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Indirect Tax Alert

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Judgment under GST era

Material Recycling Association of India v. Union of India and 2 Others[1]

Issue for Consideration

Is section 13(8)(b) of the IGST Act, 2017, which stipulates that the place of supply of intermediary services should be the location of the supplier of service, ultra vires under Articles 14,19, 265 and 286 of the Constitution of India?

Discussion

- The Petitioner is an association comprising of recycling industry engaged in manufacture of metals and casting etc. The members of the Petitioner's association ("members") facilitate sale of recycled scrap goods for their foreign principals to customers located in India and in other countries. The members are registered under the GST law.
- The foreign clients raise invoices directly on the purchaser who may be an Indian or overseas buyer. The payment is made by buyer to the foreign client. The member receives its commission from the foreign client in foreign exchange.
- As per section 13(8)(b) of the IGST Act, 2017 ("section 13(8)(b)"), the place of supply for intermediary services would be location of supplier of service (i.e. the location of the intermediary). Hence, the services provided by the members are deemed to be provided in India and liable to GST and accordingly, the transaction does not qualify as an 'export of service' as per section 2(6) of the IGST Act, 2017.
- Accordingly, the Petitioner has filed the present Special Civil Application, challenging the constitutional validity of the impugned section on the following grounds:
  - Article 286(1)[2] of the Constitution of India ("Constitution") does not empower the Parliament to determine the place of supply. The Parliament is not authorised to legislate and artificially assign the place of supply to be within India when clearly the services are being exported out of India.

[1] 2020-VIL-341-GUJ

[2] Article 286(1) of the Constitution provides that the State cannot impose a law for taxing supply of goods and services taking place outside the State or in the course of import or export of goods / services outside the territory of India. Further, Article 286(2) of the Constitution empowers the Parliament to formulate principals to determine when a supply of goods or services is either outside state or in course of import or export.

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- The State has no jurisdiction to impose tax when a supply takes place outside the State. As per section 13(8)(b) and 8(1) of the IGST Act, 2017, when services are provided by a resident supplier to a non-resident recipient, such services will be deemed to be provided within the State despite the recipient being outside India. Section 2(92)(a) of the CGST Act, 2017 defines 'recipient' as a person who is liable to pay the consideration for supply of goods / services. Therefore, the provisions under section 13(8)(b) is ultra vires to Article 286 of the Constitution and liable to be struck down.
- Furthermore, when the services are provided by the members, they are for the benefit of the recipient located outside India and therefore, such transaction can be said to be executed in the course of export and fall within the exemption of Article 286(1)(b) of the Constitution. Thus, section 13(8)(b) is in violation of the said Article.
- There is a different yardstick prescribed for the treatment of intermediary services when they are provided to a recipient located in India and when they are provided to a recipient located outside India. In the former case, the place of supply as per section 12(2)(a) of the IGST Act, 2017 is the location of the recipient and in the latter, as per section 13(8)(b), it is the location of the supplier. This is in violation of Article 14[3] of the Constitution.
- The nature of intermediary services when compared to and other services of management consultants, lawyers and portfolio managers are substantially the same except these service providers are required to perform different functions. However, the treatment for determining the place of supply for such other services is the same under section 12 and 13 of the IGST Act, 2017, whereas for intermediary services it is different. There should be intelligible differentia and such intelligible differentia shall have a rational nexus with the object sought to be achieved. Thus, there is no nexus with the object to be achieved by having a differential treatment when the intermediary services are rendered within India or to a recipient outside India. This would result in violation of Article 14 of the Constitution.
- The definition of 'intermediary' under section 2(13) of the IGST Act, 2017 excludes trading on one's own account. However, what construes as trading on one's own account requires a clear explanation to determine what is specifically included within the domain of intermediary. Thus, the definition is vague and the section 13(8)(b) needs to be struck down. In this regard, reliance was placed on the judgment of Hon'ble Supreme Court in the case of *Kartar Singh* v. *State of Punjab*[4] and *Shreya Singhal* v. *Union of India*[5].
- GST law was introduced as a destination-based tax system and section 13(8)(b) is aberration and therefore, it is necessary to preserve the basic foundation of the scheme of GST.
- A transaction of providing intermediary services would be subject to tax in the country where the recipient is located as it would be an import for the recipient. If the transaction is also taxed in India, it would lead to double taxation and would affect the margins earned by the members.
- The deeming fiction of section 13(8)(b) suffers from the defect of unreasonableness as the transaction is clearly an export of service.
- Exemption in sl. no. 12AA of notification no. 9/2017 - Integrated Tax (Rate) dated June 28, 2017 (inserted by notification no. 20/2019 – IGST dated September 9, 2019) exempts intermediary services when the location of both supplier and recipient of goods are outside India. Accordingly, there is a distinction between the services being rendered on the basis of movement of goods and service transaction. However, when there is no movement of goods, the service provider would be liable pay CGST and SGST, which is

