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INDIRECT TAX

Newsletter - April 2024

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Instructions

Central Board of Indirect Taxes and Customs issues Guidelines to field formations for conducting investigation.

Instruction No. 01/2023-24-GST (Inv.) dated March 30, 2024

The Central Board of Indirect Taxes and Customs (CBIC) has issued Guidelines to the field formations for conducting investigation and undertaking enforcement activities under the Central Goods and Service Tax Act, 2017 (CGST Act), with a view to standardize investigation protocol, avoid parallel investigation by multiple Commissionerates/ Directorate of Goods and Services Tax Intelligence (DGGI) and to promote ease of doing business. The key guidelines are highlighted hereinbelow:

- Within the allocated jurisdiction of a Commissionerate, the Principal Commissioner will be responsible for developing and approving any intelligence, conducting search, completing investigation in a case and the relevant subsequent action and any information which pertains to another Central Goods and Services Tax (CGST) field formation shall be forwarded by him to the concerned field formation or DGGI.

- Investigation is to be initiated after obtaining the prior approval of Principal Commissioner. However, in specific cases such as (i) interpretational issues seeking to levy tax for the first time, (ii) concerning big industrial house/major multinational corporations, (iii) sensitive matters or (iv) matters already before the Goods and Service Tax (GST) Council, prior written approval of Zonal Principal Chief Commissioner will be required for initiation of investigation. Additionally, in such matters, the field formations are required to collect details regarding the prevalent trade practices, nature of transactions and assess the implications/impact prior to taking any action.

- To avoid parallel investigation by multiple Commissionerates and/ or DGGI, feasibility of only one of the offices pursuing the investigation must be discussed.

- Subject to protocol as has been laid down, in case of investigation being conducted by a Commissionerate on an issue which may be relevant to some or all the GSTINs of the taxpayer, DGGI may be requested to take up the investigation.

- In cases involving interpretational issues where the taxpayer has followed a prevalent trade practice, it has been recommended that the Zonal Principal Chief Commissioner makes a self- contained reference to the relevant policy wing of the CBIC.

- For initiating investigation against listed companies, Public Sector Undertakings (PSUs), Government Agencies/Departments/Authority, official letter should be initially addressed to the officers of such entities and requesting for submission of information within reasonable time rather than issuing summons.

- Vague and cryptic letters/summons not to be issued for conducting fishing and roving inquiry. Moreover, information available on GST Portal may not be called for by way of letters/summons.

- Investigation must be concluded expeditiously and not more than one year.

- Taxpayers may approach the Additional/Joint Commissioner in-charge of the investigation in case of grievance and may consider meeting the Principal Commissioner, in case the reasonable grievance persists.

In the past, the taxpayers have been at the receiving end of multiple Commissionerates investigating the same issue resulting in duplicity of proceedings. Such actions have also been challenged by the taxpayers before the High Courts and have been subjected to judicial scrutiny. The issuance of the Guidelines, thus, is a positive step which should streamline investigation, promote transparency, and prevent undue harassment to the taxpayers. However, the efficacy of the Guidelines will ultimately depend upon the implementation and its adherence by the field formations.

Notification

Remission of Duties and Taxes on Exported Products Scheme extended to Advance Authorization holders, Export Oriented Units and Special Economic Zone units.

Notification No. 70/2023 dated March 8, 2024, issued by the Directorate General of Foreign Trade

The Government of India has extended the Remission of Duties and Taxes on Exported Products (RoDTEP) scheme even to Advance Authorization (AA) holders (except deemed exports), Export Oriented Units (EOU) and Special Economic Zone (SEZ) units. Earlier the above category of exporters had been kept outside the purview of the RoDTEP Scheme under the ineligible category.

Additionally, the RoDTEP Scheme (aimed at refunding various embedded taxes and duties on exported products), which was previously extended till June 30, 2024, has further been extended till September 30, 2024.

Extending the RoDTEP scheme to AA, EOU, and SEZ units will provide crucial support to the exporting community amid global economic uncertainties and supply chain disruptions. Key sectors such as Engineering, Textiles, Chemicals, Pharmaceuticals & Food Processing etc. stand to benefit from the measure.

Judgments

Himachal Pradesh High Court declares levy of 'water cess' under Himachal Pradesh water cess on Hydropower Generation Electricity Act and the Rules framed thereunder as ultra vires the Constitution of India.

