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EY Tax Alert

Delhi HC upholds constitutional validity of anti-profiteering provisions under GST

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Executive summary

This Tax Alert summarizes a recent ruling of the Delhi High Court (HC)[1] upholding the constitutional validity of anti-profiteering provision under the Central Goods and Services Tax Act, 2017 (CGST Act).

HC observed that:

- Article 246A of the Constitution empowers the Parliament and Legislature to make laws 'with respect to' goods and services tax. The expression "with respect to" is of wide amplitude and thus, the law making power with regard to GST includes all ancillary, incidental and necessary matters.
- Section 171 is not to be looked at as a price control measure but is to be seen to be directly connected with the objectives of the GST regime.
- As per Rule 126, National Anti-profiteering Authority (NAA) 'may determine' the methodology and not 'prescribe' it. Thus, so long as the methodology determined by NAA is fair and reasonable, objection cannot be raised that the specifics of the methodology adopted are not prescribed.
- Mandate of price reduction cannot be tampered with by the supplier by substituting the benefit with any other form such as increase in volume or weight, supply of additional or free material, or festival discount.
- If Legislature chooses not to provide for a right to appeal against an order of NAA, it cannot be a ground to declare an enactment as unconstitutional.
- Section 164 gives power to the Government to make rules for carrying out provisions of the Act and in particular to provide for penalty.
- Time limit provided for furnishing of report by DGAP is directory in nature.

Accordingly, HC upheld the constitutional validity of the anti-profiteering provisions under CGST Act.

[1] 2024-VIL-84-DEL

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Background

- Section 171 of the Central Goods and Services Tax Act, 2017 (CGST Act) pertains to anti-profiteering measure. It provides that any reduction in rate of tax on any supply of goods or services or the benefit of an input tax credit (ITC) shall be passed on to the recipient by way of commensurate reduction in prices.
- Companies engaged in different businesses ranging from hospitality, FMCG to real estate have been directed to pass on the benefit to its customers.
- Writ petitions have been filed challenging the constitutional validity of Section 171 and Rules 122, 124, 126, 127, 129, 133 and 134 of the Central Goods and Services Tax Rules, 2017 (CGST Rules).
- The legality of the notices and orders proposing penalty, passed by National Anti-Profiteering Authority (NAA) under Section 122 have also been challenged.
- Petitioners prayed that the Court may first decide the plea of constitutional validity of the provisions. Only if the Court upholds the constitutional validity, the need to examine the matters on merits arise.
- Accepting the suggestion, the HC proceeded to hear the issue of constitutional validity of the provisions.

High Court's Ruling

Court's approach while dealing with tax or economic laws

- The laws relating to economic activities have to be viewed with greater latitude than laws touching civil rights. Further, the Legislature has to be allowed some play in the joints because it deals with complex problems.

Section 171 mandates that tax foregone has to be passed on as a commensurate reduction in price

- The amounts foregone from the public exchequer in favor of the consumers cannot be appropriated by the manufacturers, traders, distributors etc.

  To allow them to do so would amount to unjust enrichment.
- The word 'commensurate' has been used in several judgments of the Supreme Court (SC)[2] for laying down yardsticks in different contexts indicating that the Courts too have a clear and definite understanding of this word.
- Consequently, the word 'commensurate' in Section 171 of the Act, 2017 means that whatever actual saving arises due to the reduction in rates of tax or the benefit of ITC, in rupee and paisa terms, must be reflected as equal or near about reduction in price.
- Section 171 is not to be looked at as a price control measure but is to be seen to be directly connected with the objectives of the GST regime.

Section 171 falls within the law-making power of the Parliament under Article 246A

- Article 246A of the Constitution of India empowers the Parliament and Legislatures to make laws 'with respect to' goods and services tax. SC has consistently held that the expression "with respect to" is of wide amplitude and thus, the law making power with regard to GST includes all ancillary, incidental and necessary matters.
- Seven judge bench of SC in case of Ajit Mills[3] observed that providing for measures dealing with aspects of unjustly retained amounts as tax in the concerned statute were necessary / ancillary aspects connected with the subject of taxation.
- Thus, anti-profiteering mechanism as incorporated in Section 171 is in the exercise of the Parliament's power.

