

# CNK & Associates LLP

## Newsflash

### In Brief

*The liaison activities undertaken by liaison office in line with conditions specified by RBI amounts to supply and is liable to GST if the place of supply is in India*

### ***KAR ADRG 50/2020 dated 8<sup>th</sup> October 2020***

(In favor of Revenue)

#### ***Relevant Facts***

M/s. Fraunhofer-Gesellschaft Zur Forderung der angewandten Forschung e.V (“Head Office” or “HO”) is incorporated in Germany and undertakes the business of promoting applied research. The HO established their liaison office in Bangalore (“Applicant” or “LO”) to act as an extended arm of the HO and to carry out the activities as permitted by RBI.

The LO does not generate any income in India and engage in any trade/ commercial activity.

The LO does not charge any commission/ fees or any other remuneration for the liaison activities/ services rendered by it or otherwise in India.

The entire expenses of LO in India is met exclusively out of the funds received from HO through normal banking channels.

#### ***Issues Involved***

- Whether the activities of an LO amount to supply of services?
- Whether the LO is required to be registered under CGST Act, 2017 (“CGST Act”)?
- Whether the LO is liable to pay GST?

#### ***Points of Arguments***

##### **By Applicant -**

The Applicant submits that they merely act as an extended arm of the HO and are not engaged in any business activity on their own. Thus, the activity does not fall within Section 7(1)(a) of the CGST Act.

The LO does not charge or collect any fee or consideration for its liaising activities and adheres to the conditions stipulated in the RBI approval letter.

The LO cannot be considered as related persons as there is only one legal entity and no relationship can be established. Further it cannot be considered as distinct persons under Section 25 of CGST Act as distinct persons should have two or more establishments. The LO is a mere extension of HO and work as employees of HO. Therefore, the activities performed by the LO for the HO customers in India are considered to be provided by the HO itself.

The LO does not account any form of income in the financials except for the remittance from the HO which is purely to meet the working of the LO.

The Applicant also cited the ruling of the Authority for Advance Rulings (“AAR”) in the case of *Takko Holding GmbH (2018 (19) G.S.T.L. 692 (A.A.R – GST))* and *Habufa Meubelen B.V. (2018 (14) G.S.T.L. 596 (A.A.R. – GST))* wherein it was held that the “*liaison activities being undertaken by the applicant when strictly in line with condition specified by RBI permission letter do not amount to supply under CGST and SGST Act*”.

Without prejudice, the Applicant also submitted that Sl. No. 10F of the Notification No. 9/2017-IGST (Rate) dated 28<sup>th</sup> June 2017 as amended, exempts any services supplied by an establishment of a person in India to any establishment of that person outside India, which are treated as establishments of distinct persons in accordance with Explanation 1 in Section 8 of the Integrated Goods and Services Tax Act, 2017 (“IGST Act”), if the place of supply for such services is outside India. The place of supply in accordance with Section 13(2) of the IGST Act would be the location of the recipient and thus, outside India.

#### **Observations of the AAR**

The term “Liaison Office” is not defined under the CGST Act. However, it is defined under Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016 and as per the said definition, primarily it is a place of business.

The Applicant also fulfils the definition of “person” in terms of Section 2(84) of the CGST Act.

The definition of term “business” is very wide and includes any trade, commerce, manufacture, profession, vocation, adventure, wager or any other similar activity, whether or not it is for a pecuniary benefit. Further “business” also includes any activity or transaction in connection with or incidental or ancillary to sub-clause (a), in terms of Section 2(17)(b) of the CGST Act. Thus, the impugned liaison activity of the Applicant actually falls under clause (b) as it is ancillary to the activities mentioned in clause (a).

The Applicant themselves have admitted that they are involved in promoting the business of the HO in India and they act on behalf of the HO for its customers in India. Thus, the Applicant and their HO are deemed to be related persons in term of Section 15 of the CGST Act.

We find that they are a distinct legal entity and are aptly covered under the definition of intermediary as per Section 2 (13) of IGST Act, 2017.

The activities performed by the applicant would fall under the scope of supply under Section 7 of CGST Act read with Schedule I as it is in relation to furtherance of business.

The activity cannot be treated as export of services as it does not fulfil the condition of not being distinct entities.

#### **Judgment**

The liaison activities being undertaken by the Applicant (LO) in line with the conditions specified by RBI amount to supply under Section 7(l)(c) of the CGST Act.

The Applicant (LO) is required to be registered under the CGST Act.

The applicant (LO) is liable to pay GST, if the place of supply of services is India.

***Any other contrary decisions and it's reasoning in brief:***

**Takko Holding GmbH (2018 (19) G.S.T.L. 692 (A.A.R – GST))**

The authority noted that the applicant/ liaison office is working as per the terms and conditions stipulated by RBI and the reimbursement of expenses and salary of employees is paid by M/s Takko Holding GmbH to the liaison office. The applicant does not receive any consideration for any activity, and it does not have any business activities of its own as specified by RBI conditions. Further, Schedule I of CGST Act specifies that supply of services between related parties or distinct persons as per Section 25, even without consideration, constitute a supply. Takko is acting as an extension of the German Office in its procurement activities from suppliers in India as has been spelt out in the RBI permission letter. Hence, they are neither related nor distinct persons, but are in fact working as employees of the foreign office. Accordingly, none of the liaison activities of Takko is covered under the definition of supply. Hence, Takko would not be a supplier under CGST/ SGST Act and hence is not required to obtain registration under Section 22 of CGST/ SGST Act or pay CGST, SGST or IGST as applicable.

**Habufa Meubelen B.V. (2018 (14) G.S.T.L. 596 (A.A.R. – GST))**

The applicants are working as the Indian Office of M/s. Habufa Meubelen B.V. which is established as a Liaison Office with the prior permission of RBI. Except proposed liaison work, this office in India does not undertake any activity of trading, commercial or industrial nature nor would they enter into any business contracts in its own name without RBIs prior permission. There are no commission/ fees being charged or any other remuneration being received/ income being earned by the office in India for the liaison activities/ services rendered by it. The HO, Netherlands reimburses the expenses incurred by the applicant for their operations in India which are in the nature of salary, rent, security, electricity, travelling etc. The applicant does not have any other source of income and it is solely dependent on the HO for all the expenses incurred by the applicant, which are subsequently reimbursed by the HO. Therefore, the HO and Liaison Office cannot be treated as separate persons. Since, HO and Liaison Office cannot be treated as separate persons, there cannot be any flow of services between them as one cannot provide service to self and therefore, the reimbursement of expenses made by the HO cannot be treated as a consideration towards any service.

***CNK Comments:***

*The recent Karnataka AAR is contrary to the view taken by the Rajasthan AAR and Tamil Nadu AAR and once again sows the seeds of doubt for Indian liaison offices. The issue whether the activities rendered by a liaison office can be treated as supply and liable to GST has become a matter of debate - with two rulings stating that they are not liable to GST and Karnataka AAR holding that they are liable. The recent Karnataka ruling appears to be incongruent with the FEMA guidelines, which prohibits liaison offices from engaging itself in any trade/ commercial activities in India. One can hope that the Central Board of Indirect Taxes and Customs (CBIC) takes cognizance of these contrary rulings and steps in to clear the controversy soon.*

## ***DISCLAIMER AND STATUTORY NOTICE***

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