



## Should Employee Welfare be Taxed - The GST Story of Canteen Services

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*"The moment a welfare obligation is treated as a taxable event, the law is no longer merely applied, it is questioned."*



### **1. Background**

The provision of canteen facilities by employers to their workforce constitutes a pervasive feature of the Indian industrial landscape. In the case of manufacturing establishments employing more than 250 workers, such provision is not merely a welfare initiative, but a statutory obligation mandated under Section 46 of the Factories Act, 1948.

In practice, employers typically engage third-party canteen service providers ('CSPs') to operate these facilities, discharge the corresponding invoices, and recover a nominal, substantially subsidized portion of the cost from employees through payroll deductions. Under the GST regime, however, this otherwise routine administrative arrangement has led to an unwanted controversy.

The disputes primarily center on whether such subsidized recoveries constitute a 'supply' under GST, the appropriate valuation of such transactions in the context of related parties, the differential treatment (if any) of contract workers vis-à-vis permanent employees, and the scope and extent of admissibility of ITC in respect of such arrangements.

## **2. Issue-Wise Analysis of Jurisprudence**

Based on a granular review of the rulings from various State Advance Ruling Authorities ('AAR') and Appellate Authorities ('AAAR'), the jurisprudence has evolved distinctly across four major battlegrounds.

### **Issue A: Taxability of Recoveries - The 'Supply' vs. 'Perquisite' Debate**

The fundamental question is whether a nominal deduction from an employee's salary constitutes 'consideration' for an outward 'supply' of catering services by the employer.

**The Facilitator and Perquisite View (Taxpayer-Favorable Approach):** A substantial line of jurisprudence particularly from authorities in Gujarat and Andhra Pradesh supports the position that the employer is not engaged in the business of providing catering services but merely acts as a facilitator.

Various rulings<sup>[1]</sup> emphasise that the employer merely collects and remits the employees' contribution to the canteen service provider without retaining any profit margin. Further, relying on [Circular No. 172/04/2022-GST](#) dated July 6, 2022 ('Circular 172'), various authorities<sup>[2]</sup> have held that provision of food being mandated under the Factories Act, 1948 and typically embedded within HR policies constitutes an employment-related perquisite. Accordingly, such arrangements fall outside the scope of GST by virtue of [Schedule III](#) to the CGST Act read with the relevant SGST Act (collectively referred as 'GST Act').

**The Taxable Supply View (Revenue-Favorable Approach):** In contrast, authorities in jurisdictions such as Karnataka and Himachal Pradesh have adopted a stricter interpretation. In Federal-Mogul<sup>[3]</sup> authorities held that the provision of canteen facilities facilitates the employer's core business operations (for instance, by minimizing time loss) and therefore qualifies as an activity

undertaken in the 'course or furtherance of business' under [Section 2\(17\)](#) of the GST Act.

Similarly, the Tamil Nadu authorities<sup>[4]</sup> held that subsidized recoveries represent valid consideration for a composite supply of services by the employer. It was further observed that the benefit of the Circular 172 is limited to cases involving fully free perquisites and does not extend to subsidized arrangements.

**The Bifurcation Approach (Emerging Maharashtra Position):** A series of recent rulings issued by the Maharashtra AAR<sup>[5]</sup> has articulated a more refined interpretative framework.

Under this approach, the value of canteen services is analytically segregated into two distinct components:

Employer-Borne Portion: The unrecovered portion of the cost borne by the employer is treated as a perquisite, representing the value of the concession extended to employees, and is accordingly not liable to GST in terms of Circular 172.

Employee-Contributed Portion: The nominal amount recovered from employees is treated as consideration for a taxable supply and is therefore subject to GST.

In the authors' considered view, this approach represents the most balanced and legally sustainable reconciliation of the statutory framework with commercial realities. It appropriately acknowledges the employment-linked character of the benefit to the extent of employer subsidy, while simultaneously recognising that actual monetary recovery from employees may satisfy the statutory threshold of 'consideration.'

Further, by restricting the taxable value to the amount actually recovered, this approach pragmatically mitigates the otherwise disproportionate consequences of related-party valuation rules, without entirely disregarding the statutory construct of 'supply.'

