India Tax Konnect

January 2025

KPMG. Make the Difference.

a. Decisions – International Tax

Amendment in the Act does not alter the taxation under the treaty: Delhi Tribunal[1]

Facts of the Case

The taxpayer, a tax resident of Singapore, provides advertising services to its clients on third-party online platforms/ websites.

During the year under consideration, it rendered the following services to its Indian group entity (a) data centre services (b) advertisement space provision (c) business support services.

The Revenue contended that the income from these services qualified as 'royalty' and 'fees for technical services' (FTS) taxable under the Income-tax Act, 1961 ('the Act') as well as the India-Singapore tax treaty ('the treaty').

Taxpayer's Contentions

Payments do not qualify as royalty

- The payments for data centre services and advertisement space do not involve the use or right to use any industrial, commercial, or scientific equipment.[2] There is no human intervention involved in the provision of data centre services.
- No tangible property or software was made available to the Indian company, and the services were accessed remotely.

Taxpayer's Contentions

Payments do not qualify as FTS

- The business support services rendered did not 'make available' technical knowledge, skills, or expertise to the Indian company as these are routine and recurring administrative services.

Revenue's contentions

Payments for data centre services constituted royalty.

Payments for advertisement space represented royalty due to the Indian company's direct access to advertising servers.

Business support services were FTS as they involved technical inputs and sub-contracting of personnel.

The Revenue relied on amendments to Section 9(1)(vi) and various judicial precedents to support their stance.

Decision

The Tribunal ruled in favour of the taxpayer, concluding that

- Payments for data centre services do not qualify as royalty under the treaty as there was no use or right to use equipment in India. Remote access for data storage does not transfer control or dominion over the equipment.
- The payments for advertisement space are not taxable as royalty as the Indian company only used third-party advertising space, with no rights or control transferred to it.

[1] ITA No. 2122/Del/2023

[2] *Asia Satellite Telecommunications Co. Ltd.* v. *DIT* [2011] 332 ITR 340 (Del)

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- The payments for advertisement space are not taxable as royalty as the Indian company only used third-party advertising space, with no rights or control transferred to it.
- The business support services rendered did not 'make available' technical knowledge, skill, or processes to the Indian company and hence did not qualify as FTS under the treaty.
- The amendments in the Act expanding the scope of royalty cannot override the restrictive definitions in the treaty.

Profit arising from hedging the business contract is business income: Delhi Tribunal[3]

Facts of the Case

The taxpayer, a tax resident of Singapore, was engaged in the trading of the agricultural commodities.

The taxpayer entered into a buying contract for palm cargo with an Indian company and subsequently, decided to settle the contract by selling the palm cargo to the same Indian company. The difference between the buying price and the selling price was received by the taxpayer as 'washout charges.'

The tax officer treated the payment as speculative income taxable under 'Other Income' article[4] of the India-Singapore treaty ('the treaty') which grants taxation right to the source state (India, in this case).

Taxpayer's Contentions

The taxpayer has undertaken the above transaction to guard against loss resulting from price fluctuation in respect of contract for actual delivery of goods sold by it.

Accordingly, washout charges arose from legitimate hedging activities integral to its business and are not speculative in nature.

The income qualifies as 'business income' under the treaty and is not taxable in India due to the absence of a Permanent Establishment (PE).

'Other Income' article does not apply since the income is dealt with under the business income article.

Revenue's Contentions

The washout charges were speculative and did not involve physical delivery, making them taxable under 'Other Income' article.

Decision

The Delhi Bench of the Tribunal ruled in favour of the taxpayer, holding that washout charges were part of hedging activities and constituted business income under the treaty.

As the taxpayer lacked a PE in India, the income was not taxable in India.

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[3] *Cargill International Trading Pte Ltd v. ACIT (ITA No. 2358/Del/2023). Source: Taxsutra*
[4] Article 23 of the treaty (Income Not Expressly Mentioned)

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b. Decisions – Domestic Tax

Interest earned on funds earmarked for acquiring a capital asset is capital in nature: Delhi High Court[5]

Facts of the case

The taxpayer was a special purpose vehicle formed as a joint venture by five public sector undertakings.

It was established to secure coal supplies for its promoter companies.

It intended to acquire a coal mine overseas.

In this regard, it received funds from one its promoter companies. A part of these funds was deposited in short-term fixed deposits yielding interest income. Simultaneously, the taxpayer paid interest to the lender company.

The transaction for the overseas coal mine acquisition was eventually aborted, and the funds were refunded to the lender.

The taxpayer argued that the interest earned is capital in nature.

The Revenue argued that the funds deposited in fixed deposits were surplus and hence the interest earned thereon was taxable as 'income from other sources' relying on the Supreme Court's judgment in *Tuticorin Alkali Chemicals & Fertilizers Ltd.*[6]

Taxpayer's contentions

The funds were not surplus but were temporarily parked in fixed deposits while awaiting deployment. Classifying these funds as surplus misconstrued their nature and purpose.

The funds borrowed were earmarked specifically for acquiring a coal mine overseas, making the interest earned an integral part of the capital asset acquisition process.

