

EY Ltd. v. Addl Commissioner, CGST: Preventing the Mischaracterization of Service Exports as Intermediary Services

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Abstract

The Indian Foreign Trade Policy (FTP), 2023- affixed 4 panoptic directives: being '(i.) Incentivized Remission; (ii.) Cohesive Export Promotion (ii.) Mitigated Transaction Costs- fostering Enterprise Viability (iv.) Emerging Sector Exports and Export Control (i.e., SCOMET) Rationalization'¹. The 'expanded ambit' of export transactions, devoid of obstructive-regulatory costs- subject to maximized prospective remission, is hence the idealized consequence. The recommendatory impetus of the 52nd GST Council (October 7th, 2023)- specifically 'Trade Facilitation Measures, ¶V': included the supply of services within the ambit of exports, fulfilling condition precedent receipt of proceeds in convertible currency/INR- prescribed by §2 (6) (iv) of the IGST Act, 2017- via the modus of evidentiarily validating export proceeds received in Special Vostro accounts (as mandated by the RBI²) for such supply of services. The ambit of such export aspirations- additionally includes incentivized foreign sponsorship (via capital infusion and technology transfer)- of domestic product/service provision to off-shore recipients (via the 'Make-in-India'

¹Foreign trade policy 2023 announced (2023) Press Information Bureau. Available at: <https://pib.gov.in/PressReleaseframePage.aspx?PRID=1912572> (Accessed: 28 April 2024).

² Reserve Bank of India - notifications. Available at: https://www.rbi.org.in/scripts/FS_Notification.aspx?Id=12358&fn=5&Mode=0 (Accessed: 28 April 2024)- Para 3 (b).

scheme³)- ultimately embodying, the **premise of legislative intent directing prospective purposive statutory interpretation**. The objective of this article is to analytically evaluate the significant implication of contemporary Indian jurisprudence (i.e., *EY Ltd v. Addl Comm CGST*) in aligning such legislative intent of export promotion aspirations, with effected tax liability and the inhibition of arbitrary regulatory wilful/negligent taxable event mischaracterization (as intermediary services).

1. Court Intervention

The Delhi High resolved the **incongruity of misguided antecedent textual-interpretation/neglect** by the Adjudicatory and Appellate Authorities of:

- i. §2 (13) [IGST Act, 2017] and CBIC Circular No.159/15/2021-GST- defining ‘intermediary services’,
- ii. §2 (6)- defining exports,
- iii. §13 (2)-affixing the *Lex Generalis* place of supply, as the location of service recipients for prospective export/import transactions and,
- iv. §13(8)(b)- upholding the *Lex Specialis* exceptional place of supply- as the supplier location, for intermediary services;

with requisite purposive interpretation- in the case of *Ernst and Young Ltd v. Additional Commissioner, CGST (EY Case)*⁴.

The primary issue of the case was whether the **provision of ‘professional services’ by an Indian branch of Ernst and Young (EY) Ltd- (U.K Incorporated)- to other off-shore EY group affiliates** (¶6 of the case): i.e., the EY LLPs based in the U.K and the U.S.A; and the EY limited enterprises based in Australia and New Zealand, **would qualify as the provision of ‘intermediary services’ by the branch, devoid of export character and hence devoid of owed**

³Government takes various export promotion initiatives like new Foreign Trade Policy, extension of Interest Equalization Scheme on pre and post shipment rupee export credit, etc.. (2023) Press Information Bureau. Available at: <https://pib.gov.in/PressReleasePage.aspx?PRID=1988823> (Accessed: 28 April 2024).

⁴ *Ernst and Young Ltd. v. Additional Commissioner, CGST, 2023 SCC OnLine Del 1764.*

Input Tax Credit (ITC) refund due to the 'Zero-Rated' stature of Exports- according to §16(1)(a) of the IGST Act.

The court ultimately upheld the lack of 'intermediary' stature of the provided services by EY Ltd.'s Indian Branch, in ¶29 of the judgement, while validating the characterization of an export transaction (¶34)- warranting the entire refund of the claimed ITC's to EY Ltd.

2. Export Mechanism

The 'Export of Services' is defined as the provision of services by an India-located supplier to an off-shore recipient; subject to extra-territorial place of supply and consideration received in convertible foreign currency/INR, devoid of intra-state, yet inter-establishment distinct person undertaking, according to §2 (6) of the IGST Act.

§16 (1) (a), re-enforced by §2 (23) - characterizes service-exports as 'Zero Rated', with the objective of export promotion. Such classification, **in effect**- mitigates IGST transaction cost obstructions for service-exports, aligned with the second pillar of the FTP, 2023. The allowance of exports devoid of requisite IGST payment (yet subject to refundable unused ITC's), by §16 (2) and (3) of the IGST Act via letter of undertaking/bond- covenanting statutory IGST payment-schedule adherence when applicable; or exports subject to refundable IGST payment, embodies the operationalization modus. Rule 96 of the CGST Rules, 2017, establishes the refund mechanism for IGST-paid on product/service exports- initiated by the exporter's filing of the shipping bill, while adhering to the compliance requisites of FORM GSTR-3/3-B. Rule 96A- prescribes adherence to FORM GST RFD-11 (for the furnishing of the stipulated Bond/Letter of Undertaking), for obtaining ITC refunds upon export transactions (devoid of IGST payment)- by service suppliers.

