

Companies remitting pay overseas to parent may face FEMA scrutiny; matter referred to RBI

Multinationals that have challenged service tax levies on salaries paid overseas to expats employed in India may be faced with a more fearsome challenge — scrutiny under the Foreign Exchange Management Act (FEMA), which deals with forex violations.

Remitting the salary of anyone employed in India by an entity in the country in foreign currency is not permitted under FEMA, said an official. Service tax authorities have already referred the matter to the Reserve Bank of India and the Enforcement Directorate (ED), the person said.

Tax authorities contend that companies may have not declared payments as salaries to their employees in the country while seeking permission from RBI before making fund transfers. "Authorities need to ascertain how these transfers are being made," said the official cited above.

Typically, companies that employ expats pay a part of the salary in India while the rest is paid by the overseas parent. This money is then reimbursed by the Indian arm to the parent.

Tax authorities, after closely scrutinising payments made to foreign parent companies, had argued that they were liable to service tax on this as these were in the category of 'manpower supply services'.

A taxable service was being rendered by a foreign company to an Indian company. Service tax was levied on the payment made to the foreign parent by the Indian arm, since it was regarded as import of service under the reverse charge mechanism.

Show-cause notices were issued to a number of companies by the audit wing of the service tax department. The companies contested this, arguing that these were payments to their own employees for work in India. This argument of theirs has raised red flags.

Tax experts said the matter needs to be explained as India is keen to attract foreign capital and needs expertise in many sectors.

"We need clarity in law as secondment of employees is a popular practice among MNCs," said Bipin Sapra, partner at EY. He said some judicial pronouncements had in fact given relief to companies on levy of service tax.

With a number of foreign investors setting up base in the country, India has become an attractive destination for expat postings. A 2014 HSBC survey said sectors such as telecommunications, information technology and Internet accounted for 21% of total expats, followed by construction and engineering at 19%.

(Economic Times)