As per the accounting standards, income derived from the temporary deployment of borrowed funds during the capital asset acquisition phase should offset the cost of the asset.

The interest paid and earned were directly related to the capital project, forming part of capital work-in-progress (CWIP). These should be adjusted against pre-operative expenses rather than being treated as revenue income.

The taxpayer relied on the decisions in cases of *Indian Oil Panipat Power Consortium Ltd.*[7] and *Bokaro Steels Ltd*[8]. where interest on funds used in the pre-commencement stage was held as capital receipt.

The Revenue rejected the taxpayer's position that the interest earned could be reduced from pre-operative expenses as the capital project (coal mine acquisition) never materialized.

[5] *PCIT* v. *International Coal Ventures Pvt Ltd* (ITA No. 1174/2018). Source: Taxsutra
[6] *Tuticorin Alkali Chemicals & Fertilizers Ltd*. v. *CIT* [1997] 227 ITR 172 (SC)
[7] *Indian Oil Panipat Power Consortium Ltd. v. ITO* [2009] 315 ITR 255 (Del)
[8] *CIT v. Bokaro Steel Ltd.* [1999] 236 ITR 315 (SC)

Decision

The Delhi High Court accepted the taxpayer's position that the interest income was not taxable as revenue income. The funds were directly tied to the proposed coal mine acquisition, making the interest earned integral to the capital asset.

Referring to Accounting Standard (AS)-16 and Ind AS-23, the Court emphasised that borrowing costs or income from temporary investments of funds during capital acquisition must be adjusted against the asset's cost. This accounting treatment is applicable if the nature of asset is such that requires time for construction or putting it in use and is not true for an off the shelf product.

The Court distinguished the facts from Tuticorin Alkali Chemicals, noting that the funds in the instant case were not surplus but were earmarked for specific capital purposes.

The funds parked temporarily in fixed deposits were not excess but awaited deployment. Therefore, the interest generated was considered a part of CWIP.

Share allotted as per the court-approved amalgamation scheme is not taxable as other income: Rajkot Tribunal[9]

Facts of the Case

The taxpayer was an Indian listed company.

During the financial year 2013-14, three private companies owned by relatives of the taxpayer's promoters got amalgamated with the taxpayer.

The taxpayer issued its shares to the shareholders of the amalgamating companies.

The shares were issued based on a swap ratio calculated using a mix of discounted cash flow and book value methods.

The tax officer alleged that the calculated swap ratio led to a favourable arrangement for related parties, ignoring the fair market value and made an addition under Section 56(2)(vii)(c)(ii) on protective basis, asserting that the share issuance at a discount benefited related parties.

Section 56(2)(vii)(c)(ii) *inter alia* provided that where an individual or HUF[10] receives property (such as shares) for an inadequate consideration, then the difference between the fair market value (FMV) and the actual consideration is treated as other income in the hands of the recipient of the property. However, there is an exclusion for some of the transactions not regarded as transfer for the purposes of capital gains[11].

Taxpayer's contentions

The taxpayer argued that Section 56(2)(vii)(c)(ii) applies only to individuals or HUFs, not to public companies.

The proviso to that section excludes the transactions not regarded as transfer for the purposes of capital gains.

It submitted a 'Fairness Report' prepared by SEBI-registered merchant bankers to justify the swap ratio.

[9] *DCIT v. Rajoo Engineers Ltd* (ITA No. 460/RJT/2024). Source: Taxsutra

[10] Hindu Undivided Family

[11] Under clauses (vicb), (vid), (vii) of section 47

Revenue's contentions

The taxpayer's argument that the allotment is not a transfer should be rejected as the taxpayer has given the benefit to the individual shareholder by adopting the colourable device and by defeating the purpose of the provisions of section 56(2)(vii).

Decision

Section 56(2)(vii)(c)(ii) does not apply to a public limited company.

Section 56(2)(vii) applies only to transfers, not to share allotments under a court-approved amalgamation.

In any case, the instant transaction is excluded by virtue of the proviso to that section.

There is no anti-abuse of the provision. The shares were allotted as per the court-approved scheme after hearing all stakeholders and such scheme is conclusive.

No requirement to deduct tax on purchase of debt instruments: Mumbai Tribunal[12]

Facts of the Case

The taxpayer, a NBFC registered with the RBI, acquired Non-Convertible Debentures (NCDs), Inter Corporate Deposits (ICDs), and term loans from its related entity (PEL).

These instruments were purchased at carrying value comprising of principle value and accrued interest.

The tax authorities alleged non-deduction of tax at source[13] on accrued interest embedded in the carrying value of these financial instruments.

Taxpayer's contentions

The payments were made for acquiring the 'right to receive' the interest and the principal amount from the borrowers on maturity, not towards the interest.

No lender-borrower relationship existed between the taxpayer and PEL for the payment to qualify as interest as defined under the Act[14].

The tax was already deducted by PEL while recording the accrued interest in its books of accounts. Deducting the tax again would amount to double deduction of tax.

Revenue's contentions

The accrued interest constituted income and was subject to tax deduction.

