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Advance Ruling and Anti Profiteering under the GST Law

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Advance Ruling

"Advance Ruling" – Meaning & its Advantages

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"Advance Ruling" means a decision provided by the Authority or the Appellate Authority to an applicant on matters or on questions specified in sub-section (2) of section 97 or sub-section (1) of section 100, in relation to the supply of goods or services or both being undertaken or proposed to be undertaken by the applicant.

- Binding on both Assessee and Government
- Greater Tax Certainty
- Reduced Litigation
- Inexpensive
- Expeditious
- Greater Transparency

Questions on which Advance Ruling can be sought

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- Classification of any goods and/ or services
- Applicability of any notification
- Determination of time and value of supply of goods and/ or services
- Admissibility of input tax credit of tax paid or deemed to have been paid
- Determination of the liability to pay tax on any goods or services or both
- Whether applicant is required to be registered
- Whether a transaction amounts to supply of goods and/ or services

Advance ruling cannot be sought on issues relating to place of supply

Constitution of the Authority and Appellate Authority

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Authority for Advance Ruling	Appellate Authority of Advance Ruling
One member from the officers of Central Tax – To be appointed by the Central Government	Chief Commissioner of Central Tax as designated by the Board
One member from the officers of Union Territory Tax/ State Tax – To be appointed by the Central Government/State Government	Commissioner of Union Territory Tax/ State Tax having jurisdiction over the Applicant

- **Both the Authority for Advance Ruling & the Appellate Authority for Advance Ruling are constituted under the respective State/Union Territory Act and not the Central Act.**
- **This means that the ruling given by the AAR & AAAR will be applicable only within the jurisdiction of the concerned state or union territory.**
- **Therefore, questions on determination of place of supply cannot be raised with the AAR or AAAR.**
- **The respective State Governments by notifications to constitute the Authority of Advance Ruling and Appellate Authority of Advance Ruling.**

Other notable aspects about advance ruling

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- No advance ruling in case the issue is already pending or is decided (in applicant's case)
- Both Authority and Appellate Authority shall grant hearing to the applicant while deciding the application.
- Members of Authority differ in opinion – reference to be made to Appellate Authority. Members of Appellate Authority differ - no advance ruling can be obtained.
- Time period for both Authority and Appellate Authority to pronounce the ruling – ninety days from date of receipt of application/appeal.
- Appeal can be filed within 30 days from the communication of the ruling which may be further extended by 30 days on sufficient cause being shown.
- Both Authority and Appellate Authority empowered to rectify an error, in the order, apparent on the face of record, within six months from the date of the order.

Other notable aspects about advance ruling

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- Ruling pronounced by the Authority/Appellate Authority shall be binding only on the Applicant and on the concerned officer.

- Ruling is not binding is the same is obtained by fraud or suppression of facts or misrepresentation of facts.

Recently, a Writ Petition has been filed in the Gujarat High Court challenging that the composition of AAR and AAAR amounts to "*Coram non-judice*" due to the absence of judicial member. The matter is now pending for adjudication before the Hon'ble Gujarat High Court

Disadvantages in the concept of advance ruling

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- Applicant will have to obtain a ruling in each State it has its business operations.
- Presence of Appellate Authority makes the complete process lengthier and costlier.
- In case the appeal is not filed within the stipulated time – ruling will become final on the applicant.
- **Ruling binding on the 'concerned officer'** – Does it mean that any other Departmental officer can initiate investigation, against the Applicant, on the same issue, irrespective of the fact that both Authority and Appellate Authority held in favour of the Applicant?
- In case of difference in opinion the whole process becomes redundant
- Ruling can be obtained at any time – In case applicant obtains ruling post the starting of its new business – Ruling is against the applicant – what is treatment of the transactions already undertaken by the applicant?
- Issues relating to place of supply cannot be dealt-with by the Authority / Appellate Authority.