NHPC Ltd. & Ors. vs. State of H.P. and Anr. [CWP No. 2916/2023]

The Petitioners, being power generation companies, challenged the legislative competence, constitutionality, and the vires of the Himachal Pradesh water cess on Hydropower Generation Act, 2023

(Impugned Act), whereunder a 'water cess' was liable to be paid for the water drawn from any source for generation of hydropower.

The High Court, after threadbare analysis and examination of the underlying statutory provisions, held against the constitutionality of the Impugned Act, basis the following reasoning:

On nature and taxable event: The High Court noted that the cess had not been levied on 'water' but on 'generation of electricity'. The taxable event was 'hydropower generation' and not the 'usage of water' as no tax was to be levied in the absence electricity generation. In other words, the 'user of water' is not being taxed but the 'user of water for generation of electricity', who is being taxed. Further, the Impugned Act did not provide for the measure of levy as the cess had been calibrated with the height from which the water fell on the turbine, which the Court found to be wholly irrelevant.

On legislative competence: The High Court, after considering the charging Section, taxable event and the nature of levy as well as subjecting the Impugned Act to the test of 'pith and substance', concluded that the said Act sought to impose tax on generation of electricity and not merely on water as subject or the event of drawl of water, which is beyond the legislative competence of the State. It is the Central Government alone which could levy tax on generation of electricity. The Court found that the competence of the State to promulgate the Impugned Act could not be traced to either Entry 49 (Taxes on land and building) or Entry 50 (Taxes on mineral rights subject to any limitations imposed by Parliament by law relating to mineral development) or Entry 45 (Land revenue, including the assessment and collection of revenue, the maintenance of land records, survey for revenue purposes and records of rights and alienation of revenues) of List II of the Seventh Schedule of the Constitution of India. The Court also rejected that such power could be traced to Entry 17 & 18 of List II, which were general entries pertaining to land and water and it is settled law that taxation entries are distinct from general regulatory entries.

On excessive delegation of power: The High Court held that Impugned Act suffered from the vice of excessive delegation of power by the State Legislature insomuch as that the power of fixation of rates had been delegated to the executive i.e., the Government of Himachal Pradesh, without any legislative policy or guidance.

Consequently, the Impugned Act and the rules framed thereunder were declared to be beyond the legislative competence of the State and ultra-vires the Constitution of India.

Previously, the Ministry of Power, Government of India had issued a letter, which was followed by a circular, to the State Governments whereby it was directed not to levy/ remove any kind of tax/ duty/ cess levied in the guise of development fee/ charges/ fund on generation of electricity as the same is beyond their legislative competence. However, contrary to the stand of the Central Government, the State Government of Himachal Pradesh proceeded to levy 'water cess' on the power generation companies. The present judgement of the Himachal Pradesh High Court has reinforced the position of the Central Government and has consequently brought major relief to the power generation companies.

Hostel services to working women exempt from GST.

Thai Mookambikaa Ladies Hostel vs Union of India [W.P No. 28486 of 2023]

The Karnataka High Court, quashing the ruling passed by the Authority of Advance Ruling (AAR), has held that the renting out of hostel rooms to girl students and/ or working women is exempt from the levy of GST.

The Petitioner ran hostels providing accommodation and food to girl students and working women and had sought an advance ruling on the taxability thereof. The AAR held that the services by way of providing hostel accommodation were not eligible for exemption and consequently, the supply of in- house prepared food to the inmates of the hostel, being composite supply, was also taxable.

The High Court, upon examining the relevant Exemption Notification, noted that services provided by way of renting 'residential dwellings' for 'residential purpose' were exempt from GST. The High Court observed that in order to claim GST exemption, the end-use should be 'residential', which cannot be decided either by the nature of the property or the nature of business of the service provider, but by the purpose of which it is used, 'residential dwelling'.

The High Court observed that the exemption was given to any person who may engage in renting residential dwellings used as residence. The Court observed that for the working women and professionals, the said hostel room was residential dwelling unit. The inmates of the respective hostels run by the Petitioner were girl students and the working women who are not registered persons and using the premises as their residence, for which, they were paying fee, which can be termed as rent and such inmates were not carrying on any commercial activities or using the hostel for commercial purpose. No commercial activities could also be attributed against the Petitioner/ owners of the hostels since they had been providing only 'residential accommodation' to the girl students, working women, etc., who are using the 'hostel premises' as their residence and not for business purpose by using the common kitchen and sharing the food among themselves.