The payments were not purely for asset transfer but included accrued interest, making tax deduction applicable.

Cited the Bombay High Court decision in the case of *American Express*[15] treating accrued interest as revenue expenditure for the buyer and taxable income for the seller.

[12] *Piramal Capital and Housing Finance Ltd*. v. *ACIT* (ITA No. 2351/Mum/2024)

[13] Under sections 193 and 194A of the Act.

[14] Section 2(28A) of the Act

[15] *American Express International Banking Corpn.* v. *CIT* [2002] 258 ITR 601 (Bom)

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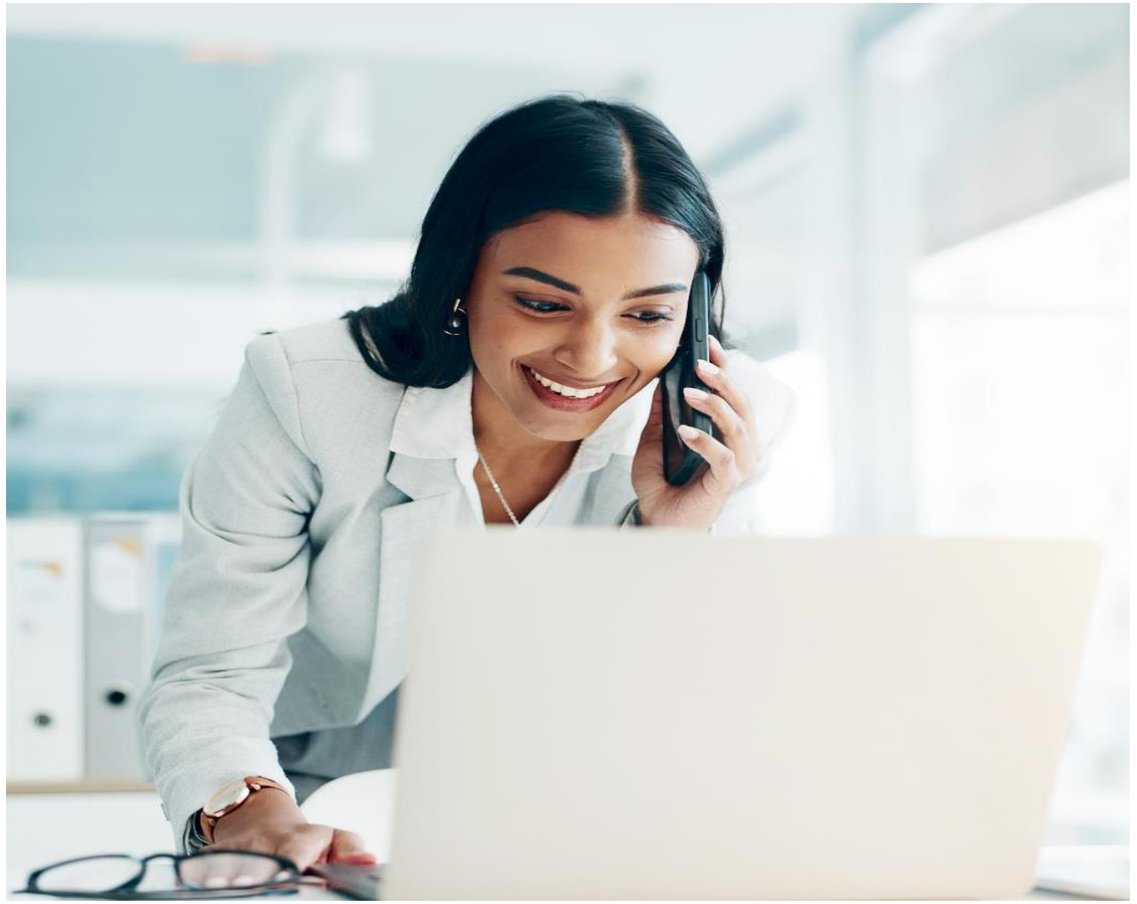
Decision

When the interest accrued to PEL, there existed lender-borrower relationship between PEL and the borrower. Subsequently, the taxpayer stepped into the shoes of PEL and such relationship between the taxpayer and the borrower came into existence. There is no lender-borrower relationship between the taxpayer and PEL and the tax deduction provisions did not apply to such transaction.

The Bombay High Court decision was in the context of determining the nature of payment as revenue or capital. It was not in the context of tax deduction provisions.

Tax on accrued interest was already deducted at the time of credit of interest in the books. There is no need to deduct tax on the same interest amount again at the time of payment.



Foreign Exchange Management Act

Exporters permitted to open and hold a Foreign Currency Account with a bank outside India

The Reserve Bank of India amends the Foreign Exchange Management (Foreign Currency Accounts held by a person resident in India) Regulations 2015[16] FEMA 10(R) vide notification dated 14 January 2025

- A new sub regulation has been inserted which permits resident exporters to open, hold and maintain a Foreign Currency Account with a bank outside India for realization of export receivables including any export advance for export of goods or services
- The funds lying in such bank account can be utilized by Exporters for paying their import payables for imports into India or repatriated into India within a period not exceeding the end of the next month from the date of receipt of the fund after adjusting for forward commitments
- The realisation and repatriation in this bank account also need to comply with the requirements of Regulation 9 of the Foreign Exchange Management (Export of Goods and Services) Regulations, 2015.

