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Indirect Tax Alert

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Rulings under GST era

M/s. Emcure Pharmaceuticals Limited, Maharashtra Authority for Advance Ruling[1]

Issue for Consideration

Whether GST would be payable on the recoveries made from the employees in respect of canteen facility, bus transportation service and notice pay?

Discussion

- The Applicant is engaged in the manufacturing of pharmaceutical products.
- The Applicant has engaged third party service providers to provide canteen and bus transportation facilities to its employees. The Applicant recovers a part of the consideration, payable to such third-party service providers, from its employees.
- Furthermore, if an employee resigns from employment without serving the mandatory notice period, the Applicant deducts an amount (i.e. notice pay) from the employee's salary in terms of the employment agreement.
- The Applicant believes that such recoveries are not liable to GST and has approached the Authority for Advance Ruling, Maharashtra ('the Authority') and raised the following contentions:

Recovery of canteen charges

- Applicant is engaged in the manufacturing of pharmaceutical products and the canteen facility is being provided in terms of the Factories Act, 1948. The business would continue even if the said facility were not provided.
- Such recovery is not covered within the ambit of supply as per section 7(1)(a) of the CGST Act.
- Canteen facility cannot be regarded as incidental or ancillary to the main business of the Applicant.
- The said transaction is undertaken in the course of employment and does not qualify as a supply in terms of section 7(2) read with clause 1 of the Schedule III of the CGST Act.
- As per section 7(2)(a) of the CGST Act read with clause 1 of Schedule III of the CGST Act, services provided by an employee in the course of employment is not a supply.

[1] 2022 (1) TMI 186

Recovery of Bus transportation facility

- Similar contentions were raised regarding the bus transportation facility as for canteen charges.
- In addition, even if the said facility amounts to supply, it shall be exempt in terms of sl. no. 15(b) of notification no. 12/2017-Central Tax (Rate) dated June 28, 2017.

Notice pay recovery

- Notice pay recovery is merely recovery of the salary paid to the employees. It is an integral part of the salary benefits. GST should not be payable on such recovery in terms of clause 1 of the Schedule III of the CGST Act.
- Notice pay recovery is in the nature of penalty and there is no obligation on the Applicant to tolerate the act of non-compliance by the employee. It is not a consideration being received for any activity being done by the Applicant.
- Recovery of notice pay is not the business of the Applicant and hence cannot be treated as a supply as per section 7(1)(c) read with clause 2 of Schedule I of the CGST Act.
- The Madras High Court in the case of *GE T&D India Ltd.*[2] has held no service tax is payable on notice pay recovery. Reliance was also placed upon various other pre-GST judgments.

- The Authority observed as follows:

Recovery of canteen and bus transport facility

- The provision of canteen facility and bus transportation to employees is a welfare measure and is not connected to the business of the Applicant.
- The Applicant is neither supplying the canteen services or bus transportation services nor it is an output service. The said facilities are provided by third party vendors and the Applicant is a recipient of such services.
- The partial amount recovered from employees for use of such facilities is part of the amount paid to third party vendors which has already suffered GST.
- The canteen facility / bus transportation service is not a transaction made in the course of or for furtherance of business and hence cannot be treated as a "supply".
- Reliance was placed on various advance rulings.

Notice pay recovery

- The employee opting to resign by paying the amount in lieu of notice has acted in accordance with contract and no forbearance or toleration arises. Furthermore, the resignation by the employee is not subject to any acceptance or approval and the employee is free to tender his resignation, make payment of notice period salary and leave. Hence, there is no role played by the employer. There is no consideration flowing from an act of forbearance in as much as there is no breach of contract.
- In the case of *Bharat Oman Refineries Ltd.*[3], the Appellate Authority for Advance Ruling has held that no GST is payable on notice pay recovery. Reliance was also placed upon judgment of GE T&D India Ltd.

Ruling

The Authority held that recovery of canteen facility, bus transportation service and notice pay recovery from employees is not leviable to GST.

Dhruva Comments:

Levy of tax on recoveries made from employees has always been a subject matter of litigation under both the Service tax and GST regime.