Despite, the regulatory export-characterization of the services rendered by E.Y U.K's Indian Branch to other off-shore EY group affiliates, prior to the GST Regime (subject to court cognizance in ¶29 of the case); the Adjudicatory Authority (subsequently validated by the Appellate Authority)- discredited such export-characterization, by:

- i. Issuing Show Cause Notices- specific to every ITC refund application.
- ii. Denying such ITC refunds claimed and

- iii. Wrongfully classifying the services provided as 'intermediary services' - subject to Place of Supply- mirroring service supplier location, due to IGST Act §13(8)(b).

The High Court however, ultimately vitiated the intermediary service classification (in ¶29); due to the **distinctly direct provision of professional consultancy services by EY UK's Indian branch to the off-shore service recipients- separable from the auxiliary facilitation of such service provision** (deemed intermediary function), while purposively applying §13(2)- resulting in the place of supply being service recipient location; rationalizing export characterization and unutilized ITC claim refund.

3. Intermediary Service Provision

The Intermediary classification- is dualistic: in terms of defined 'Intermediary Persons'- in §2 (13) of the IGST Act, and 'Intermediary Services' - subject to 6 requisite constituent elements (inclusive of the intermediary person character of the service provider), as stipulated by the CBIC via Circular No. 159/15/2021-GST. The individualized intermediary conception entails the **auxiliary facilitation/arrangement** of the supply of goods/services/securities through an agency/brokerage/other representative capacity, **excluding the direct supply of such goods/services /securities**. There is hence a codified distinction between the **facilitation of service supply**; and **direct service supply** (*irrespective of external controlling interest/asset-ownership, as in the case of EY U.K, over the Indian Office*).

The CBIC prescribes the following constituent elements:

- i. A minimally tripartite- intermediary service transaction structure: with a service provider; an intermediary-facilitator and a service recipient.
- ii. The undertaking of 2 distinct supply transactions, being:
 - a. A main supply- of goods/services/securities- between the principal provider and recipient.
 - b. An Ancillary Supply-of facilitation/arrangement (clearly discernible and intermediary) of such main supply.

- iii. The undertaking of such ancillary supply via agency/brokerage/other representative capacity;
- iv. Wholly exclusionary of direct principal service supply (on an individual's own accord) and service receipt.
- v. The further exclusion of sub-contracting by the principal service provider in furtherance of direct service supply from the ambit of intermediary service;
- vi. The jurisdictional loci of the transaction intermediary and/or principal service recipient- being outside India, for regulatory applicability.

The implication of §13(8)(b) of the IGST Act- affixing the place of supply for intermediary service transactions as the location of suppliers as opposed to service-recipients (prospectively off-shore), is contrary to the 'destination-based' taxation objective of the GST Regime.⁵ Additionally, I believe, by excluding transactions of ostensible 'auxiliary supply' from the ambit of prospective 'Zero Rated export classification subject to unused ITC claim refundability', there is no intelligible differentia-justifying varied regulation from proclaimed 'main supply'- thereby inducing 'class legislation character' for the provision; being contrary to Article 14 of the Constitution, on the basis of arbitrariness-according to *Maneka Gandhi v. Union of India* (Pp. 57-58)⁶.

The Mumbai and Gujarat High Court Verdicts of *Dharmendra Jani v. U.O.I* (W.P No. 2031 of 2018)- specifically ¶84 and *Material Recycling Association of India v. U.O.I* (C/SCA/13238/2018) - ¶68-69: however upheld the constitutional validity of intermediary service exclusion from export characterization- due to 'presumption of constitutionality centric interpretation' and the unsatisfied onus probandi of evidencing distinct constitutionally ultra vires stature of §13(8)(b). The Gujarat High Court perceived the administrative exception of intermediary services subject to intermediary and service-recipient off shore locus- from the ambit of operationalized IGST via Entry No. 12AA of Notification No. 20/2019-Integrated Tax; as the proactive inhibition of arbitrariness. In neither case however did the respective High Court's proactively rationalize the alleged intelligible

⁵An overview of GST. Available at:

<https://pib.gov.in/newsite/printrelease.aspx?relid=161273#:~:text=GST%20is%20a%20destination%20based,the%20next%20stage%20of%20transaction.> (Accessed: 28 April 2024).

