



IN THE HIGH COURT OF KARNATAKA AT BENGALURU

DATED THIS THE 20TH DAY OF AUGUST, 2024

BEFORE

THE HON'BLE MR JUSTICE S.R.KRISHNA KUMAR

WRIT PETITION NO.7227 OF 2023 (T-RES)

BETWEEN:

M/S A O SMITH INDIA WATER PRODUCTS PVT. LTD,
PLOT NO.300, KIADB INDUSTRIAL AREA PHASE II,
HAROHALLI, KANAKAPURA TALUK,
RAMANAGARA DISTRICT,
KARNATAKA – 562 112.
(REPRESENTED BY
RAJESH ARORA-HEAD-FINANCE
INCORPORATION UNDER THE COMPANIES ACT,1956)
(NO.1 OF 1956)

...PETITIONER

(BY SRI. RAVI RAGHAVAN, ADVOCATE AND
MS. SNEHA PHILIP, ADVOCATE)

AND:

1. STATE OF KARNATAKA,
THROUGH ITS PRINCIPAL SECRETARY,
FINANCE DEPARTMENT,
VIDHANA SOUDHA,
BANGALORE – 560 001.
2. THE COMMISSIONER OF COMMERCIAL TAXES
VANIJYA THERIGE KARYALAYA,
GANDHINAGAR, BANGALORE – 560 009.
3. DEPUTY COMMISSIONER OF COMMERCIAL TAXES
(AUDIT-2.2), DGSTO-2, NO.642, PIONEER PLAZA,
2ND FLOOR, KENCHANAHALLI MAIN ROAD,
RAJARAJESHWARI NAGAR,
BANGALORE – 560 098.

...RESPONDENTS

(BY SRI.K HEMAKUMAR, AGA)





THIS WRIT PETITION IS FILED UNDER ARTICLES 226 AND 227 OF THE CONSTITUTION OF INDIA, PRAYING TO QUASH THE IMPUGNED SHOW CAUSE NOTICE NO.DCCT/AUDIT/GST/73/2022-23 T.NO.490 DATED 04.02.2023 ISSUED BY R3 AT ANNEXURE-A PROPOSING TO DEMAND AND RECOVER TOTAL IGST AMOUNTING TO RS.4,12,17,787/- ALONG WITH INTEREST AND PENALTY FOR THE PERIOD JULY 2017 TO MARCH 2018 AND ETC.,

THIS WRIT PETITION, COMING ON FOR *PRELIMINARY HEARING IN 'B' GROUP*, THIS DAY, ORDER WAS MADE THEREIN AS UNDER:

CORAM: HON'BLE MR JUSTICE S.R.KRISHNA KUMAR

ORAL ORDER

In this petition, petitioner seeks the following reliefs:

“a) Issue a writ in the nature of Certiorari or any other appropriate writ or order or direction quashing the impugned Show Cause Notice No.DCCT/AUDIT/GST/73/2022-23 T.No.490 dated 04.02.2023 issued by Respondent No.3 at Annexure-A proposing to demand and recover total IGST amounting to Rs.4,12,17,787/- along with interest and penalty for the period July 2017 to March 2018;

b) Hold that the levy of GST on the activity of holding equity capital by the Holding Companies in the Petitioner company and on the ECB received by the Petitioner from AOSH is illegal and without jurisdiction;

c) Pass such further order(s) and other reliefs as the nature and circumstances of the case may require.”