Comparison in the provisions of advance ruling – Pre & Post GST

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Particulars	Pre – GST regime	GST regime
Certainty of Tax Position	Distinct Advance Ruling mechanism for Central Tax Laws and State Tax Laws – thus, more conclusive position regarding the law	Orders of Authority & Appellate Authority applicable only within the jurisdiction of the concerned state – Objective of uniformity of tax position continues to be a dream
Expeditious Disposal	No Appellate Authority – under the erstwhile regime. However, despite provisions for time bound disposal – Authority had often been unable to decide timely, for reasons such as vacancy of members, etc.	Provisions for time bound disposal provided – however, our experience in the past do not allow us to be optimistic on this count. Provision of appeal means no immediate finality of the issue as is being envisaged.
No judicial member in Authority or Appellate Authority	The Bench included a retired High Court/ Supreme Court judge – ensuring the application of a judicial mind in deciding the matter	Authority/Appellate Authority comprise of Revenue officers – No judicial member – Possibility of a revenue bias cannot be ruled out.

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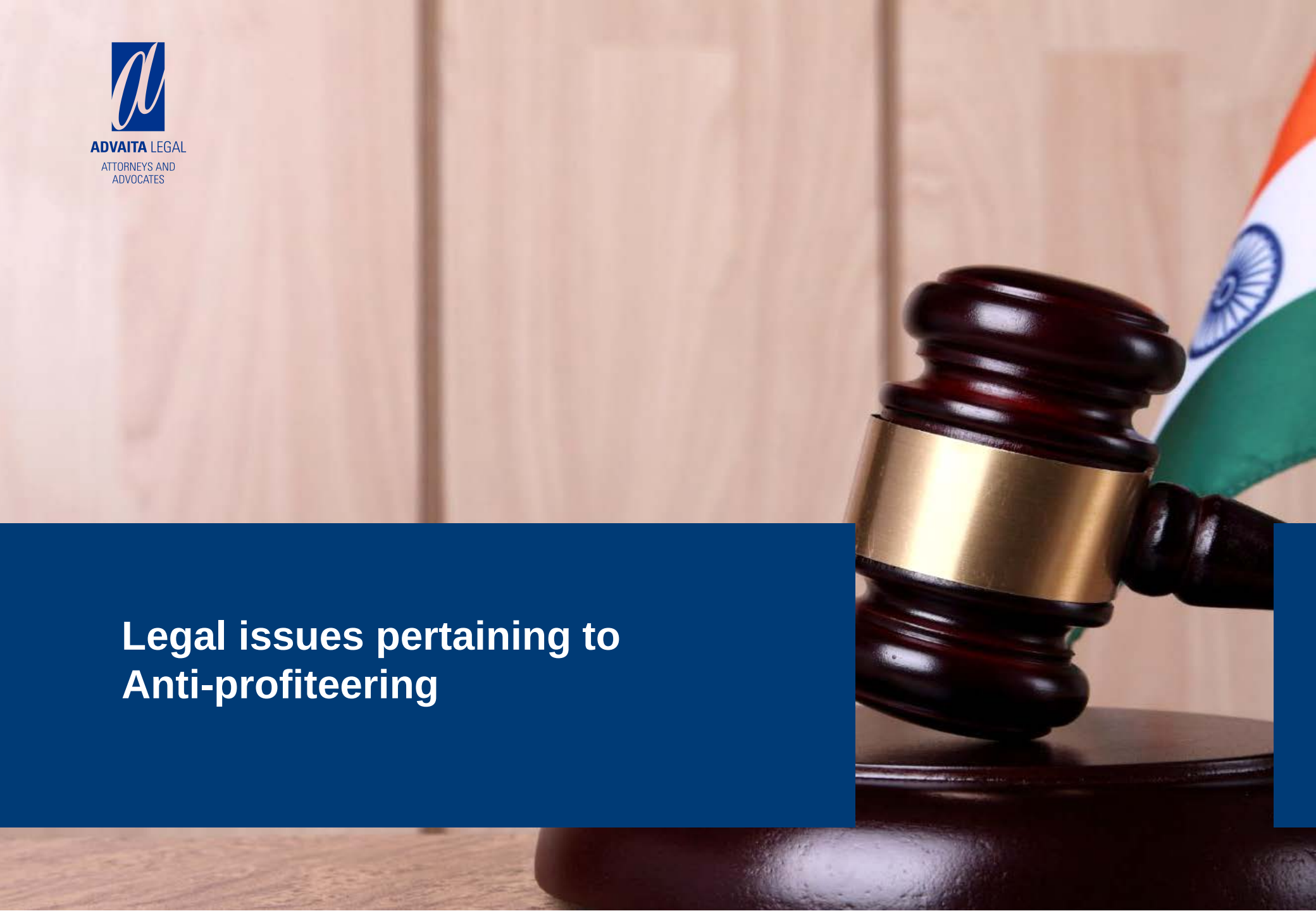
Legal issues pertaining to Anti-profiteering