⁶ *Maneka Gandhi v. U.O.I*, 1978 SCR (2) 621 [Pages 57-58].

differentia, ostensibly characteristic of the IGST Act- export exclusion. Hence, the characterization of transactions as 'intermediary service Provision, devoid of exception' has remained an avenue for the Adjudicatory Authority (subject to Appellate Authority validation) to inhibit the loss of IGST Revenue, resultant from export classification 'Zero Rating', and prospective unused ITC claim refund. **In the EY case however, the Delhi High Court- inhibited administrative transaction mischaracterization, sanctifying the 'Zero Rating + unused ITC claim refund' incentives for Indian export promotion.**

4. Material Fact and Procedural History Analysis

The ambit of services provided by EY Ltd. (U.K) via its Indian branch to off-shore service recipients (being EY Group Affiliates: i.e., the U.S and U.K LLP's and Ltd. Corporations based in New Zealand and Australia), were ascertained by the Court, with specific reliance on the Service Agreement (29th September, 2009), between EY Limited and EY U.S, as a common-terms template, according to ¶8. The range of services provided were: assurance/business-advisory services; technical expertise-consultancy specific to expatriate persons and enterprise American Tax Statute- requisite compliance; Knowledge Transfer; American income tax returns-assessment and validation; American Audit-requisite- compliance centric technical expertise. In every case- the services were provided directly by EY Ltd., via it's Indian Office-¶22, and there was no intermediary facilitation/arrangement of service supply.

Upon the provision of such services to the off-shore clientele- EY Ltd. via it's Indian Office, applied for ITC refunds- at 3 separate intervals, starting from December 2017 and concluding at March 2020. The Adjudicatory Authority attempted to discredit the validity of every such ITC refund application- by notifying EY of the requisite of showing- cause 'specific to the basis for the export classification of the service-supply (disregarding pre-GST status Quo); the stature of the ultimate services (output); with document submission of service agreements, and raised invoices- subject to the off-shore clientele'- ¶12. Additionally, the Adjudicatory Authority required clarification regarding the manner of use of the input services subject to ITC claim- with the requisite justification of nexus/proximity to the ultimate service. Post EY Ltd.'s response; the Adjudicatory Authority- accepted EY Ltd's ITC refund requests for the duration post March 2020- as observed in ¶29, however, while primarily relying upon the RBI's authorization letter (2008)- authorizing EY's establishment of an Indian Office: The

Adjudicatory Authority denied the residual ITC refund requests- on the basis of non-export and intermediary characterization of the service supply. The letter authorizes the direct provision of Consultancy Services by the Indian branch in addition to operating as a buying-selling agent. The Adjudicatory Authority, wrongfully relying upon the latter allowance- solely characterized the function of the Indian office- as intermediary buying and selling agency. In no way however did the RBI's letter- restrict the functional scope of the Indian branch to the rendering of auxiliary buying-selling agency-services- according to ¶25.

Upon appeal however, the jurisprudential basis- pivoted from the misconceived application of IGST Act § 2 (13) on the RBI's authorization letter, to the affixation of place of supply-specific to intermediary supply regulation via § 13(8)(b), as supplier location. Both the Adjudicatory and Appellate Authorities were found to have wrongfully **neglected the ultimate exclusion of direct service supply on an individual's own accord from the ambit of 'defined intermediary services'** in §2 (13), as well as the 4th constituent element, in the CBIC circular 159/15/2021; according to ¶33 of the EY case.

Ultimately, in the absence of the constitution of the GST Appellate Tribunal (deemed the appropriate forum of recourse against Appellate Authority verdict, by §112 of the CGST Act, 2017), at the time, the modus of Writ Recourse for the issue; was validated as constitutionally intra-vires (within the ambit of Article 226 of the Indian Constitution)- according to ¶3. Post the invalidation of intermediary service transaction classification; the High Court- applied the requisite constituent elements of export transactions- stipulated in §2 (6) of the IGST Act, to find the due presence of export character (warranting 'Zero Rated GST applicability + owed unutilized ITC claim refundability)- via ¶30 and ¶33. The 'destination-based' IGST-place of supply affixation of §13 (2)- being the service-recipient location for export transactions, as *Lex Generalis*, was hence applied.

5. Intermediary Supply Jurisprudence

The transaction structure of the EY case entailed the direct provision of professional consultancy services by an Indian asset of EY Ltd., to related off-shore clientele on an arm's length basis- ¶6 of the case. In case there is indirect provision of service however (irrespective of degree/quantum of third party arrangement/facilitation)- 'intermediary stature' defined

by the CBIC's 6 constituent elements (as aforementioned) and § 2 (13) of the IGST Act, may be affixed- according to ¶17 of the M/s Airbus Group India Pvt Ltd.⁷ case. Additionally, contrary to the material reliance on- the direct raising of invoices by EY Ltd., as against the Offshore service-recipients (¶13 of the EY case); in the case of intermediary supply (subject to third party arrangement/facilitation in an agency/brokerage/other representative capacity)- the 'non-payment of commission' by either the service recipient/service provider to such intermediary- was found to be immaterial.

6. Conclusion

The Delhi High Court's ultimate ascertainment of service export character for the services rendered by the Indian EY affiliate, to off-shore EY entities (as conclusive clientele), devoid of any concession being made to the misplaced 'intermediary-service' claims by the antecedent adjudicatory/appellate authorities & CGST commissioner, renders security (from unwarranted tax liability/administrative overreach) to prospective foreign investors seeking to establish production units within India for the pursuit of export promotion (benefiting from India's regulatory & incentive arbitrage potency).

⁷ Airbus Group India P. Ltd.-2016 (45) STR 120 (Tri.-Del).