

# EY Tax Alert

HC holds unutilised CGST and IGST credit can be transferred on business transfer between distinct persons

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## Executive summary

This Tax Alert summarizes a recent ruling of the Andhra Pradesh High Court (HC)<sup>1</sup> on the Goods and Services Tax (GST) implications on business transfer between distinct persons.

The assessee transferred its Research and Development unit in Andhra Pradesh (AP) to its Karnataka unit. The Appellate Authority for Advance Ruling (AAAR)<sup>2</sup> held such transfer as taxable supply of goods and disallowed transfer of unutilized ITC. Aggrieved the assessee filed a writ petition before the HC.

The key observations of the HC are:

- ▶ Various judgments under the erstwhile regime have made it clear that only supplies made in the course or furtherance of business are taxable and not the sale of the business itself.
- ▶ While a question arises as to whether such services could have been brought within the purview of GST regime, the Court is leaving this issue open, as the assessee would, in any event, be entitled to exemption under the notification.
- ▶ The phrase “change in the constitution of the registered person” under section 18(3) of the Central Goods and Services Tax Act, 2017 (CGST Act) cannot be narrowly interpreted to mean only an internal change in the transferor, as such an interpretation would exclude transfers like sale, merger, or lease of business.
- ▶ Although the AP and Karnataka units form part of the same legal entity, the GST law deem such units as “distinct persons” for GST purposes. The authorities cannot contend that they are part of the same legal entity and hence, there is no transfer of business.
- ▶ There is no issue in transferring ITC of central tax or integrated tax as these are administered by the Central Government. However, transferring ITC of state tax from AP to Karnataka involves both the States and the matter should be referred to the respective State authorities for a decision.

Basis above, HC set aside the ruling of AAAR and allowed the writ petition.

<sup>1</sup> TS-46-HC(AP)-2026-GST

<sup>2</sup> TS-1258-AAARAP-2020-GST



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## Background

- ▶ Assessee undertakes research and development in pharmaceutical products and had Research and development units in Karnataka and Andhra Pradesh (AP) having separate registrations under the same permanent account number (PAN).

It transferred its Research and development unit in AP to Karnataka registration as a going concern under a business transfer agreement for zero consideration.

- ▶ Assessee sought advance ruling pursuant to such transfer on the following questions:
  - ▶ Whether the transaction would amount to supply of goods or services or both?
  - ▶ Whether the transaction would be exempt under entry 2 of the Notification No.12/2017- Central Tax (Rate) dated 28 June 2017?
  - ▶ Whether unutilized input tax credit (ITC) from AP unit can be transferred to Karnataka as per Section 18(3) of the Central Goods and Services Tax Act, 2017 (CGST Act).

Authority for advance ruling held the transaction as a supply of service exempt under entry 2 of the above stated notification. The authority also held that unutilized ITC can be transferred from AP to Karnataka unit<sup>3</sup>.

The Appellate Authority for Advance Ruling (AAAR) reversed this decision, holding the transaction to be a taxable supply of goods and denied the transfer of ITC<sup>4</sup>.

- ▶ Aggrieved by the decision of AAAR, assessee filed a writ petition before the Andhra Pradesh High Court (HC).

## Assessee Contentions

- ▶ The definition of the term business would exclude the sale of entire business undertaking as a going concern.
- ▶ The transaction would not be a supply of service as the transfer of goods, in the course of sale of a business, would not constitute a taxable supply and as such, cannot be treated as supply of services.
- ▶ Even if the transfer of business is to be treated as "a supply of services", the same would be exempt in view of entry No.2 of Notification No.12/2017.
- ▶ The finding of the AAAR that the provisions of Section 18(3) of the CGST Act, read with relevant rules, apply only to transfers between two separate

legal entities and not to transfers within branches is incorrect.

- ▶ Further, the AAAR's finding that ITC cannot be transferred because it would deprive AP State of its share of tax is incorrect, as the GST law provides for settlements between the Centre and States based on gross utilization.

## Revenue Contentions

- ▶ ITC can be transferred only where there is a business transfer for consideration. In the present case, the transfer agreement itself states that there is no consideration paid for the transfer. Consequently, the question of transfer of ITC does not arise.