However, considering the judgment of GE T&D (*supra*) by the Madras High Court, the Courts have started to

[2] 2020 (1) TMI 1096
[3] Ruling No. MP/AAAR/07/2021 dated November 8, 2021

uphold the non-levy of service tax on notice pay recovery. However, under GST divergent rulings are still being issued by the Authorities. Similar divergent rulings are there in respect of other recoveries of canteen / bus transportation, under GST. It will have to be seen how these issues evolve under GST when placed before the judiciary.

Cummins India Limited – Maharashtra Appellate Authority for Advance Ruling[4]

Issues for Consideration

- Whether the Head office ('HO') is eligible to claim ITC of tax paid on common services procured on behalf of its units under the Central Goods and Services Tax Act, 2017 ('the Act')?
- Valuation of facilitation services provided by the HO to its units.
- Whether ISD registration is required to be mandatorily obtained by the HO?

Discussion

- The Appellant is engaged in the manufacture and sale of various diesel engines, parts thereof, and related services. It procures certain common input services on behalf of its various units located in several states.
- ITC of these common costs is availed by the HO and subsequently recovered proportionately, along with GST from the respective units.
- Based on the application filed by the Appellant, the Maharashtra Advance Ruling Authority ('the Authority') had ruled[5] ('the impugned order') that:
  - The ITC relating to common input services is not eligible to the Appellant, and recovery of such costs from the units qualifies as 'supply' under the Act and is liable to GST.
  - The value of supply shall be computed at 110% of the cost of services as per rule 30 of the CGST Rules, 2017 ('the CGST Rules').
  - The Appellant is required to mandatorily obtain an ISD registration to distribute the ITC of common credits.
- Aggrieved by the impugned order, the Appellant has preferred an appeal before the Maharashtra Appellate Authority for Advance Ruling ('the Appellate authority') and contended as follows:
  - Section 24 of the Act prescribes mandatory separate registration as an ISD if a person intends to avail the facility of ISD. However, it does not mandate availing the ISD facility compulsorily, and the same appears to be an option given to the registered person to be exercised at his own discretion.
  - A unit can be treated as an ISD once it issues a prescribed document to distribute the ITC of common credits. Thus, a unit can be treated as an ISD only if it fulfils the above condition. Furthermore, the definition does not create any compulsion to avail the ISD facility. It can be said that a unit that does not opt to issue the prescribed document to distribute the common ITC does not have to obtain registration as an ISD.
  - The Appellant has nowhere submitted its willingness to act as an ISD in order to pass on the common credits to its units. A registered person has the option to opt for the ISD mechanism if it so wishes, or to refrain from it.
  - The Authority has erroneously ruled that supply made between distinct persons qualifies as supply even in absence of a consideration, and it includes the cost of employees recovered from the units, and GST is payable on it. The services provided by an employee to the employer have been covered under schedule III of the Act and kept out of the GST ambit.
  - It is a settled principle that the employee-employer relationship extends to the whole company and not merely to its HO / any particular unit. Hence, the employee cost

[4] TS-747-AAAR(MAH)-2021-GST
[5] 2019 (3) TMI 538

recovered by the HO from the units shall be excluded from the value of facilitation services provided by the HO.

- Rule 28 of the CGST Rules prescribes that the value of supply between distinct persons who are eligible to avail the ITC shall be the transaction value of such supply. However, the impugned order ruled that valuation of the supply should be done at 110% of the cost of service, ignoring the above provision. In the present case, any nominal value declared on the invoice shall be considered as the value of such supply.

- The contentions of the GST authorities were as follows:
  - The Appellant wishes to operate as an ISD and hence should obtain ISD registration mandatorily.
  - The facilitation services provided by the HO is specific to the business model of the Appellant, and hence the open market value and the value of goods of 'same kind and quality' prescribed under rule 28 of the CGST Rules cannot be applied and instead rule 30, which prescribes a value of 110% of cost of the services, has to be considered.
  - The services provided by an employee of one unit for another unit does not get covered under the employee-employee relationship and, hence, are taxable under GST.

