

Karnataka HC grants ad-interim stay on adjudication proceedings denying ITC on secondment of employees

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Summary

The Karnataka High Court (HC) has granted an ad-interim stay on the departmental proceedings wherein the input tax credit (ITC) of the IGST paid on a reverse charge basis on the payments made to seconded employees/related entities has been denied. The HC observed that the department did not consider the apex court's decision in the case of Northern Operating Systems Private Limited and proceeded to deny the ITC availed by invoking the limitation provisions prescribed under GST law.

Facts of the case

- The Supreme Court, in the case of *M/s. Northern Operating Systems Private Limited [CA No. 2289-2293/2021]*, had held that the secondment of employees by the overseas entity qualifies as 'manpower supply services' provided to the Indian entity, and therefore, the salaries and other expenses recovered from the Indian entity would be exigible to service tax.
- In furtherance of the above decision, *M/s. Toyota Kirloskar Motor Private Limited* (the petitioner) had discharged the IGST liability under the reverse charge mechanism (RCM) and subsequently availed ITC of the same.
- However, three different authorities had issued show cause notices (SCNs) in the quest to deny the ITC availed by invoking the limitation period as prescribed under Section 16(4) of the CGST Act, which restricts ITC availment for a given financial year till 30 November of the subsequent year, or the date of filing an annual return, whichever is earlier.
- The department contended that the prescribed limitation period for availing the ITC shall apply from the date such liability arises, i.e., the time of supply of the underlying transaction.
- On the other hand, the petitioner has contested the applicability of such limitation and asserted that the department has failed to take into consideration the decision of the SC, which has finalised the levy of GST.

Karnataka HC's observations and *ad-interim* order [WP No. 22952/2023; Order dated 12 October 2023]

- The HC observed that the department had not considered the SC's decision in the case of Northern Operating Systems (supra) and granted an interim stay on the adjudication of the SCNs issued by the central and state tax authorities.
- The HC also granted liberty to the authorities to seek vacation of such stay.

Our comments

Pursuant to the judgement of Northern Operating Systems, the Directorate General of Goods and Services Tax Intelligence (DGGI) initiated inquiries into similar arrangements. To safeguard against potential penal implications, the taxpayers voluntarily paid the GST tax liability under the reverse charge mechanism and availed the ITC for the same. However, the GST department has raised disputes on several occasions regarding these ITC claims.

The taxpayers opine that the ITC under the RCM is eligible on payment basis and from the date of self-invoice in terms of the provisions of GST law. This has become a contentious issue, which requires clarification to prevent any dispute between the taxpayers and the department.

It may be noted that before the decision of the SC, there was no clarity on the taxability on the secondment of employees and the assesseees cannot be held liable retrospectively. The department should take into consideration the decision of the SC before proceeding to deny the ITC availed on the transaction. Accordingly, precluding the taxpayers from obtaining the ITC in such cases would be manifestly arbitrary.

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