[3] Article 14 of the Constitution reads as The State shall not deny to any person equality before the law or the equal protection of the laws within the territory of India.
[4] (1994) 3 SCC 569
[5] (2015) 5 SCC 1

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discriminatory. Also, when the supplier of goods is outside India and the buyer of goods is in India, then the intermediary service provider is required to pay GST, which is discriminatory. The object sought to be achieved by such differential treatment is not clear and notification no. 20/2019 *(supra)* is also violative of Article 14 of the Constitution.

- Circular no. 107/26/2019 – GST dated July 18, 2019 which was issued in the context of intermediaries who were providing Information Technology enabled services also did not clarify the meaning of 'on his own account' as appearing in the definition of 'intermediary'. Furthermore, the said circular was also withdrawn later due to the confusion created by it. Therefore, it would not be right to deny the benefit of export to the members engaged in providing intermediary services.

- The Respondents contended as follows:
  - Supply of services by intermediaries to the recipients outside India are not export of services irrespective of the mode of payment.
  - In various advance rulings under GST, it has been held that services provided by an intermediary to the recipients located outside India are not export of service.
  - The place of supply provision for intermediaries under GST law are in consonance with the provisions under the erstwhile Service Tax regime. Therefore, a policy decision of the Government in respect of the levy cannot be said to be unlawful or violating the tenets of the Constitution.
  - The Parliament has got wide amplitude to create deeming fiction under taxation matters and to levy tax thereon. Reliance was placed upon Article 246A of the Constitution. Reliance was also placed upon several Supreme Court judgments.
  - Benefits accruing to the exporter of services are meant for those who actually export the service and not to intermediaries who are directly or indirectly associated with the exporter. If export benefits are extended to intermediaries, it will result in non-exporters being treated at par with exporters which would end up negating the benefits to exporters.
  - One service cannot be compared with another service to justify the violation of Article 14 of the Constitution.
  - There is no conflict resulting in absurdity in section 13(8)(b) and section 13(2) of IGST Act, 2017. Both sections are clear in nature.
  - It is very much within the powers of the Government to categorize goods and services for the purpose of taxation in the manner that meets the policies and objectives of the Government.
  - Reliance was placed on the judgment of the Hon'ble Supreme Court in the case of *East India Tobacco Co.* v. *State of Andhra Pradesh*[6] wherein it was held that the State is allowed to pick and choose objects, methods, persons and even rates of taxation, if it does so reasonably.
  - With regard to GST being a destination-based tax, taxation laws can have exceptions and such exceptions are governed by revenue considerations and based on judgments of the Supreme Court, and are within the legislative competence as the legislature is free to pick and choose the supply that it intends to tax and the manner in which it intends to tax and hence section 13(8)(b) is not violative of Article 14 of the Constitution.
  - Levy of tax on the impugned intermediary service does not infringe the right of the members from practising any profession or carrying on business and hence there is no violation of Article 19(1)(g)[7] of the Constitution.
  - Intermediary is a go-between two persons i.e. the main service provider and service recipient. An intermediary provides service to both persons although he may have contractual obligation only with one and hence it is not feasible to prescribe one person as the recipient of service in case of intermediary

[6] 1962-VIL-02-SC

[7] Article 19(1)(g) of the Constitution provides that every citizen has a right to practice any profession, or to carry on any occupation, trade or business.

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services. Hence differential treatment is accorded to such services.

- There is no double taxation as the tax paid on import by the recipient under a reverse charge basis would be available to him as input tax credit in many international jurisdictions.

- The Hon'ble High Court after taking into account various provisions of the IGST Act, 2017, observed as follows:
  - On a co-joint reading of section 2(6) and 2(13) of the IGST Act, 2017, which defines export of service and intermediary service, the person who is an intermediary cannot be regarded as an exporter of services because he is only a broker who arranges and facilitates the supply of goods or services or both.
  - There is no distinction between the intermediary services provided by a person in India or outside India. Just because the invoices are raised on the person outside India and foreign exchange is received in India, it would not qualify to be export of services more particularly when the legislature has thought it fit to consider the place of supply of service as place of the person who provides such service in India.
  - There is no deeming provision as canvassed by the Petitioner but instead a stipulation by the GST law legislated by the Parliament to consider the location of service provider of intermediary service as the place of supply. Similar provisions existed even in the Service Tax regime (w.e.f. October 1, 2014) and continue under the GST regime.
  - There is no double taxation because the services provided by the Petitioner would not be taxable in the hands of the recipient of such service but on the contrary the commission paid by the recipient outside India would be entitled to a deduction by way of expenses.
  - If the intermediary service is not taxed in India, it would lead to a situation where such services are not taxed anywhere. Hence, the Respondents have provided exemption from tax for intermediary service only when the supplier and recipient of goods are outside India.

