

# Bimal Jain

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**Dear Professional Colleague,**

## **Supply of Goods Vs. Supply of Services in GST: Test of Constitutional Validity**

Owing to the federal structure of India, where there are two taxing authorities – the Central Government and the State Government(s), the Country has witnessed overlapping of powers of the State Government(s) and the Central Government. Even though the current indirect tax system treats goods and services differently, in certain cases where goods and services with other types of supplies are being packaged as composite bundles & offered for sale to consumers under a variety of supply-chain arrangements, there is double taxation. This is evident in the following exemplary cases:

### **Excise Vs. Service Tax:**

- Drawings and designs,
- Commissioning and installations,
- Software etc.

### **Service Tax Vs. VAT:**

- ACRestaurant services,
- Works contract,
- Construction Services
- Right to use of movable goods,
- Software,
- Intellectual Property Services,etc.

Adopting conservative approach to avoid unnecessary litigation, Trade & Industry charges both the taxes, on such litigated transactions.

To overcome these issues of double taxation that has plagued our present indirect taxation structure for long, GST is being expected to provide a resolution thereof. Though the Model GST Law placed on public domain on June 14, 2016, has made sensible efforts to put rest to some of the issues of double taxation, vide Schedule II to the Model CGST/SGST Act, 2016 but the same do not appear to have passed the test of constitutional validity, in certain areas.

## **Supply of goods Vs. Supply of services**

Schedule II to the Model CGST/SGST Act, enumerates the matters to be treated as ‘supply of goods’ or ‘supply of services’ in the following manner:

### **Matters to be treated as supply of goods:**

1. Transfer of title in goods

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2. Transfer of future goods (i.e. property therein will pass at future date)
3. Transfer/disposal of business assets with or without consideration
4. Sale of business assets by any other person to recover debt
5. Goods forming part of business assets on ceasing to be a taxable person
6. Supply of goods by an unincorporated association to its members

## **Matters to be treated as supply of services:**

1. Transfer of right to use goods
2. Lease, tenancy, easement, licence to occupy land
3. Lease or letting out of building
4. Job work on others' goods
5. Personal use/making available for non-commercial use of business assets
6. Renting of immovable property
7. Construction of a complex, building, civil structure or a part thereof, including a complex or building intended for sale to a buyer, wholly or partly, except where the entire consideration has been received after issuance of completion certificate, where required, by the competent authority or before its first occupation, whichever is earlier
8. Temporary transfer or permitting the use or enjoyment of any intellectual property right
9. Development, design, programming, customization, adaptation, upgradation, enhancement, implementation of information technology software
10. Agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act;
11. Works contract including transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract
12. Transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration
13. Supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (other than alcoholic liquor for human consumption), where such supply or service is for cash, deferred payment or other valuable consideration

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*(Services specified in points 6 to 13 are declared services as per Section 66E of the Finance Act)*

Manifestly, present disputes of goods vs. services have been very decently handled in the Model GST Law which has been for ages, marred the current tax regime. But, threadbare analyses of the same would reveal that the settlement of goods vs. services may not fade away so easily in GST when the Schedule II is tested on the scale of constitutional validity. Few of such important points are summarised as under:

## **Is it constitutionally valid to treat intangibles as services?**

The Model GST Law has made it explicit that intangibles would be treated as supply of services (as per definition of 'services' under Section 2(88) of the Model CGST/SGST Act, 2016), while the same has been excluded from the definition of 'goods' given under Section 2(48) of the Model CGST/SGST Act, 2016.

However, the definition of 'goods' given under Article 366(12) of the Constitution of India is defined in inclusive manner to provide that *"goods includes all materials, commodities, and articles"*, and even there are settled judgments of the Hon'ble Supreme Court to provide that this inclusive definition of goods incorporates both tangible as well as intangible goods. In the case of ***Tata Consultancy Services Vs. State of Andhra Pradesh [2004 (178) ELT 22 (S.C.)]***, the Hon'ble Apex Court held that: *"....In our view, **the term "goods" as used in Article 366(12) of the Constitution of India and as defined under the said Act are very wide and include all types of movable properties, whether those properties be tangible or intangible.** We are in complete agreement with the observations made by this Court in Associated Cement Companies Ltd. (supra). A software programme may consist of various commands which enable the computer to perform a designated task. The copyright in that programme may remain with the originator of the programme. But the moment copies are made and marketed, it becomes goods, which are susceptible to sales tax....."*

Thus, it may raise eyebrows as to whether for the limited purpose of GST, 'intangibles' (i.e. copyright, goodwill, software, trademark, etc.) can be considered as 'service', when the Constitution does not allow so. In case, tax is levied on the basis of definition provided in Model GST Law, it would tantamount to defiance of sanctity of the Constitution, which is ultra-virus.

## **Packaged software – whether goods or services?**

Even if the bifurcation of goods and services created in Model GST Law by virtue of Schedule II is accepted (leaving aside the contraction with the Constitutional provisions), still there are certain matters where litigation may continue such as likely issue of dispute in case of packaged software (i.e. software provided in physical forms like CD/DVD, etc.), where a contrary view might be possible contending that by supplying software on CDs (being

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tangible property), the intention is to supply the 'software' essentially (being intangible property) and not the CDs etc.

## **Deemed sale of goods concept in the Constitution Vs. Schedule II**

As per Article 366(29A) of the Constitution, certain items such supply of food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration and Works contract etc. are deemed to be sale of goods. Article 366(29A) of the Constitution is reproduced hereunder for ease of reference:

*“(29A) tax on the sale or purchase of goods includes*

*(a) a tax on the transfer, otherwise than in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration;*

*(b) a tax on the transfer of property in goods (whether as goods or in some other form) invoked in the execution of a works contract;*

*(c) a tax on the delivery of goods on hire purchase or any system of payment by instalments;*

*(d) a tax on the transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;*

*(e) a tax on the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration;*

*(f) a tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration, and such transfer, delivery or supply of any goods shall be deemed to be a sale of those goods by the person making the transfer, delivery or supply and a purchase of those goods by the person to whom such transfer, delivery or supply is made.”*

While the 122<sup>nd</sup> Constitutional Amendment Bill, 2014 has chosen to continue with Article 366(29A) of the Constitution (as against 115<sup>th</sup> Constitutional Amendment Bill, 2011 wherein it was proposed to be deleted), on the contrary, as per the Model GST Law, the same i.e. AC Restaurant Services and Works Contract has been deemed to be as supply of services in terms of Schedule II to the Model CGST/SGST Act. There would be a constitutional contradiction in this regard, though it may not affect taxability under GST if rate of GST is kept same for goods and/or services but, may be of great importance if different GST rates are being prescribed for goods and services.

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In the nutshell, when the India Inc is pinning hopes on GST to eradicate present issues of double taxation, it is imperative that the Government should realise the importance and true intent of introduction of most powerful transformational tax reform in India, to ensure that the issues of Constitutional validity are properly taken care of, to allow the taxpayers to yield the true benefits of GST.

Thanks & Best Regards,

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