Intermediary service to non-resident- validity of s.13(8)(b) of IGST Act

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RECENTLY Hon'ble ***Justice Ujjal Bhuyan*** of the Bombay High Court in the case of Dharmendra M Jani Vs UOI - 2021-TIOL-1297-HC-MUM-GST has held that section 13(8)(b) of the IGST Act, 2017 isÂ***ultra viresÂ*** the said Act besides being unconstitutional. A dissenting view has been taken by Hon'ble ***Justice Abhay Ahuja***, which order would be recorded when the matter is listed next week.

Section 13(8)(b) of the IGST Act states that the place of provision of service by the intermediary is the location of the service provider. So, if the intermediary provides service to the recipient located outside India, still it will not qualify as export of service.

It is in this context, the Hon'ble High Court held that

section 13(8)(b) of the IGST Act read with section 8(2) of the said Act has created a fiction deeming export of service by an intermediary to be a local supply i.e., an inter-state supply. This is definitely an artificial device created to overcome a constitutional embargo. Question for consideration is whether creation of such a deeming provision is permissible or should receive theÂ imprimaturÂ of a constitutional court? â€¦â€¦â€¦â€¦â€¦.. Having regard to the discussions made in the preceding paragraphs it is evider section 13(8)(b) of the IGST Act not only falls foul of the overall scheme of the CGST Act and the IGST Act but also offends Articles 245, 246A, 269A and 286(1) (b) of the Constitution. The extra-territorial effect given by way of section 13(8)(b) of the IGST Act has no real connection or nexus with the taxing regime in India introduced by the GST system; rather it runs completely counter to the very fundamental principle on which GST is based i.e., it is a destination based consumption tax as against the principle of origin based taxationâ€¦â€¦â€¦ Thus having regard to the discussions made above and upon thorough consideration, we have no hesitation in holdin that section 13(8)(b) of the Integrated Goods and Services Tax Act, 2017 isÂ ultra viresÂ the said Act besides being unconstitutional.

Interestingly, Gujarat High Court in **Material Recycling Association of India** - ***2020-TIOL-1274-HC-AHM-GST***, held that section 13(8)(b) of the IGST Act cannot be said to beÂ***ultra viresÂ***or unconstitutional in any manner.

In view of the contradiction, the author submits his own views as per his understanding -

+ Government introduced taxation law as per the socio-economic policy of the Government broadly based upon public interest. It is a known fact that the exports are incentivized by way of exemption from taxation, purely for the purpose of augmenting the inflow of the foreign currency which is of immense importance for the economic growth of our country. In the case of intermediary service, the implications need to be understood from macro-economic point of view. An illustration would make the position clear.

+ Suppose A is the intermediary in India providing intermediary service to B in London. B supplies goods to its customer C in India. B charges 50,000 US Dollar to C for the sale of goods. C remits the said foreign exchange to B. B then pays 5000 US Dollar to A as commission for providing the intermediary service. Hence the net effect is that there is an outflow of foreign exchange of 45,000 US Dollar (50,000 minus 5,000). So, from the macroeconomic point of view, India as a country is losing foreign exchange because of the intermediary service, which facilitates the net outflow of foreign exchange from the country. + ***That is why the government has decided not to recognize the intermediary service as export of service.*** In case of regular export of goods or services (other than intermediary), there is net inflow of foreign exchange into the country. Hence the said supplies are treated as export of service and is exempted from tax. The message is clear that there should not be any exemption from tax where the export transaction ultimately results into net outflow of the foreign exchange. If such

intermediary service is treated as export of service, then the object and purpose of legislation to incentivize export would be defeated.

+ The above view is fortified by the fact that in case where the intermediary service is provided to a non-resident located abroad and then the said non-resident supplies goods to another non-resident located outside India, then the intermediary is exempted from payment of tax as per Notification no. **20/2019â€“IGST**
dated 30th September 2019. This is because, in such a case intermediary earns foreign exchange but there is no corresponding outflow of foreign exchange from the country as the recipient of the supply of the non-resident principal of the Indian intermediary is also outside India. In the above illustration, If B, the recipient of intermediary service supplies goods to C who is also a non-resident located abroad, then there is no outflow of foreign exchange from India. Hence the exemption is justified to promote inflow of foreign exchange into our country

+ In GVK Industries Ltd. V. Income Tax Officer - **2011-TIOL-128-SC-IT-CB**
, the Apex Court examined the limitation of Parliament in enacting legislations with respect to extraterritorial aspects. It held that - ***Parliament may exercise its legislative powers with respect to extraterritorial aspects or causes - events, things, phenomena (howsoever commonplace they may be), resources, actions or transactions, and the like - that occur, arise or exist or may be expected to do so, naturally or on account of some human agency, in the social, political, economic, cultural, biological, environmental or physical spheres outside the territory of India, and seek to control, modulate, mitigate or transform the effects of such extra-territorial aspects or causes, or in appropriate cases, eliminate or engender such extra-territorial aspects or causes, only***
when such extra-territorial aspects or causes have, or are expected to have, some impact on, or effect in, or consequences for: (a) the territory of India, or any part of India; or
(b) the interests of, welfare of, well-being of, or security of inhabitants of India, and Indians.

In view of the above, as per the understanding of the author, there is a macro economic justification for the legislation that the intermediary service provided by Indian service provider to foreign recipient of the said service should **NOT**
qualify as export of service and thereby exempt from taxation.

(The views expressed are strictly personal.)