

# EY tax alert

**Bombay HC third judge upholds constitutional validity of place of supply provision for intermediary services confining only to IGST**

## Executive summary

This tax alert summarizes the recent ruling<sup>1</sup> by the third judge of the Bombay High Court (HC). The issue relates to constitutional validity of Section 13(8)(b) of the Integrated Goods and Services Tax Act, 2017 (IGST Act). The place of supply as per the said provision in case of intermediary services is the location of supplier.

Earlier, the petitions were heard by the Division Bench of HC, wherein the first judge struck down Section 13(8)(b) as *ultra vires* IGST Act and the Constitution. However, the second judge took a dissenting view and upheld the validity of the said provision. In view of the Division Bench recording the disagreement, matter was referred to a third judge.

The key observations of the third judge are summarized below:

- ▶ Goods and Services Tax (GST) is a destination-based tax and hence, intermediary services provided in the present case are “export of services” as recipient of the service is a foreign principal and consumption of said services takes place outside India.
- ▶ On cumulative reading of Article 246A, 269A and 286 of the Constitution, no law of State can impose tax on supply which takes place outside its State and in the course of import or export.
- ▶ The transactions in question would fall within the framework of IGST Act only. It is too far-fetched to consider that certain provisions of IGST Act are framed not to give relevance to the IGST Act but for Central Goods and Services Tax Act, 2017 (CGST Act) and State Goods and Services Tax Acts.
- ▶ None of the provisions under IGST Act can be considered to be meaningless if they are applicable within the framework of the IGST Act. Therefore, Section 13(8)(b) and section 8(2) cannot be struck down.

Accordingly, the third judge held that Section 13(8)(b) and 8(2) of the IGST Act are valid, provided that these provisions are confined in their operation to the said Act only. The same cannot be made applicable for levy of tax under the CGST Act or the Maharashtra Goods and Services Tax Act, 2017.

<sup>1</sup> TS-138-HC(BOM)-2023-GST

# Background

- ▶ Petitioners in the present case are engaged in providing “intermediary services”, as defined under Section 2(13) of the Integrated Goods and Services Tax Act, 2017 (IGST Act), to its customers located outside India.
- ▶ As per Section 2(6) of the IGST Act, one of the conditions for a supply to qualify as “export of services” is that the place of supply should be outside India.
- ▶ Section 13(8)(b) of the said Act provides that in case of intermediary services, where either the supplier or the recipient is located outside India, the place of supply shall be the location of the supplier. Therefore, the service provided by petitioners in the present case did not qualify as export of services.
- ▶ Further, Section 8(2) states that if location of the supplier and place of supply are in the same state, then such transaction will be treated as “intra-state supply”.
- ▶ Thus, petitioners discharged central tax (CGST) and Maharashtra State tax (MGST) on amount received from its foreign principal.
- ▶ On this premise, petitioners filed writ petitions before the Bombay High Court (HC) challenging constitutional validity of Section 13(8)(b) read with Section 8(2) of the IGST Act.
- ▶ Earlier, the petitions were heard by the division bench of HC, wherein the first judge struck down Section 13(8)(b) of the IGST Act as *ultra vires* the IGST Act and the Constitution.<sup>2</sup> However, the second judge took a dissenting view and upheld the validity of the said provision.<sup>3</sup>
- ▶ In view of the Division Bench recording the disagreement, matter was referred to a third judge.
- ▶ In this tax alert, we have summarized the contentions of petitioners, Revenue and the ruling of the third judge.

## Petitioners' contentions

- ▶ Intermediary services are consumed by customers located outside India, thereby such services qualify as export of services.
- ▶ Article 246A read with Article 269A and 286 of the Constitution of India are violated in as much as Section 13(8)(b) read with Section 2(13) and 2(6) of the IGST Act, creates a legal fiction to treat such services as “intra-state supply” to levy CGST and MGST.
- ▶ Goods and Services Tax (GST) is levied on destination-based principle, wherein place of supply of service, necessarily would be location of the recipient.

- ▶ In view of above, Section 13(8)(b) read with other provisions would de'hors the fundamental principles laid down for levy of GST.
- ▶ Once the services are consumed outside India, Parliament has no jurisdiction to levy tax on such services.
- ▶ As per Article 246A and 269A, the Constitution only grants power to the Parliament to frame laws for inter-state trade and commerce. It does not permit imposition of tax on export of services by treating the same as a local supply. Hence, Section 13(8)(b) is *ultra vires* Articles 246A and 269A.
- ▶ In terms of Article 286(1), no law of a State shall impose tax on supply of goods or services where such supply takes place outside the State or in the course of export. Section 13(8)(b) deems an export to be a local supply and the same is violative of the said Article.
- ▶ Levy of tax on such services provided to customers located outside India is arbitrary, unreasonable, discriminatory and violative of Article 14 of the Constitution.
- ▶ From an analysis of the scheme, scope and object of IGST Act, it is evident that the same provides for levy of IGST on inter-state supplies. However, Section 13(8)(b) runs contrary to the overall scheme of IGST Act because it deems a supply out of India as an intra-state supply.
- ▶ By levying CGST and MGST on such services provided to customers located outside India, an unreasonable restriction is created upon the right to carry on trade under Article 19(1)(g) of the Constitution.
- ▶ Further, the impugned provisions lead to double taxation. Firstly, the petitioners would pay tax in India. Again, following the destination-based principle, it would be an import of service for the foreign service recipient and would be taxed in the importing country.
- ▶ Basis above contentions, Section 13(8)(b) should be struck down being unconstitutional.