Need for Anti Profiteering

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To curb inflation:- Anti-profiteering provisions were needed as introduction of GST in other countries showed that there had been inflation and prices had increased after GST implementation.

Learnings from VAT introduction in 2005

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- VAT was introduced across Indian States from 1st April 2005 onwards albeit without any mechanism for price monitoring. There was a presumption that VAT would have no adverse impact on prices due to elimination of cascading effect.

- In reality, studies found that the introduction of VAT resulted in an unexplained increase in prices. Report headlined '***Lessons for transition to Goods and Services Tax***' in June 2010 – key extracts below:

> "*Impact of VAT on prices:*
>
> *2.43 The white paper was sanguine that implementation of VAT will bring down the prices of goods due to rationalization of tax rates and abolition of cascading tax effects in the legacy systems.* ***But there was no system to monitor this impact and ensure that the benefits were indeed being passed on to the common man****.*
>
> *2.44 We selected a basket of goods and* ***checked the records of 13 manufacturers in a state in three initial months of implementation of VAT, to check its impact on prices****. We found that manufacturers did not reduce the maximum retail prices (MRP) after introduction of VAT though there was substantial reduction of tax rates. The* ***benefit of Rs. 40 Crore which should have been passed on to the consumer was consumed by the manufacturer and the dealers across the VAT chain. The dealers have undoubtedly enriched themselves at the cost of the common man****."*

Anti-profiteering measure envisaged under Section 171

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- **Section 171 of the CGST Act:**

  *"(1) Any **reduction in rate of tax on any supply of goods or services** or the **benefit of input tax credit** shall be passed on to the recipient by way of **commensurate reduction** in prices.*

  *(2) The Central Government may, on recommendations of the Council, by notification, **constitute an Authority**, or empower an existing Authority constituted under any law for the time being in force, **to examine whether input tax credits availed by any registered person or the reduction in the tax rate have actually resulted in a commensurate reduction** in the price of the goods or services or both supplied by him.*

  *(3) The Authority referred to in sub-section (2) shall **exercise such powers and discharge such functions as may be prescribed**."*

Anti-profiteering measure envisaged under Section 171

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- The first part Sec. 171(1) casts responsibility to pass on benefit of GST to recipient for following two aspects:

a) Benefit on account of reduction in effective rate of tax: While originally the GST rates were based on the '*principle of equivalence*', that no longer remains a guiding factor – rates were reduced significantly post GST too, once in November 2017 (pruning the 28% slab to just 50 items from 227 items earlier) and once on January 2018.

If the sum total of taxes being levied on a supply prior to GST regime is more than the GST levy on the said supply, then there has to be equivalent reduction in prices of the supply. E.g. if sale of a manufactured good subject to levy of a total tax of approx. 25% (12.5% as ED and 12% as VAT) in the pre-GST regime presently attracts 18% GST, there is a reduction in rate of tax of about 6.5%.

b) Benefit of increased availability of input tax credit: As regards passing of benefit due to a better credit chain under GST, it is going to affect almost all industries. In most places, be it service sector, manufacturing, trading or any specific industry, all are going to get advantage of better flow of Input Tax Credit. This is the benefit that is expected to be passed

But, how much of the benefit needs to be passed on? What does 'commensurate reduction' mean?

