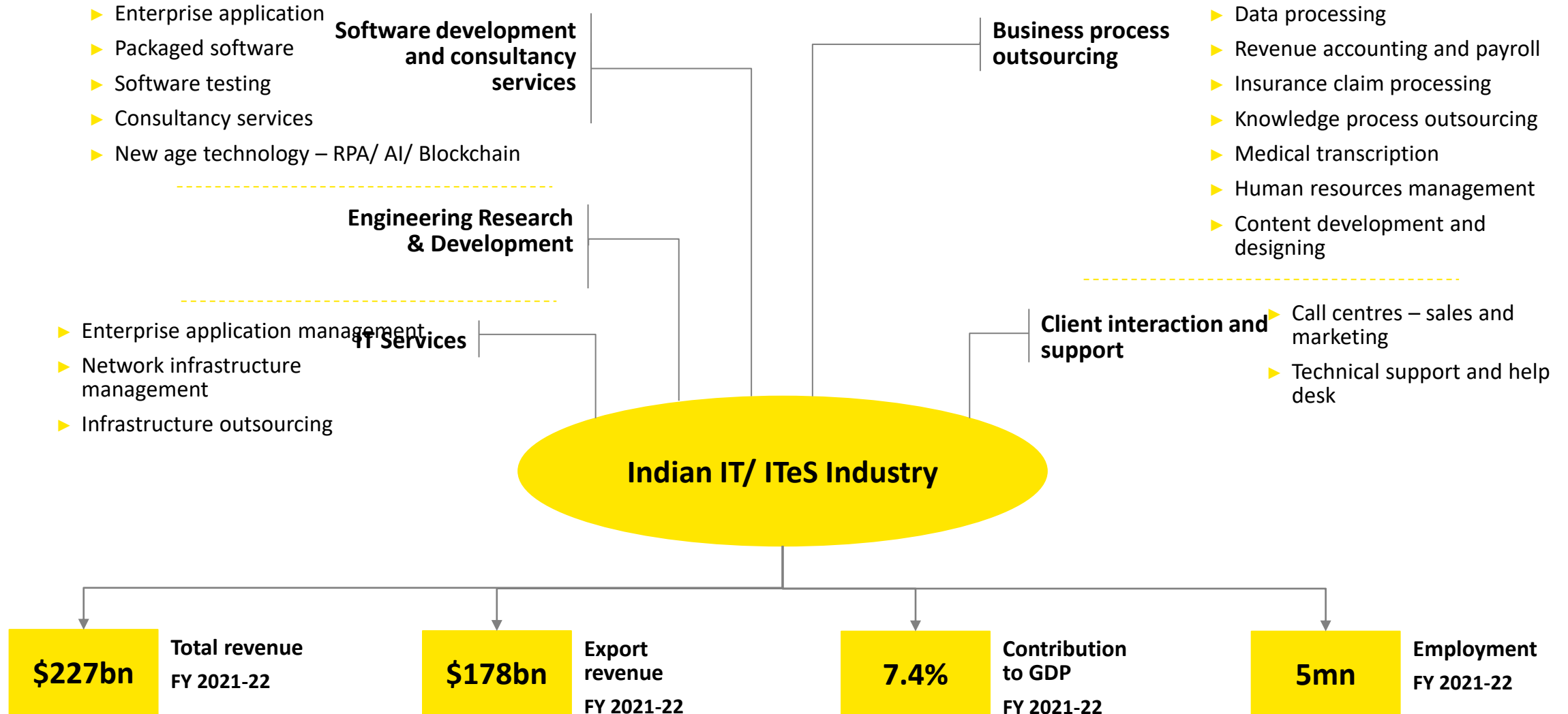


# **IT & Software Industry**

***GST Relearn Refresher Series – Part II***

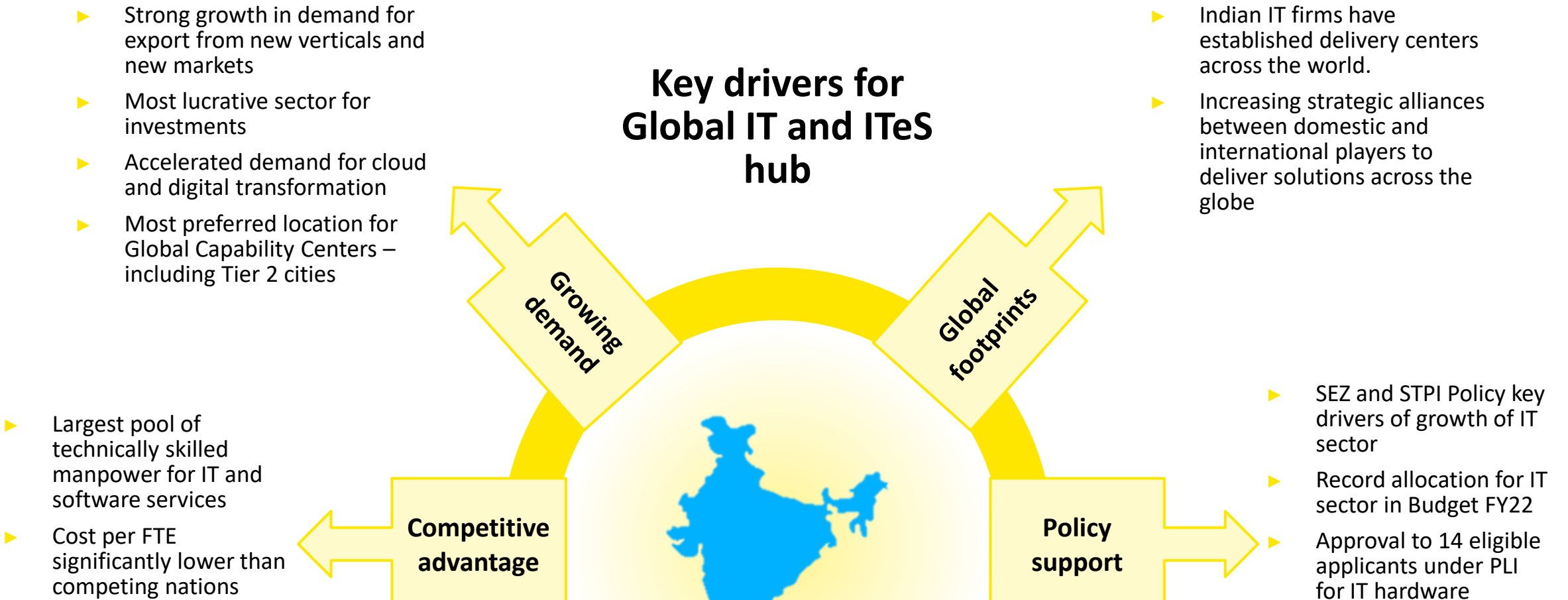
April 2023

# Overview of Indian IT/ ITeS Industry



# The INDIA Advantage

## Key drivers for Global IT and ITeS hub



# Broad GST implications

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## Domestic supply of services

- ▶ Domestic supply of IT/ITeS services liable to GST @ 18%
- ▶ Type of taxes to be charged based on the location of service recipient (i.e. place of supply)
- ▶ Supply of services to SEZ unit/ developer for authorised operations to be treated as zero-rated

## Cross-border supplies

- ▶ Typically, the place of supply of IT/ITeS services should be the location of service recipient (i.e. outside India)
- ▶ However, In case of intermediary services, the place of supply to be the location of service supplier (i.e. within India) – **CGST + SGST to be discharged**
- ▶ In case of non-intermediary services, provided conditions under Section 2(6) of the IGST Act, 2017, are met, services to qualify as ‘exports’ and treated as zero-rated
- ▶ The exporter of service has been provided with following options:
  - ▶ Supply of services without payment of IGST and claim refund of unutilized ITC on inputs and input services
  - ▶ Supply of services with payment of IGST and claim refunds of such IGST paid

# Export of services

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- ▶ Service to qualify as 'exports' upon fulfilment of following conditions:
  - ▶ Supplier of services should be located in India
  - ▶ Recipient of services should be located outside India
  - ▶ Place of supply should be outside India
  - ▶ Payment for such services should be received by the supplier in convertible foreign exchange or such other mode permitted by RBI
  - ▶ Supplier and recipient of services should not be merely establishments of a distinct person
- ▶ Exporters seeking to claim zero-rating benefit of providing services without payment of tax required to file LUT at the start of every of financial year.
- ▶ As per Rule 96(10), the export proceeds to be realised within 1 year from the invoice date, failing which supplier is required to discharge IGST along with interest (from invoice date) within 15 days from lapse of 1 year.