### **Issue B: The Valuation Conundrum (Rule 28 Trap vs. Actual Recovery)**

The controversy surrounding valuation in employer-employee canteen recoveries arise from the statutory deeming fiction that such parties constitute 'related persons' under [Section 15](#) of the GST Act. This characterization triggers a departure from transaction value and necessitates application of the valuation rules, often leading to disproportionate outcomes under a strict interpretational framework.

**The Rule 30 Escalation:** Under a strict interpretation of Section 15 read with [Rule 28](#), transaction value becomes inapplicable in employer-employee arrangements owing to their characterization as 'related persons,' thereby necessitating recourse to prescribed valuation rules and in the absence of an ascertainable open market value or comparable supply, the valuation inevitably escalates to [Rule 30](#) (cost plus 10%) or, residually, Rule 31. This position stands affirmed in *Federal-Mogul (supra.)*, wherein it was held that the employer-employee relationship constitutes a related party nexus mandating valuation under Rule 30 or 31 in the absence of benchmarks.

**Bypassing Rule 28 via the Bifurcation Theory:** The recent Maharashtra AAR rulings (e.g., in Wika Instruments, Piaggio Vehicles, and KSB Limited) effectively neutralize the harsh implications of valuation by holding that the unrecovered portion representing the employer's subsidy is a perquisite not liable to GST and therefore cannot be included in the taxable value.

Consequently, notwithstanding the related party relationship, GST liability stands confined strictly to the actual amount recovered from employees.

In the authors' view, the bifurcation approach represents a more legally sound and commercially pragmatic interpretation of the GST valuation framework. By segregating the actual recovery from employees as taxable consideration and treating the employer-borne portion as a perquisite falling under Schedule III, this approach confines taxation strictly to the real economic value of the supply. It also ensures that valuation provisions are not used to artificially inflate the taxable base, as would occur under a rigid application of Rule 28 read with Rule 30, thereby preserving the fundamental principle that GST is leviable only on actual consideration and not on notional values.

### **Issue C: Admissibility and Quantum of ITC**

The battle over ITC admissibility pits legislative intent against administrative rate notifications.

**The Legislative Carve-Out and Cost Borne Restriction:** [Section 17\(5\)\(b\)](#) blocks ITC on food and catering. However, the legislature inserted a proviso allowing ITC where the provision of the facility is obligatory under any law. Guided by Circular 172, authorities<sup>[6]</sup> confirmed that since the Factories Act mandates the canteen, ITC is eligible. However, it was held that ITC is admissible only to the extent of the cost actually borne by the employer.

**The 5% Rate Trap (Total Blockage):** A deeply problematic view, spearheaded by the Maharashtra and Uttarakhand AARs (*Tube Investment, Bridgestone, Carraro India, Sigma Electric, Kion India*), completely blocks ITC. They argue that the 'Restaurant Services' which attract a mandatory, concessional GST rate of 5% under Notification No. 11/2017-CT(R) dated

June 28, 2017 ('Service Rate Notification'). The rigid condition for this 5% rate is the non-availment of ITC. These authorities hold that the 5% rate carries an absolute bar on ITC under a rate notification, the enabling proviso of Section 17(5)(b) cannot override it. Thus, the employer is denied ITC in its entirety.

In the authors' view, once canteen provision is a statutory obligation, ITC under the proviso to Section 17(5)(b) should not be denied merely because part of the cost is recovered from employees; recovery may impact taxability, but not the fundamental eligibility of credit. This view is also supported by the Kerala AAR in ***Plant Lipids Private Limited***, [2025-VIL-103-AAR](#).

As regards the 5% rate condition, the restriction on ITC should, at best, apply only to inputs and input services attributable to the recovered portion, and not to the employer-borne perquisite portion falling outside the scope of supply. That said, the larger issue whether a rate notification can override or restrict ITC otherwise allowed under the Act remains open and awaits authoritative judicial determination.

### **Issue D: The Contract Worker Divide**

A significant compliance friction arises from the treatment of contract/temporary workers vs. permanent employees.

