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GST Judicial Decisions

Supreme Court has struck down the levy of IGST on importers for ocean freight services provided by foreign shipping lines to foreign suppliers in a CIF contract for import of goods

Union of India vs. Mohit Minerals (P.) Ltd. [2022] 138 taxmann.com 331 (Supreme Court Of India)

In favour of Assessee

Relevant Facts

The respondent imported non-cooking coal from Indonesia, South Africa and the U.S. by ocean transport on Cost Insurance Freight (CIF) basis. The respondent paid customs duties on the import of coal, which included the value of ocean freight. In the case of a CIF contract, the freight invoice was issued by the foreign shipping line to the foreign exporter, without the involvement of the importer. Ocean freight was paid by the importer only when goods were imported under Free-on-Board contract.

Entry No. 9 of Notification No. 8/2017 – IGST (Rate) notified GST @ 5% on ocean freight services provided or agreed to be provided by a person located in a non-taxable territory to another person located in a non-taxable territory by way of transportation of goods by a vessel from a place outside India up to the customs stations of clearance in India. The said notification was issued by the Central Government on the advice of the GST Council in exercise of the powers under Sections 5(1), 6(1) and 20(iii)-(iv) of the IGST Act, 2017 read with Sections 15(5) and 16(1) of the CGST Act, 2017. Further, Notification No. 10/2017 IGST (Rate) notified that for the supply of said services, IGST would be payable under reverse charge mechanism **(RCM)** by the importer located in the taxable territory, as defined in clause 2(26) of the Customs Act, 1962.

The respondent filed a writ petition before the Gujarat High Court challenging Notifications 8/2017 and 10/2017. The Gujarat High Court held the notifications unconstitutional for exceeding the powers conferred by the IGST Act and CGST Act on the following basis:

i. There is no territorial nexus for taxation as the services are provided by a person in non-

taxable territory to another person in non-taxable territory.

ii. There is double taxation of GST under RCM as customs duties are paid by the importer on the value which includes ocean freight which is legally impermissible.

iii. The importer is not the recipient of the transport services as no consideration is paid by him. Section 5(3) of the IGST Act enables the Government to stipulate categories of supply and not specify a third party as recipient of such supply.

A batch of Special Leave Petitions were filed before the Supreme Court by the Department against the decision of the Gujarat High Court.

Held

The Hon'ble Supreme Court held that:

i. The impugned levy imposed on the 'service' aspect of the transaction is in violation of the principle of 'composite supply' enshrined under Section 2(30) read with Section 8 of the CGST Act. Since the Indian importer is liable to pay IGST on the 'composite supply', comprising of supply of goods and services in a CIF contract, a separate levy on the Indian importer for the 'supply of services' by the shipping line would be in violation of Section 8 of the CGST Act.

ii. Importer of goods in India is to be considered as recipient of service of transportation of goods by vessel from outside India to a place in India as he is ultimate beneficiary though shipping service is provided by foreign shipping line to foreign exporter in a CIF contract. Mere payment of consideration by foreign exporter to foreign shipping line in CIF imports does not mean that there was no supply of freight service to importer.

iii. Levy of GST on supply of transportation service by foreign shipping line to foreign exporter to import goods into India is not extra-territorial as services are rendered for benefit of Indian importer and transaction has nexus with territory of India.

iv. Specification of Indian importer as recipient of service by Notification No. 10/2017 IGST (Rate) is only clarificatory; this notification does not specify taxable person different from recipient prescribed in Section 5(3) IGST Act for reverse charge.

v. The recommendations of the GST Council only have persuasive value as they are the product of a collaborative dialogue involving the Union and States. Legal enaction of the recommendations would disrupt fiscal federalism.

CNK Comments

Huge respite to the importers who were subject to levy of GST under RCM on ocean freight services in a CIF contract. However, the judgement opens a pandora's box with respect to the findings that the importer is the recipient which may have implications in other similar cases; the recommendations of the GST Council are non-binding; and that the Centre and States are at liberty to use different means of persuasion ranging from collaboration to contestation as they are conferred with equal power to legislate on GST.

Supreme Court upholds the levy of service tax under RCM mechanism on secondment of employees

C.C.,C.E. & S.T. Bangalore vs. Northern Operating Systems (P.) Ltd. [2022] 138 taxmann.com 359 (Supreme Court Of India)

In favour of Revenue

Relevant Facts

The assessee was registered as a service provider under the categories of Manpower Recruitment Agency Service, Business Auxiliary Service, Commercial Training and Coaching Service, TTSS, Telecommunication and Legal Consultancy Service etc., under the Finance Act, 1994. Following an audit by the revenue, proceedings were initiated against the assessee for alleged non-payment of service tax concerning agreements entered into by it with its group companies located in USA, UK, Dublin (Ireland),

Singapore, etc. to provide general back-office and operational support to such group companies.

The nature and contents of the agreements were as follows:

i. When required the respondents requested the Group Companies for managerial and technical personnel for assistance in business and accordingly the employees were selected by the group company, and they would be transferred to the respondents.
ii. The employees acted in accordance with the instructions and directions of the respondents. The employees would devote their entire time and work to the employer seconded to.
iii. The seconded employees would continue to be on the payroll of the group company (foreign entity) for the purpose of continuation of social security/retirement benefits, but for all practical purposes, the respondents would be the employer. During the term of transfer or secondment the personnel would be the employee of the respondents. The respondents issued an employment letter to the seconded personnel stipulating all the terms of the employment.
iv. The employees so seconded would receive their salary, bonus, social benefits, out of pocket expenses and other expenses from the group company.
v. The group company would raise a debit note on the respondents to recover the expenses of salary, bonus etc. and the respondents would reimburse the group company for all the expenses and there would be no mark-up on such reimbursement.