Anti-profiteering measure envisaged under Section 171

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- Unfortunately, no further guidance has emerged from the Government on the connotation of '*commensurate reduction*' and its applicability in various specific scenarios.
- Given the lack of guidance, one needs to resort to the rules of statutory interpretation
- **The word 'profiteering' finds no place in the text of section 171**; however, the **marginal note to the section states "*Anti-profiteering measure*"**. In ***Commissioner of Income Tax, Gujarat vs. Vadilal Lallubhai, AIR 1973 SC 1016a***, reference was made to marginal note for understanding the intention of the legislature.

  "The marginal note for Section 44-F reads 'avoidance of tax by sales cum dividend'. This marginal note also gives an indication as to what exactly was the mischief that was intended to be remedied. The legislature was evidently trying to circumvent the devices adopted by some of the assessees to convert their revenue receipts into capital receipts."

- Thus, the phrase **'*commensurate reduction*' needs to be interpreted in a manner that deals with the mischief of profiteering.** As per Black's Law Dictionary – *'Profiteering'* is *"taking advantage of unusual or exceptional circumstances to make excessive profits…"*

Possible Argument? - the mischief sought to be tackled under section 171 is not profit *per se* but 'profiteering', i.e., making unjustifiable, excessive and exorbitant profits. Hence, **'*commensurate reduction*' has to be interpreted only in a manner that tackles unreasonable exploitative profit. If it is interpreted in a manner that prohibits/restricts profit *per se*, then, it would be an unreasonable interpretation**

International Experience – Malaysia

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- During its GST tax transition period in 2015, Malaysia enacted a similar provision to control price inflation through the 'Price Control and Anti-Profiteering Regulation' (PCAPR).

- The mandate of the PCAPR was to ascertain a reasonable 'Net Profit Margin' for every product. Any profit charged over and above the determined NPM during the given time frame was considered 'Unreasonably High Profit' and was liable to penalty as per law.

- The PCAPR utilized a specific formula to arrive and ascertain the NPM. The NPM was arrived at by keeping the conditions as on January 1, 2015 and was thereafter fixed.

- It is pertinent to note that the anti-profiteering provisions were originally applicable only for 18 months beginning from January 2, 2015 till June 30, 2016 but later got extended further. Effective from January 1, 2017, a new set of anti-profiteering provisions have come into force which cover only food grains and other day-to-day use items.

- The prescribed formula for determination of net profit margin took into account factors such as impact of taxes on pricing, supplier costs, supply and demand conditions, circumstances of the geographical and product market etc. - **in other words, existence or otherwise of 'profiteering' was determined keeping in mind the overall commercial and economic scenario and not merely on the basis of tax rates or availability of tax credits**

International Experience- Australia

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- **Australia** introduced its GST in the year 2000. The Australian Competition and Consumer Commission (ACCC) was specially empowered to oversee the pricing responses during the three year transition period from July 8, 1999 to June 30, 2002.

- The Anti-Profiteering Measures in Australia aimed to stop 'price exploitation' based on the '**Net Dollar Margin Rule**'. In essence the principle states that if the GST caused taxes and costs to fall by $1, then prices should also fall by $1. At the same time, if the cost of the business rose by $1, then prices may rise by not more than $1.

- It defined a business as considered to be engaged in price exploitation in the process of GST implementation if (i) it regulates the supply; (ii) **it increases net profit margin by not reducing its prices adequately or by increasing prices by more than the quantum of rise in taxes**; and (iii) it charges **unreasonably high prices even after taking into account supplier costs, supply and demand conditions, and exceptional circumstances** like long-term non-reviewable price contracts entered into by businesses and the price regulation prevalent in an industry – **commercial realities factored**

- During the transition period of Australia's 17-year-old Goods and Services Tax regime, the Australian Competition and Consumer Commission (ACCC) considered over 51,000 complaints, investigated approximately 7,000 matters and obtained refunds of around $21 million on behalf of approximately two million consumers.