## Revenue's contentions

- ▶ Generally, value addition of the service provided by an intermediary is at the place where the intermediary is located. If location of recipient was made place of supply for intermediary services, all intermediaries located in taxable territory providing service to a person outside India, would go out of the tax net.

Issue of place of supply of intermediaries was discussed during the drafting stage of GST law and the above reasoning was adopted by GST Council.

- ▶ Even in the erstwhile regime, the place of supply of intermediary services was the location of the supplier.

<sup>2</sup> Refer our alert “HC judges differ on constitutional validity of Place of Supply provision for Intermediary services under GST” dated 12 June 2021

<sup>3</sup> Refer our alert “HC passes dissenting judgment and refers matter relating to Intermediary services under GST to the Chief Justice” dated 21 June 2021

- Taxing such services provided by Indian suppliers to foreign companies incentivizes the foreign company to start manufacturing in India in order to reduce the tax burden. Therefore, the same is in consonance with "Make in India" program.
- There is always a presumption in favor of constitutionality of a statute. No statute can be struck down as arbitrary unless it is unconstitutional. Greater latitude vests with the Parliament in taxing statutes.
- Considering the scheme of GST laws, it is evident that these laws function harmoniously and as part of a well thought of statutory mechanism to tax goods and services. These laws operate harmoniously but in different spheres, as they lay down how the supply is to be taxed, nature of supply and their place of supply.
- Article 269A of the Constitution authorizes the Parliament to frame laws in respect of two aspects, firstly, for determining the place of supply, and secondly, when the supply takes place in the course of inter-state trade or commerce. Articles 246A and 286 also manifest and grant similar powers.

Such powers are unbridled and unrestricted. Hence, the Parliament is within its domain to determine the place of supply.

- In exercise of the above powers, the Parliament has enacted Section 13(8)(b) and the same cannot be said to be *ultra vires* the provisions of the Constitution.
- Intermediary service providers are a separate class of service providers. Once a class of person can be distinguished by the test of reasonable classification, the impugned provision cannot be violative of either Article 14 or Article 19(1)(g) of the Constitution.

## Third judge's ruling

- In case of All India Federation of Tax Practitioners<sup>4</sup>, Supreme Court (SC) observed that Value Added Tax (VAT) is a destination-based consumption tax, logically leviable only on services provided within the country. Therefore, GST is also destination-based consumption tax, as it has been founded on the principle of VAT.
- Article 246A and 269A of the Constitution has empowered only the Parliament to frame laws pertaining to levy and collection of GST in the course of an inter-state trade or commerce.
- Article 286(1) forbids State to impose any tax in relation to supply outside the State or in the course of import or export.
- Further, in terms of Article 286(2), only Parliament can formulate principles for determining when a supply of goods or services takes place in any of the ways mentioned in Article 286(1).

- The transactions in question are transactions of "export of services" as recipient of the service is a foreign principal and consumption of said services takes place in a foreign land.
- As per Section 7(5) of the IGST Act, in a transaction where the supplier is in India and the place of supply is outside India, such transaction shall be treated as "inter-state supply".
- A transaction of export of services as that of the petitioners, on one hand is treated as inter-state supply by Section 7(5), and on the other hand, the same transaction is treated as an intra-state trade and commerce by virtue of Section 13(8)(b).
- Provisions of law are required to be interpreted to forward the intent of legislation and the purpose sought to be achieved.
- Further, the Courts should endeavor to presume constitutionality of the legislative provisions rather than to declare them invalid.
- Insofar as impugned services are concerned, it would fall within the framework of IGST Act only. It is too far-fetched to consider that certain provisions of IGST Act are framed not to give relevance to the IGST Act but for Central Goods and Services Tax Act, 2017 (CGST Act) and Maharashtra Goods and Services Tax Act, 2017 (MGST Act).
- The provisions of Section 13(8)(b) are contextually neither attracted nor provided under the CGST Act. Therefore, it is impermissible to apply CGST and MGST on Section 13(8)(b) transactions.
- Moreover, it may also be required to observe that none of the provisions under the IGST Act can be considered to be meaningless insofar as they are applicable within the framework of the IGST Act.
- Therefore, the provisions contained in Section 13(8)(b) and Section 8(2) of the IGST Act cannot be struck down, however, the particular transaction would purely fall under the IGST Act.
- In view of the above, it was held that Section 13(8)(b) and Section 8(2) of the IGST Act are legal, valid and constitutional, provided that the said provisions are confined in their operation to IGST Act only. The same cannot be made applicable for levy of tax under the CGST Act or MGST Act.