Held

The Hon'ble Supreme Court after referring to its previous judgments, wherein it was held that 'control' alone cannot be a factor to decide as to who is the employer stated that there is no one single determinative factor, which the courts give primacy to, while deciding, whether an arrangement is a contract of service or a contract for service and stated that 'Substance over form' is the one test that had been consistently applied requiring a detailed examination of the contracts/agreements.

In the current case, while the control over performance of the seconded employees' work and the right to ask them to return, if their functioning is not as is desired, was with the assessee, the fact remains that their overseas employer in relation to its business, deployed them to the assessee, on secondment. Secondly, the overseas employer- for whatever reason, paid them their salaries.

Their terms of employment even during the secondment were in accord with the policy of the overseas company, who is their employer. Upon the end of the period of secondment, they returned to their original places, to await deployment or extension of secondment.

The earlier cases had limited precedential value as independent reasonings were not detailed. The question of revenue neutrality was set aside as the Court was called upon to adjudicate the nature of transaction and whether the incidence of service tax aroused by virtue of provision of secondment services. The assessee was the service recipient of manpower recruitment and supply services by the overseas entity, with respect to the employees it seconded to the assessee for the duration of their deputation and was liable to pay service tax under RCM.

CNK Comments

This judgement has unsettled the once settled principle which can have implications even under the GST regime. Secondment arrangements are common among multi-national corporations wherein employees are deputed to subsidiary companies for specified projects/period. There are a series of judgements wherein the Tribunals have held that there would be no service tax liability under reverse charge as there are no manpower supply services provided by the overseas entity when they send their employees

on secondment agreements to the Indian entities as the Indian entities would be the employer for the employees on secondment. However, while applying the judgement, the provisions under the Income Tax Act, 1961 will also require consideration to ensure uniformity in the tax position adopted under all taxation laws.

Actual cost of land, if available, shall not be subject to GST. The prescribed rate of deduction of 1/3rd of total amount towards land value is ultra-vires the CGST Act and is discriminatory, arbitrary and violative of Article 14 of Constitution of India

Munjaal Manishbhai Bhatt vs. Union of India [2022] 138 taxmann.com 117 (Hight Court of Gujarat)

In favour of Assesee

Relevant Facts

The writ applicant entered into an agreement for purchase of a plot of land and construction of bungalow. Separate and distinct consideration was agreed upon between the parties to the agreement for the sale of land and construction of a bungalow on the land. The writ applicant believed that he would be liable to pay GST on the consideration payable for construction of bungalow in as much as it would constitute supply of construction service under the GST Acts. However, the Developer relied on Entry No. 3(if) of Notification No. 11/2017 – Central Tax (Rate) read with Paragraph 2 of the said notification and informed the applicant that he would be liable to GST on the entire consideration payable for land as well as construction of bungalow after deducting 1/3rd of the value towards the land in accordance with the paragraph 2 of the said notification.

The writ application was filed as the actual consideration paid towards the sale of land had not been excluded for computation of liability and instead 1/3rd of the total consideration was deemed to be the land value in accordance with paragraph 2 of the said notification.

The Appellate Authority for Advance Ruling upheld the decision by the Advance Ruling Authority in a related matter concerning the developer where the deduction for sale of land (developed plots) was admissible only to the extent of 1/3rd of the total consideration based on the notification.

A common judgement was issued to dispose of the above cases.

Held

Paragraph 2 of the Notification No. 11/2017-Central Tax (Rate), which provides for a mandatory fixed rate of deduction of 1/3rd of total consideration towards the value of land was ultra-vires the provisions as well as the scheme of the GST Acts. Application of such mandatory uniform rate of deduction is discriminatory, arbitrary and violative of Article 14 of the Constitution of India. The said paragraph would have to be read down to the effect that the deeming fiction of 1/3rd will not be mandatory in nature. It will only be available at the option of the taxable person in cases where the actual value of land or undivided share in land is not ascertainable.

Legislative intent was to impose tax on construction activity undertaken by a supplier at behest of or pursuant to contract with recipient. There is no intention to impose tax on supply of land in any form and it is for reason that it is provided in Schedule III to CGST Act. Charge of tax is only on supply of goods or services made or agreed to be made for a consideration. Imposition of tax can only be on construction activity which is undertaken by supplier at behest of proposed buyer.

Deduction was contemplated in the 14th GST Council Meeting where ascertaining land value in flats was difficult. Mandatory deduction would be available only as an option to a taxable person in cases where actual value of land or undivided share of land is not ascertainable. Where a detailed statutory mechanism for determination of value was available, then deeming fiction cannot be justified on basis that it is meant to

curb avoidance of tax when such fiction leads to arbitrary consequences.

Measure of tax imposed has no nexus with charge of tax on supply of construction. Prescription under Section 15(5) of CGST Act must be by way of Rules and not by notification. Challenge of delegated legislation as being ultra vires provisions of CGST Act as well as violation of Article 14 of Constitution of India, cannot be defended merely on ground that Government had competence to issue such delegated piece of legislation.

CNK Comments

A welcome judgement clarifying the intent of the Government to not impose tax on the sale of land. In cases where the value of land is available, the same will not form part of the taxable value subject to GST.

KEY TAKE AWAY

- GST is not applicable under RCM on ocean transport services received in a CIF contract for import of goods.
- Service tax applicable on secondment agreements.
- For valuation of applicable GST on sale of land with construction services, actual cost of land, if available, will be excluded. If not, 1/3rd of the total consideration will be deemed to be the cost of land.

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