

## **Whether ITC is eligible on employee gratuity insurance?**

Recently Govt. of Karnataka has brought a notification dated 10-01-2024 by exercising powers given under section 4A(4) the Payment of Gratuity Act 1972 - where it has mandated companies registered in Karnataka to obtain gratuity insurance policy for their employees. The said move has been taken to protect employee rights and to provide them financial security in future. Similar rules have been placed Telangana State, Andhra Pradesh, Kerala.

In this short article, we discuss – Whether employers are eligible to avail ITC on GST paid against premium payments w.r.t gratuity insurance services? Before that let us obtain clarity on some important aspects.

### **What is Gratuity?**

- ❖ Gratuity has not been defined either under the CGST Act 2017 or in the Payment of Gratuity Act 1972. Therefore, the same can be understood from the below case law and general meaning.
- ❖ Gratuity is like pension, is retirement benefit for long and continuous services as a provision of old age. It is earned as a matter of right on fulfilling the conditions subject to which it is earned. It is not a gratuitous payment depending upon the discretion or sweet will or fancy of the employer. (Sudhir Chandra Sarkar v. Tata Iron and Steel Co. Ltd., AIR 1984 SC 1064)
- ❖ In general meaning gratuity is the amount paid by an employer for the services rendered by an employee during their employment period.

### **Whether Gratuity Insurance includes Life insurance?**

Payment of Gratuity Act, 1972, requires that the gratuity is paid to terminated employees who rendered 5 continuous years of service. 'Terminated employees' situation may arise as follows:

1. Superannuation of employees
2. Retirement or Resignation
3. On their death or
4. Disablement due to accident or illness.

In case of death, the gratuity payment is made to the nominee. The computation nor the application of gratuity provision changes upon death, only the payout method for obvious reasons.

Therefore, we can safely conclude that although, payment is made upon death, gratuity insurance cannot be categorised as a life insurance service.

#### **What is the HSN/SAC for Gratuity Insurance?**

There is no specific classification for gratuity insurance therefore, HSN/SAC code "997139" which is for "Other Non-Life Insurance services", can be used by the insurance service provider for gratuity insurance while issuing invoice to the service recipient. Blocked credit w.r.t Insurances separately listed in explanatory notes issued by GST Council.

997132 Life insurance services

997133 Accident and health insurance services

#### **GST Provisions:**

- ❖ In terms of section 16 of CGST Act a taxpayer is entitled to take ITC on goods or services availed which are used or intended to be used in the course or furtherance of the business.
- ❖ In terms of section 17(5)(b)(i) ITC on insurance purchased for life and health is not available. Provided that the input tax credit in respect of such goods or services or both shall be available, where it is obligatory for an employer to provide the same to its employees under any law for the time being in force.

#### **Judicial Precedent:**

- ❖ In the case of *M/s Hydus technologies India Pvt. Ltd. Versus CCE, C & ST, Hyderabad* the department had rejected the refund of ITC on gratuity insurance stating the same is personal in nature, as it is ultimately consumed by employee, which is excluded from the definition of input service under service tax law hence appellant is not eligible on refund on the same. Whereas the appellant contended asserting group gratuity has been taken as it is a statutory obligation as per the Payment of gratuity act. Therefore, the same is for the benefit employer. The benefit bestowed by one legislation cannot be taken away difficult and impractical to be adhered to by another field of law. Therefore, it was concluded that the appellant is eligible for the refund.
- ❖ The above case has also been relied upon in the case of *M/S. Ganesan Builders Ltd vs The Commissioner Of Service Tax* where department has denied taking cenvat credits on workmen compensation policy on the appellant.

**Analysis:**

- ❖ Commonly, most of the taxpayers are of the view that all the insurance service would fall under blocked ITC category which will lead to loss of ITC benefit, eventually, leading to an excess cost and cash flow for the business.
- ❖ For the given scenario, gratuity insurance taken by the employer will not fall under the section 17(5) as it is not relating to life insurance or health insurance.
- ❖ ITC on the same can be availed directly as per section 16 as it is intended to be used for furtherance of business of making taxable supplies or zero-rated supplies.
- ❖ On the other hand, numerous notices have been issued by GST department to the innocent taxpayers for every type of insurance service demanding to reverse the ITC which is ineligible as per section 17(5)(b). Therefore, for the given case the taxpayer can substantiate by asserting 17(5)(b) only blocks health insurance and life insurance and the said section is not applicable on gratuity insurance.
- ❖ An additional defence to substantiate the claim for ITC – one can take shelter under proviso to section 17(5)(b) stating insurance on gratuity for employees is mandated by the notification issued by Govt of Karnataka under the Payment of Gratuity Act 1972.

Note - Taxpayer is expected to comply with all the conditions of the Payment of Gratuity Act, 1972, such as gratuity given to employees are eligible employees; such insurance has to be taken from Life insurance corporation or any other insurance companies registered under the Companies Act 2013 etc.

**Conclusion:**

Personal view of the author remains that the ITC is eligible on gratuity insurance, irrespective of whether it is mandated by the government. If so, there is always an additional defence to claim said ITC for businesses as it is obligatory now for employers to take gratuity insurance by law.

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