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Has the Supreme Court clipped the wings of GST Council?

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Certain observations made by the Hon'ble Supreme Court, in the context of demand of GST on Ocean Freight from the importers in CIF (Cost, Insurance and Freight) transactions has triggered a major debate.

Let us first try to understand the issue before the Supreme Court.

Imports are normally made under two modes, viz., FOB (Free on Board) and CIF (Cost, Insurance and Freight). Under FOB model, the responsibility of the foreign supplier would end with loading the consignment on board the ship and the transportation has to be arranged by the importer himself. Under CIF model, the foreign supplier is responsible to deliver the goods at the port of import and hence transportation would be arranged by the foreign supplier and the price of the goods would include the freight incurred by the foreign supplier also. The Indian importer would only pay such CIF price to the foreign supplier.

Under FOB model, if the Indian importer engages an Indian Shipping line, the Shipping line is providing transportation services and would charge GST. If the Indian importer is engaging a foreign shipping line, then the GST is payable by the importer under reverse charge mechanism. The above requirement under GST law is never in dispute. Same was the position under Service Tax era also.

If CIF model is adopted by the importer, then the transportation services would be provided by a foreign shipping line to the foreign supplier (who would recover the freight cost also from the Indian importer, by incorporating the freight element also as part of the price of the goods being sold). Since both the service provider and recipient of the service are outside India, such CIF transactions were exempted from payment of Service tax and would not attract any Service Tax on the ocean freight component.

The Indian Shipping industry complained that the above anomaly is detrimental to them and hence sought levy of Service Tax on CIF transactions also. (It is another story that upto May 2016 even Indian Shipping lines are not liable to pay any Service Tax on their import transportation and they only wanted Service Tax to be levied on them as they are losing the benefit of input tax credit).

So, in order to fulfil the demand of the Indian Shipping industry, the Central Government started levying Service Tax on ocean freight on the importers in case of CIF imports from early 2017 and the practice continued even after introduction of GST from 01.07.2017.

This levy was challenged by the importers on various grounds, such as

- When both the Supplier of the service (shipping line) and the recipient of the service (foreign supplier) are outside India, this levy is extra-territorial in nature.
- The Indian importer is not the recipient of service of transportation as transportation is arranged for and paid only by the foreign supplier and hence the importer cannot be made liable to pay GST as recipient of the service.
- As per the GST Acts only service recipient can be made liable to pay tax under reverse charge mechanism and hence the notifications casting the levy in the hands of the importers, who are not recipients of the service of transportation, are ultra vires the Acts.
- When the goods are imported, Customs duties and IGST are paid on the CIF price, which includes the freight component also and hence levying GST once again on the freight component in the hands of the importer amounts to double taxation.

Earlier, the Hon'ble Gujarat High Court has held the issue in favour of the importers and quashed the levy.

Even in the Agenda prepared for one of the GST Council meetings, it was recorded that the decision of the Gujarat High Court is based on sound principles and it would be difficult to succeed before the Supreme Court and hence some alternative methods have to be implemented to bring in level playing field for the Indian Shipping lines. But, no discussion took place on this agenda and the Union Government has filed appeal against the Gujarat High Court order before the Supreme Court.

One of the arguments made by the Union Government before the Supreme Court was that once GST Council has decided to levy GST on CIF imports in the hands of the importers, absence of any enabling provision in the Statute, would not make the notifications ultra vires. It was in this context, the Supreme Court has pointed out that the GST Council is only a recommendatory body as per Article 279 A of the Constitution and unless such recommendations are acted upon by the Parliament and State Legislature, there cannot be a valid legislation. In other words, notwithstanding the constitutional status enjoyed by the GST Council, the supremacy of the legislative bodies of our federal set up are intact. Thus, what was so obvious has only been reiterated and reinforced by the Supreme Court.

During the last five years, the GST Council had very fruitful discussions on so many issues and all decisions taken by the council are unanimous (except on one occasion where a voting was resorted to), which shows the maturity of the constituents of the GST Council and their belief in co-operative federalism. If the same spirit is followed by all concerned, one need not fear that the concept of "One Nation One Tax" would derail because of the Supreme Court verdict. We cannot allege that the Supreme Court has emboldened the divisive mindsets, to deviate from the co-operative spirit, as it has only reiterated what is already envisioned in the Constitution. Further, article 279 (11) provides for creation of a mechanism for adjudicating inter-se disputes among the constituents of GST council in the matter of its recommendations.

Whatever be the pitfalls and technical glitches and procedural wrangles of GST, the great achievement of GST is that it has brought about uniformity in taxation in our Country to a great extent and it is hoped that all constituents of GST Council would continue to uphold the spirit.

Coming back to the main issue, the Supreme Court has held that since the import of goods is taxed, including the value of freight, which constitute a "composite supply", the freight element cannot be taxed once again in the hands of the importer.

To be noted that this judgement is relevant only for CIF imports and not for FOB imports where the liability to GST still continues.

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