Accordingly, the Court held that the word 'residential dwelling' referred in the relevant Exemption Notification would include the hostel facilities provided by the Petitioners to the inmates of the hostels insomuch as the hostel room is a residential dwelling unit for them. Accordingly, the 'hostel services' provided by the Petitioners were exempted from the levy of GST.

The Karnataka High Court in the afore-mentioned decision has interpreted 'residential dwelling' for the purpose of exemption under GST, thereby, clarifying the issue much to the relief of service providers rendering hostel accommodation services. This may be relevant for universities and coaching centers which may also be providing hostel facilities to their enrolled students.

Madras High Court quashes proceedings initiated by Central GST Authorities in the absence of any cross- empowerment.

Tvl. Vardhan Infrastructure vs. The Special Secretary and Ors. [W.P. Nos. 34792, 29878, 30607 of 2023]

In the present case, whereas the Petitioners were assigned jurisdiction of State Tax Authorities, proceedings against them had been initiated by the Central Tax Authorities, which was accordingly challenged before the Madras High Court.

The High Court, after thoroughly examining the legislative history, noted that Section 6(1) of the respective GST enactments (CGST Act and State Goods and Services Tax Act) empowers the Government to issue notification for cross-empowerment on the recommendations of the GST Council. However, under the said Section of the respective GST enactments, no notifications had been issued for cross- empowerment except for the purpose of refund of tax.

The High Court held that the Officers under the State or Central Tax Administration cannot usurp the power of investigation or adjudication of a taxpayer who is not assigned to them. Thus, if a taxpayer is assigned to the Central Tax Authorities, the Officers of the State Tax will have no jurisdiction to interfere in assessment proceedings and vice versa although such Officers may have intelligence regarding the alleged violation of the GST laws by the Taxpayer.

The cross-empowerment of Central and State Tax Authorities to take intelligence- based reinforcement action against the taxpayer was first deliberated by the GST Council in its 9th Council meeting held on 16 January 2017, i.e., prior to the enactment of GST Laws. However, no notification, except for the purpose of refund of tax, has been issued till date regarding the cross-empowerment. Despite the absence of such notification, the Central/State Tax Officers often initiate intelligence-based investigations against the taxpayers who are not assigned to them, which often leads to parallel proceedings. The decision of the Madras High Court will likely reduce such parallel proceedings against the taxpayer and enhance the coordination between Central and State Tax Authorities in intelligence-sharing to curb evasion of tax.

Bombay High Court holds Deputy Commissioner of CGST (Audit) to be proper officer for issuance of audit report.

Formento Resorts and Hotels Ltd. vs. Union of India & Ors. [Writ Petition No. 662/2023]

The Bombay High Court has upheld the constitutional validity of Circular No. 3/3/2017- GST dated July 5, 2017 (Impugned Circular) and subsequent amendments made thereto, whereby the CBIC assigned functions as 'proper officers' to various officers of Central Tax under different sections of the CGST Act.

The Impugned Circular, issued under Section 2(91) of the CGST Act, was challenged on the ground that under Section 2(91), no powers have been conferred upon the CBIC to issue circulars and confer any power of assignment of functions of proper officer. Section 2(91) defines 'proper officer' in relation to any function to be performed under the CGST Act, to mean the Commissioner or the officer of the central tax who is assigned that function by the Commissioner in the Board.

The High Court examined Section 2(91) of the CGST Act as well as the provisions of Section 3 (which empowers the Central Government to appoint Central Tax officers), Section 5 (which provides that a Central Tax Officer can exercise the powers and discharge the duties conferred or imposed under the CGST Act) and Notification No. 2/2017- Central Tax dated June 19, 2017 (issued under Section 3 and 5 of the CGST Act) whereby certain Central Tax Officers have been appointed for the purpose of CGST Act and vested with powers under the CGST and IGST Act.