# Test of 'intermediary'



- ▶ Global presence has resulted in cross border transactions being tested for 'intermediary'
- ▶ 'Intermediary' has been defined vide Section 2(13) of the IGST Act, 2017 as under:

*Intermediary means 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.*

## Circular no. 159/15/2021

- ▶ Pre-requisites for 'intermediary' services are:
    - ▶ Minimum of 3 parties to be involved
    - ▶ Two distinct supplies – main supply and ancillary supply
    - ▶ Intermediary service provider to have the character of agent, broker or any other similar person
    - ▶ Does not include a person who supplies such goods or services or both on his own account
  - ▶ Subcontracting of service is not intermediary
- ▶ Illustrations for 'intermediary' services provided under the circular:
    - ▶ Selling agent – Intermediary
    - ▶ Procurement agent – Intermediary
    - ▶ Subcontract – not an intermediary
    - ▶ Outsource – not an intermediary

# Test of 'intermediary'



## *Illustrations of IT/ITeS provided under Circular no. 159/15/2021*

### **Selling agent**

- ▶ 'A' is a manufacturer and supplier of machine. 'C' helps 'A' in selling the machine by identifying prospective buyer 'B'.
- ▶ 'C' charged 'A' for his services of locating 'B' and helping in finalizing the sale between 'A' and 'B'.
- ▶ 'C' is providing 'intermediary services' to 'A'.

### **Subcontract**

- ▶ 'A' has a contract with 'B' for providing customized software.
- ▶ 'A' outsources the task of design and development of a particular module of the software to 'C' for which 'C' may have to interact with 'B'.
- ▶ 'C' does not qualify as an 'intermediary' in this case.

### **Procurement agent**

- ▶ 'P' is an insurance company located outside India which requires insurance claim processing services in India.
- ▶ 'Q' has been approached for arranging such services in India.
- ▶ 'Q' contacts 'R' who provides insurance claim processing services in India.
- ▶ 'Q' is providing 'intermediary' services to 'P'.

### **Outsourcing**

- ▶ 'A' is a manufacturer and supplier of computers based in USA.
- ▶ 'A' outsources the task of providing customer care services to a BPO firm 'B'.
- ▶ 'B' provides services to 'A' by interacting with customers of 'A' and addressing their queries/ complains.
- ▶ 'B' does not qualify as an 'intermediary' in this case.

# Delhi HC Ruling on ‘intermediary’

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## Facts of the case:

- ▶ ***M/s Ernst and Young Limited (UK)*** has entered into agreements with group entities across the globe for providing professional consultancy services through its Indian branch office
- ▶ The Indian branch office invoices the group entities directly on an arm’s length basis and claims zero-rating benefit on such export of services
- ▶ Refund claims filed by the Indian branch on export of services have been rejected by department holding the Indian branch as ‘intermediary’

## Ruling of Delhi HC:

- ▶ From the definition it is clear that an intermediary merely ‘arranges or facilitates’ supply of goods and/ or services between two or more persons – obviously a person who supplies the goods and/ or services is not an intermediary
- ▶ The last line of the definition - *but does not include a person who supplies such goods or services or both or securities on his own account* – merely clarifies that the definition is not to be read in an expansive manner and does not control the definition
- ▶ Outsourcing a constituent to a third party would not be construed as ‘intermediary’



# Balancing the expansion – ISD v/s Cross charge



- ▶ Growing demand has pushed IT firms to expand offices nationally as well as internationally
- ▶ With expansion across states in India, the major challenge being faced is around valuation of supplies between distinct persons and distribution of common credits

## Input Service Distributor

- ▶ **Definition of ISD:**

*"Input Service Distributor" means an office of the supplier of goods or services or both which receives tax invoices issued under section 31 towards the receipt of input services and issues a prescribed document for the purposes of distributing the credit of central tax, State tax, integrated tax or Union territory tax paid on the said services to a supplier of taxable goods or services or both having the same Permanent Account Number as that of the said office*

