INDIRECT TAX UPDATE- AUG 2020- I ST ISSUE FOR AUGUST

S.K.KANODIA & ASSOCIATES

CHARTERED ACCOUNTANTS

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VKC Footsteps India Pvt. Ltd. Versus Union of India & 2other(s) - HC allows Refund of INPUTS in case of Inverted duty structure refund

2020-TIOL-1273-HC-AHM-GST

The Appellant i.e. VKC Footsteps in involved in the business of footwear manufacturing where the rate of input tax credit for inputs and input services is higher than the rate of output. It applied for refund on ITC under inverted duty structure. **Section 54(3) (ii) of the CGST Act lays down the eligibility criteria for the grant of refund on account of inverted duty structure or condition precedent.** It states that "no refund of unutilized input tax credit shall be allowed in cases other than where, as per clause (ii) to the said proviso, the credit has accumulated on account of rate of tax on inputs being higher than the rate of tax on output supplies", where Input tax credit includes both inputs and input services. However, **Rule 89(5) of the CGST Rules, 2017 (as amended retrospectively, vide Notification No. 26/2018-CT dated 13th June 2018) explicitly restricts such refund on input services**. Further, **Circular No. 79/53/2018-GST, dated 31st December 2018**, had also been issued to clarify that refund of input tax credit ('ITC'), would be permitted only to the extent of ITC which has 'accumulated on account of rate of tax on inputs being higher than the rate of tax on output supplies'. The **Appellant challenges the provision regarding the restriction of refund of input tax credit on input services**. It is of the opinion that refund shall be allowed for both, inputs as well as input services.

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RECENT CASE LAWS

Decision of the Court: The High Court of Gujarat held that **no rule/notification/circular can override the Act.** In the given case, the intent of the ACT is that refund of inverted duty structure shall be allowed for input tax credits which includes inputs and input services. Hence the Rules/Law cannot bar the refund of input tax credit on input services and thus the Rule was quashed as ultra vires the act.

SKKA Comments: In lieu of the above judgement, it is stated that the HC has overruled the Rules/Notification/Circular which overrides the Act. Further **emphasis is given to the intent of the law.** On plain reading of the law it is clear that refund on inverted duty structure shall be allowed on inputs tax credit other than input services. However, the intent cannot be to restrict the input tax credit on input service while allowing the credit of inputs. The **non-availability of refund of accumulated credit, as attributable to credit on input services, results in blockage of credit and consequent financial strain.**

Moreover various assessees across the country are facing the issue of accumulation of credit on account of inverted duty structure on input services. The refund application filed by the assessees have been rejected by the authorities. The judgement of Hon'ble High Court of Gujarat has far reaching impact in improving the cash flow in the ongoing difficult times of Covid – 19.

RECENT CASE LAWS

Material Recycling Association of India Versus Union of India - **POS for Intermediary services as provided by statue is binding**

2020-TIOL-1274-HC-AHM-GST

The Appellant i.e. Material Recycling Association of India is involved in the manufacture of metals & Castings etc. for various upstream industries in India. They also act as an agent for scrape, recycling companies recycling companies based outside India engaged in **providing business promotion and marketing services for principals located outside India**. The Appellant files a petition under **Article 226 of the Constitution of India challenging the constitutional validity of Section 13(8)(b) of the Integrated Goods & Services Tax Act, 2017.** Further it was contended that the said section of the IGST Act was ultra vires Articles 265 and 286 of the Constitution of India. The Appellant demanded refund of IGST paid on services provided by the members of the petitioner association and to their clients located outside India.

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RECENT CASE LAWS

Decision of the Court: The High Court of Gujarat disposed off the petition upholding the **validity of section 13(8)(b) read with Section 2(13) of the IGST Act, 2017 held that the service provided by the intermediary in India cannot be treated as "export of services". It was observed that it is rightly included in Section 13(8) (b) of the IGST Act** to consider the location of supplier of service as place of supply so as to attract CGST and SGST. However, it asked the revenue to consider the representations made by the Appellants in this regard.

SKKA Comments: Article 265 of the Constitution of India provides that "no tax shall be levied or collected except by the authority of law". Therefore, no tax can be levied or collected in India, unless it is explicitly and clearly authorized by way of legislation. Considering the contents of the article, tax is to be levied when authorized by the legislation. **In the given scenario, IGST Act constitutes a legislation and hence any item being declared as taxable under the IGST Act shall be valid.**

Further, Article 286 of the Constitution of India imposes restrictions on the imposition of tax on sale and purchase of goods. This article is explicitly in respect of sale/purchase of goods. The given case in in regards to provision of service. Hence, Article 286 of the constitution does not fall applicable.

RECENT CASE LAWS

Linde Engineering India Private Limited Versus Union of India - Export of Service under Service Tax regime- meaning of distinct establishment not to include holding and subsidiary entitiy

2020-TIOL-1285-HC-AHM-ST

The petitioner i.e. Linde Engineering Private limited **is a subsidiary of Linde AG**, Germany and is engaged in the business of providing taxable output service under the category of consulting engineer services, erection, commissioning and installation service, construction other than residential complex, including commercial/industrial building or civil structure and works contract service etc. to **various entities located in and outside India**. In the given case law it was alleged that **Linde AG, Germany and the petitioner are mere establishment of each other** and the services rendered by the Petitioner to Linde AG, Germany **would not fall within the ambit of "Export of Services" and** would therefore fall within the definition of the term 'exempted service' as defined in Rule 2(e) of the Cenvat Rules. In lieu of the same, Rule 6(3) of the Cenvat Credit Rules, 2004 shall apply.

