

Inter-State supplies under Model IGST Law – Treatment of FOR & Ex-works supplies

One of the many disputes that have continued to exist in the present regime of taxation of sale of goods are the disputes pertaining to determination of the nature of transaction as inter-State sale subject to Central Sales Tax or local sale subject to VAT. Such disputes especially arise when assessee in a State sells goods to a buyer located in a different State. Sales of this nature are often made with variety of permutations of terms and conditions pertaining to transfer of title, transfer of risk, transfer of possession and obligation to transport the goods, etc.

These disputes could not be settled by the enactment of the CST Act despite one of its objectives itself being '*to formulate the principles for determining when a sale or purchase of goods takes place in the course of inter-state trade or commerce*'. Nor could these disputes be put to rest by the courts of law for the simple reason that, principle laid down by the CST Act for determining the nature of transaction is rather subjective and the determination can only be done after a careful factual analysis of the transaction itself. This means, no rule of thumb could apply to two transactions in the same manner.

Now, with the advent of Goods and Service Taxes ("GST") which aims to simplify indirect taxation in India it would be interesting to investigate whether the legislature has been mindful of this conundrum or not and if so, how has it sought to address it.

Inter-State supplies under Model IGST Law

Section 3 of the Model Integrated Goods and Services Tax Act ("Model IGST Act") states that supply of goods in the course of inter-State trade and commerce means any supply where the location of the supplier and the place of supply are in different States. Thus, in a marked departure from the principle laid down under Section 3 of the CST Act, which places emphasis on inter-State movement of goods occasioned by sale for deeming a sale to be in the course of inter-State trade and commerce, under the Model IGST Act determination of inter-State sale / supply hinges on dual factors i.e. location of the supplier and the place of supply.

Section 7 of the Model IGST Act details out various principles for determining the place of supply of goods which are applicable in different contexts. Two principles which are most relevant for the present analysis are contained in Section 7(2) and Section 7(4) of the Model IGST Act. As per Section 7(2) *if the supply involves movement of goods, whether by the supplier or the recipient or by any other person, the place of supply of goods shall be the location of the goods at the time at which the movement terminates for delivery to the recipient*. Section 7(4) provides that where the supply does not involve movement of goods, whether by the supplier or the recipient, the place of supply shall be the location of such goods at the time of delivery to the recipient.

Supply involving movement of goods

The first question that is required to be answered for determining the place of supply i.e. whether the supply involves movement of goods or not, can only be answered on a case to case basis. As regards time of delivery, in the absence of any definition of the terms 'delivery' or 'time of delivery' under the Model GST legislations, the definition provided in the Sale of Goods Act, 1930 ('Act') becomes relevant. Section 2(2) of the Act defines delivery as *voluntary transfer of possession from one person to another*. *Pollock and Wright on Possession* points out that 'in all cases the essence of delivery is that the deliveror, by some apt and manifest act, puts the deliverree in the same position of control over the thing, either directly or through a custodian, which he held himself immediately before the act.'

An obvious example of a transaction where the supply involves movement of goods is a transaction which is known as FOR destination sale. That is a transaction where as per the terms of the supply contract, the supplier is bound to move the goods up-to the place of the recipient which is where the supply gets

completed upon delivery of goods by the supplier to the recipient. As the goods would be located at the recipient's premises at the time of termination of movement of goods for delivery to the recipient, the place of supply would be the place of the recipient.

Supply not involving movement of goods

Similarly, an obvious example of a transaction where the supply does not involve movement of goods is where the manufacturer/supplier of goods develops moulds and jigs required for the manufacture of goods, sells the moulds and jigs to the recipient before using them for manufacture of goods, but does not move the same and uses the moulds for manufacture of goods for sale to the recipient. By application of Section 7(4) of the model IGST Act the place of supply of such moulds and jigs will be the factory of the supplier.

Ex-factory or ex-works sale – Can it be treated as intra-State supply?

