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EY Tax Alert

HC interprets scope of intermediary services in case of sub-contracting service agreements

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Executive summary

This Tax Alert summarizes a recent ruling[1] of the Punjab and Haryana High Court (HC). The issue involved in the writ petition was whether the services provided by the petitioner under sub-contracting agreement fell within the scope of intermediary service and, therefore, ineligible for refund.

Petitioner contended that the services were provided on own account, and not in the capacity of agent. Hence, they do not qualify as an intermediary.

Further, reliance was placed on Circular[2] issued by Central Board of Indirect Taxes and Customs (CBIC) which clarified that sub-contracting services do not fall under the ambit of intermediary.

Revenue contended that the petitioner fulfills all the ingredients to qualify as an "intermediary". Also, the principle of res-judicata does not apply in taxation matters.

HC held that agreement clauses do not indicate that services rendered by petitioner fall under the ambit of an intermediary. Further, there is no change in the scope of "intermediary" services in the Goods and Services Tax (GST) regime *vis-a-vis* the service tax regime.

Applying the principles of consistency, Revenue cannot take a different view for periods where there is no change of facts. Accordingly, HC allowed the writ petition.

[1] 2022-TIOL-1413-HC-P&H-GST
[2] Circular No. 159/15/2021-GST dated 20 September 2021

Background

- The petitioner is a Business Process Outsourcing (BPO) service provider in India. It filed a refund application for unutilized Input Tax Credit (ITC) used in making zero rated supplies of services without payment of Integrated Goods and Services tax (IGST). Revenue, *vide* order-in-original (OIO), rejected partial refund amount.
- Aggrieved, the petitioner preferred an appeal before the Joint Commissioner of Central Tax (Appeals) (Appellate Authority).
- Meanwhile, Central Board of Indirect Taxes and Customs (CBIC) issued a Circular[3] clarifying whether "intermediary services" to overseas entities qualify as exports. The said Circular was subsequentially withdrawn[4].
- Revenue also filed an appeal against the OIO, contesting that the services rendered by petitioner are in the nature of intermediary services and hence the partial refunds sanctioned were erroneous.
- The Appellate Authority allowed the appeal filed by the Revenue and held that petitioner had received erroneous refund.
- Consequently, petitioner filed a writ petition before Punjab and Haryana High Court (HC). HC set aside the matter and remanded it back to the Appellate Authority for a fresh decision.
- The Appellate Authority again rejected the appeal filed by the petitioner and allowed the appeal filed by the Revenue.
- Aggrieved, petitioner has filed the present writ petitions before the HC.

Petitioner's contentions

- As per the definition of "intermediary" under Section 2(13) of the Integrated Goods and Services Tax Act, 2017 (IGST Act), a person who provides services "on his own account" is not an "intermediary".
- No evidence is on record to establish that the petitioner had not provided the main service. Further, there was no allegation that the petitioner had arranged third party to provide main services.
- Petitioner entered into a Master Services Sub-Contracting Agreement (MSA) with an entity outside India (client). Actual deliverables under MSA were on "own account" and provided from India remotely through telecommunication/ internet links using its infrastructure and workforce.
- MSA provides for rendering services to the client on a "principal-to-principal" basis and not in the capacity of an agent. There is no separate agreement between the petitioner and client's customers, and therefore, in no manner can the petitioner be equated to an agent or broker.
- Since the petitioner is performing the actual service under the MSA and it does not "arrange" or "facilitate" the service, it cannot be regarded as an "intermediary".
- In addition, the petitioner is responsible for all risks related to the performance of services and pricing of the services.
- Further, in the present case, turnover is the price charged for the main service, unlike an "intermediary" where turnover is a mere commission or a facilitation fee.
- Also, services rendered by petitioner were held to be export of service under the erstwhile service tax regime and Revenue sanctioned refund claims. Principle of consistency should apply to tax proceedings as well.
- Appellate Authority has relied on the ruling of Infinera India[5] and Vservglobal[6] and held that there was a material change in the definition of "intermediary" under the GST (Goods and Services Tax) regime. In contrast, the ruling of Infinera (*supra*) is in favor of the petitioner, wherein it held that definition of intermediary under GST and service tax regime is the same.
- Reliance was also placed on Circular[7] issued by CBIC wherein it was clarified that sub-contracting arrangements do not fall under "intermediary Services."