2. Heard learned counsel for the petitioner and learned counsel for the respondents and perused the material on record.

3. In addition to reiterating the various contentions urged in the petition and referring to the material on record, learned counsel for the petitioner invited my attention to the Audit report dated 24.11.2022 issued by the respondent under Section 65(6) of the CGST Act, pursuant to which, intimation under Section 73(5) of the CGST and KGST Acts, 2017, was issued by respondent No.3 to which the petitioner submitted a detailed response on 16.01.2023 pointing out that the demands were not sustainable in law and placing reliance upon several documents including the notifications bearing No.9/2017 dated 28.06.2017 in which at Sl.No.28, respondents have themselves stated that extending deposits, loans or advances insofar as the consideration is represented by way of interest or discount (other than interest involved in credit card services) and *interse* sale or purchase of foreign currency amongst banks or authorised dealers of foreign exchange or amongst banks and such dealers were exempt from payment of GST where consideration were in the form of interest payable. It is submitted that despite the aforesaid detailed objections submitted by the petitioner, the respondents have



proceeded to issue the impugned Show Cause Notice, which is illegal, arbitrary and without jurisdiction or authority of law and the same deserves to be quashed.

4. It is further submitted that during pendency of the present petition, the Central Board of Indirect Taxes and Customs has issued a Circular dated 26.06.2024 bearing No.218/12/2014 – GST, in which they have stated at Sl.No.1 that they have clarified regarding the said exemptions available to the petitioner in the earlier Notification No.12/2017 – Central Tax (Rate) and consequently, the impugned Show Cause Notice insofar as it relates to proposal to levy tax in respect of the Table No.IX deserves to be quashed. It is also submitted that insofar as the proposal in Show Cause Notice proposing to levy taxes in relation to Table No.VII of the Show Cause Notice is concerned, the petitioner is not liable to pay the said amount in the light of the judgments of this Court in ***M/s. Yonex India Private Limited Vs. Union of India and others – W.P.No.2301/2023 dated 18.01.2024*** and ***M/s. Metro Cash and Carry Pvt. Ltd., Vs. State of Karnataka and others – W.P.No.25142/2022 dated 14.03.2024***



5. Per contra, learned AGA for the respondents submits that there is no merit in the petition and the same is liable to be dismissed.

6. As rightly contended by learned counsel for the petitioner insofar as the proposal to demand / levy GST in relation to Table No.VII of the Show Cause Notice is concerned, the said issue is directly and squarely covered by the judgment of this Court in *Yonex's* case supra, which was followed in the subsequent judgment of this Court in *Metro's* case supra, in which it was held as under:

In this petition, petitioner seeks for the following reliefs:

a) *Issue a writ in the nature of Certiorari or any other appropriate writ or order or direction quashing the impugned Show Cause Notices Nos.ACCT/LGSTO-140/T-336/2022-23 Assignment No.07/2022-23 dated 15.11.2022, ACCT/LGSTO-140/T-336/2022-23 Assignment No.08/2022-23 dated 15.11.2022, ACCT/LGSTO-140/T-336/2022-23 Assignment No.09/2022-23 dated 15.11.2022 and ACCT/LGSTO-140/T-336/2022-23 Assignment No.10/2022-23 dated 15.11.2022 issued by Respondent No.3 enclosed at **Annexure-A, Annexure-A1, Annexure-A2 and Annexure-A3** respectively, proposing to demand and recover total IGST amounting to Rs.48,44,27,296/- [Rs.12,11,06,824/- per tax period] along with interest and penalty for the periods 2017-2018, 2018-2019, 2019-2020 and 2020-2021.*

b) *hold that the levy of GST on the activity of holding equity capital by the parent Company in the Petitioner is illegal and without jurisdiction and is ultra-vires Section 5 of the IGST Act, 2017 read with Section 7 of the CGST Act, 2017;*



c) *pass such further order(s) and other reliefs as the nature and circumstances of the case may require.*"

2. *Heard learned counsel for the petitioner and learned counsel for the respondents and perused the material on record.*

3. *In addition to reiterating the various contentions urged in the memorandum of petition and referring to the material on record, learned counsel for the petitioner invited my attention to the judgment of this Court in the case of **M/s. Yonex India Private Limited Vs. Union of India and others – W.P.No.2301/2023 dated 18.01.2024** in order to point out that issue involved in the present petition is directly and squarely covered by the aforesaid judgment and consequently, the present petition deserves to be allowed and disposed of in terms of the said judgment.*