RBI consolidates all previous circulars and directions to regulate non-resident investment in debt instruments in India

On 7 January 2025, the Reserve Bank of India released its new master directions- Reserve Bank of India (Non-resident Investment in Debt Instruments) Directions, 2025[17] to regulate non-resident investment in debt instruments in India consolidating all previous circulars and directions into a comprehensive single master direction.

SNRR account can be opened with authorized dealers in India or its branches outside India

The Reserve Bank of India amends the Foreign Exchange Management (Deposit) Regulations, 2016[18] [FEMA 5(R)] vide a Notification dated 14 January 2025

- Person resident outside India can now open, hold, and maintain an SNRR Account, not only with an authorised dealer in India but also with a branch of the authorised dealer located outside India.
- Such account may be used for conducting permissible current and capital account transactions with residents of India, in accordance with the relevant rules or regulations and may also be used for transactions with non-residents.
- The tenure of the SNRR account shall now be concurrent to the tenure of the contract / period of operation / the business of the account holder accordingly, Various paragraphs of Schedule 4 of the regulation have been amended.
- An unit in an International Financial Services Centre (IFSC) may open an SNRR account with an authorised dealer in India (outside IFSC) for its business related transactions outside IFSC
- A new regulation(9) has been inserted which will permit transfer of funds, for all bona fide transactions between repatriable rupee accounts which are maintained in accordance with these regulations

[16] Notification No. FEMA 10(R)(5)/2025-RB) issued by RESERVE BANK OF INDIA (Foreign Exchange Department) on 14 January 2025

[17] Master Direction RBI/2024-25/126 - Reserve Bank of India (Non-resident Investment in Debt Instruments) Directions, 2025 dated 7 January 2025

[18] Notification No. FEMA 5(R)(5)/2025-RB. issued by RESERVE BANK OF INDIA (Foreign Exchange Department) on 14 January 2025

Reserve Bank of India (RBI) issues amendments to the Foreign Exchange Management (Mode of Payment and Reporting of Non-Debt Instruments) Regulations, 2019

RBI issues Foreign Exchange Management (Mode of Payment and Reporting of Non-Debt Instruments) (Third Amendment) Regulations, 2025[19] vide notification dated 14 January 2025. By virtue of this notification, the entries at Schedule. No. I, VI, VIII, and X of Regulation 3.1 of FEMA 395 are substituted as below

- In Schedule No. I in Para A and B regarding mode of payment, the amount of consideration shall now be paid out of funds held in any repatriable foreign currency or Rupee account instead of funds held in NRE/ FCNR(B)/ Escrow account. Same is applicable in case of issuance of Convertible Notes by an Indian start-up company
- In Schedule No. VI and VIII in Para A and B regarding mode of payment the amount of consideration shall now be paid out of funds held in any repatriable foreign currency or Rupee account instead of funds held in NRE or FCNR(B) account.
- In Schedule No. X in Para A regarding mode of payment the amount of consideration an FPI may pay in the IDRs out of funds held in a foreign currency account and/or an SNRR account and in Para B Redemption/ conversion of IDRs into underlying equity shares of the issuing company shall be in compliance with the Foreign Exchange Management (Overseas Investment) Rules, 2022.

Banking channels shall include any rupee vostro accounts, including Special Rupee Vostro Accounts, permitted to be held by a person resident outside India in terms of FEMA regulations.

[19] Notification No. FEMA 5(R)(5)/2025-RB. issued by RESERVE BANK OF INDIA (Foreign Exchange Department) on 14 January 2025

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Circulars

1. **Circular No. 240/34/2024-GST dated 31 December 2024** – Clarification on requirement for proportional reversal of Input Tax Credit ('ITC') in the hands of Electronic Commerce Operator ['ECO'].

   The ECO makes supplies on two counts:

   a) Supplies notified under section 9(5) of CGST Act, 2017 for which he is liable to pay tax as if he is the supplier.

   b) Supply of his own services by providing electronic platform for which platform fee / commission, etc. is charged.

   The circular clarifies that for the tax liable to be paid under section 9(5) of the CGST Act, 2017, the ECO is required to pay tax only through cash.

   The ITC on inputs and input services procured for providing services at (b) above can be used against the tax liability under (b).

   The proportionate reversal of ITC under sections 17(1) and 17(2) of the CGST Act, 2017 on the said inputs and input services is not required.

2. **Circular No. 241/35/2024-GST dated 31 December 2024 -** Clarification on availability of ITC under Ex-Works ('EXW') supply contracts

   The circular clarifies the eligibility of ITC where goods are delivered under EXW contracts, and ownership of the goods is transferred to the buyer at the supplier's premises upon the handover of goods to the transporter, as instructed by the buyer.