Even if there is a business transfer, SGST credit accumulated under the State of AP cannot be transferred to Karnataka, as the GST law does not provide for cross-State transfer of ITC and such transfer would be contrary to law.

- ▶ Entry 4(c) of Schedule II to the CGST Act applies only where a business is transferred as a going concern to another person. In the present case, the transfer is between two units of the same entity with the same PAN, and therefore it cannot be treated as a sale of business.
- ▶ Section 18(3) of the CGST Act applies only where there is a change in the constitution of the registered person due to a transfer of business. No such change occurs in the present case and accordingly Section 18(3) and the relevant rules shall not be applicable.

## HC ruling

- ▶ The provisions of the erstwhile Sales Tax and Value Added Tax Acts are similar to those under the GST regime.

Judicial precedents under the erstwhile laws have held that only sales made in the course or furtherance of business are taxable, and not the sale of the business itself<sup>5</sup>.

In the present case, the transaction constitutes a sale of the business as a whole and not a sale or supply of individual goods.

As per Entry 2 of the Notification No. 12/2017, services by way of transfer of a going concern is exempt from GST. While a question arises as to whether such services could have been brought within the purview of GST regime, the Court is leaving this issue open, as the assessee would, in any event, be entitled to exemption under the notification.

<sup>3</sup> AAR 05/AP/GST/2020

<sup>4</sup> TS-1258-AAARAP-2020-GST

<sup>5</sup> 1999 (112) STC 1; 1977 (39) STC 325 (Madras)

- ▶ The term “change in the constitution” has been understood, by the AAAR, to mean that the structure of the registered person has to change from a proprietary firm to a partnership firm or from a partnership firm to a company etc. This construction of the term does not appear to be correct.

In case of a sale, the transaction would be between a seller and buyer, who are two separate persons or entities. There would not be any change in the constitution on account of sale. However, the language of Section 18(3) provides for transfer of ITC in cases of sale also.

Similarly, in the case of a merger or amalgamation or lease, the registered person who is transferring the business goes out of the picture and it is only the transferee of the business that would be given the benefit of transfer of ITC. In such cases also, there would be no change in the constitution of the registered person.

The phrase “change in the constitution of the registered person” cannot be narrowly interpreted to require only an internal change, as such an interpretation would exclude transactions like sale, merger, or lease of business.

- ▶ Further, the ITC reflected in the transferor’s ledger represents tax paid on inputs and is intended to be used to discharge future tax liabilities, making it an asset of the transferor. In the case of a sale of the entire business, it is reasonable that this asset, in the form of ITC, is also transferred. Section 18(3) provides the statutory basis for such transfer.
- ▶ Although the AP and Karnataka units ordinarily form part of the same legal entity, Section 25(4) and 25(5) of the CGST Act require separate registrations and deem such units as “distinct persons” for GST purposes.

Having treated the two units as separate persons and sought to tax the business transfer between them, the authorities cannot contend that they are part of the same registered person or that no transfer has occurred.

- ▶ There is no issue in transferring ITC available under the CGST Act or the Integrated Goods and Services Tax Act, 2017 as these are administered by the Central Government.

In case of transfer of ITC (SGST), from the State of AP to the State of Karnataka, any decision would affect both the States.

The issue should be placed before the authorities under both the States for a decision as to the admissibility of such a transfer.

Accordingly, HC set aside the ruling of AAAR and allowed the writ petition.

## Comments

- This ruling is important for taxpayers planning to shift business operations from one State to another.
- Goa Bench of the Bombay High Court (Writ Petition No. 463 of 2024) had earlier permitted inter-State transfer of CGST and IGST credits in the context of amalgamation between separate legal entities.
- The judgment may be cited in disputes where authorities have refused ITC transfers based on State-specific registrations. It strengthens the principle that ITC can move seamlessly across State boundaries in cases involving transfer of business.
- It is relevant to note that the position on SGST credit transfer remains unsettled.
- The Government may need to issue a Circular to clarify the process and mechanism for transferring credits in case of inter-state business transfers. Also, the GST portal might need to be aligned to enable the transfer of credits in such cases.

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