Revenue's contentions

- Referring to various clauses of MSA and Transfer Pricing report, it was contended that two broad categories of services are envisaged. First being the "main services" provided by the client to its customers, and second, being ancillary and support services provided by the petitioner to facilitate the client to provide main service to its customers.
- Further, an arrangement where one party possesses the authority to take day-to-day management decisions regarding actions taken by another party, can only be referred to as a principal-agent

[3] Circular No. 107/26/2019-GST dated 18 July 2019
[4] Circular No. 127/46/2019-GST dated 4 December 2019
[5] [2020] 112 taxmann.com 500 - AAAR
[6] 2018 (11) TMI 959 -AAR
[7] Circular No. 159/15/2021-GST dated 20 September 2021

relationship. The petitioners' role is supportive and does not act autonomously.

- Also, the client is responsible to its customers for any fault/lapse on the part of the petitioner in providing service to its customers and hence petitioner cannot be said to be providing services on his own account.
- Thus, petitioner fulfills all the ingredients to be termed as an "intermediary".
- Regarding allowing refund in pre-GST regime, the principle of res-judicata does not apply in tax matters for different assessment years. Tax matters for each year's assessment is final only for that year and does not govern later years.

HC ruling

- The scope of an "intermediary" is to mediate between two parties, i.e., the principal service provider and the beneficiary who receives the main service and expressly excludes any person who provides such main service "on his own account."
- On perusal of MSA clauses, it is clear that the petitioner is rendering sub-contracting services to client and receives fees/charges as a consideration.
- MSA clauses provide the modalities of how actual services will be performed and states that petitioner would be responsible for all risk related to performance of services which would be akin to services provided on "its own account".
- Further, MSA do not establish that the petitioner was required to arrange/ facilitate a third party to render the main service which the petitioner has rendered.
- Supreme Court (SC) in the case of Bharat Sanchar Nigam Ltd.[8] had held that where facts and law in a subsequent assessment year are the same, no authority whether quasi-judicial or judicial can generally be permitted to take a different view.

  Also, In the case of Radhasoami Satsang[9], SC held that although principles of res-judicata do not apply to taxation matters, but where parties have accepted fundamental aspects/facts permeating through different years, it would be inappropriate to change the position in subsequent years.

  There is no change in the scope of "intermediary" services in the GST regime *vis-a-vis* the service tax regime. Therefore, the principle of consistency ought to apply, and there being no change in facts, Revenue cannot take a different view for different periods.
- Further, the Appellate Authority has misread the ruling of Infinera (Supra) as the said ruling also held that no difference is found in the definition of intermediary under service tax regime and GST regime.
- Also, Circular (*supra*) clarified that sub-contracting for a service is not an "intermediary".
- Accordingly, High Court allowed the writ petition filed by the petitioner and set aside the order which held the petitioner to be an intermediary.

Comments

a. Amidst divergent advance rulings on the scope of intermediary, this HC ruling is likely to provide certainty w.r.t tax position to be adopted by taxpayers engaged in a similar line of business.

   This could also potentially result in tax cost savings.

b. As per the settled principle, decision of the High court, unless overruled or in the absence of any contrary rulings, shall have a binding effect across jurisdictions in India.

c. Taxpayers facing similar demands/refund rejections may persuade adjudicating/ appellate authorities by drawing support from the above HC ruling.

d. Earlier, constitutional validity of place of supply provision relating to intermediary service was challenged before the Division Bench of Bombay High Court. Considering the split verdict, the final decision is awaited.

[8] (2006) 3 SCC 1

[9] (1992) 1 SCC 659

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