Key Anti-profiteering Rules under GST

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Rule 126 of the Anti-profiteering rules provide – Authority may determine the methodology and procedure for determination as to whether the reduction in rate of tax on the supply of goods or services or the benefit of input tax credit has been passed on by the registered person to the recipient by way of commensurate reduction in prices

Rule 127 of the Anti-profiteering rules stipulated the duties of the Authority –

- Determine within 3 months from the date of receipt of the report of the report from DG Safeguard – whether any reduction in rate of tax on any supply of goods or services or the benefit of the input tax credit has been passed to the recipient by way of commensurate reduction in prices
- Opportunity of hearing shall be granted to the interested parties
- Order -
  - reduction in prices;
  - return to the recipient, an amount equivalent to the amount not passed on by way of commensurate reduction in prices along with interest at the rate of 18% from the date of collection of higher amount till the date of return of such amount or recovery of the amount not returned in case the eligible person does not claim return of the amount or is not identifiable, and depositing the same in the Fund referred to in section 57
  - imposition of penalty under the Act
  - cancellation of registration under the Act

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Anti-profiteering under GST – Issues, Challenges & learnings

Questions unanswered

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Neither the CGST Act nor the CGST Rules provide the guidelines for determining the methodology and procedure, for ascertaining the fact of profiteering by the supplier, and the same has been left to the discretion of the authority ?

'Any other person' eligible to make complaint of profiteering ?

No time limit prescribed for forwarding application received by State-level Screening committee to Standing Committee ?

How to apportion common credit to each product or service and ensure that the benefit has been passed on to customer ?

Confusion amongst the industry

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- The anti profiteering provisions have created a lot of confusion amongst the industries resulting in numerous complaints being filed more so when “any person” can file a complaint.

  “The anti-profiteering authority set up to look into complaints of profiteering from the goods and services tax has so far received 169 complaints alleging that suppliers of goods/ services have not passed on the GST benefits to customers.

  //economictimes.indiatimes.com/articleshow/62302428.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst”

- **Renegotiation and resultant delays** – Almost every contractor is in the process of invoking the change in law clause to re-negotiate the prices of the contracts especially EPC contracts. Due to unclear provisions and mechanism for calculating the “commensurate reduction” under the GST law, the negotiation process gets stretched which is leading to delay in completion of ongoing projects.

- Acceptance of liability -

  “Hindustan Unilever Ltd. had already offered to set aside Rs 119 crore towards the consumer safeguard fund, the FMCG major said after it received a notice from the anti-profiteering body for not passing on the benefits of lower GST rates to the consumer.

  The maker of Wheel detergent said it has proactively disclosed an estimated value of Rs 119 crore to the Central Board of Excise and Customs and offered to pay this amount suo motu to the government. “This amount is not recognized as revenue and is accounted as a liability as on 31st December 17," the company said in a press release accompanying its earnings statement.”
  https://www.bloombergquint.com/gst/2018/01/17/hul-offers-to-pay-rs-119-crore-after-gst-profiteering-notice

Other issues

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- Computational Mechanism – Practically it is very difficult to establish one to one correlation between ITC on inward supplies and Tax payable on outward supplies. How the margins and prices are to be checked is a subjective matter:
  - ✓ Does one factor profit on products in absolute terms or as a percentage, on each type of product/service or company as a whole, make customer-wise bifurcations (in B-to-B scenarios)?
  - ✓ Does one recoup the increase in compliance and infrastructure cost for implementation of GST?
  - ✓ What if prices are controlled/regulated statutorily or aligned with an international benchmark?
  - ✓ What is the accepted guideline for specific sectors with inherent complexities like real estate?

- Breach of Confidentiality - The cost structure and pricing mechanism is something which is very confidential to a business, given the competition in the market. In such a scenario, ascertainment of profit being made on taxes by the consumers/ affected party becomes impossible.

Government's thought process: Real Estate – Press release

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PRESS RELEASE

The CBEC and States have received several complaints that in view of the works contract service tax rate under GST at 12% in respect of under construction flats, complex etc., the people who have booked flats and made part payment are being asked to make entire payment before 1st July 2017 or to face higher tax incidence for payment made after 1st July 2017. This is against the GST law. The issue is clarified as below:-

1. Construction of flats, complex, buildings will have a lower incidence of GST as compared to a plethora of central and state indirect taxes suffered by them under the existing regime.