- ▶ **As per GST FAQs issued by CBIC for IT/ ITeS sector:**

*Question 26: Is the requirement of transferring of credit through ISD mechanism mandatory?*

*Answer: The ISD provision under the CGST Act, 2017 is not mandatory. It only provides the manner of distribution of ITC wherever the business entity wishes to distribute the ITC as an Input Service Distributor.*

# Balancing the expansion – ISD v/s Cross charge



## Cross charge

### ▶ Concept of 'Distinct person':

*Section 25(4). A person who has obtained or is required to obtain more than registration, whether in one State or Union Territory or more than one State or Union Territory shall, in respect of each such registration, be treated as distinct persons for the purposes of this Act*

### ▶ Deeming fiction on supplies between 'Distinct person':

*Schedule I. Activities to be treated as supply even if made without consideration*

*(2) Supply of goods or services or both between related persons or between distinct persons as specified in section 25, when made in the course or furtherance of business*

### ▶ Valuation of supplies between 'Distinct person':

*Proviso to Rule 28. Provided further that where the recipient is eligible for full input tax credit, the value declared in the invoice shall be deemed to be the open market value of the goods or services*

# Balancing the expansion – ISD v/s Cross charge



## Cross charge

- ▶ Deemed to be a supply involving supply of goods and/ or services between distinct persons
- ▶ Deeming fiction makes it mandatory to undertake cross charge in case of supply of goods and/ or services between distinct persons free of cost
- ▶ Specific valuation provisions prescribed – *relaxation extended to entities where the recipient is eligible to avail full ITC*
- ▶ *Requires issuance of a tax invoice and reporting in GSTR-1 and 3B*

## Input Service Distributor

- ▶ Merely a mechanism for distribution of input tax credit on common input services
- ▶ Legislation does not make it mandatory to obtain ISD registration – *clarified by CBIC*
  - ▶ Maharashtra AAAR in the case of Cummins India held that ITC on common input services can be distributed only through ISD
  - ▶ HO can undertake cross charge for facilitation services of procuring common input services – *but common input services should be excluded from such cross charge and routed through ISD only*
- ▶ Distribution mechanism prescribed involving attribution of common input services to beneficiary registrations
- ▶ Requires issuance of an ISD invoice and reporting in GSTR-6

# Transactions with workforce



## Taxability of perquisites paid to employees

**Circular No. 172/04/2022 – GST dated 6 July 2022**

- ▶ As per Schedule III to CGST Act, 2017, “Services by employee to the employer in the course of or in relation to his employment” will not be considered as supply of goods or services and hence GST is not applicable on the same.
- ▶ Any perquisites provided by the employer to its employees in terms of contractual agreement entered into between the employer and the employee are in lieu of the services provided by employee to the employer in relation to his employment.
- ▶ Therefore, perquisites paid in terms of the employment contract should not be subjected to GST.

## Taxability of notice pay/ bond recovery

**Circular No. 178/08/2022 – GST dated 3 August 2022**

- ▶ As per industry practice, in the event of the employee leaving the employment before the minimum agreed period incorporated in the employment contract, the employee typically makes a recovery from such employee in the form of notice pay recovery/ salary forfeiture/ bond recovery.
- ▶ Such deterrent clauses are incorporated in the employment contract to dissuade non-serious employees from taking up the job and to discourage employees from leaving prior to minimum agreed period.
- ▶ These recoveries are in the nature of penalties and not as a consideration for tolerating the act of such premature quitting of employment.
- ▶ Therefore, such amounts are not taxable as consideration for the service of agreeing to tolerate an act or situation.