- The Appellate Authority considered the submission of both the parties and observed as follows:
  - The definition of 'service' under the Act is wide enough to adequately include the nature of facilitation services provided by the HO to its units and, hence, it qualifies as 'supply' under the Act liable to tax.
  - Section 16 of the Act provides that any registered person can avail the ITC on goods / services used in the course or furtherance of business. The ITC of common services availed by the HO is being consumed by the units and not by the HO itself, and hence, the HO is not entitled to avail such credit.
  - Section 24 of the Act prescribes separate mandatory registration as an ISD. It is evident that all ISDs intending to distribute the ITC of common credits must mandatorily obtain registration as an ISD under the Act. In the present case, the HO receives the invoices for common credits and distributes them among the respective units. Hence, it is clear that it acts as an ISD and has to register as an ISD.
  - The Appellant's argument that the HO avails the ITC of common credits and utilises it against the output tax on supply of facilitation services is not tenable.
  - The HO procures the common input services on behalf of its units and, hence, it acts as a **'pure agent'** to such extent as per rule 33 of the CGST Rules and, hence, the same amount should not be subjected to GST. The value of facilitation services provided by the HO shall exclude the cost of such common services as per rule 33 of the CGST Rules.
  - The employees of the HO are working at the behest of HO and not at the behest of branches. Furthermore, the HO is using its human resources to facilitate the operational requirement of the branches. Therefore, recovery of any amount, including employees' salary cost should be subjected to GST.
  - The supply of facilitation service is between the HO and its units and not with the employees. Therefore, the contention of the appellant that such services are provided by an employer to employee is not tenable. The service is between two distinct units as per Section 24 of the Act, 2017, and the same is taxable as per section 7 of the Act. Hence, the value of supply shall include the employee cost.
  - The assessable value of services provided by the HO to a branch can be determined as per the second proviso to rule 28 of the CGST Rules, where invoice value is deemed to be the open market value.

Ruling

The Appellate authority held as follows:

- The availment of common input services by HO on behalf of its branches, and recovering the same from its branches, qualifies as a supply of service. However, the same should not be subjected to GST as per rule 33 of the CGST Rules, as the HO is acting in the capacity of pure agent for its branches. The said cost should be excluded from the value of supply of facilitation services.
- The assessable value can be determined as per the second proviso to rule 28 of the CGST Rules, which provides that the value declared on the invoice is deemed to be the open market value.
- The HO is not entitled to avail ITC on the common input services procured by the HO on behalf of its branches.
- The Appellant should mandatorily obtain a separate ISD registration in order to distribute the ITC to its respective units.

Dhruva Comments:

For common input services, whether ISD registration is mandatory or could be transferred through cross charge mechanism has been a matter of constant debate. The instant ruling mandates compulsory registration as an ISD for common input services. Another connected issue has been whether the HO is rendering any facilitation services to its branches. For employees who are working on common functions like finance / tax / HR are working for the Company and the employer-employee relationship exists qua the organisation and not towards any specific location. In a similar case, the Karnataka Appellate authority for advance ruling[6] had also held that the common costs recovered by the HO from its units amounts to 'supply' under the Act and that the ITC of common costs should be distributed through the ISD mechanism only as prescribed under GST.

It is worth noting that the advance ruling authorities are viewing employee-employer relationships qua each distinct person and not qua the entire company. The Appellant has filed an appeal before the High Court in respect of the Karnataka Appellate Authority ruling and the same is pending before the High Court. It remains to be seen how the Court interprets the said matter.

Judgment under GST era

Quest Global Engineering Services Pvt. Ltd. v. The Deputy Commissioner[7]

Issues for Consideration

Is the time limit prescribed under section 54 of the CGST Act for filing a refund claim applicable in a case in which tax was mistakenly discharged where there was no supply involved and where no invoice was raised?

Discussion

- Quest Global Engineering Private Limited ('transferor Company') has been merged with the Petitioner as per the order dated October 1, 2017.
- The Transferor Company had raised invoices during the months of June, July, August and September 2017 on their customer M/s Caterpillar India Private Limited and had discharged the relevant Service tax / GST.
- Furthermore, pursuant to the amalgamation, the data in the system of the Transferor Company was integrated with the data of the Petitioner.
- However, during such integration, the Petitioner's system by mistake pulled the same invoices which had already been reflected in the returns of the Transferor Company and on which tax had already been discharged by the Transferor Company.
- The Petitioner disclosed all the said invoices dated November 1, 2017 in its returns and also discharged tax. However, for the said invoices, the Petitioner had neither actually supplied any service nor had raised any invoice on the customer.