   The circular explains that, for the purpose of ITC eligibility, the 'receipt' of goods can be deemed to occur when the supplier hands over the goods to the transporter on buyer's behalf, even if the physical delivery to the buyer's premises takes place later. This aligns with the Explanation to section 16(2)(b) of the CGST Act, 2017, which allows deemed receipt through any other person *(in this case, the transporter)*.

   It further clarifies that ITC is available at the time the goods are handed over to the transporter, provided all other conditions under sections 16 and 17 of the CGST Act, 2017 are satisfied, such as the use of goods in the course or furtherance of business. However, ITC will not be available if the goods are diverted for non-business purposes or lost after such deemed receipt.

3. **Circular No. 242/36/2024-GST dated 31 December 2024 -** Clarification on place of supply of online services supplied to unregistered recipients

   The clarification deals with non-compliance by suppliers in not recording the state name of the unregistered recipient on the invoice and thereby declaring the place of supply of such services as the location of the supplier as per section 12(2)(b)(ii) of the IGST Act, 2017. This resulted in a wrong declaration of the place of supply, resulting in the flow of revenue to the wrong state.

   It has been clarified that section 31(2) of the CGST Act, 2017, read with proviso to rule 46(f) of the CGST Rules, 2017, mandates that a supplier supplying any online/ digital services records the name of the state of the recipient on the tax invoice, irrespective of the value of supply of such services, and declare the place of supply of the said services as the location of the recipient.

   It has also been clarified that if the supplier fails to record the name of the

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state of the unregistered recipient on the invoice, penal consequences under the provisions of section 122(3)(e) of the CGST Act, 2017 will be attracted.

4. Circular No. 243/37/2024-GST dated 31 December 2024

- GST applicability on sale of vouchers

Whether voucher covered as a pre-paid instrument recognized by RBI	Whether supply of voucher is a 'supply' under GST?
Yes	• Will be considered as 'money' • Thus, excluded from definition of 'goods' and 'services' • Therefore, not a supply of goods and/or services
No	• Will be considered as an 'actionable claim' • Thus, as per entry 6 of Schedule III, will not be considered as a supply of goods and/or services

- GST treatment of transactions in vouchers by distributors/Sub-distributors/agents

Distribution of vouchers on	Mechanism	GST applicability
P2P basis	• Purchase of voucher by distributor/dealer from voucher issuer at a discounted rate • Sale of voucher to sub-distributors/corporates/end customers after retaining a margin	• Distributors/dealers own the vouchers in this case; • Transaction in vouchers including trading in vouchers is neither supply of goods nor supply of services; • Thus, no GST
On commission /fee basis	• Distributors/sub-distributors work as agent in this model. • The voucher issuer specifies a set of obligations on such agents such as marketing & promotion and other related support activities against a commission/fee.	• Distributors/dealers do not own the vouchers in this case; • Thus, GST will be payable on the commission/fee

- GST treatment of transactions in vouchers by distributors/sub-distributors/ agents

  Additional services such as advertisement, co-branding, marketing, customisation, technology support, and customer support provided by distributors or other parties to the voucher issuer are subject to GST.

- GST treatment of unredeemed vouchers (breakage)

  In case of vouchers remaining unredeemed/unused at the end of their expiry period, businesses make book adjustments and account for the same as income in their books terming it as 'breakage'.

  There would be no GST on breakage in case of unredeemed vouchers due to the following reasons:

  - No underlying supply of goods and/or services on account of such unredeemed vouchers
  - Amount retained for unredeemed vouchers cannot be considered as consideration for any supply.
  - There is no agreement between voucher issuer and redeemer for payment of any amount in case of non-redemption of voucher. Therefore, in terms of the Circular 178/10/2022-GST, it cannot be considered as 'monetary value of any act or forbearance, in respect of, in response to, or for the inducement of, the supply of goods or services or both, whether by the recipient or by any other person.'
  - Thus, the amount attributable to unredeemed vouchers (breakage) would not be subject to GST.

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Notifications

1. **Notification 1/2025- Central Tax (Rate) dated 16 January 2025** (effective from 16 January 2025)

   - GST rate on Fortified Rice Kernel ('FRK') has been reduced to 5%.
   - Definition of 'pre-packaged and labelled' amended in rate notification 1/2017-Central Tax (rate) dated 28 June 2017 to cover all commodities that are intended for retail sale and containing not more than 25 kg or 25 litre, which are 'pre-packed' as defined under the Legal Metrology Act, or a label affixed thereto is required to bear the declarations under the provisions of the Legal Metrology Act and Rules made thereunder.

2. **Notification 2/2025- Central Tax (Rate) dated 16 January 2025** (effective from 16 January 2025)

   - Gene therapy exempted from GST
   - Definition of 'pre-packaged and labelled' amended in exemption notification 2/2017-Central Tax (Rate) dated 28 June 2017 to cover all commodities that are intended for retail sale and containing not more than 25 kg or 25 litre, which are 'pre-packed' as defined under the Legal Metrology Act, or a label affixed thereto is required to bear the declarations under the provisions of the Legal Metrology Act and Rules made thereunder.