**Kerala HC in case of WP filed by Manapurram Finance Limited**

# SEZ & STPI Regulations at a glance



Key features	SEZ	STPI
Governing regulations	Special Economic Zones Act, 2005	Foreign Trade Policy
Locational bounding	SEZ unit has to be set-up within a notified demarcated zone	STPI unit can be set-up at any place of export
Broad benefits available	<ul style="list-style-type: none"> <li>• Upfront exemption of GST/ customs duty on import of goods</li> <li>• Upfront exemption of GST on procurement of goods or services</li> <li>• No GST on import of services</li> <li>• Permissibility to apply under Service Export Incentive Scheme for eligible services (scheme is likely to be discontinued and replaced with a drawback scheme for eligible services)</li> <li>• Refund/ rebate of input GST in case input tax is charged</li> </ul>	<ul style="list-style-type: none"> <li>• Upfront exemption of GST/ customs duty on import of goods</li> <li>• Refund of GST paid on domestic procurement of goods</li> <li>• Refund/ rebate of input GST in case input tax is charged</li> </ul>

# SEZ & STPI Regulations at a glance



Key features	SEZ	STPI
Territorial jurisdiction	For various regulations, SEZ is considered as a territory outside India	STPI is treated as a territory in India
Movement of assets	Inward and outward movement of assets is regulated – generally physical verification is performed by Customs officer at zone entry points. Even temporary removal of asset for repairs, replacement, WFH, etc. is regulated by Customs officer.	While there is no physical verification involved, movement of assets can be undertaken based on intimations.
Access to unit	Access to unit is regulated by Customs officer by way of issuance of ID cards to authorised employees.	Access to unit is not regulated – assets could be used only for authorised operations.

# Work from Home Policy under SEZ



Particulars	Earlier provisions of Rule 43A of SEZ Rules	New provisions of Rule 43A of SEZ Rules
% of WFH allowed	50% (dispensation possible on reasoned requests)	100% WFH allowed
Duration of approval	1 year from the date of application	Till 31 December 2023
Application for permission	Before 11th October 2022 for existing units/employees. For new employees and units, an application has to be filed 15 days in advance.	Before 31st January 2023 for existing units/employees. For new units or units who have not opted for WFH earlier, units to send intimation on or before the date on which facility of WFH is provided.
Manner of application	Application in a covering letter along with the list of employees for whom WFH facility is granted. For approvals beyond 50%, detailed reasons for such higher %.	E-Mail to be sent to the Authorities intimating them about the WFH facility granted. Details of employees not required to be provided.
Operating of premise	No such condition prescribed.	Units shall be allowed to obtain WFH permission only if the Unit continues to operate from the premises as mentioned in the LOA.
Approval for movement of duty free goods	Approval from Specified Officer required to be obtained along with an endorsement on certificates recording such transfers.	Units are allowed to send duty free assets outside SEZ for WFH without payment of duties on a temporary basis until the validity of WFH permission. No approval required to be obtained on such transfers.

# Work from Home Policy under SEZ



Particulars	Earlier provisions of Rule 43A	New provisions of Rule 43A
Scope of 'employees' covered	Not clarified	"Employees" to also include persons who are employed in the Unit under a contract of manpower supply, where the Unit is the principal employer.
Other provisions	There is no change in the provisions related to tagging of employees to the project of SEZ, proper accounting of export revenue and surrender of ID cards.	

**Presently, Rule 43A does not prescribed any provision for renewal of the WFH permission post 31 December 2023. Clarity required regarding process to be followed post 31 December 2023.**



# Opportunities for CA fraternity

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## Inception/ Conceptualisation

- ▶ Assistance in identifying key benefits under various regulations
- ▶ Advising on structure as so avail maximum available benefit
- ▶ Representation to State authorities for seeking a customised package of incentives

## Setting up operations

- ▶ Assistance in obtaining GST registration
- ▶ Assistance in obtaining SEZ/ STPI registration
- ▶ Assistance in obtaining approval under State incentives scheme

## Commencing operations

- ▶ Assistance in undertaking GST compliances
- ▶ Assistance in obtaining GST refunds
- ▶ Assistance in compliances under SEZ/ STPI

