



# Impact of GST on Export of Services



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### Levy of GST and Supply

Section 5 of the Integrated Goods and Services Tax Act, 2017 states that a tax called as Integrated Goods and Services Tax is levied on all inter-state supplies of goods or services. To qualify as a supply, the transaction should be covered within the definition of supply as per Section 7 of the Central Goods and Services Tax Act, 2017.

### Inter-state supply

For the applicability of Integrated Goods and Services tax, there should be an inter-state supply of goods or services. The fact that the said transaction is a supply has already been discussed above. Next, it needs to be tested whether the supply can be considered as inter-state or not. Now, section 7(5) of the Integrated Goods and Services Tax Act, 2017 states that when the supplier is located in India and the place of supply is outside India, the supply of goods or services or both will be treated to be in the course of inter-state trade or commerce.

Example: X Ltd provides IT enabled services to a person Y Ltd in Germany. The consideration payable by Y Ltd will be \$1,00,000.

Let us analyse the example above if it amounts to export of service.

As per the extract of Section 2(15) of the Integrated Goods and Services Tax Act, 2017, “location of supplier of services means -

where supply is made from a place of business for which the registration has been obtained, then the location of the said place of business.”

Since, X Ltd will be making IT related services from Kolkata, then the location of supplier will be within India i.e. West Bengal.

(iii) Section 13 of the Integrated Goods and Services Tax Act depicts the place of supply wherein the location of the supplier or recipient is outside India. In the case of IT enabled services in the form of assurance, audit and tax, Section 13(2) of the IGST Act, 2017 should be reviewed to find the place of supply. As per this Section, the place of supply as described above will be the location of recipient of service.

As per the extract of Section 2(14) of the Integrated Goods and Services Tax Act, 2017:

*“location of recipient of services means:*

*where a supply is received at a place of business for which the registration has been obtained, the location of such place of business*

*where supply is received at a place other than the place of business for which registration has been obtained (a fixed establishment elsewhere), the location of such fixed establishment”*

*“Fixed establishment means a place (other than the registered place of business) which is characterised by a sufficient degree of permanence and suitable structure in terms of human and technical resources to supply services or to receive and use services for its own needs”*

Since, the location of recipient of service i.e. Y Ltd is in Germany, place of supply will also be outside India as per Section 13(2) of the IGST Act, 2017. As the location of the supplier will be considered as West Bengal and the place of supply outside India, the provisions of Integrated Goods and Services tax will be applicable in the given supply.

### **Zero rated supply and Export of Services**

Section 16(1) of the Integrated Goods and Services Tax, 2017 purports to cover export of goods or services or both within the ambit of Zero rated supply. The test to determine whether a supply is an export of service, one needs to refer to Section 2(6) of the Integrated Goods and Services Tax Act, 2017:

*“Export of services means the supply of any service when –*

*The supplier of service is located in India*

*The recipient of service is located outside India*

*The place of supply of service is outside India*

*The payment for such service has been received by the supplier of service in convertible foreign exchange and*

*The supplier of service and the recipient of service are not merely establishments of a distinct person in accordance with Explanation 1 in Section 8”*

(i) As per the definition of location of supplier of service discussed above, it can be inferred that the location of supplier will be in West Bengal i.e. within India.

(ii) As already explained above, X Ltd will be considered to be located outside India as per the definition of location of recipient of service and fixed establishment given above.

Also, the extract of the definition of recipient is given below:

*“recipient of supply of goods or services or both means –*

*(a) Where a consideration is payable for the supply of goods or services or both, the person who is liable to pay that consideration;”*

In the example of X Ltd, the consideration is liable to be paid by Y Ltd from Germany. So, the recipient will be considered as outside India.

(iii) Section 13 of the Integrated Goods and Services Tax Act depicts the place of supply wherein the location of the supplier or recipient is outside India. As already stated above, the place of supply will be the location of recipient of service in respect of the given IT enabled services. As the location of recipient of service will be outside India, the place of supply will also be outside India.

(iv) The consideration to be received should be in convertible foreign exchange. In the example above, the consideration is \$1,00,000 to be paid by Y Ltd. Since, the payment is in convertible foreign exchange, this condition gets fulfilled.

