

# RCM on Remuneration to the Director



*Shri Tapas Majumder,  
Advocate*

## **Ambiguity under Reverse Charge Mechanism in respect of certain payment of remuneration to the directors of the company**

The causes of the Reverse Charge Mechanism popularly called as RCM is inclusively and absolutely listed under the law, where the listed elements are being brought under the RCM and out of such some elements are either covered under the Forward Charge Mechanism (Herein after called as FCM) else under Reverse Charge Mechanism and as an element of charges of the company paying to the directors is also covered mostly under the RCM and in frequent cases under FCM.

**As per Schedule III** any services rendered by an employee to the employer in course of or in relation to his/her employment is absolutely beyond the purview of Supply under GST. And as such the remuneration received by an employee in course of his/her employment is not covered under Supply which entails no GST will be applicable thereon. And based on the entity concept under the historical accounting method any service provided by the director to his/her company is off course a service rendered to his/her employer. During the course of the employment it's also inherent that apart from his/her service to the company such director may provide

any rental facility derived from that particular director's property under the capacity of pure assignment basis such as tenancy, lease, leave and license facility etc. and/or any service under his/her professional capacity derived from that particular director's office or under his/her professional capacity.

The relevant questions are appearing herein whether the service generated under professional capacity derived from the separate office of the director or within the premises of the company where such director is rendering his/her pure professional services thereon are absolutely beyond the purview of in course of employment but the same is very much difficult to ascertain whether such director is rendering services in course of his/her employment or not, although the other services such as assignment of the property, sale or purchase of the property are undoubtedly covered under other heads of income except from the source of employment but the professional service can hardly be identifiable whether such is in course of the employment or purely a professional service.

In order to resolve such disputes the department lately after almost three years from the inception of its applicability issued a circular vide no.140/10/2020 dt.10.06.2020 where the services rendered by the director

is categorically divided into two parts as under.

- (i) *leviability of GST on remuneration paid by companies to the independent directors defined in terms of section 149(6) of the Companies Act, 2013 or those directors who are not the employees of the said company; and*
- (ii) *leviability of GST on remuneration paid by companies to the whole-time directors including managing director who are employees of the said company.*

3. In order to ensure uniformity in the implementation of the provisions of the law across the field formations, the Board, in exercise of its powers conferred under section 168(1) of the CGST Act hereby clarifies the issue as below:

***Leviability of GST on remuneration paid by companies to the independent directors or those directors who are not the employee of the said company***

4.1 The primary issue to be decided is whether or not a "Director" is an employee of the company. In this regard, from the perusal of the relevant provisions of the Companies Act, 2013, it can be inferred that:

- a. *the definition of a whole time-director under section 2(94) of the Companies Act, 2013 is an inclusive definition, and thus he **may be a person who is not an employee** of the company.*
- b. *the definition of "independent directors" under section 149(6) of the Companies Act, 2013, read with Rule 12 of Companies (Share Capital and Debentures) Rules, 2014 makes it amply clear that **such director should not have been an employee** or proprietor or a partner of the said company, in any of the three financial years immediately preceding the financial year in which he is proposed to be appointed in the said company.*

4.2 Therefore, in respect of such directors who are not the employees of the said company, the services provided by them to the Company, in lieu of remuneration as the consideration for the said services, are clearly outside the scope of Schedule III of the CGST Act and are therefore taxable. In terms of entry at Sl. No. 6 of the Table annexed to notification No. 13/2017 – Central Tax (Rate) dated 28.06.2017, the recipient of the said services i.e. the Company, is liable to discharge the applicable GST on it

on reverse charge basis even recently it's clarified in the Circular vide no. 201/13/2023 dt.01.08.2023.

4.3 Accordingly, it is hereby clarified that the remuneration paid by such independent directors, or those directors, by whatever name called, who are not employees of the said company, is taxable in hands of the company, on reverse charge basis.

