖ Who is Director of the company?

The term "Director" has not been defined under the GST Law and accordingly reference may be made to the provisions of Companies Act. According to section 2(34) of the Companies Act "Director" means a director appointed to the board of a company.

- There are different types of director as per the Companies Act such as -
 - Executive Director
 - Non-Executive Director
 - Whole Time Director
 - Managing Director
 - Independent Director

Directors are the individuals who are appointed to manage the business affairs of a company. Directors hold different positions and powers in a company. The division of power helps in maintaining a fair and transparent system. Moreover, the distribution of control keeps a check on abuse of power and increases efficiency. It may be relevant to highlight that in spite of the above different nomenclature of Director's, one can broadly classify the types of Directors into two broad categories. One, a person who is actively involved in the day to day operations of the Company and the other who is not involve in the day to day activities but merely overlooks the policies of the Company.

These directors are paid for their services in form of percentage of profits, monthly remuneration, sitting fees, sweat equities, ESOP or combination of the above. Generally, the

remuneration to be paid to the directors is covered under Article of Association (AOA) or is decided at the time of their appointment in Board/General meeting along with relevant roles and responsibilities. Generally, the first set of Directors as explained above are not provided with sitting fees whereas the second set of Directors are provided only with sitting fees.

So one can determine the nature of payment made to director from the roles and responsibilities he is entrusted with.

❖ **Schedule III of CGST Act**

Activities or transactions which shall be treated neither as a supply of goods nor a supply of services are provided in Schedule III of CGST Act wherein clause 1 read as “**Services by an employee to the employer in the course of or in relation to his employment**”, hence any services provided by employee in course of employment are not liable to GST.

❖ **Treatment under Income Tax Act, 1961**

Under the Income tax Act **Section 194J (1)** provides that
“Any person, not being an individual or a Hindu undivided family, who is responsible for paying to a resident any sum by way of –
(ba) any remuneration or fees or commission by whatever name called, **other than those on which tax is deductible under section 192, to a director of a company**, shall, at the time of credit of such sum to the account of the payee or at the time of payment thereof in cash or by issue of a cheque or draft or by any other mode, whichever is earlier, deduct an amount equal to ten per cent of such sum as income-tax on income comprised therein”

Thus, from the above we can say that the remuneration paid to directors can be subject to TDS u/s 192 of the Income Tax Act, 1961. Section 192 provides for deduction of TDS in case of payments which are Salary.

Also, Directors file their income tax return showing remuneration under the head Income from Salary. Income Tax Department also assesses the same under the head “Income from Salary”.

One should also refer to the judicial decision which are decided in the context of Income Tax Law.

In case of CIT v. Gira Sarabhai (Smt.) [1994] 209 ITR 356 (Guj.), Gujarat High Court stated that the nature of a director’s employment may be determined by the Articles of Association of a company and the service agreement, if any, under which a contractual relationship

between the director and the company has been brought about to check the existence of the relationship of a master and servant.

In the case of *Satya Paul vs CIT* [1979] 116 ITR 335 (Cal.), it has been stated that if Articles of the company confers a specific right to the company to remove any director before the expiration of his period of office by an extraordinary resolution and if he were so removed he would automatically be dismissed from the office of the managing director, the director could be considered as an employee of the company.

Further, Hon'ble Supreme Court in the case of *Ram Pershad vs Commissioner of Income Tax* [1972 1973 AIR 637], it was held that the Director in question had to exercise his powers within the prescribed terms and conditions and subject to the supervision and control of the Directors which indicated his employment as a servant of the company. Therefore, his remuneration was to be categorized as salary.

❖ **Judicial updates under Service Tax Law**

Effective from 7th August 2012, Notification no. 30/2012-ST dated 20th June 2012 was been modified to include services provided by Director under reverse charge mechanism. Further, the taxability of services by director was brought within the Service tax ambit from 1st July 2012 after introduction of negative list.

There have been judicial pronouncements pertaining to the period after July 2012 which have considered the liability of Service tax on such services.

In the case of *Maithan Alloys Ltd vs CCE & ST* [2019-CESTAT-KOL], it has been provided that remuneration paid to whole time director was pursuant to employer - employee relationship and the mere compensation through variable pay could not alter or dilute the position. The provisions of Companies Act 2013 considering the whole-time director as officer in default and deduction of TDS under salary within the Income Tax Act 1961 further fortified this position.

In the case of *Allied Blenders and Distillers Pvt Ltd* [2019 Mumbai - CESTAT), the company had paid to four whole-time Directors for managing day to day affairs and had made relevant deductions for TDS, Professional Tax and Provident Fund. It was held that it was crystal clear from the documents of such statutory authorities that the remuneration paid by the company was in the nature of salary and such directors were only employees of the company.

In *Brahm Alloy Limited vs Commissioner Durgapur* [2019 Tri - Cal], it was held that the Resolution of the company should cover both, the terms of appointment/hiring of the services of the individual and similarly it should also cover that in case of non-performance of the

specified duties, the individual shall be fired and/or his appointment would be terminated which should be essential ingredients of the employer employee relationship.

❖ **Advance ruling on RCM in case of remuneration to Director under GST Act**

➤ 1st AAR ruling

AAR of Rajasthan in case M/s Clay Craft India Private Limited [RAJ]/AAR/2019-20/33] has held that remuneration paid to director is liable for reverse charge and ignored the following submissions made by the applicant -

- 1) Directors are also working apart from working as Board of Directors in the company at different level like procurement of raw material, production, quality checks, dispatch, accounting etc.
- 2) They are working as an Employee of the company.
- 3) Salary is regularly paid to the directors, TDS is also being deducted as applicable on salary u/s 192, Provident Fund and other benefit is also the same at par with other employees and as per company policy, etc.

Despite above submission AAR has held that director is not the employee of the company and the Consideration paid to director is covered under RCM

➤ 2nd AAR ruling

Advance Ruling No. KAR ADRG 30/2020 in case of M/s. Anil Kumar Agrawal -

In this case, the applicant being a unregistered person seeking Advance Ruling as to whether income received from various sources form part of the “Aggregate Turnover” for the purpose of obtaining registration under section 25 of GST Act in which the **applicant was also in receipt of certain amount as salary in capacity of Director of a private limited company**, thus this preposition fairly relates to issue in hand wherein it was ruled as under -

Two possibilities where decided in the said ruling which are as under -

The first possibility that the applicant is the employee of the said company (Executive Director), in which case the services of the applicant as an employee to the employer are neither treated as supply of goods nor as supply of services, in terms of Schedule III of CGST Act 2017.

The second possibility that the applicant is the nominated director (non Executive Director) of the company and provides the services to the said company. In this case the remuneration paid by the company is exigible to GST in the hands of the company under reverse charge mechanism under section 9(3) of the CGST Act 2017.

In view of the above, the remuneration received by the applicant as Executive Director is not includable in the aggregate turnover, as it is the value of the services supplied by the applicant being an employee. Further if the applicant receives the remuneration as a Non-Executive Director, such remuneration is liable to tax under reverse charge mechanism under section 9(3) of the CGST Act 2017.

❖ **Conclusion**

Services in the capacity of a non-employee director shall only be chargeable to GST under the reverse charge mechanism. Services of a director can be determined by nature of a director's employment as specified by the Articles of Association of a company and the service agreement, if any, and thus if such services rendered result in services provided in capacity of an employee it shall be outside the ambit of GST. However, Ruling pronounced in the case of Clay Craft India Pvt Ltd by Rajasthan Authority of advance ruling required reconsideration in our opinion.

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