3. **Notification 3/2025- Central Tax (Rate) dated 16 January 2025** (effective from 16 January 2025)

   - Concessional 5% GST rate extended to food inputs used for food preparations

   covered under chapters 19 or 21 which are intended for free distribution to economically weaker sections by Government.

4. **Notification 4/2025- Central Tax (Rate) dated 16 January 2025** (effective from 16 January 2025)

   - GST rate on old and used vehicles including EVs increased from 12% to 18% on the margin.

5. **Notification 5/2025- Central Tax (Rate) dated 16 January 2025** (effective from 1 April 2025)

   Notification 11/2017 amended for the following changes:

   - Definition of 'declared tariff' omitted,
   - Definition of 'specified premises' amended to mean:
     - Premises for which actual rent of any unit in the hotel in the preceding financial year exceeded INR 7500
     - Premises for which the registered person furnished a declaration, on or after 1 January and 31 March of the preceding financial year, declaring the said premises to be a specified premises
     - Premises for which the registered person furnished a declaration, within 15 days of obtaining acknowledgement for the registration application, declaring the said premises to be a specified premises

6. **Notification 6/2025- Central Tax (Rate) dated 16 January 2025** (effective from 16 January 2025

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- Insurance services provided by the Motor Vehicle Accident Fund[20], against contributions made by insurers out of the premiums collected for third party insurance of motor vehicles exempted

7. **Notification 7/2025- Central Tax (Rate) dated 16 January 2025** (effective from 16 January 2025)

   - A body corporate providing sponsorship services to a body corporate or partnership firm brought out of reverse charge.

   - Notification 9/2024-Central Tax (Rate) dated 8 October 2024 that prescribed reverse charge on renting of any immovable property other than residential dwelling by any person to a registered person amended to exclude the registered recipients who are composition taxpayers from the levy.

8. **Notification 8/2025- Central Tax (Rate) dated 16 January 2025** (effective from 1 April 2025)

   - Definition of 'specified premises' for the purpose of Notification 17/2017-Central Tax (Rate) dated 28 June 2017[21] amended to provide that the same shall be as mentioned in Notification 11/2017-Central Tax (Rate) dated 28 June 2017

9. **Notification 1/2025- Compensation Cess (Rate) dated 16 January 2025** (effective from 16 January 2025)

   - Compensation Cess on supplies to merchant exporters reduced to 0.1% subject to fulfilment of certain conditions.

10. **Notification 1/2025- Customs dated 16 January 2025** (effective from 16 January 2025)

    - BCD and IGST on imports of all equipment and consumable samples by Inspection Team of IAEA[22] exempted subject to certain conditions

11. **Notification 2/2025- Customs dated 16 January 2025** (effective from 16 January 2025)

    - BCD and IGST exemption extended to systems, sub-systems, equipment, parts, sub-parts, tools, test equipment, software meant assembly/manufacture of LSRAM[23] system

Instructions

1. **Instruction 1/2025- GST dated 13 January 2025**

   - This instruction has been issued to amend earlier instruction providing guidelines for arrest and bail in relation to offences punishable under the CGST Act, 2017.

   - The earlier instruction provided that the grounds of arrest must be explained to the arrested person and this fact must be noted in the arrest memo. This instruction, in lieu of the Hon'ble Delhi High Court judgement in case of Kshitij Ghildiyal[24], provides that along with explaining the grounds of arrest to the arrested person, he should be communicated such grounds in writing as an annexure to the arrest memo and acknowledgement of the same shall be obtained.

[20] Constituted under section 164B of the Motor Vehicles Act, 1988 (59 of 1988)
[21] Notified services on which tax is liable to be paid by ECOs and includes restaurant service other than services supplied by restaurant, eating joints etc. located at specified premises

[22] International Atomic Energy Agency
[23] Long Range Surface to Air Missile System
[24] [W.P. (CRL) No. 3770/2024]

Indirect Tax...

High Court decisions

ITC availed under incorrect heads not required to be reversed[25]

The petitioner had inadvertently availed credit of IGST as CGST and SGST in GSTR-3B. The petitioner received a show cause notice ('SCN') under section 73 of the CGST Act, 2017 for recovery of such CGST and SGST along with interest and penalty. The adjudicating and appellate authority also confirmed the demand. Aggrieved by the order, the petitioner approached the Kerala High Court.

The High Court relied on its own judgement in the case of *Rejimon Padickapparambil Alex*[26] ('Rejimon') in an almost similar situation. The High Court view in Rejimon held as follows:

- In this judgement, the Court agreed with the view taken in the order passed by a Bengaluru Officer[27] on a similar issue which was shown to the Court by the petitioner. The view was as follows:
  - ✓ Section 49(5) of the CGST Act, 2017 permits utilisation of IGST against IGST, CGST and SGST. The only restriction is for utilisation of CGST against SGST liability and vice-versa.
  - ✓ In the instant case, the petitioner availed ITC under CGST and SGST instead of IGST and utilised the same for payment of CGST and SGST on outward supplies. Therefore, based on the interpretation of section 49(5) of the CGST Act, 2017 and the specific order of priority for utilising ITC, the petitioner's actions are consistent with the legal framework.
  - ✓ Further, CBIC Circular No.192/04/2023-GST dated 17 July 2023 had given clarification on charging of interest under section 50(3) of the CGST Act, 2017, in cases of wrong availment and subsequent reversal of IGST. The circular clarified that the total ITC (i.e. IGST+CGST+ SGST) available in electronic credit ledger ('ECrL') has to be considered for calculation of such interest and not ITC under individual heads.
  - ✓ Thus, the essence of the circular is that the ITC available in the ECrL should be considered as a pool of funds designated for different types of taxes, such as IGST, CGST and SGST. These accounts represent a wallet with compartments for IGST, CGST, and SGST funds. Therefore, while determining interest under rule 88B of the CGST Rules, 2017, the entire wallet has to be taken into consideration, not just individual compartments.
  - ✓ Therefore, the GST system treats the ECrL as a unified resource, and interest is incurred if, collectively, the available funds fall below the amount of wrongly availed credit.
  - ✓ Adopting the same analogy in the instant case, since there is no loss of revenue to Center/State arising from the utilisation of CGST/SGST instead of IGST, reversal of ITC is not required and SCN is dropped.
- In furtherance to the above, the Court held that section 73 of the CGST Act, 2017 applies where ITC has been wrongly availed or utilised. In the instant case, there is no wrong availment of ITC.

Relying upon the above analysis in the case of Rejimon, the High Court quashed the order in this case.

[25] *Kalleppuram Metals* [2025-VIL-10-KER]
[26] 2024-VIL-1284-KER
[27] Assistant Commissioner of Central Tax, East Division-6, Bengaluru

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Assignment of Leasehold Rights in Land Not Liable to GST[28]

The petitioner was established under the Gujarat Industrial Development Act, 1962, and it functions as the nodal agency for industrial development. The petitioner has allocated plots of land to industrial entities on a long-term lease for a period of 99 years. The lease deed permits the lessee to assign their leasehold rights and interests in the plot to another party, subject to the petitioner's approval. The GST authorities issued summons and SCNs to the allottees of the petitioner who assigned their leasehold rights, demanding GST at the rate of 18% on the lump sum consideration received from the assignee, treating it as a taxable supply of service under GST. In response, writ petitions were filed before the Gujarat High Court by the affected parties.

The petitioner contended that leasehold rights are immovable property, as defined under various laws, including the Transfer of Property Act, 1882, and the General Clauses Act, 1897. Assignment of leasehold rights constitutes an absolute transfer of property, extinguishing the assignor's legal relationship with the property. Para 5 of Schedule III of the CGST Act, 2017 excludes the sale of land and buildings from GST. Imposing GST on such transactions amounts to double taxation, given the payment of stamp duty.

Revenue's contentions were that the leasehold rights do not qualify as immovable property under GST law and their transfer constitutes a 'supply of service'. GST applies to such transactions. GST and stamp duty are separate levies that address different aspects of the transaction.

In this case, the Gujarat High Court ruled that leasehold rights include benefits arising from land and are thus considered immovable property. In a lease arrangement, the title to the property remains with the petitioner, with all rights reverting to it upon expiry of the lease. However, the transfer of leasehold rights by the assignor to the assignee results in the assignor divesting all absolute rights in the property. The outright transfer of leasehold rights extinguishes the assignor's relationship with the property, constituting a sale. Such transactions are explicitly excluded from GST under Para 5 of Schedule III of the CGST Act, 2017. The court underscored that extending GST to immovable property would contradict constitutional and legislative provisions. Therefore, the High Court held that the assignment of leasehold rights is not subject to GST.

Amended formula for Inverted duty refund under rule 89(5) of the CGST Rules, 2017 is applicable retrospectively[29]

The petitioner filed application for refund of unutilised ITC on account of inverted duty structure ('IDS refund') prior to 5 July 2022 [i.e. date of amendment in formula under rule 89(5) of CGST Rules, 2017]. The petitioner was granted refund by the unamended formula. Thereafter, the petitioner filed a refund application for differential refund as per the new amended formula that was introduced from 5 July 2022. The refund was rejected on the ground that refund as per amended formula is not admissible to petitioner. The petitioner, therefore, approached the High Court against such refund rejection.

[28] *Gujarat Chamber of Commerce and Industry* [TS-03-HC(GUJ)-2025-GST]

[29] *Tirth Agro Technology Private Limited* [2025-VIL-16-GUJ]

Indirect Tax...

In this case, the Gujarat High Court discussed the following:

- Judgement of VKC Footsteps India Private Limited[30] that upheld the validity of rule 89(5) of the CGST Rules, 2017 but observed anomalies in the formula prescribed therein,
- The amended and unamended formula under rule 89(5) of the CGST Rules, 2017;
- Notification 14/2022-Central Tax dated 5 July 2022 bringing this amendment;
- Circular 181/13/2022-GST dated 10 November 2022 explaining that the amendment is clarificatory and is applicable prospectively w.e.f. 5 July 2022;
- The relevant extract from the minutes of the 47th GST Council Meeting discussing about anomalies observed by Supreme Court in the formula under rule 89(5) of the CGST Rules, 2017 in case of VKC Footsteps India Private Limited *(supra)* and thus, the need to revise the formula.