4. *Per contra, learned AGA does not dispute that the aforesaid judgment in M/s. Yonex India Private Limited case it is held that mere holding of shares by the holding company in the subsidiary company cannot be classified, treated or construed as 'supply of service'.*

5. *A perusal of the material on record will indicate that in M/s. Yonex India Private Limited case supra, this Court has held as under:*

"3. In addition to reiterating the various contentions urged in the petition and referring to the material on record, the learned Senior counsel for the petitioner invited my attention to the Circulars dated 17.07.2023 and 21.07.2023 issued by the Central Government and the State Government



clarifying that the activity of holding of shares of subsidiary company by holding company per se cannot be treated as a supply of services by a holding company to the said subsidiary company and cannot be taxed under the GST.

4. In this context, it is pointed out that the petitioner is a subsidiary company of M/s. Yonex, Japan [a holding company] and mere holding of shares in a subsidiary company by the holding company cannot be construed or treated as "supply of service" in the light of the Circulars issued by the Central Government and the State Government. It is therefore submitted that in the light of the Circulars referred to supra, the impugned order dated 02.11.2022 is without jurisdiction or authority of law, and the same deserves to be quashed. Under these circumstances, the learned Senior counsel submits that the petitioner would not press Prayer Nos. A and B sought for in the petition.

5. Per contra, the counsels for the respondents, submit that there is no merit in the petition and the same is liable to be dismissed. However, they do not dispute issuance of the Circulars by the Central Government and the State Government.

6. As rightly contended by the learned Senior counsel for the petitioner, the Central Government has issued Circular dated 17.07.2023, which reads as under:

"Representations have been received from the trade and field formations seeking clarification on certain issues whether the holding of shares in a subsidiary company by the holding company will be treated as 'supply of service' under GST and will be taxed accordingly or whether such transaction is not a supply.

2. In order to clarify the issue and to ensure uniformity in the implementation of the provisions of law across the field formations, the Board, in exercise of its powers conferred by section 168 (1) of the Central Goods and Services Tax Act, 2017 (hereinafter referred to as "CGST Act"), hereby clarifies the issues as under:

Issue	Clarification
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Taxability of share capital held in subsidiary company by the parent company



<p>1. <i>Whether the activity of holding shares by a holding company of the subsidiary company will be treated as a supply of service or not and whether the same will attract GST or not</i></p>	<p><i>Securities are considered neither goods nor services in terms of definition of goods under clause (52) of section 2 of CGST Act and the definition of services under clause (102) of the said section. Further, securities include 'shares' as per definition of securities under clause (h) of section 2 of Securities Contracts (Regulation) Act, 1956.</i></p> <p><i>This implies that the securities held by the holding company in the subsidiary company are neither goods nor services. Further, purchase or sale of shares or securities, in itself is neither a supply of goods nor a supply of services. For a transaction/activity to be treated as supply of services, there must be a supply as defined under section 7 of CGST Act. It cannot be said that a service is being provided by the holding company to the subsidiary company, solely on the basis that there is a SAC entry '997171' in the scheme of classification of services mentioning; "the services provided by holding companies, i.e, holding securities of (or other equity interests in) companies and enterprises for the purpose of owning a controlling interest.", unless there is a supply of services by the holding company to the subsidiary company in accordance with section 7 of CGST Act.</i></p> <p><i>Therefore, the activity of holding of shares of subsidiary company by the holding company per se cannot be treated as a supply of services by a holding company to the said subsidiary company and cannot be taxed under GST.</i></p>
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3. It is requested that suitable trade notices may be issued to publicize the contents of this Circular.



4. Difficulty, if any, in implementation of this Circular may please be brought to the notice of the Board, Hindi version would follow.

Similarly, the State Government also issued Circular dated 21.07.2023 on the same lines, which reads as under:

Representations have been received from the trade and field formations seeking clarification on certain issues whether the holding of shares in a subsidiary company by the holding company will be treated as 'supply of service' under GST and will be taxed accordingly or whether such transaction is not a supply.