<sup>4</sup> 2007 (7) STR 625

## Comments

- a. As all the three judges have divergent opinions, it is likely that the matter will be placed before the Full Bench for consideration.
- b. In view of this ruling, businesses may have to analyze the type of tax required to be paid on intermediary services due to the observation of third judge that CGST and State GST cannot be levied on intermediary services. Further, on plain reading of the provisions of IGST Act, such transactions may not fall within the ambit of inter-state supplies.
- c. One may also need to evaluate the taxability of other services provided to overseas recipient where the law treats place of supply of such services to be in India.
- d. In case it is concluded that CGST and SGST is not leviable, taxpayer may explore possibility of claiming refund of tax already paid.
- e. It is relevant to note that Gujarat HC had earlier upheld the constitutional validity of Section 13(8)(b) and considered the intermediary services provided to overseas customers as intra-state supplies [2020-TIOL-1274-HC-AHM-GST].
- f. While on one hand, the validity of place of supply of intermediary service is under question, on the other hand there is an ambiguity in interpreting the scope of intermediary which is leading to unwarranted disputes between Revenue and taxpayers.

# Our offices

## Ahmedabad

22nd Floor, B Wing, Privilon  
Ambli BRT Road, Behind Iskcon  
Temple, Off SG Highway  
Ahmedabad - 380 059  
Tel: + 91 79 6608 3800

## Bengaluru

12th & 13th floor  
"UB City", Canberra Block  
No. 24, Vittal Mallya Road  
Bengaluru - 560 001  
Tel: + 91 80 6727 5000

Ground Floor, 'A' wing  
Divyasree Chambers  
# 11, O'Shaughnessy Road  
Langford Gardens  
Bengaluru - 560 025  
Tel: + 91 80 6727 5000

## Chandigarh

Elante offices, Unit No. B-613 & 614  
6th Floor, Plot No- 178-178A  
Industrial & Business Park, Phase-I  
Chandigarh - 160 002  
Tel: + 91 172 6717800

## Chennai

Tidel Park, 6th & 7th Floor  
A Block, No.4, Rajiv Gandhi Salai  
Taramani, Chennai - 600 113  
Tel: + 91 44 6654 8100

## Delhi NCR

Golf View Corporate Tower B  
Sector 42, Sector Road  
Gurugram - 122 002  
Tel: + 91 124 443 4000

3rd & 6th Floor, Worldmark-1  
IGI Airport Hospitality District  
Aerocity, New Delhi - 110 037  
Tel: + 91 11 4731 8000

4th & 5th Floor, Plot No 2B  
Tower 2, Sector 126  
Gautam Budh Nagar, U.P.  
Noida - 201 304  
Tel: + 91 120 671 7000

## Hyderabad

THE SKYVIEW 10  
18th Floor, "SOUTH LOBBY"  
Survey No 83/1, Raidurgam  
Hyderabad - 500 032  
Tel: + 91 40 6736 2000

## Jamshedpur

1st Floor, Shantaniketan Building,  
Holding No. 1  
SB Shop Area, Bistupur  
Jamshedpur - 831 001  
Tel: + 91 657 663 1000

## Kochi

9th Floor, ABAD Nucleus  
NH-49, Maradu PO  
Kochi - 682 304  
Tel: + 91 484 433 4000

## Kolkata

22 Camac Street  
3rd Floor, Block 'C'  
Kolkata - 700 016  
Tel: + 91 33 6615 3400

## Mumbai

14th Floor, The Ruby  
29 Senapati Bapat Marg  
Dadar (W), Mumbai - 400 028  
Tel: + 91 22 6192 0000

## Mumbai

5th Floor, Block B-2  
Nirlon Knowledge Park  
Off. Western Express Highway  
Goregaon (E)  
Mumbai - 400 063  
Tel: + 91 22 6192 0000

## Pune

C-401, 4th floor  
Panchshil Tech Park, Yerwada  
(Near Don Bosco School)  
Pune - 411 006  
Tel: + 91 20 4912 6000

## Ernst & Young LLP

EY | Building a better working world

### About EY

EY exists to build a better working world, helping to create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Information about how EY collects and uses personal data and a description of the rights individuals have under data protection legislation are available via [ey.com/privacy](http://ey.com/privacy). EYG member firms do not practice law where prohibited by local laws. For more information about our organization, please visit [ey.com](http://ey.com).

Ernst & Young LLP is one of the Indian client serving member firms of EYGM Limited. For more information about our organization, please visit [www.ey.com/en\\_in](http://www.ey.com/en_in).

Ernst & Young LLP is a Limited Liability Partnership, registered under the Limited Liability Partnership Act, 2008 in India, having its registered office at 9th Floor, Golf View Corporate Tower B, Sector 42, Golf Course Road, Gurugram, Haryana - 122 002.

© 2023 Ernst & Young LLP. Published in India.  
All Rights Reserved.

This publication contains information in summary form and is therefore intended for general guidance only. It is not intended to be a substitute for detailed research or the exercise of professional judgment. Neither EYGM Limited nor any other member of the global Ernst & Young organization can accept any responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication. On any specific



Download the EY India Tax Insights App

[ey.com/en\\_in](http://ey.com/en_in)

@EY\_India EY EY India EY Careers India @ey\_indiacareers