The High Court relied upon its decision taken in the case of Ascent Meditech Ltd[31] on this matter which is as follows:

- The amendment made in rule 89(5) of the CGST Rules, 2017 is clarificatory only as it is made as per the decision of the GST council pursuant to the direction of the Supreme Court.

- Circular No. 181/13/2022 dated 10 January 2022 which provides that the amendment is not clarificatory in nature is contrary to the purport of the amendment brought to correct the anomaly in the formula under rule 89(5) of the CGST Rules, 2017.

- Decision in case of Allied Motors (P.). Ltd[32] (referred by petitioner) is squarely applicable in this case. In this case, the issue involved was whether proviso to section 43B of Income Tax Act, 1961 is to be given prospective or retrospective effect and the Supreme Court held as follows:

  "*A proviso which is inserted to remedy unintended consequences and to made the provision workable, a proviso which supplies an obvious omission in the section and is required to be read into the section to give the section a reasonable interpretation, requires to be treated as retrospective in operation so that a reasonable interpretation can be given to the section as a whole*."

- As observed by G.P. Singh in his Principles of statutory Interpretation, 4th Edn. Page 291, "*It is well settled that if a statute is curative or merely declaratory of the previous law, retrospective operation is generally intended.*"

- Denying the refund only because the petitioner has been granted the refund prior to 5 July 2022 would create a discrimination resulting into inequality between the assesses who have been granted refund prior and post 5 July 2022. The impugned circular is therefore contrary to the provisions of the Act.

- As per the provisions of section 54(1) read with section 54(3) of the CGST Act 2017, if the assessee has made refund application within the prescribed period of two years, then the assessee would be entitled to the refund as per the amended formula.

- Therefore, the amendment in rule 89(5) of the CGST Rules, 2017 is applicable retrospectively. Thus, the impugned order and Circular 181/2022 are quashed and set aside.

- Relying upon the above judgement, the court directed the respondents to release the differential refund amount.

[30] 2021-VIL-81-SC
[31] 2024-VIL-1273-GUJ
[32] (1997) 3 SCC 472

Indirect Tax...

Negative blocking of electronic credit ledger is permissible under rule 86A of the CGST Rules, 2017[33]

The petitioner was issued orders directing blocking of the electronic credit ledger ('ECrL') by State Tax authorities. The amount blocked by such orders was more than the amount available in the ECrL at the time of blocking i.e. negative blocking. Aggrieved by such order, the petitioner approached the Madras High Court.

The petitioner contended that for blocking of ECrL, the credit should be available in ECrL at the time of blocking. If there is nil balance in the ECrL, there cannot be any negative blocking of credit since it is not permissible under rule 86A of the CGST Rules, 2017. The petitioner also relied on the judgements of Gujarat High Court in case of *Samay Alloys India Pvt. Ltd*.[34] and Delhi High Court in case of *Best Crop Science Pvt. Ltd*.[35]

In this case, the High Court discussed the decisions pronounced by the Gujarat and Delhi High Courts *(supra)*. These decisions had interpreted the first part of rule 86A of the CGST Rules, 2017 literally that uses the phrase 'credit of input tax available in the electronic credit ledger' and accordingly, held that if no ITC is available in the ECrL or if such ITC has already been utilised, rule 86A of the CGST Rules, 2017 cannot be invoked.

However, the High Court analysed the second part of rule 86A of the CGST Rules, 2017 and held that 'amount equivalent to such credit for discharge of liabilities' used therein would mean an amount equivalent to fraudulently availed credit even if utilised for discharge of liabilities under section 49 of the CGST Act, 2017.

Thus, the Court held that a conjoint reading of first and second parts of rule 86A of the CGST Rules, 2017 would clearly reveal that the word 'available in the ECrL' referred in first part would mean that the amount available after the fraudulent availment of ITC at any point of time, whether available in the ECrL or already utilised, at the time of passing the blocking orders.

The Court further held that rule 86A of the CGST Rules, 2017 nowhere states that the negative blocking is prohibited. If such was the intention of the legislature, they would have done so by way of proviso or otherwise. Rule 86A of the CGST Rules, 2017 was incorporated keeping in mind that in majority cases, the authorities may come to know about wrongful availment of ITC after its utilisation by the registered person. Thus, when a literal interpretation of rule provides a meaning, which is not in consonance with its object and purpose, the Court necessarily has to look into the object and purpose of the Statute and interpret it in a manner to reflect the real intention, object and purpose of the rule. In this case, rule 86A of the CGST Rules, 2017 was incorporated to stop debiting the fraudulently availed ITC in ECrL.

Based on the above analysis, the Court held that the authorities are empowered to pass negative blocking orders.

[33] *Tvl. Skanthaguru Innovations Private Limited* [TS-793-HC (MAD)-2024-GST]
[34] 2022 (61) GSTL 421 (Guj.)
[35] (2024) 22 Centax 531 (Del.)

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