



SC Ruling on Service Tax on secondment services of employees of overseas group company

Northern Operating Systems Private Limited

Background

Recently, the Supreme Court decided on the taxability of secondment arrangements in the context of service tax in the case of Northern Operating Systems (NOS). Secondment arrangements have been in litigation for their implications under the income tax and other allied laws. This article seeks to evaluate the effect of the above decision on income tax and the allied laws.

Typical structure of secondment and the Supreme Court's decision

The Supreme Court captured the essence of the secondment arrangement in the following words:

‘The contemporary global economy has witnessed rapid cross-border arrangements for which dynamic mobile workforces are optimal. To leverage talent within a transnational group, employees are frequently seconded to affiliated or group companies based on business considerations. In a typical secondment arrangement, employees of overseas entities are deputed to the host entity (Indian company in the present context) on the latter's request to meet its specific needs and requirements. During the arrangement, the secondees work under the control and supervision of the Indian company. Social security laws of the overseas country (of the secondees) and business considerations result in payroll retention and salary payment by the overseas entity, which is claimed as reimbursement from the Indian company’.

The court noted the following terms and conditions of the arrangement:

1. The overseas entity assigns certain tasks to the Indian company.
2. The Indian company is remunerated on a cost-plus model.
3. Through the secondment agreement, the parties agree that the overseas employee is temporarily loaned to the Indian company.
4. During the period of secondment, the Indian company exercises control and supervision over the employee and (as contented by the taxpayer) becomes its contractual employer.
5. The Indian company can require the seconded employee to return, and, likewise, the employee has the discretion to terminate the relationship.
6. The overseas entity, viz. the legal employer, pays the seconded employee and is later reimbursed by the Indian company.
7. The Indian company is responsible for the work of the seconded employee, i.e. during the secondment period, and the overseas entity is absolved of any liability for the job or work of its seconded employees.
8. The secondment is for a specified duration.
9. At the conclusion of secondment, the secondees rejoin the overseas entity.



After deliberations, the court drew inferences and made the following observations:

1. There is no single determinative factor to decide whether a contract is for service or of service.
2. A vital fact to be considered in this case is that the nature of the overseas entity's business appears to be to secure contracts, which can be done by its highly trained and skilled personnel. Taking advantage of the globalised economy, and having regard to locational advantages, the overseas entity enters into agreements with its affiliates or local companies, such as the Indian company. The overseas employer deploys the secondees to the Indian company in relation to its business requirements, as it has sub-contracted some of its work to the Indian company.
3. The fact remains that secondees are on the payroll of their overseas employer and return to it after the tenure of secondment expires.
4. The letter of understanding between the Indian company and seconded employee states nowhere that the latter would be treated as the former's employee after the secondment period.
5. The nature of the salary and other perks underscores the fact that the seconded employees possess a certain skill and expertise the Indian company requires.
6. The overseas employer, for whatever reason, pays salary to the secondees.
7. The secondees' terms of employment, even during the secondment, are in accordance with the policy of the overseas company, which is their employer.

After noting the above facts and inferences, the Supreme Court held that the overseas company remains the employer and tacitly denied the secondees' employment relationship with the Indian company. This led to the conclusion that the case involved the provision of manpower supply services that are taxable under the service tax law.