Now the provisions are to be analyzed to test a transaction which is popularly known as an ex-factory or ex-works sale of goods. Typically, in such transactions the supplier is responsible for making goods available at its factory site, the title, risk and possession of the goods are transferred by the supplier to the recipient at the supplier's factory gate, where after the recipient is responsible for transportation of goods up to the destination, bears the risk of any loss in transit and is free to dispose the goods in any manner it deems fit. Further, the address in the 'bill to' field of the invoice raised by the seller would be the recipient's location, where the goods may or may not be shipped to by the buyer.

While some may argue that the supply in this case does not involve movement because the movement of goods by the recipient is only a post supply activity invoking Section 7(4), it is also possible to argue that usage of the words 'whether by the supplier or by recipient' after the words 'where the supply involves movement of goods' has widened the scope to include such transactions where the movement is a direct result of the supply of goods and therefore, the transaction in question will be governed by Section 7(2).

For the sake of exhaustiveness, it would be appropriate to examine the results by applying both the provisions. However, for application of both the provisions it is relevant to determine what constitutes 'delivery to the recipient'. As per the definition of delivery discussed *supra* the delivery to recipient would be the point where voluntary possession of goods is given to the recipient and the recipient is put in the same position of control over the goods which the supplier himself had immediately before such delivery.

Thus, in this example it can undoubtedly be said that the delivery takes place at the factory of the supplier. Now by application of Section 7(4) of the Model IGST Act, the place of supply of goods would be the factory site of the supplier. Interestingly, for the purposes of Section 7(2), termination of movement for delivery would also be the factory gate of the supplier resulting in the place of supply again being the factory site of the supplier. Thus, irrespective of the provision applied, in case of an ex-factory transaction the place of supply would be the supplier's factory, which being the same as the location of the supplier will make the transaction an intra-State supply of goods.

However, this interpretation of the provisions may result in various complications and contradictions. Firstly, if an ex-factory transaction is treated as an intra-State supply subject to levy of CGST-SGST in the supplier's State, then will a recipient located in a State outside such supplier's State, without business or registration in the supplier's State, be allowed to avail and utilize the SGST credit of the purchase while making output GST payment in its home State? If the SGST credit of one State is blocked for availment and utilization in another State, then GST model is not very different from the current VAT regime for the purpose of cross utilization of credit under different VAT legislations. Secondly, if the recipient dealer is expected to take registration in each of the States of suppliers and then stock transfer the goods to its own unit in the other State by charging IGST which can be paid by utilizing the CGST-SGST credit of the procurement, then the same will be in complete contradiction of not only prudent business practices but also the 'hub and spoke' model in which GST in India is expected to operate.

Place of supply – Can ultimate destination provide the solution?

In view of the above, one may take a view that it is the location of goods at the time of ultimate termination of movement by the recipient himself that would be relevant for determining the place of supply. However, it is not for the supplier to be sure of whether and where the recipient chooses to move the goods as the recipient is free to move or dispose the goods in any manner in transit itself. This will result in taxability of transaction in the hands of the supplier contingent upon events not under its control. In order to avoid such uncertainties, the buyer's 'bill to'/'ship to' address can be assumed to be the place where the movement of goods will eventually terminate after making necessary modifications in the agreement curtailing the buyer's right of diversion. If the address of the recipient is outside the supplier's State, then the transaction will be deemed to be an inter-State supply irrespective of the terms of supply.

This view, though meritorious on account of its simplicity and objectivity, may be prone to dispute because it does not flow from an interpretation of the draft provisions as they currently exist. The view is especially disputable in light of the fact that the draft law makers have defined the phrase 'address of delivery' but refrained from using it in this provision. Further, if the intention was to make the 'bill to' address of the recipient as the place of supply then the draftsmen could have done so by adopting the phrase 'principal place of business' of the recipient which has been done in sub-section (3) of Section 7 and also other provisions of the Model IGST Act determining place of supply of goods and services in different contexts.

Thus, the Model IGST Act in its current form, though clearly had intended to and seeks to address the problem, has only ended up creating more peculiar ones.