Analysis on Supreme Court Judgment in Mohit Minerals – Striking Down the Levy on Ocean Freight

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Introduction:

The entire country is swayed by the Honourable Supreme Court's verdict in the matter of Mohit Minerals Private Limited[1]. This is completely unexpected decision after what we have seen in VKC Footsteps India Private Limited. The Supreme Court has struck down the obligation to pay tax under reverse charge mechanism by the importer. Earlier, the Gujarat High Court qua writ petition filed by Mohit Minerals Private Limited[2], has held the notifications bringing the tax under reverse charge mechanism are ultra-vires the law. The said judgment was appealed before the Supreme Court by Revenue, which led to the current judgment. In this write -up, we shall analyse the decision delivered by Supreme Court.

The entire issue is, whether the importer is liable to pay tax on ocean freight services provided by foreign shipping line qua the foreign supplier under the reverse charge mechanism for the CIF contracts? The position under service tax law[3] and the analysis of the decision of Gujarat High Court[4] can be accessed here.

The Supreme Court after listening to the appellant (the Union of India) and the respondent (Mohit Minerals Private Limited) has opined on various issues, which are summarised hereunder:

On Nature of Recommendations of GST Council:

The whole issue arose as to whether the recommendations made by the GST Council are binding on the Union and States? The Supreme Court stated that the role of GST Council is a recommendatory body aiding the Government in enacting the legislation on GST and cannot be said to have a binding power on the Union and States. The conclusion was arrived on the reasoning that the provisions of Article 246A does not contain force which would convert the recommendations of GST Council into legislation. The Court stated that neither Article 279A does not also begin with a non-obstante clause nor does Article 246A provide that the legislative power is 'subject to' Article 279A. In absence of such a language, the argument canvassed by the Union of India that the recommendations of the GST Council are binding on Union and States is farfetched. The Court also stated that repugnancy provision that was contained as in Article 254 which was not present in Article 246A further indicates that recommendations of the GST Council cannot be said to be binding. The Court stated that there concurrent power exercised by the legislatures under Article 246A is termed as 'simultaneous power' to differentiate it from the constitutional design on exercise of concurrent power under Article 246, the latter being subject to repugnancy clause under Article 254. The Court stated that it is in the context of simultaneous legislative power conferred on Parliament and State legislatures, the role of GST Council has to be understood as a constitutional and recommendatory body and cannot be said the recommendations are binding on the Union and States.

[1] [2022] 138 taxmann.com 331 (SC)
[2] [2020] 113 taxmann.com 436 (Gujarat)
[3] https://www.sbsandco.com/blog/sbs-wiki-e-journal-aprl-2018
[4] https://www.sbsandco.com/blog/mohit-minerals-recipient-of-service-to-be-revisited

On the Aspects of Recipient of Supply and Others:

The Court has struck down all the various submissions made by the respondent dealing with the taxable person, Section 5(1) to be only the charging provision, the prescription of rate of 10% of CIF through the main act and not through delegated legislation and others. The Court was seized only with the aspects – Whether classification of imports as a specific category of supply of shipping service is valid under Section 5(3) read with Section 5(1) of IGST Act and Whether the recipient of the imported goods is also a recipient of shipping services in CIF transactions under Section 5(3)?

Whether classification of imports as a specific category of supply of shipping service is valid under Section 5(3) read with Section 5(1) of IGST Act?

The respondent's (Mohit Mineral Private Limited) main argument is that the supply of service of shipping in a CIF contract is from the foreign shipping line to the foreign exporter and the transaction has no territorial nexus to India and hence does not constitute 'supply' that can be taxed. The Court stated that in terms of Section 7(4) of IGST Act, supply of services imported into a territory of India shall be treated to be supply of services in course of a inter-state trade or commerce and accordingly an Indian importer could also be considered as importer of service of shipping which is liable to IGST, if the activity falls within the definition of 'import of service'. After tracing out the definition of 'import of service' in terms of Section 2(11) of CGST Act, the court noticed that condition of import of service entails three aspects – (i) supplier of service must be located outside India, (ii) the recipient of service must be located in India and (iii) the place of supply of service ought to be in India. The Court stated the respondent's argument that conditions (ii) and (iii) have not satisfied since the recipient of shipping services would be foreign exporter and place of supply shall be place of business of foreign exporter should not be taken on the face value, since the 'recipient' and 'place of supply' has to be analysed in the context of the GST laws and not based on contracts.

The Court brushed away the argument canvassed by the respondent that since there was no consideration payable for the import of services, the same cannot be called as 'supply' by stating that the 'consideration' is satisfied even it is made by another person in terms of Section 2(31) and accordingly held that even if the importer is not liable to pay consideration directly, still the said transaction would fall under the ambit of 'supply'. The Court also brushed away the aspect of extra-territorial by making reference to the decision of GVK Industries Limited[5] and held that since there is clear territorial nexus, the question of challenge on grounds of extra territorial does not arise.