Judgment

- Section 13(8)(b) read with section 2(13) of the IGST Act, 2017 is not ultra vires or unconstitutional.
- The Respondents are open to consider the representations made by the Petitioner so as to redress the Petitioner's grievances in suitable manner and in consonance with the provisions of the GST law.

Dhruva Comments:

Article 246A of the Constitution empowers the Parliament to frame laws for inter-state supply of goods and services.

The scope, coverage and taxability of intermediary service has been a subject matter of litigation since the service tax regime. Enactment of laws is within the purview of the Legislature and can be challenged if it can be established to be arbitrary or unreasonable. The Courts have consistently held that the Legislature has wide powers to determine the scope and coverage of law.

Judgment under Pre GST era

Linde Engineering India Pvt. Ltd. and Other v. *Union of India*[8]

Issues for Consideration

Do the services provided to the holding company and its subsidiaries located outside India qualify as an export of services?

Discussion

- The Petitioner, a 100% subsidiary of Linde AG, Germany, is engaged in the business of providing taxable output services under the categories of consulting engineering services, erections, commissioning and installation services, construction services other than residential

[8] TS-587-HC-2020(GUJ)-ST

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complex, including commercial / industrial buildings or civil structures and works contract services etc. to entities located both in and outside India.

- The Petitioner provides consulting engineering services to its parent company and other establishments located outside India without payment of Service tax treating it as an export of service.
- The Petitioner received a communication from the Authorities with a direction to submit various documents on the basis of the audit objections issued by the Central Excise Revenue Audit ("CERA"). The Petitioner made required submissions and believed that the authorities were satisfied with the same.
- Thereafter, the Petitioner received a Show Cause Notice ("SCN") stating that the services provided to Linde AG or any subsidiary of Linde AG located outside India are exempt. Such services do not come under the purview of export and consequently are in violation of rule 6(3) of the Cenvat Credit Rules, 2004 ("CCR"), which requires the proportionate reversal of Cenvat credit.
- Aggrieved, the Petitioner filed the present Writ Petition before the Hon'ble Gujarat High Court.
- After perusing the facts of the case, the Hon'ble High Court observed as follows:
  - Perusing the provisions of the Finance Act, 1994 and the rules thereunder the Court observed that the Petitioner has been fulfilling the conditions mentioned under clauses (a) to (e) of rule 6A of the Service Tax Rules, 1994.
  - The Court examined in detail rule 6A(f) of the Service Tax Rules, 1994, which stipulates that the provider and the recipient are not merely establishments of a distinct person. The Petitioner, which is an establishment in India, along with its 100% holding company which is located in a non-taxable territory, cannot be said to be mere establishments of distinct persons as per explanation 3(b) to section 65B(44) of the Finance Act, 1994.
  - The Court held that services rendered by the Petitioner outside the territory of India to its parent company would have to be considered an "export of service" as per rule 6A of the Service Tax Rules, 1994. The Court also held that the condition in clause (f) of the said rule would not be applicable due to the facts of the present case.
  - In the event of the services being considered an 'export of service', the Respondent shall have no jurisdiction to invoke provisions of the Finance Act, 1994 and the rules thereunder to bring the services rendered by the Petitioner within the purview of the levy of Service tax.
  - The Court observed that there has been no wilful misstatement or suppression as the Petitioner and its parent company are not the establishments of the same company.
  - The Petitioner was incorporated under the provisions of the Companies Act, 1956, and its holding company, which was incorporated in Germany, are both distinct persons and consequently neither can be treated as establishments of the same Company.
  - Reliance was placed on the judgment pronounced by the Hon'ble Supreme Court in the case of *Whirlpool Corporation* v. *Registrar of Trade Marks*[9] to state that the present Writ Petition is maintainable under Article 226 of the Constitution of India.

Judgment

The Hon'ble High Court held that the services provided by the Petitioner to its parent company qualify as an export of service.

Dhruva Comments:

The judgment critically examines the contingencies under which a Writ Petition is maintainable and one of which is proceeding initiated without jurisdiction or vires of an Act being challenged.

The judgment reinforces the tax position by concluding that a subsidiary company providing services to a

[9] 1998-VIL-09-SC

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parent company located outside India are distinct persons and not establishment of same Company and shall qualify as an export of service upon fulfilment of the necessary conditions.

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