2. Central Excise duty is payable on most construction material @12.5%. It is higher in case of cement. In addition, VAT is also payable on construction material @12.5% to 14.5% in most of the States. In addition, construction material also presently suffer Entry Tax levied by the States. Input Tax Credit of the above taxes is not currently allowed for payment of Service Tax. Credit of these taxes is also not available for payment of VAT on construction of flats etc. under composition scheme. Thus, there is cascading of input taxes on constructed flats, etc.

3. As a result, **incidence of Central Excise duty, VAT, Entry Tax, etc. on construction material is also currently borne by the builders, which they pass on to the customers as part of the price charged from them. This is not visible to the customer as it forms a part of the cost of the flat**.

4. The current headline rate of service tax on construction of flats, residences, offices etc. is 4.5%. Over and above this, VAT @1% under composition scheme is also charged. The buyer only looks at the headline rate of 5.5%. In other cities/states, where VAT is levied under the composition scheme @2% or above, the headline rate visible to the customer is above 6.5%. What the customer does not see is the embedded taxes on account of cascading and sticking of input taxes in the cost of the flat, etc.

5. This will change under GST. Under GST, full input credit would be available for offsetting the headline rate of 12%. As a result, the input taxes embedded in the flat will not (& should not) form a part of the cost of the flat. **The input credits should take care of the headline rate of 12%** and it is for this reason that refund of overflow of input tax credits to the builder has been disallowed.

6. The builders are expected to pass on the benefits of lower tax burden under the GST regime to the buyers of property by way of reduced prices/ installments. It is, therefore, advised to all builders / construction companies that in the flats under construction, they should not ask customers to pay higher tax rate on instalments to be received after imposition of GST.

7. Despite this clarity on law position, if any builder resorts to such practice, the same can **be deemed to be profiteering under section 171 of GST law.**

Government's thought process: Telecom Services - Press Release

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PRESS RELEASE

GST on Telecom Services

1. Telecommunication services presently attract service tax of 14% along with Swachh Bharat Cess (SBC) of 0.5% and Krishi Kalyan Cess (KKC) of 0.5%. While service tax is a pure value added tax, the above mentioned cesses are not. This is for the reason that **while no ITC (input tax credit) of SBC is available, the ITC of KKC is allowed to be set off only against KKC**. Therefore, both the cesses are turnover tax.

2. As against the above, the telecommunication services will attract GST of 18% in the GST regime, which is a pure value added tax because full ITC of inputs and input services used in the course or furtherance of business by the telecommunication service provider would be available.

3. Moreover, presently **telecom service providers are neither eligible for credit of VAT paid on goods nor of special additional duty (SAD) paid on imported goods/equipment**. However, under GST, telecom service providers would avail credit of IGST paid on domestically procured goods as also imported goods. As per some estimates, this **additional input tax credit would be as much as 2% of the turnover of the telecom industry**. Further, ITC of service tax paid on assignment of spectrum by the Government in 2016 is presently allowed to be availed of by the telcos over a period of 3 years. In the GST regime, the entire credit can be taken in the same year. Resultantly, the balance two-thirds credit of the previous year would be admissible in the current financial year itself. All of these would reduce the telcos liability to pay GST through cash to about 87% of what they paid in the last fiscal.

4. Thus, the **telcos are required to re-work their costing and credits availability and re-jig their prices** and ensure that the increased availability of credits is passed on to the customers by lowering their costs.

Result of the Confusion - Anti Profiteering Notices

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- The Directorate General of Safeguards ("DGS"), the investigating agency supporting the National Anti-profiteering Authority to apply anti-profiteering measures issued the first set of notices to:

  (i) M/s Lifestyle International Private Limited, Mahagun Metro mall, Vaishali, Ghaziabad;

  (ii) M/s Sharma Trading Company, Mahesh Colony, Jaipur;

  (iii) M/s Hardcastle Restaurants Pvt. Ltd. (McDonalds Family Restaurant), Indiabulls Finance Centre, Mumbai;

  (iv) M/s Vrandavaneshwaree Automotive Pvt. Ltd. (dealer for Honda cars in Bareilly, UP); and

  (v) M/s Pyramid Infratech Pvt. Ltd. (real estate player with office in Golf Course road, Gurgaon).