2. In order to clarify the issue and to ensure uniformity in the implementation of the provisions of law across the field formations, the Board, in exercise of its powers conferred by section 168 (1) of the Karnataka Goods and Services Tax Act, 2017 (hereinafter referred to as "KGST Act"), hereby clarifies the issues as under.

Sl. No.	Issue	Clarification
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Taxability of share capital held in subsidiary company by the parent company

1	Whether the activity of holding shares by a holding company of the subsidiary company will be treated as a supply of service or not and whether the same will attract GST or not	<p>Securities are considered neither goods nor services in terms of definition of goods under clause (52) of section 2 of KGST Act and the definition of services under clause (102) of the said section. Further, securities include "shares" as per definition of securities under clause (h) of section 2 of Securities Contracts (Regulation) Act, 1956.</p> <p>This implies that the securities held by the holding company in the subsidiary company are neither goods nor services. Further, purchase or sale of shares or securities, in itself is neither a supply of goods nor a supply of services. For a transaction/activity to be treated as supply of services, there must be a supply as defined under section 7 of KGST Act. It cannot be said that a service is being provided by the holding company to the subsidiary company, solely on the basis that there is a SAC entry '997171' in the scheme of classification of services mentioning: "the services provided by holding companies, ie, holding securities of (or other equity interests in) companies and</p>
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	<p><i>enterprises for the purpose of owning a controlling interest.", unless there is a supply of services by the holding company to the subsidiary company in accordance with section 7 of KGST Act. Therefore, the activity of holding of shares of subsidiary company by the holding company per se cannot be treated as a supply of services by a holding company to the said subsidiary company and cannot be taxed under GST.</i></p>
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3. Difficulties, if any, in implementation of this circular may be brought to the notice of this office.

As it is clear from the aforesaid Circulars issued by the Central Government and the State Government, mere holding of shares by the holding company in the subsidiary company cannot be classified, treated or construed as "supply of service" as clearly clarified and confirmed by the aforesaid Circulars by both the Central Government and the State Government.

7. Under these circumstances, I am of the view that in the light of the issuance of Circulars by the Central Government and the State Government during the pendency of the present petition, clarifying that holding of shares by M/s. Yonex Co., Japan [the holding company] in its subsidiary, the petitioner herein at Bengaluru cannot be treated or classified as "supply of service". The impugned order dated 02.11.2022 passed by the respondent No.4 which proceeds on the basis that the said holding of shares amounts to "supply of service" is clearly illegal, arbitrary and without jurisdiction or authority of law, and the same deserves to be quashed.

8. In the result, the following:

ORDER

i. The petition is hereby allowed.



ii. *The impugned order dated 02.11.2022 issued by the respondent No.4 is hereby quashed.*

The submission made on behalf of the petitioner that Prayer Nos.a and b are not pressed, is placed on record."

6. *In the instant case, the parent company is M/s. Metro Cash and Carry International GmbH of which the petitioner herein i.e., M/s. Metro Cash and Carry Pvt. Ltd., is a subsidiary and merely because the parent company – M/s. Metro Cash and Carry International GmbH holds shares in its subsidiary i.e., the petitioner herein, the said circumstance cannot be classified, treated or construed as 'supply of service' for the purpose of GST. Under these circumstances, since the issue in controversy involved in the present petition is directly and squarely covered by the judgment of this Court in M/s. Yonex India Private Limited case supra, I am of the view that the impugned Show Cause Notices issued are without jurisdiction or authority of law and the same deserves to be quashed.*

7. *In the result, I pass the following:*

ORDER

(i) *Petition is hereby **allowed** and disposed of in terms of M/s. Yonex India Private Limited case supra.*

(ii) *The impugned Show Cause Notices at Annexures – A, A1, A2 and A3 are hereby quashed."*

7. The factual situation obtaining in the aforesaid two judgments are directly and squarely covered to the facts of the instant case and consequently, the proposal to demand / levy GST at Table No.VII in the impugned Show Cause Notice, is illegal,



arbitrary and without jurisdiction or authority of law and the same deserves to be quashed.