Section 171 lays out a clear legislative policy and does not delegate any essential legislative function

- The necessary navigational tools, guidelines as well as checks and balances have been incorporated in the provision itself to guide any authority tasked with ensuring its workability. Consequently, Section 171 neither delegates any essential legislative function nor violates Article 14 of the Constitution of India.
- On a conjoint reading of Sections 171(2) and 171(3), it is evident that the powers conferred on NAA by the Central Government under Rule 126 were intended by the Legislature to be exercised by the NAA itself.

Impugned provisions are not a price fixing mechanism

- If there is any variation on account of other factors, such as any costs necessitating the setting off of such reduction of price, the same needs to be justified by the supplier.
- If the supplier is to assert reasons for offsetting the reduction, it must establish the same on cogent basis and must not use it merely as a device to circumvent the statutory obligation of reducing the prices in a commensurate manner contemplated under Section 171.

[2] P.K. Chinnasamy v. Govt. of T.N., (1987) 4 SCC 601, Centre for PIL v. Housing & Urban Development Corpn. Ltd., (2017) 3 SCC 605, Dinesh v. State of Rajasthan, (2006) 3 SCC 771, Vimala (K.) v. Veeraswamy (K.) (1991) 2 SCC 375

[3] (1977) 4 SCC 98

Reference to anti-profiteering provisions of Australia and Malaysia is misconceived

- The anti-profiteering provisions under the Australian Trade Practices Act prohibits 'price exploitation' in relation to the New Tax System i.e., the Act by its nature regulates prices.
- Similarly, Malaysian Price Control and Anti-Profiteering Act, 2011 prohibits suppliers from 'making unreasonably high profit'.
- Therefore, the reference to Anti-Profiteering provisions of Australia and Malaysia is misconceived.

No fixed/uniform method or mathematical formula can be laid down for determining profiteering

- There is 'no one size that fits all' formula or method that can be prescribed. Consequently, NAA has to determine the appropriate methodology on a case to case basis keeping in view the peculiar facts and circumstances of each case.
- It is also well-established that where a power exists to prescribe a procedure and such power has not been exercised, the implementing authorities are at liberty to determine and adopt such procedure as they may deem fit subject to the same being fair and reasonable.
- As per Rule 126, NAA 'may determine' the methodology and not 'prescribe' it. Consequently, so long as the methodology determined by NAA is fair and reasonable, the petitioners cannot raise the objection that the specifics of the methodology adopted are not prescribed.
- The methodology adopted by NAA is flawed as in the real estate sector, there is no direct correlation between the turnover and the Input Tax Credit availed for a particular period.

  The Court, while hearing the matter on merits, shall take the aforesaid direction/ interpretation into account.

It is the prerogative of the legislature to decide how the benefit is to be passed on to the consumers

- The legislative mandate is that reduction of the tax rate or the benefit of ITC must not only be reflected in reduction of prices, but it must also reach the recipient of the goods or services.
- Such a mandate cannot be tampered with by the supplier by substituting the benefit in the form of reduction of actual price with any other form such as increase in volume or weight or by supply of additional or free material or festival discount or cross-subsidisation.
- The contention of the petitioners that it is legally impossible to pass on the benefits by reducing the price of goods in cases of low-priced products is untenable in law.
- HC referred the provisions of Legal Metrology (Packaged Commodities) Rules, 2011 and stated that there would be no legal impossibility in reducing the MRP even in such cases.

CGST Act does not fix a time period during which price-reduction has to be offered

- It is not proper or feasible to contemplate any specific period of time for application of the reduced price, as the same has to take effect so long as the direct relation between the reduction of tax rate or the benefit of ITC exists and there is no other factor effecting/countering the same.

A statutory provision cannot be struck down on the ground of possibility of abuse

- Petitioners advanced a number of hypothetical situations to suggest that there is a possibility of abuse of Section 171.
- However, it is settled law that Acts and their provisions are not to be declared unconstitutional on the fanciful theory that power would be exercised in an unrealistic fashion or in a vacuum or on the ground that there is an apprehension of misuse of statutory provision or possibility of abuse of power.
- It must be presumed, unless the contrary is proved, that administration and application of a particular law would be done "not with an evil eye and unequal hand".