RECENT CASE LAWS

Decision of the Court: In the given case, the High Court of Gujarat held that the **revenue misinterpreted the provisions of Explanation 3 (b) to Section 65B (44) of the Act, 1994 read with Rule 6A of the Rules, 1994. I**t can be said that the rendering of services by the petitioner No.1 to its parent Company located outside India was service rendered to its other establishment so as to deem it as a distinct person as per Item (b), explanation 3 of clause (44) of Section 65B of the Act, 1994, the **petitioner No.1 which is an establishment in India, which is a taxable territory and its 100% holding Company, which is the other company in non taxable territory cannot be considered as establishments so as to treat as distinct persons for the purpose of rendering service**. Therefore, the services rendered **by the petitioner No.1-Company outside the territory of India to its parent Company would have to be considered "export of service".**

SKKA Comments: A service shall qualify as export of service if: the provider is located in the taxable territory; the recipient is located outside India; Service is not a service specified in Section 66D of the Act; The place of provision of service is outside India; The payment has been received in convertible foreign exchange; The provider of service and recipient of service are not merely establishments of a distinct person in accordance with item (b) of Explanation 3 of clause (44) of section 65B of the Act.

Understanding the concept of '**merely establishments of a distinct persons' – it has to be the same company one of which is located in the taxable territory and other of which is located in the non-taxable territory.** In the present case, the petitioner **is a subsidiary of the company located outside India. Hence it cannot be regarded as mere establishment of the same company.** Hence the same can be treated as an export of service and not as provision of 'exempt service'.

RECENT CASE LAWS

Delhi International Airport Ltd. Versus Union of India and others - Block Credit of works contract

2020-TIOL-1270-HC-DEL-GST

The petitioner i.e. Delhi International Airport Ltd. has challenged the constitutional validity of **section 17(5)(c) & Section 17(5)(d) of the Central Goods & Services Tax Act, 2017 and Delhi Goods and Services Tax Act, 2017.** The petitioner had taken up the work of repair, maintenance and upgradation of the airport premises wherein many inputs and input services were used. However, the petitioner was denied the input tax credit of tax paid by it on works contract services as well as goods and services used in the construction of an immovable property (other than plant and machinery), despite such goods and services being used for purposes of business and to provide taxable supplies liable to GST.

Decision of the Court: the decision of the High Court has been deferred. it shall be listed along with W.P.(C) No.5457/2019 and W.P.(C) No.11633/2019 on 15th September, 2020. Counter-affidavits be filed within a period of four weeks and rejoinder-affidavits, if any, be filed before the next date of hearing: High Court.

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RECENT CASE LAWS

SKKA Comments: The facts of the case is similar to that **of M/s Safari Retreats Pvt Ltd of Orissa High Court which had allowed the credit and read down section 17(5)(c) and 17(5)(d) of the Act as ultra vires, However the said judgment has been challenged before the Apex Court and the decision is pending.** Intent of the law was to restrict the undue credit/credits used for purpose of other than business activities. Hence it denied credit on immovable property other than plant & machinery. However, for the business places such as Hospitality Sector or the Airport as in the given case, their premises is as good as plant and machinery for others. If that is not upbeat, it shall directly hit the revenue generation. Hence, the petition shall be allowed in favour of the assessee.

RECENT JUDGMENT REGARDING FORECLOSURE CHARGES BY LB OF CESTAT- IMPACT IN GST

RECENT JUDGMENT REGARDING FORECLOSURE CHARGES BY LB OF CESTAT- IMPACT IN GST

In a recent judgement of the Larger Bench of Hon'ble Madras CESTAT ***2020-TIOL-1039-CESTAT-MAD-LB CST Vs Repco Home Finance Ltd (Dated: June 08, 2020)*** held that foreclosure charges levied by banks and NBFCs on **premature termination of loan is not liable to service tax**. Even though the Judgement pertains to Service Tax and to a period prior to 2007, its far reaching impact on GST needs to be considered as principles of taxation on contractual penalties have been discussed.

As per Schedule II of the CGST Act, 2017- Activities to be treated as a supply of goods or services, in clause 5(e), where supply of services include *"agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act"*.

RECENT JUDGMENT REGARDING FORECLOSURE CHARGES BY LB OF CESTAT- IMPACT IN GST

There have ben countless Advance Rulings wherein it has been held that such contractual penalties would be **liable to GST as it tantamount to toleration of an act.**

The authorities have failed to consider the findings of the Larger Bench that:-

- *These contractual penalties are for disruption of terms between agreeing parties to a contract.*
- *It in antithesis to what the concerned parties are agreeing to.*
- *Such penalties are not an alternate mode of performance of the contract, in fact only when the contract is repudiated such penalty is applicable.*
- *The intention is to compensate the aggrieved party*
- *Merely because the contract contains a clause referring to damages/penalties, it cannot be considered as an option to violate the contract*

The above entry is to be used only in cases where the agreement itself is to tolerate or refrain from act. For example non-compete fees, tolerate of factory noise etc. The judgement of the Larger Bench should be upheld even in GST considering the fundamentals.

We need to wait and watch if CBIC comes to rescue of taxpayer clarifying the issue or another aggrieved one knocks the doors of the High Court for relief

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THANK YOU

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