**The Divisive Approach:** In various rulings<sup>[7]</sup>, authorities emphasize the lack of a direct employer-employee relationship. Consequently, they rule that recoveries from contract workers do not enjoy Schedule III perquisite protection and are fully taxable as an outward supply. Furthermore, these rulings often deny ITC on the food supplied to contract workers, claiming the statutory obligation falls on the labor contractor under the Contract Labour (Regulation and Abolition) Act, not the principal employer.

**The Inclusive Approach:** Conversely, a progressive ruling by the Kerala AAR in *Plant Lipids (supra.)* systematically dismantles this divide. It highlights that the definition of 'worker' under Section 2(1) of the Factories Act explicitly includes any person employed through an agency or contractor. Relying on Supreme Court precedents, the AAR noted that the statutory welfare obligation extends uniformly to contract labor. Therefore, perquisites provided to them enjoy the same non-taxability, and the employer is entitled to full ITC on inward supplies used in the statutory canteen, irrespective of the worker's direct payroll status.

### **3. Conclusion**

The jurisprudence on canteen services under GST continues to remain fragmented, reflecting a deeper tension between statutory principles, delegated legislation, and evolving judicial interpretations. While emerging approaches particularly the bifurcation theory, attempts to reconcile legal provisions with commercial realities, significant questions persist on valuation mechanics, the true scope of 'supply,' and the extent to which ITC can be curtailed through notifications. The divergence across authorities, including on issues such as contract labour and ITC eligibility, underscores the absence of a uniform interpretative framework.

In this backdrop, the law appears to be in a state of transition, where competing schools of thought coexist without definitive resolution. It remains to be seen how higher judicial forums will harmonize these inconsistencies and whether a principled balance can be achieved between revenue considerations and the foundational GST doctrine of taxing real economic value.

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*(The views expressed in this article are strictly personal.)*

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- [1] Amneal Pharmaceuticals Pvt. Ltd., [2021-VIL-44-AAAR](#); Dishman Carbogen Amcis Ltd, [2021-VIL-334-AAR](#); and Cadmach Machinery Pvt. Ltd., [2022-VIL-122-AAR](#).
- [2] AIA Engineering Limited, [2023-VIL-67-AAR](#); Dormer Tools India P Ltd., [2024-VIL-79-AAR](#) and Kohler India Corporation Pvt Ltd, [2024-VIL-06-AAR](#).
- [3] Federal Mogul Goetze India Ltd., [2022-VIL-301-AAR](#); and Federal-Mogul Anand Bearings India Limited, [2023-VIL-38-AAAR](#)
- [4] Sundaram Clayton Limited, [2023-VIL-211-AAR](#); and Kothari Sugars and Chemicals Limited., [2023-VIL-30-AAAR](#)
- [5] Ferrero India Pvt. Ltd., [2025-VIL-220-AAR](#); Kion India Pvt. Ltd., [2025-VIL-58-AAR](#); Lear Automotive India Private Limited, [2025-VIL-221-AAR](#); Spicer India Private Limited, [2025-VIL-219-AAR](#); Sigma Electric Manufacturing Corporation Pvt. Ltd., [2026-VIL-90-AAR](#); KSB Limited, [2026-VIL-12-AAR](#); Carraro India Private Limited, [2026-VIL-71-AAR](#); and Piaggio Vehicles Pvt. Ltd., [2026-VIL-70-AAR](#).
- [6] Kirby Building Systems & Structures India Private Limited, [2023-VIL-198-AAR](#); KSH Automotive Pvt Ltd, [2023-VIL-176-AAR](#); Tata Motors Limited, [2022-VIL-100-AAAR](#); AIA Engineering Limited, [2023-VIL-67-AAR](#); Dormer Tools India P Ltd., [2024-VIL-79-AAR](#); Alleima India Private Limited, [2024-VIL-113-AAR](#)
- [7] Troikaa Pharmaceuticals Ltd., [2025-VIL-22-AAAR](#); Eimco Elecon India Limited, [2023-VIL-179-AAR](#); Suzuki Motor Gujarat Pvt Ltd., [2024-VIL-26-AAR](#); Zydus Hospira Oncology Private Limited, [2025-VIL-203-AAR](#)