**Leviability of GST on remuneration paid by companies to the directors, who are also an employee of the said company**

5.1 Once, it has been ascertained whether a director, irrespective of name and designation, is an employee, it would be pertinent to examine whether all the activities performed by the director are in the course of employer-employee relation (i.e. a "contract of service") or is there any element of "contract for service". The issue has been deliberated by various courts and it has been held that a director who has also taken an employment in the company may be functioning in dual capacities, namely, one as a director of the company and the other on the basis of the contractual relationship of master and servant with the company, i.e. under a contract of service (employment) entered into with the company.

5.2 It is also pertinent to note that similar identification (to that in Para 5.1 above) and treatment of the Directors remuneration is also present in the Income Tax Act, 1961 wherein the salaries paid to directors are subject to Tax Deducted at Source ('TDS') under Section 192 of the Income Tax Act, 1961 (IT Act). However, in cases where the remuneration is in the nature of professional fees and not salary, the same is liable for deduction under Section 194J of the IT Act.

5.3 Accordingly, it is clarified that the part of Directors remuneration which are declared as "Salaries" in the books of a company and subjected to TDS under Section 192 of the IT Act, are not taxable being consideration for services by an employee to the employer in the course of or in relation to his employment in terms of Schedule III of the CGST Act, 2017.

5.4 It is further clarified that the part of employee Directors remuneration which is declared separately other than "salaries" in the Company's accounts and subjected to TDS under Section 194J of the IT Act as Fees for professional or Technical Services shall be treated as consideration for providing services which are outside the scope of



Schedule III of the CGST Act, and is therefore, taxable. Further, in terms of notification No. 13/2017 – Central Tax (Rate) dated 28.06.2017, the recipient of the said services i.e. the Company, is liable to discharge the applicable GST on it on reverse charge basis.

Hence on the basis of such circular the ambiguity appears where a director is providing his/her services not as a whole time director whether such remuneration will be covered under RCM or not even the remuneration is deductible U/s 192 of the IT Act but due to the threshold limit such remuneration is not deductible under income tax.

To resolve such disputes recently on 01.8.2023 a circular vide no.201/13/2023-GST has been issued and clarified as under.

“2.1 Entry No. 6 of notification No. 13/2017 CTR dated 28.06.2017 provides that tax on services supplied by director of a company or a body corporate to the said company or the body corporate shall be paid by the company or the body corporate under Reverse Charge Mechanism.

2.2 It is hereby clarified that services supplied by a director of a company or body corporate to the company or body corporate in his private or personal capacity such as services supplied by way of renting of immovable property to the company or body corporate are not taxable under RCM. Only those services supplied by director of company or body corporate, which are supplied by him as or in the capacity of director of that company or body corporate

shall be taxable under RCM in the hands of the company or body corporate under notification No. 13/2017-CTR (Sl. No. 6) dated 28.06.2017.

Hence it creates some ambiguity whether services rendered under the capacity of a director is covered under RCM or not in respect of the quantum of services which is below the taxable limit under the Income Tax Act where deduction of tax U/s 192 of the said Act is at all not been made by the company. But as per my view if we conjugate the mandate as provided under Schedule III as well as the departmental directives vide Circular no. 201/13/2023 dt.01.08.2023 it may be appreciated that when the director is providing his/her services in general nature as a director having whole time duty thereon without any independent professional capacity and in lieu of that the said director is getting remuneration from the company it can be undoubtedly treated as director's remuneration without any applicability of RCM. However from the face of the Schedule III read with the recent circular vide no. 201/13/2023 dt.01.08.2023 read with the circular vide no.140/2020 it's absolutely cleared that any service made by an employee (may be the director) in course of his/her employment with deduction of TDS if applicable made U/s 192 of the Act will neither be covered under the FCM nor RCM. But any other service made by the director under the independent capacity of his/her directorship not covered within the course of the employment is applicable under the RCM, excluding those services rendered by the director under his/her personal sources and capacity thereon is absolutely covered under the FCM.

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