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GST Blow For Entities Servicing Foreign Clients In India?

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It is common practice for foreign entities to engage service providers in India at the time of market entry for a host of services that could range from market research, advertising and promotion services, liaising with prospective customers etc. While such services were treated as exports and not subjected to service tax under the earlier service tax regime, these services now potentially face a Goods and Services Tax of 18 percent based on a recent ruling.

The ruling concerned Global Reach Education Services Pvt Ltd. – the applicant – an Indian overseas education consultant that promoted foreign universities' courses in India and also provided market intelligence about latest educational trends in India. Additionally, it also ensured payment of requisite fees by Indian students enrolling in foreign courses through the applicant. For providing such services, Global Reach was paid based on a formula i.e. as a percentage of the tuition fee for each student recruited/enrolled through it and the payments were made in foreign currency.

Although cross-border services agreements are usually executed between an Indian services entity and a foreign recipient of services, in some cases, the ultimate benefit of services provided may flow to an Indian customer of the foreign recipient as well. For instance, when an e-commerce platform delivers a gift parcel to a consignee based on a customer's request, the beneficiary is the consignee, not the customer.

But does that mean that the customer's customer (i.e. the consignee) becomes the e-commerce platform's customer as well?

The answer to this question appears to be 'yes', if one is to go by the reasoning given in a recent tax ruling of the West Bengal Authority for Advance Rulings.

Due to this reasoning, transactions that were previously considered tax-free exports suddenly appear to be taxable as 'intermediary services' under the Goods and Services Tax regime. This appears to be incorrect in law, and contrary to previous decisions on the same point under the erstwhile service tax regime.

It is important to note that GST defines an 'intermediary' to mean "a broker, an agent, or any other person, by whatever name called, who arranges or facilitates the supply of goods or services or both, or securities, between two or more persons, but does not include a person who supplies such goods or services or both or securities on his own account".

> The law, therefore, makes a distinction between entities that provide services on their account and entities that arrange or facilitate the provision of services between two or more persons.

It is only the latter category of entities are classified as 'intermediaries' for the purposes of GST.

Applying these principles, Global Reach should not have been considered an intermediary for the purposes of GST. The rationale being that the applicant was only providing marketing and

promotion services on its own account to its clients (i.e. foreign universities), and was not concerned/involved with the provision of education services by foreign universities to Indian students. Hence, no GST should have been payable on such services.

Unfortunately, the AAR appears to have effectively nullified the distinction between an 'intermediary' and an independent service provider, thereby paving the way towards greater taxation. In order to determine whether the applicant had provided services on its own account, or as a representative of foreign universities, the AAR relied almost exclusively on the payment mechanism agreed between Global Reach and foreign universities.

> In the AAR's view, the fact that the applicant was paid on a commission basis necessarily meant that it did not provide services on its own account.

However, it is difficult to reconcile this reasoning with the settled understanding of what an intermediary is. Several decisions under the erstwhile service tax regime (which contained a near identical definition of the expression 'intermediary') have clarified that when services are provided by a service provider on its own account, it cannot be considered to be intermediary services.

If this reasoning is to apply, every single internet-based payment gateway would be treated as an intermediary even though for all intents and purposes, the payment gateway operator would be providing payment processing services on its own account, and not on behalf of someone else.

The only saving grace is that advance rulings are strictly binding only on the applicant seeking the ruling, and the concerned jurisdictional GST officer. Therefore, this ruling does not affect the services industry as of today technically. If the rationale adopted by the AAR is followed, nearly every commission-based supply of goods or services could be classified and taxed as an intermediary supply. This would greatly add to the overall cost of doing business in the country and make exports of services uncompetitive.

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