8. Insofar as the proposal to demand / levy GST as indicated in Table No.IX is concerned, the said issue also was the subject matter of the Notification dated 28.06.2017, in which the respondents have stated that the petitioner was exempted from payment of GST as under:

28	Heading 9971	Services by way of - (a) extending deposits, loans or advances in so far as the consideration is represented by way of interest or discounts (other than interest involved in credit card services); (b) inter se sale or purchase of foreign currency amongst banks or authorised dealers of foreign exchange or amongst banks and such dealers.	Nil	Nil
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9. The said exemption granted in favour of the petitioner has been reiterated and clarified in the subsequent Circular dated 26.06.2024, which states as under:

“Subject: Clarification regarding taxability of the transaction of providing loan by an overseas affiliate to its Indian affiliate or by a person to a related person-reg.

Representations have been received from trade industry seeking clarity on whether there is any supply involved in the transaction of granting of loan by a person to



a related person or by an overseas affiliate to its Indian entity, where the consideration bearing paid is only by way of interest or discount, and whether any GST is applicable on the same.

2. In order to clarify the issue and to ensure uniformity in the implementation of the provisions of law across the field formations, the Board, in exercise of its powers conferred by section 168(1) of the Central Goods and Services Tax Act, 2017 (hereinafter referred to as “CGST Act”), hereby clarifies the issues as under:

Sl No.	Issue	Clarification
Clarification regarding taxability of the transaction of providing loan by an overseas entity to its Indian related entity or by a person in India to a related person.		
1.	Whether the activity of providing loans by an overseas affiliate to its Indian affiliate or by a person to a related person, where there is no consideration in the nature of processing fee/ administrative charges loan granting charges etc., and the consideration is represented only by way of interest or discount, will be treated as a taxable supply of service under GST or not.	<p>1. As per clause (c) of sub-section (1) of <u>section 7</u> of the CGST Act, read with S.No.2 and S.No.4 <u>Schedule I</u> of CGST Act, supply of goods or services or both between related persons, when made in the course or furtherance of business, shall be treated as supply, even if made without consideration. Therefore, it is evident that the service of granting loan / credit / advances by an entity to its related entity is a supply under GST.</p> <p>2. Services by way of extending deposits, loans or advances in so far as the consideration is represented by way of interest or discount (other than interest involved in credit card services) are exempted under sub entry (a) of entry 27 of <u>Notification No.12/2017-Central Tax (Rate)</u>. Therefore, it is clear that the supply of services granting loans / credit / advances, in so far as the consideration is represented by way of interest or discount, is fully exempt under GST.</p> <p>3. It is mentioned that overseas affiliates or domestic related persons are generally charging no consideration in the form of processing fee / service fee, other than the consideration by way of interest or discount on the loan amount. Doubts are being raised regarding the taxability of the services of processing / administering / facilitating the loan in such cases, by deeming the same as supply as per clause (c) of sub-section (1) of section 7 of the CGST Act, read with S.No.2 and S.No.4 of <u>Schedule I</u> of CGST Act. The processing fee/ service fee is generally a</p>