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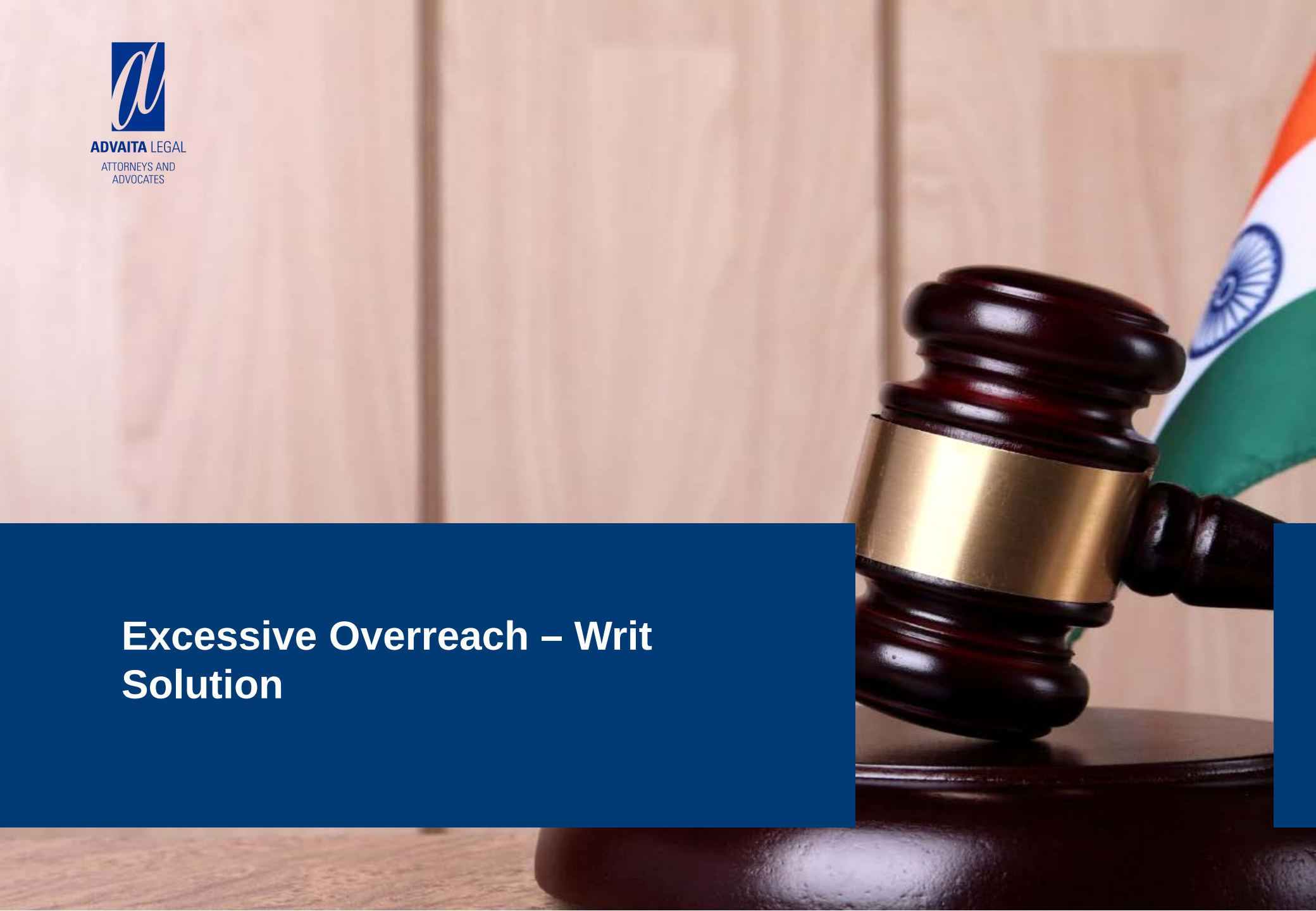
Excessive Overreach – Writ Solution



Vice of Excessive Delegation

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- The Notices issued (and proceedings that would follow) by DGS can be challenged through a writ petition before the relevant High Court on account of the anti-profiteering mechanism being unconstitutional owing to the vice of 'excessive delegation'.

