

Karnataka Authority for Advance Ruling: GST not payable on the remuneration paid to the executive directors

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1 Background

One of the major concerns of companies since the introduction of Goods and Services Tax (GST) laws in India has been the taxability of remuneration paid by them to their directors.

Directors, based on their role and relationship with the company, can be categorised as:

- a. executive directors,
- b. non-executive directors, and
- c. independent directors.

While all three categories of directors are considered agents and 'trustees' of a company, only executive directors additionally share an employer-employee relationship with the company.

Under GST laws, services rendered by an employee to an employer in the course of employment are not taxable. However, services provided by a director to a body corporate are treated as a taxable supply under GST laws, and is expressly recognized under notification no. 13/2017-Central Tax (Rate) dated 28 June 2017 (**Notification**). In terms of the Notification, the services provided by a director to a company are taxable on reverse charge basis i.e. the tax would be payable by the company, who is the recipient of the service.

Therefore, there is an apparent contradiction between the two sets of provisions of GST. The provisions seeking to tax services rendered by a director does not take cognizance of various types of directorship which exist in companies. Consequently, it purports to tax even such activities of directors that are carried out in the capacity of an employee of a company, which are otherwise not taxable.

Karnataka Authority for Advance Ruling, in the application made by Mr. Anil Kumar Agarwal, has held that GST would not be payable on the remuneration paid to an executive director of a company as such engagement would be in the nature of employment.

Previously, taxpayers have approached the Authorities for Advance Ruling (**AAR**), in Karnataka in the case of *M/s. Alcon Consulting Engineers (India) Pvt. Ltd.*, and in Rajasthan, in the case of *M/s. Clay Craft India Pvt. Ltd.*, to obtain clarity on this issue. In both these rulings, the AAR failed to take into consideration the distinction between different types of directors and summarily held the remuneration being paid to the director to be taxable.

2 Karnataka AAR Ruling in Anil Kumar Agarwal

In the present ruling, the Karnataka AAR examined the capacity in which the director was receiving remuneration. The AAR noted that there could be two possible scenarios in relation to the remuneration being received by the applicant.

The first, is where the applicant is an executive director of the company. In this case, the applicant would be considered an employee of the company and the remuneration received by him in that capacity would not be included in the aggregate turnover for GST purposes.

The second possibility is where the applicant is a non-executive or independent director. In this case, the remuneration received by the director would be taxable in accordance with the Notification.

In the present case, the AAR observed that since the applicant had failed to provide documentation like appointment letter, employee state insurance details or provident fund deductions to evidence that the remuneration received by him was in the capacity of an employee, it was not possible to conclude the status of the applicant. However, the AAR recorded that the taxability of the remuneration would be guided by the two scenarios discussed by it.

3 Conclusion

This ruling is a step in the right direction as it not only acknowledges the distinction between different types of directors but also lays down the correct guiding principles regarding the taxability of remuneration paid to directors. It is also indicative of the documentary evidence which companies or the directors may rely on to determine the treatment of the remuneration and also, for defending such treatment before the GST authorities, if required.

However, an order of the AAR is technically only binding on the specific applicant and the tax department with respect to that applicant's case. As mentioned earlier in our update, there are a couple of AAR rulings where a contrary view has been taken (one of them being the same Karnataka AAR). Therefore, this issue remains far from settled.

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