Upon its analysis, the Court concluded that the Centra Government and the Board have exercised powers vested in them by Section 3 and 5, respectively, in the context of assigning the functions of "proper officer" upon the Commissioner or the officers of the Central Tax. The Central Government has issued the Notification dated June 19, 2017, in the exercise of powers conferred by Section 3 r/w Section 5 of the CGST Act which constitutes the Commissioner of Central Tax (Audit) and Central Tax officers subordinate to him as central tax officers. The Impugned Circular dated July 05, 2017, was issued by the Board which is the proper authority in terms of Section 2(91) of the CGST Act and this was the reason for referring to Section 2(91) of the CGST Act. Thus, while the Impugned Circular refers to inter alia Section 2 (91) of the CGST Act, which provides the definition of 'Proper Officer', the source of power is contained in other provisions of the CGST Act, which were also referred to in such Circular. The High Court cited various decision of the Hon'ble Supreme Court wherein it was held that mentioning of wrong provision or omission to mention the provision which contains the source of power will not vitiate the exercise of the power so long as the power exits and can be traced to an available source of law. Thus, the Circulars were held to be intra-vires and resultantly, the audit report and show cause notices issued were held to be valid.

The High Court further distinguished the judgement of the Supreme Court in *Canon India Private Limited vs. Commissioner of Customs [Civil Appeal No. 1875 OF 2018]* observing that in the said judgment the Board had assigned the functions of the 'Proper Officer' on the officers of Directorate of Revenue Intelligence (DRI), which were not 'Custom Officers'. However, in the present case, the Assistant/Deputy Commissioner of CGST (Audit) were 'Central Tax Officers'.

The decision of the Bombay High Court marks a significant development in the ongoing discourse surrounding the designation of various officers of the Revenue as 'Proper Officers' under the GST regime. Earlier, the Allahabad High Court in R.C Infra Digital Solutions vs. Union of India [Writ Tax No. 229 of 2023] and Gujarat High Court in Yasho Industries Limited versus Union of India [R/Special Civil Application No. 7388 of 2021] had held that the Officers of the DGGI are 'Proper Officers' to issue summons and to conduct search and seizure.

No service tax in case of non-compete clause.

Shri Aprameya Radhakrishna vs. Commissioner of Central Tax [Service Tax Appeal No. 20227 of 2020]

The Appellant entered into a share purchase agreement for transfer of its shares. The said agreement contained a non-compete clause requiring the Appellant to not compete with the purchaser-transferee. The Revenue Authorities proposed and confirmed service tax demand on the ground that the agreement clause requiring the Appellant to not compete with the purchaser- transferee amounts to rendering a taxable service of toleration of an act. Regarding consideration for the said service, Revenue Authorities alleged that the consideration for sale of shares mentioned in the agreement was sufficient to constitute consideration for the alleged service. The Appellant being aggrieved, filed an appeal before the Customs, Excise and Service Tax Appellate Tribunal, Bangalore (Tribunal).

The Tribunal observed that the transfer carried out by the Appellant vide share purchase agreement was related to an ongoing concern and was exempted from the levy of service tax. Further, such non-compete clause was normal in case of transfer of business to deter the transferor from starting the same business. However, the presence of such non- compete clause cannot be separated from the main contract executed between the parties to bring the transaction within the ambit of service tax by denying the benefit of Mega Exemption Notification.

Regarding consideration, the Tribunal referred to Circular No. 178/10/2022 dated August 03, 2022, wherein it has been clarified that unless payment has been made for an independent activity of tolerating an act, under an independent arrangement entered in to for such activity of tolerating an act, such payments will not constitute 'consideration' for service. In the present case, the Tribunal noted that there was no consideration provided in the share- purchase agreement regarding the non- compete clause to warrant the service tax demand. Therefore, the service tax demand was set- aside.

The decision of the Tribunal provides clarity and protection to businesses engaging in share transfer agreements with non-compete clauses. It highlights that non-compete clauses are integral to business transferer agreements and cannot be isolated to impose service tax liability in an unfair manner.

KEY PEOPLE

Shashank Shekhar

Partner

Shashank Shekhar is a Partner in the Indirect Tax Practice at DMD Advocates, bringing over two decades of experience to the role. He has extensive court-room experience while representing clients at various fora including Supreme Court of India, High Courts and Tribunals and has obtained favourable judgments and orders for the clients from Courts and Tribunals.

Tushar Joshi

Principal Associate

Tushar Joshi is a Principal Associate with 10 years of experience in indirect tax litigation and advisory. He handles a wide range of matters related to GST, Customs, Service Tax, SEZ, Foreign Trade Policy, etc., and has represented clients at the adjudication and appellate stages, as well as before Tribunals, High Courts, and the Supreme Court.

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