# Questions?

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*Thank  
you*



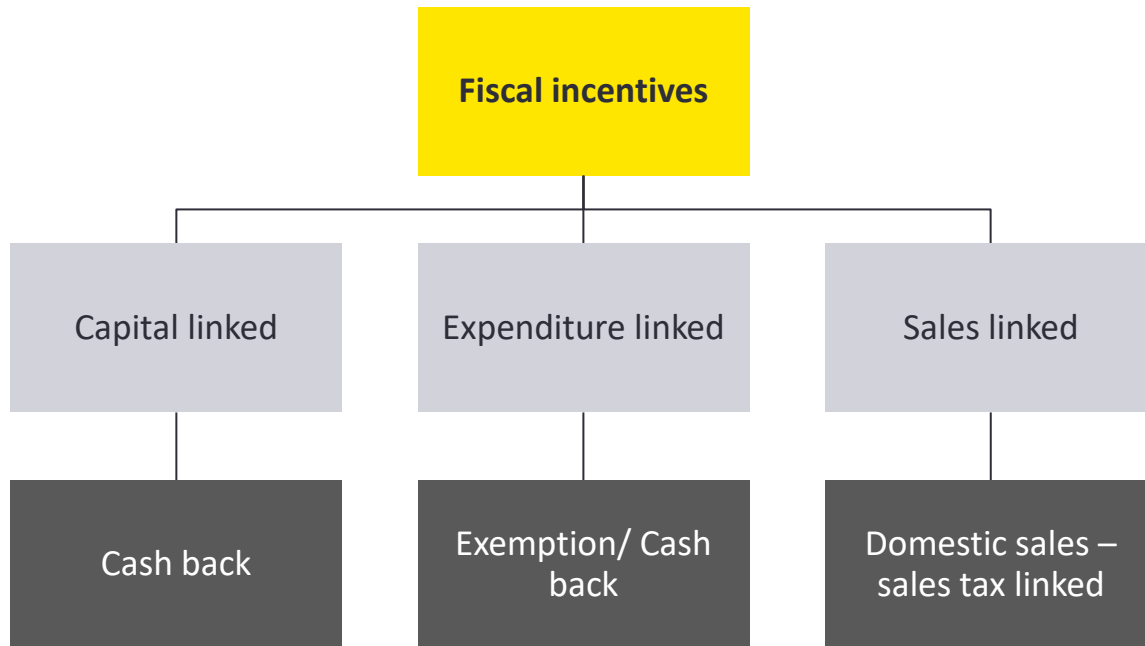
# State incentives to IT/ITeS

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- ▶ Centre & many states have recognized IT/ITeS as a thrust sector and have introduced sector specific policies. Advertisement campaigns also have been taken up by some states
- ▶ State-level incentives for such new or significant expansion projects may include:
  - ▶ Partial/Full exemption from stamp duty
  - ▶ GST reimbursements
  - ▶ Concessions on electricity tariff/duties
  - ▶ Subsidized power tariff
  - ▶ Continuous industry status
- ▶ Benefits defined by the size of eligible investment, location and employment generation
  - ▶ The nature, quantum of incentives may vary depending on whether the investment is classified as a new unit or an expansion unit
  - ▶ State may be divided into groups/zones depending on the development index, quantum of incentives may vary
  - ▶ The definition of eligible fixed capital investment varies in each state, which effects the eligibility of incentives in that state
  - ▶ Investment period is the time period within which the investment made is considered for eligibility of incentives
  - ▶ Operative period is the minimum number of years for which a unit has to be in commercial production
  - ▶ The states provide customized incentive packages to mega projects/ thrust sectors
  - ▶ The states prescribe the minimum percentage of local labour that must be employed by the unit

# Nature of fiscal incentives in India

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1

**Capital linked:** A percentage of capital investment is received as a capital subsidy

2

**Expenditure linked:** Incentive is available as cash refund/exemption of costs like electricity duty, power tariff, stamp duty

3

**Sales linked:** Specified percentage of sales tax paid (VAT/CST/GST) to the state government is given as a subsidy

# Key parameters reviewed by State authorities

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## Location and investment

**1**

To evaluate the maximum benefits that can be availed

## Sector

**2**

To identify the incentives by sector specific policies

## Sales pattern

**3**

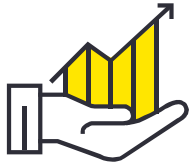
To identify and quantify incentives available under the foreign trade policy and state industrial policy

## Expenditure

**4**

To quantify the incentives linked to expenditure

# Overview of Gujarat IT/ITeS Policy



## Objective

- ▶ Encourage Mega and Large Scale Investment which act as catalyst for growth in IT/ ITeS sector
- ▶ Generate high skilled IT skilled human resources
- ▶ Establish Gujarat as a hub for innovation in emerging and advanced technologies