[6] 2018 (2) TMI 1604
[7] TS-749-HC(MAD)-2021-GST

- The Petitioner was of the view that it is eligible for refund of tax mistakenly paid on such invoices. Accordingly, the Petitioner filed a refund claim with the Authorities on May 30, 2020.
- However, the Department rejected the refund claim as being time-barred.
- Aggrieved, the Petitioner filed the present Writ Petitioner with the Hon'ble High Court at Madras.
- The Petitioner relied upon GST circular[8] and judicial precedents in support of their contention that they are eligible for a refund claim.
- On the other hand, the Department contended as follows:
  - The Petitioner had not filed any records to substantiate that tax on the invoices was already paid earlier and had also not produced any proof that the customer has not availed input tax credit based on the invoice raised by the Petitioner.
  - Section 54[9] of the CGST Act makes it clear that the limitation period for filing refund claim would apply even in cases in which tax was paid by mistake on account of non-supply of any service for which no invoice was raised.
  - Refund claim should have been filed within two years from the date of payment of tax. However, the refund claim was actually filed long after expiry of the said period of two years. Hence, the Department was justified in rejecting the refund claim as time-barred.
  - Reliance was placed on various judicial precedents in support of their contention
- After perusing the facts of the case and the relevant provisions of the GST law, the Hon'ble High Court observed as follows:
  - Since tax was paid on December 12, 2017, the refund claim should have been filed by December 19, 2019. However, the refund claim was filed on May 30, 2020, which is beyond the period of limitation prescribed by section 54 of the CGST Act.
  - In the case that there was a wrong entry, steps for rectification of return should have been taken as per section 39(9)[10] of the CGST Act.
  - The GST circular relied upon by the Petitioner would apply only in cases where the Company has reported the supply twice. However, in the present case, the Petitioner has generated invoice numbers and date and paid tax on the same.
  - The Petitioner has the option to request the customer to issue appropriate credit notes to neutralize the alleged excess payment of GST while generating invoices dated November 11, 2017.
  - The refund claim of the Petitioner is clearly barred by limitation as per section 54 of the CGST Act.

Judgment

The Hon'ble High Court dismissed the Writ Petition filed by the Petitioner against the rejection of the refund claim.

Dhruva Comments:

In terms of judicial precedents, the term 'mistake' in terms of section 72 of Indian Contract Act, 1972 would encompass mistake of law as well as mistake of fact and accordingly should arguably not be affected by time limit stipulated under the GST law.

[8] Circular no. 26/26/2017-GST dated December 29, 2017

[9] Section 54 of the CGST Act, 2017: *"(1) Any person claiming refund of any tax and interest, if any, paid on such tax or any other amount paid by him, may make an application before the expiry of two years from the relevant date in such form and manner as may be prescribed:….. (8) Notwithstanding anything contained in sub-section (5), the refundable amount shall, instead of being credited to the Fund, be paid to the applicant, if such amount is relatable to-…..(c) refund of tax paid on a supply which is not provided, either wholly or partially, and for which invoice has not been issued, or where a refund voucher has been issued;…… (2) "relevant date" means-….(h) in any other case, the date of payment of tax"*

[10] Section 39(9) of the CGST Act, 2017: *"(9) Subject to the provisions of sections 37 and 38, if any registered person after furnishing a return under sub-section (1) or sub-section (2) or sub-section (3) or sub-section (4) or sub-section (5) discovers any omission or incorrect particulars therein, other than as a result of scrutiny, audit, inspection or enforcement activity by the tax authorities, he shall rectify such omission or incorrect particulars in such form and manner as may be perscribed, subject to payment of interest under this Act:"*

On a separate note, the Hon'ble High Court has observed that the customer should issue a credit note to neutralize the impact of excess tax paid. Interestingly, the Court has not made any reference to provisions dealing with issuance of credit notes or time limit for issuing the same.

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