(v) The supplier and recipient of service should not be merely establishments of a distinct person. This basically means that the supplier and recipient should be separate legal persons altogether. The supplier and recipient should not be merely two branches/establishments of the same legal person. In the instantaneous case, X Ltd and Y Ltd are two separate legal persons and have distinct identities in the eyes of law. Hence, these establishments cannot be considered merely as establishments of a distinct person.

From the above, it can be inferred that the supply falls perfectly within the definition of export of service. Since, export of service is covered within zero rated supply, the given supply is also considered to be a zero-rated supply.

### **Input Tax Credit and Zero rated supply**

Section 16(2) of the IGST Act, 2017 states that credit of input tax can be availed for making zero rated supply. It may be noted that the treatment of input tax credit is different from that of an exempt supply. As per Section 17(2) of the CGST Act, 2017, input tax credit attributable to making exempt supplies will not be allowed whereas input tax credit will be allowed for making taxable supplies including zero rated supplies. So, as per the given sub-section, zero rated supplies are treated as part of taxable supplies and not exempt supplies for the purpose of allowing the benefit of Input Tax Credit.

### **Compliance alternatives for zero rated supplies**

In case of a zero rated supply, no tax is required to be paid. However, to ensure compliance, GST law has prescribed two alternatives when making a zero rated supply. As per Section 16(3) of the Integrated Goods and Services Tax Act, 2017:

*“A registered person making zero rated supply shall be eligible to claim refund under either of the following options, namely: -*

- (a) he may supply goods or services or both under bond or Letter of Undertaking, subject to such conditions, safeguards and procedure as may be prescribed, without payment of integrated tax and claim refund of unutilised input tax credit or*
- (b) he may supply goods or services or both subject to such conditions, safeguards as may be prescribed, on payment of integrated tax and claim refund of such tax paid on goods or services or both supplied*

*in accordance with the provision of section 54 of the Central Goods and Services Tax Act or the rules made thereunder”*

So as per the above, there are two options available with the exporter in making export of services:

- (a) Export on payment of Integrated tax and refund under Section 54 of CGST Act, 2017
- (b) Export without payment of tax on furnishing of bond/Letter of Undertaking

As per point (a) above, one can make the payment of output taxes on the export of services after utilising the input tax credit and then claim a refund of the complete tax amount. This will be a complete revenue neutral exercise but it will involve a working capital blockage and any administrative delays in discharge of refunds may further compound the problem.

Under point (b) above, one needs to only furnish a bond/letter of undertaking with the Department. Once that happens, no output taxes are required to be paid. Also, the entire amount of unutilised input tax credit is available as a refund. Though this option may involve a few compliances but it is usually preferred because the working capital blockage can be avoided.

Also, among the two options of furnishing bond and Letter of Undertaking, usually the Letter of Undertaking is preferred. As per Notification no. 37/2017-Central Tax dated 4<sup>th</sup> October, 2017, all registered persons who intend to supply goods or services for export without payment of integrated tax are eligible to furnish a Letter of Undertaking instead of a bond except those who have been prosecuted for any offence under the CGST Act, IGST Act or any of the existing law where the amount evaded is Rs. 250,000. For persons who have been prosecuted under these laws for more than Rs. 250,000, furnishing of bond is mandatory. Also, it has been stated vide Circular no. 8/8/2017-GST dated 4<sup>th</sup> October, 2017 that a bank guarantee of 15% is required in all cases wherein a bond is furnished in respect of a zero rated supply. Assuming that there has been no prosecution in the given case, a Letter of Undertaking may be furnished by the client and avoid payment of Integrated tax altogether on export of services.

Summarizing the above analysis, it can be safely opined that the services provided by X Ltd is an export of service under the GST law. Being an export of service, such supplies fall within the ambit of zero rated supplies. Such zero rated supplies are eligible for the purpose of claiming of input tax credit. Being zero rated supplies, no

output taxes are leviable on such supplies. For the purposes of compliance, there are two alternatives – either export upon making of the payment of IGST and then claiming the refund of taxes paid or export without making the payment of IGST and claim the refund of unutilized Input Tax Credit.

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