## Targets

- ▶ Place Gujarat as Top 5 performing states in Indian IT sector
- ▶ Increase Gujarat annual IT exports from INR 3,000 Crore to Rs 25,000 Crore
- ▶ Generate 1 lakh new jobs



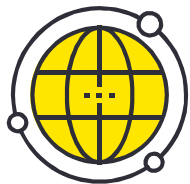
## Operative Period

- ▶ Scheme is valid for 5 years from 7 February 2022 to 31 March 2027
- ▶ Eligible entities who have applied for assistance on or before 31 March 2027 and commenced operations on or before 31 March 2028 shall be eligible



## Applicability

- ▶ IT/ITeS Units
- ▶ IT City / Townships
- ▶ IT Parks
- ▶ Mega Project: Minimum investment of Rs 250 Cr or minimum direct employment of 2,000 IT positions



## Eligible Activities/ Services

- ▶ IT software
- ▶ IT enabled services like BPO, KPO, non-banking services including insurance, website services, etc
- ▶ Emerging Technologies like cyber tech, Big Data, AI, Blockchain, Machine Learning, etc

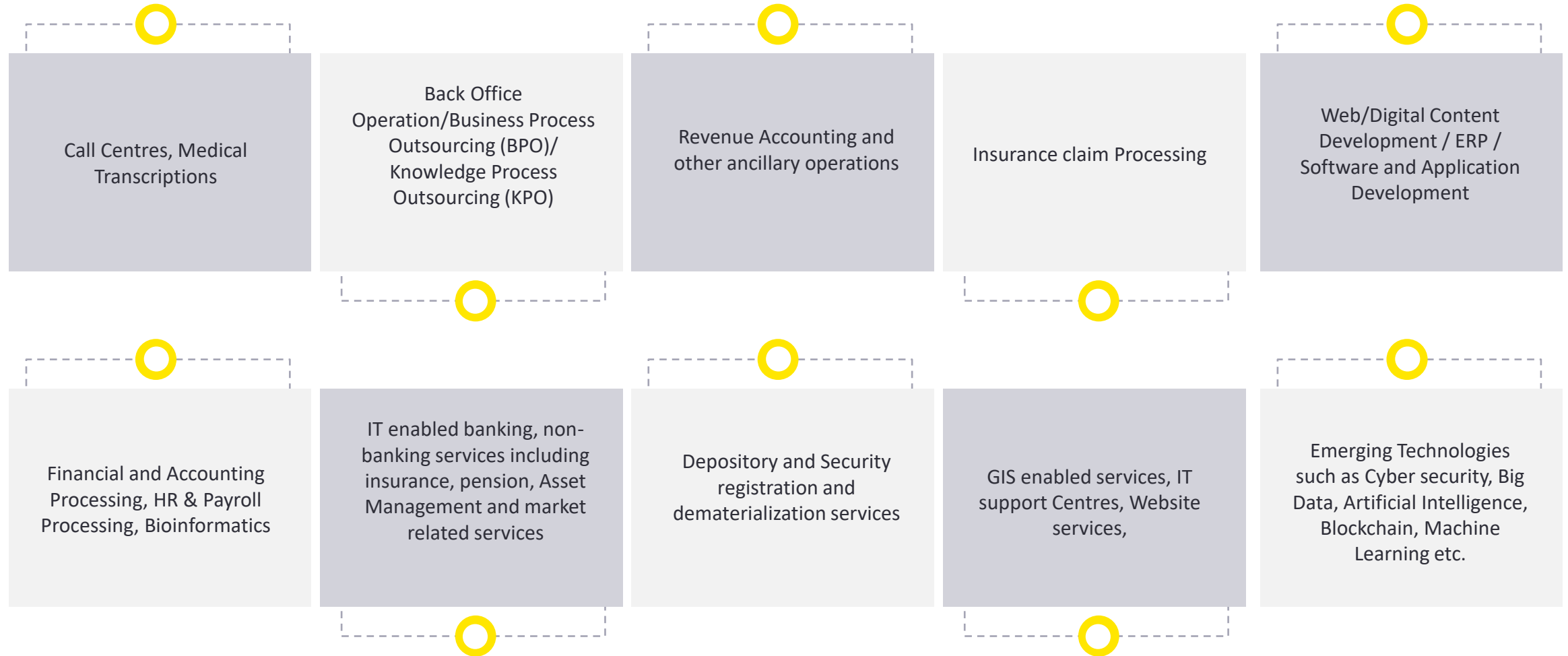


## Incentives

- ▶ Capex Support - One time reimbursement upto 25% of eligible Capex with a maximum cap
- ▶ Opex Support - Upto 15% of annual eligible opex with a maximum cap
- ▶ Special incentives like EGI, EPF, etc

# Scope of IT/ITeS industry under the Policy

IT Enabled Services (ITeS) implies service rendering through application of IT and will include the following:






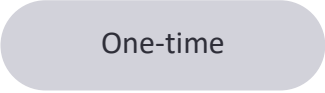

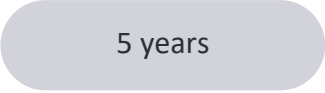

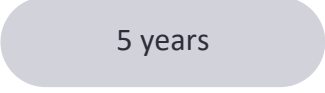


# Incentive on eligible opex for 5 years

- Opex support for Annual Eligible operational expenditures for a period of 5 years from date of commencement of operations or in-principle approval which ever is later.
- Upto 15% of annual eligible opex with maximum yearly cap of INR 20/40 crores
- The disbursement of Opex Support would be quarterly

Nature of benefits	Description of benefits
○ Lease rental Expenditure	<ul style="list-style-type: none"><li>• Expenditure incurred on lease rental of office space from third party</li><li>• Maximum upto INR 50/sq.ft. of build-up area per month or actual expenditure whichever is less</li></ul>
○ Bandwidth Expenditure	<ul style="list-style-type: none"><li>• Actual expenditure incurred on subscribing or leasing bandwidth from the licensed ISP with valid GST number</li></ul>
