

Punjab and Haryana HC stays the operation of circular to the extent of clarifying the taxability of corporate guarantee

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Summary

The Punjab and Haryana High Court (HC) has stayed the operation of the Central Board of Indirect Taxes and Customs (CBIC) circular to the extent it clarified that the provision of corporate guarantee by a company to banks/financial institutions on behalf of its related company is to be treated as a supply of service liable to the Goods and Services Tax (GST). The HC further noted that the appellate authority should be free to decide the matter without being influenced by the clarification.

Facts of the case

- M/s. ACME Cleantech Solutions Private Limited (the petitioner) has challenged the Circular No. 204/16/2023-GST dated 27 October 2023 (Impugned Circular) on the premise that it takes away the adjudicatory powers of the assessing authority and the appellate authority by clarifying provisions in the nature of adjudication.
- The impugned circular had clarified that the provision of a corporate guarantee by a company on behalf of another related company to the banks/financial institutions would be a supply of service even in the absence of consideration and would be liable to GST.
- Further, the taxable value of such deemed supply would be determined as

per Rule 28(2), as amended vide Notification No. 52/2023-CT dated 26 October 2024, prescribing the value to be higher than 1% of the amount of such guarantee or the actual consideration received.

Punjab and Haryana HC's observations and order [CWP 10249/2024; Order dated 03 May 2024]

- Taking note of the interim relief granted by the Delhi HC in the case of Sterlite Power Transmission Limited, the HC has stayed the operation of the impugned circular.
- It further noted that the appellate authority should be free to decide the matter without being influenced by the clarification.

Our comments

The taxability of corporate guarantee has been a contentious and highly litigative issue even before the inception of GST. In the erstwhile Service Tax regime, the SC, in its landmark decision in the case of Edelweiss Financial Services Limited, ruled that issuance of corporate guarantee on behalf of group companies would not be liable to Service Tax in the absence of consideration.

Under GST, transactions between the related parties, even without consideration, are deemed to be a supply of service liable to GST. Although the principle established by the SC in the case of Edelweiss Financial regarding consideration is not squarely applicable, the SC did not explicitly address the scope of 'service' per se, leaving room for interpretation. Accordingly, after much deliberation, the GST Council, in its 52nd GST Council Meeting, had clarified that the transaction would be liable to GST by way of issuance of impugned circular and incorporated new valuation rules prescribing 1% of the guarantee amount to be construed for the value of corporate guarantee arrangements.

It may be noted that the Delhi HC, in the case of Sterlite Power Transmission Limited, and the Telangana HC, in the case of GVK Power and Infra Limited, have already granted ad-interim protection against any recovery.

While the said ruling would provide significant relief to the taxpayers grappling with the notices from GST authorities, it would be interesting to observe how different HCs interpret and determine the tax implications of such arrangements.

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