Comparison of GST with a basket of earlier distinct indirect taxes

- CGST Act has subsumed the earlier catena of indirect taxes (Central as well as State indirect taxes), inasmuch as, it levies a single tax on the supply of goods and services.
- Consequently, the submission of the petitioners that Section 171(1) does not contemplate a comparison of the taxes levied after the introduction of GST with a basket of distinct indirect taxes applicable on goods and services before GST goes against the grain, intent and object of the CGST Act.

There is no vested right of appeal

- If Legislature chooses not to provide for a right to appeal against an order of the authority, that itself cannot be a ground to declare an enactment as unconstitutional.
- Further, the decisions of NAA are subject to judicial review under Article 226 before the jurisdictional High Courts.

There is no requirement of judicial member in NAA

- The mandate of NAA is very specific in nature and is akin to a fact-finding exercise.
- NAA has not assumed any jurisdiction which was hitherto being exercised by the High Court or any other judicial body, and so, the principle that there must be a judicial member in quasi-judicial entities as laid down in the decisions relied upon by the petitioners does not apply.
- Statutory bodies like TRAI, Medical Council of India, Institute of Chartered Accountant of India etc., perform quasi-judicial functions but do not have judicial members.

Second/ casting vote of chairman/ validity of constitution of NAA

- While Court is in agreement with the petitioners that the provision of a second or casting vote to the Chairman in the event of a tie/equality of votes as was given in Rule 134(2) is impermissible, yet as the Department has stated that the said provision has never been used, the Court does not deem it necessary to delve into a detailed discussion of the same.
- Additionally, the petitioners have challenged the validity of the constitution of the NAA on account of absence of a gazette notification as allegedly required under Section 171(2) of the Act. Court is of the opinion that this issue does not affect the constitutional validity of the impugned section which is presently under consideration and so this issue is not being dealt with in the judgment.

Levy of interest and penalty is within the rule making powers

- Section 164 gives power to the Government to make rules for carrying out provisions of the CGST Act and in particular to provide for penalty.
- Accordingly, Rule 133(3)(b) and (d) which empower the authority to levy interest @ 18% as well as imposition of penalty, are intra vires and within the Rule making power of the Central Government.

Time limit for furnishing of report by DGAP is directory and not mandatory

- Beneficial legislation must receive liberal construction that favors the consumer and promotes the intent and objective of the Act. That being the scenario, it cannot be said that the proceedings as a whole abate on lapse of time limit of furnishing of report by DGAP.
- Consequently, the time limit provided for furnishing of report by DGAP is directory in nature and not mandatory.

Expansion of investigation beyond the scope of the complaint is not ultra vires the statute

- From a reading of the Rule 129 especially the expression 'any supply of goods or services', it is apparent that the scope of the DGAP's powers is very wide and is not limited to the goods or services in relation to which a complaint is received. The word 'any' includes within its scope 'some' as well as 'all'.

Conclusion

- The constitutional validity of Section 171 as well as Rules 122, 124, 126, 127, 129, 133 and 134 is upheld.
- It is possible that there may be cases of arbitrary exercise of power under the anti-profiteering mechanism by enlarging the scope of the proceedings beyond the jurisdiction or on account of not considering the genuine basis of variations in other factors such as cost escalations on account of which the reduction stands offset, skewed input credit situations etc.

  The remedy for the same is to set aside such orders on merits.
- The matters are listed before the Division Bench for appropriate direction.

Comments

a. While the anti-profiteering provision is held constitutional, the NAA orders are still open to challenge on ground of unreasonableness or for not adopting appropriate methodology for computing profiteering.

b. For real estate sector, the Court observed that the methodology adopted by NAA is flawed. Those who are impacted basis the orders passed by NAA may have to wait for the Court to consider and adopt any particular methodology while setting aside such orders for re-computation of price.

c. The ruling reiterates several settled principles like non-requirement of judicial member in the performance of quasi-judicial functions, vested right of appeal etc.

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