		<p><i>one-time charge that lenders levy on applicants when they apply for a loan. This fee is generally non-refundable and is used to cover the administrative cost of processing the loan application. Charges of any other nature in respect of loan, other than by way of interest or discount, would represent taxable consideration for providing the facilitation / processing / administration services for the loan and hence would be liable to GST. This has been clarified at serial number 42 in the Sectoral FAQ on Banking, Insurance and Stock Brokers Sector issued by CBIC.</i></p> <p><i>4. It is significant to note that the processing / service fee is generally charged by the bank / financial institution from the recipient of the loan in order to cover the administrative cost of processing the loan application. An independent lender may carry out a thorough credit assessment of the potential borrower to identify and evaluate the risks involved and to consider methods of monitoring and managing these risks. Such credit assessment may include understanding the business of the applicant, as well as the purpose of the loan, financial standing and credibility of the applicant, how it is to be structured and the source of its repayment which may include analysis of the borrower's cash flow forecasts, the strength of the borrower's balance sheet, and where any collateral is offered, due diligence on the collateral offered may also be required to be carried out. To cover such costs, the independent lender generally collects a fee that is in the nature of processing fee / administrative charges/ service fee / loan granting charges, which is leviable to GST.</i></p> <p><i>5. However, when an entity is extending a loan to a related entity, it may not require to follow such processes as are followed by an independent lender. For example, it may not need to go through the same process of information gathering about the borrower's business, his financial standing and credibility and other details, as the required information may already be readily available within the group, or between related persons. The lender may not also take any collateral from the borrower. Accordingly, in case of loans provided between related parties, there may not be the activity of 'processing' the loan, and no administrative cost may be involved in granting such a loan. Therefore, it may not be desirable to place the services being provided for processing the loans by banks or independent lenders vis-a-vis the loans provided by a related party, on equal footing.</i></p> <p><i>6. Even in case of loans provided between unrelated parties, there may not be any processing fee /</i></p>
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		<p><i>administrative charges / loan granting charges etc., based on the relationship between the bank/ independent lender and the person taking the loan. The lender might waive off the administrative charges in full, based on the nature and amount of loan granted, as well as based on the relationship between the lender and the concerned person taking the loan.</i></p> <p><i>7. Accordingly, in the cases, where no consideration is charged by the person from the related person, or by an overseas affiliate from its Indian party, for extending loan or credit, other than by way of interest or discount, it cannot be said that any supply of service is being provided between the said related persons in the form of processing / facilitating / administering the loan, by deeming the same as supply of services as per clause (c) of sub-section (1) of section 7 of the CGST Act, read with S.No.2 and S.No.4 of Schedule I of CGST Act. Accordingly, there is no question of levy of GST on the same by resorting to open market value for valuation of the same as per <u>rule 28</u> of Central Goods and Services Tax Rules, 2017.</i></p> <p><i>8. However, in cases of loans provided between related parties, wherever any fee in the nature of processing fee, administrative charges/ service fee/ loan granting charges etc. is charged, over and above the amount charged by way interest or discount, the same may be considered to be the consideration for the supply of services of processing/facilitating/administering of the loan, which will be liable to GST as supply of services by the lender to the related person availing the loan.</i></p>
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3. *It is requested that suitable trade notices may be issued to publicize the contents of this Circular.*

4. *Difficulties, if any, in implementing this Circular may please be brought to the notice of the Board. Hindi Version would follow.”*

10. Though the petitioner submitted a response on 16.01.2023 specifically referring to the aforesaid Notification dated 28.06.2017, respondents have not considered nor referred to the



same in the impugned Show cause Notice. Consequently, the same deserves to be quashed and matter remitted back to respondent No.3 for reconsideration after providing an opportunity to the petitioner to the limited extent of Table No.IX referred to in the impugned Show Cause Notice.

11. In the result, I pass the following:

ORDER

(i) The petition is hereby ***allowed***.

(ii) The impugned Show Cause Notice at Annexure – A dated 04.02.2023 insofar as it relates to proposal to levy / demand GST at Table No.VII under the heading '*Continuous Equity Share holding*' is hereby quashed.

(iii) Insofar as the impugned Show Cause Notice relating to proposal to levy / demand GST at Table No.IX under the heading '*Value of the Credit Grant in Service determined as a service fee @1%*' is concerned, petitioner is reserved liberty to submit its response / reply to the same within a period of four weeks from today.



(iv) Liberty is reserved in favour of the petitioner to produce documents, etc., in support of their response / reply, which shall be considered by the respondents bearing in mind the aforesaid Notification dated 28.06.2017 and Circular dated 26.06.2024, in accordance with law.

Sd/-
(S.R.KRISHNA KUMAR)
JUDGE

SV
List No.: 1 Sl No.: 51