- Whatever be the merits of individual anti-profiteering investigations, the provisions relating to anti-profiteering are prone to constitutional challenge as they provide unbridled and uncanalised powers to the executive.

- Understanding the 'vice of excessive delegation' –

  - ✓ 'Separation of power' is a fundamental feature of the Indian Constitution; what this means is that of the three wings - Judiciary, Legislature and Executive/bureaucracy, the law has to be made by the Legislature and implemented by the bureaucracy. Thus, the legislative policy has to be enshrined in the law, which is the statute itself that is made by the legislature (the Parliament) and not in the Rules (or in any other manner) which are made by the bureaucracy.

  - ✓ Essential legislative functions which comprise of the determination of the legislative policy and its formulation as a binding rule of conduct cannot be delegated by the legislature to the bureaucracy. What can be delegated to the bureaucracy is only the task of regulating the procedural aspects of implementation of the legislative policy necessary for implementing the purpose and objects of a legislation; anything more, and the bureaucracy would have impinged in the field of the legislature – which is violative of our Constitution and is commonly referred to as the 'vice of excessive delegation'.

Vice of Excessive Delegation - Conti...

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- In case of anti-profiteering, the legislature has given a very vague idea and guidance in the form of Section 171 of the CGST Act. None of the powers of the NAA viz. return of amount, levy of interest, imposition of penalty, cancellation of registration, etc., flow directly from the CGST Act – all these powers flow solely from the CGST Rules.

- *De hors* the merits in individual anti-profiteering investigations initiated against various companies, anti-profiteering provisions appear to be a textbook case of delegation of essential legislative functions to the bureaucracy and thus suffer from the vice of "excessive delegation" on that account.

- **The power to cancel GST registration as under the CGST Rules, without any guidance/power for the same in the CGST Act, is wholly discretionary and may also fall foul of the freedom of trade and profession as envisaged under Article 19 (g) of the Constitution**.

- **Given that anti-profiteering provisions under the CGST Act and Rules clearly suffer from the 'vice of excessive delegation' and are vulnerable to be struck down as unconstitutional**, assessees may explore contesting anti-profiteering investigations at the very inception by challenging the unbridled and uncanalised powers given to the NAA vide appropriate writ petitions before the jurisdictional High Court.

Overreach and excess delegation

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Provision under CGST Act	CGST Rules, 2017	Observation
171(1) – Reduce the price commensurate with reduction in rate of tax or the benefit of ITC	**127(iii)(a) –** Authority to order reduction in prices	Both the provision and the corresponding rule are in consonance
171(3) – The authority shall exercise such powers and functions as may be prescribed	**127(iii)(b) –** Return the amount along with interest @ 18%	Levy of interest being an essential legal function **cannot be delegated**
	127(iii)(b) – Recover the amount and deposit it in Consumer Welfare Fund	Recovery of the amount – not specified under the CGST Act – **excessive delegation**
	127(iii)(c) – Impose penalty as specified in the Act	Provision in the CGST Act does not provide for imposition of penalty – **excessive delegation**
	127(iii)(d) – Cancellation of registration under the Act	**Section 171 of the CGST Act does not contemplate** the cancellation of registration
No guidelines provided for determining the methodology and procedure for ascertaining whether the reduction in rate of tax or the benefit of ITC has been passed to the recipient	**126 –** Provides that the authority may determine the methodology and the procedure for ascertaining whether the benefit has been passed to the recipient	Rule has travelled beyond the scope provided under the statute – **excessive delegation**

Essential legislative function cannot be created by delegated legislation

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