The Court then stated that since in terms of Section 13(9) of IGST Act, since the place of supply of transportation services is destination of goods and clearly the supplier of service that is foreign shipping line is located outside India, then by applying the provisions of Section 13 and Section 13(9), the place of supply of service is India. The Court then proceeded with the only remaining question, whether the importers can be called as recipients?

Whether the recipient of the imported goods is also a recipient of shipping services in CIF transactions under Section 5(3)?

The Court stated that the argument made by Revenue that in light of the usage of the expression 'unless the context otherwise requires' in Section 2, makes the ambit larger and accordingly the importer should be treated as recipient in terms of Section 2(93) would be farfetched. The reason for such a conclusion

[5] [2011] 197 Taxmann 337 (SC)

was that such an argument would overlook the context of Section 5(3) which reiterates that the taxable person to be the recipient of service and since the importer was not specifically mentioned as taxable person in the statute, the argument should be required to be set aside. In simple words, as we understand the relevant para of the judgment, it is evident that the Court is trying to find a specific mention of 'importer' as recipient of service in the IGST Act and just because a person is required to pay tax under reverse charge and requires registration cannot be called as recipient of service. Further, the Court observed that the current provision of Section 5(3) delegates the power to notify the good or services that are required to be paid under reverse charge but does not have the power to delegate and specify the person who would be recipient and the same has to be found in the IGST Act. Since, in the instant case, there is nothing in the IGST Act to make the importer as recipient, the arguments of Revenue would have to be struck down but for the provisions of Section 13(9) read with Section 2(93)(c). Any reference to a person to whom a supply is made shall be construed as a reference to the recipient of the supply, which is found in Section 2(93)(c), when read with Section 13(9), which makes the destination of goods as the place of supply, then it can be inferred that supply of services would have been made to the Indian importer and thus thereby he can be considered as recipient of supply. The Court stated that the conclusion comports with the philosophy of GST to be consumption and destination based tax and accordingly held that since the ultimate benefactor of shipping service is also the importer in India who will finally receive the goods at a destination which is within the taxable territory of India and hence the importer can be called as 'recipient'.

Having concluded all the aspects in favour of the Revenue, the Court then proceeded with the main question as to the composite supply and issues of double taxation.

On Composite Supply and Issues of Double Taxation:

The transaction involves three parties – the foreign exporter, the Indian importer and the shipping line. The first leg of the transaction involves a CIF contract, wherein the foreign exporter sells the goods to the Indian importer and the cost of insurance and freight are the responsibility of the foreign exporter. The second leg of the transaction involves an agreement between the foreign exporter and the shipping line for providing services for transport of goods to India.

On the first leg of the transaction between the foreign exporter and Indian importer, the Indian importer is liable to pay IGST on the transaction value which includes the provision of services such as insurance and freight making it classifiable as 'composite supply' under Section 2(30). Since as per Section 8, the principal supply is to be subjected to tax qua a composite supply and since the principal supply in the instant case would be the goods, the tax would be leviable as if the transaction was one of supply of goods.

The Respondent (Mohit Minerals Private Limited) has contended that the current levy which seeks to impost IGST on the 'service' aspect of transaction would be in violation of principle of composite supply. This is for the reason that the impugned levy is trying to break a part of the composite supply and try to bring the same under the tax net. The Revenue contended that impugned levy is on the second leg of transaction, which is standalone contract between foreign exporter and shipping line and accordingly stated that contract between the foreign exporter and shipping line of which the Indian importer is not a party cannot be deemed to be a part of composite supply. The Revenue contended that while the first leg of the transaction is a composite supply, the second leg is an independent transaction and relying

the decision of McDowell[6] to contend that a single element can constitute a levy and a part of value for another transaction and urged that concept of aspect theory has to be applied.

The Court rejected the application of aspect theory and stated that the Revenue cannot take contradictory stands, which would imply that while on one hand the Revenue seeks to levy tax on importer by going beyond the text of contract between the foreign shopping line and foreign exporter and on the other hand, as far as submissions on composite supply are concerned, urges that the contract should viewed as separate transactions, operating in silos. Accordingly, the court rejected the levy of tax on the freight services.

Points to Ponder:

From the above analysis, it is evident that though the Revenue/Union of India/Appellant has won all the major concepts, what struck the levy was the application of concept of composite supply to the whole transaction. The question that arises is, can the foreign exporter be said to be a 'taxable person' to fall under the definition of 'composite supply'. The definition of 'composite supply' vide Section 2(30) uses the expression 'taxable person'. The said expression is defined under Section 2(107) to mean a person who is registered or liable to be registered under Section 22 or Section 24. The IGST Act or CGST Act does not mandate the foreign exporter to obtain registration. In such a case, can one say that foreign exporter is a 'taxable person'? If no, how can one apply the concept of composite supply to such a situation. Alternatively, is the Supreme Court trying to state that importer would be a taxable person and the concept of composite supply has to be applied at his end instead of foreign exporter? We feel that more time would have been spent on the aspect of aspect theory and applicability of composite supply than what has been spent by the Supreme Court. May be the job is left to another bench when it comes again in another proceeding. We have to wait and see, till then, we have to live with this judgment.

[6] 1985 (3) SCC 230