



DETERMINATION OF EMPLOYEE COST INCASE OF SHARED SERVICES

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Karnataka Advance Ruling on the issue of whether activities performed by employees at Corporate Office in course of employment for units located in other States as well shall be treated as 'supply' within the GST statute.

FINDINGS & DISCUSSION

Entry No.1. of the Schedule III which is related to the activities which are to be treated neither as a supply of goods nor supply of services reads as under:

1. "Services by an employee to the employer in the course of or in relation to his employment."

The services provided to the employer, i.e. the corporate office by the persons employed by the corporate office are in the nature of the employee-employer relationship. Further, since the corporate office and the units are distinct persons under the Act, there is no such relationship between the employees of one distinct entity with another distinct entity, at least as per the Goods and Service Tax Acts, even if they are belonging to the same legal entity.

Further, the activities made between the related persons are treated as supplies and the valuation includes all costs, the employee cost also needs to be taken into consideration at the time of valuation of goods or services provided by one distinct entity to the other distinct entities.

RULING

The activities performed by the employees at the corporate office in the course of or in relation to employment such as accounting, other administrative and IT system maintenance for the units located in the other states as well i.e. distinct persons as per Section 25(4) of the Central Goods and Services Tax Act, 2017 (CGST Act) shall be treated as supply as per Entry 2 of Schedule I of the CGST Act.

The ruling implies that companies with offices in many cities will need to raise invoices for in-house service functions and pay GST. Determination of the

Employee cost has been challenging for many and they have been opposing the taxing of the inter-state shared services.

Extract of the Companies (Cost Records and Audit) Rules, 2014 is reproduced below:

Employee Cost:-

- a) Proper records shall be maintained in respect of employee costs in such a manner as to enable the company to book these expenses cost centre wise or department wise with reference to goods or services under reference and to furnish necessary particulars. Where the employees work in such a manner that it is not possible to identify them with any specific cost centre or department, the employees cost shall be apportioned to the cost centre or service centre or departments on equitable basis and applied consistently.
- b) Employee Cost shall be ascertained taking into account the gross pay including all allowances payable along with the cost to the employer of all the benefits, including the cost of retirement benefits charged in the financial statements in an accounting period. In case of companies to which Indian Accounting Standards apply, any re-measurement of such costs recognized in other comprehensive income shall not form part of the employee cost.
- c) Bonus whether payable as a statutory minimum or on a sharing surplus shall be treated as part of employee cost. *Ex gratia* payable in lieu or in addition to bonus shall also be treated as part of the employee cost.
- d) Remuneration payable to managerial personnel including Executive Directors on the Board and other officers of a corporate body under a statue shall be considered as part of the employee cost of the year under reference whether the whole or part of the

- remuneration is computed as a per cent of profits. Remuneration paid to non-executive directors shall not form part of employee cost but shall form part of administrative overheads.
- e) Separation costs related to voluntary retirement, retrenchment, termination and other related matters shall be amortized over the period benefitting from such costs.
 - f) Employee cost shall not include imputed costs.
 - g) Cost of idle time is accounted by the idle hours multiplied by the hourly rate applicable to the idle employee or a group of employees.
 - h) Where employee cost is accounted at standard cost, variances due to normal reasons related to the idle employee cost shall be treated as part of employee cost. Variances due to abnormal reasons shall be treated as part of abnormal cost.
 - i) Subsidy or grant or incentive any such payments received or receivable with respect to any employee cost shall be reduced from cost of the cost object in the financial year when such subsidy or grant or incentive and any such payment is recognized as income.
 - j) Any abnormal cost where it is material and quantifiable shall not form part of the employee cost.
 - k) Penalties, damages paid to statutory authorities or other third parties shall not form part of the employee cost.
 - l) The cost of free housing, free conveyance and any other similar benefits provided to an employee shall be determined at the total cost of all resources consumed in providing such benefits.
 - m) Any recovery from the employee towards and any benefit provided, namely, housing shall be reduced from the employee cost.
 - n) Any change in the cost accounting principles applied for the determination of the employee cost should be made only if it is required by law or a change would result in a more appropriate preparation or presentation of cost statements of an enterprise.
 - o) Where the employee services are traceable to a cost object, such employees' cost shall be assigned to the cost object on the basis such as time consumed or number of employees engaged or other related basis or similar identifiable measures.
 - p) While determining whether a particular employee cost is chargeable to a separate cost object, the principle of materiality shall be adhered to.
 - q) Where the employee costs are not directly traceable to the cost object, the same shall be assigned on suitable basis like estimates of time based on time study.
 - r) The amortized separation costs related to voluntary retirement, retrenchment and termination or other related matters for the period shall be treated as indirect cost and assigned to the cost objects in an appropriate manner provided that unauthorised amount related to discontinued operations, shall not be treated as employee cost.
 - s) Recruitment costs, training cost and other such costs shall be treated as overheads and dealt with accordingly.
 - t) Overtime premium shall be assigned directly to the cost object or treated as overheads and dealt with accordingly.
 - u) Idle time cost shall be assigned direct to the cost object or treated as overheads depending on the economic feasibility and the specific circumstances causing such idle time.

Further reference to **Cost Accounting Standard on Employee Cost** will be handy in determination of employee cost.