○ Cloud rental Expenditure	<ul style="list-style-type: none"><li>• Actual expenditure incurred on subscribing or leasing bandwidth from the licensed CSP with valid GST number</li></ul>
○ Power Tariff Expenditure	<ul style="list-style-type: none"><li>• Actual expenditure incurred on energy units consumed</li><li>• Banking charges paid as per provisions laid down under Section 10 of the Gujarat Solar Power Policy, 2021.</li></ul>
○ Patent Expenditure	<ul style="list-style-type: none"><li>• Actual expenditure incurred upto INR 5 Lakh per patent</li><li>• Claim for maximum upto 10 patents per years are only admissible</li></ul>

# Special incentive (in addition to capex and opex support)

- Opex support for Annual Eligible operational expenditures for a period of 5 years from date of commencement of operations or in-principle approval which ever is later.
- The disbursement of Opex Support would be quarterly

Nature of benefits	Description of benefits	Period of benefit*
 Employment Generation Incentives#	<ul style="list-style-type: none"> <li>• For every new and unique job created in the State</li> <li>• Applicable for new local employees hired and retained for a minimum period of one year at 50% of one month's CTC upto INR 50,000 for male employees and INR 60,000 per female employees</li> </ul>	 One-time
 Interest Assistance	<ul style="list-style-type: none"> <li>• Interest subsidy at 7% on term loan or actual interest paid which ever is less with maximum cap of INR 1 Crore per annum</li> <li>• Interest re-payment period to begin during operative period of the policy</li> </ul>	 5 years
 Atmanirbhar Gujarat Rojgar Sahay	<ul style="list-style-type: none"> <li>• EPF reimbursement upto 100% for female employees and 75% for male employees</li> <li>• Reimbursement for only employees residing and working from Gujarat shall be admissible</li> </ul>	 5 years
 Electricity Duty Incentive	<ul style="list-style-type: none"> <li>• 100% of Electricity Duty paid to Gujarat Government</li> </ul>	 5 years

Note:

# Employment Generation Incentives and Atmanirbhar Gujarat Rojgar Sahay are available even in case employees work from home located in Gujarat

\*Period of benefit shall be counted from date of commencement of operations or in-principle approval which ever is later