GST on Corporate Guarantees

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GST ARTICLE

1. INTRODUCTION

The Goods and Services Tax Regime brought plethora of changes to the pre-existing taxation regime of the country. In the current paper, the author has made efforts to take into account a wholesome view of taxability of corporate guarantees without consideration under GST regime. In Chapter 2, the scope of guarantees and indemnities are deliberated upon. Chapter 3 refers to understanding the meaning of corporate guarantees and how it is different from personal guarantee and bank guarantee. Chapter 4 refers to the taxability of corporate guarantee under the GST Regime.

2. GUARANTEES AND INDEMNITIES (INDIAN CONTRACT ACT, 1872)

2.1. Guarantee is defined under Section 126 of the Indian Contracts Act, 1872. A guarantee is a contract to perform the promise, or discharge the liability of a third person in case of his default. The three parties to the contract are:

a. the person who gives the guarantee is called the **Surety**,
b. the person for whom the guarantee is given is called the **Principal Debtor**, and
c. the person to whom the guarantee is given is called the **Creditor**[1].

For example, if A advances a loan of Rs. 1,000 to B and C promises to A that if B does not repay the loan, C will repay it on his behalf. This is a contract of guarantee. Here B is the principal debtor, A is the creditor and C is the surety or guarantor\

2.2. A contract of indemnity as defined under Section 124 of the Indian Contracts Act, 1872, is a contract by which one party promises to save the other party from loss caused to him **by the conduct of the promisor himself, or by the conduct of any other person**[2].
For example, C enters into a contract to indemnify B against a consequence of legal suit that may be filed by F in respect of a certain sum of money of Rs. 500. Such a contract may be expressed or implied. The above example is of an expressed contract, however; if any person acts on request of another and incurs any expenses, then such a person can recover such expenses from the person who requested the same. This instance is an implied contract of indemnity. The two relevant parties are:

a. The **Indemnifier** (person who makes good of the loss), and
b. The **Indemnified or indemnity holder** (person whose loss is made good).

2.3. A contract of insurance is also one of the examples of an indemnity contract under the English Law. Such a contract has a consideration attached to it in form of the insurance premium. However, under the Indian Contracts Act, 1872, the contract of indemnity is restricted to the indemnification of the loss caused by the promisor or any other person. Therefore, the loss caused by any accidents or event that are not concerned with the conduct of any person, appears to be out of scope of such indemnification.

[1] Section 126 of the Indian Contract Act, 1872 (Act No. 9 of 1872)
[2] Section 124 of the Indian Contract Act, 1872 (Act No. 9 of 1872)

2.4. Therefore, a contract of guarantee and such as of indemnity must satisfy all the elements of a valid contract. However, when it comes to consideration of a contract, there is a special feature with regard to contract of guarantee. The consideration received by the principal debtor is sufficient for surety for the purpose of this contract of guarantee. Thus, anything done or any promise made for the benefit of the principal debtor may be a sufficient consideration to the surety for giving the guarantee[3].

2.5. Distinction between the Indemnity and guarantees:

Basis	Indemnity	Guarantee
Parties	There are only two parties: the indemnifier and the indemnified.	There are three parties: the surety, the principal debtor and the creditor.
Liability	The liability of the indemnifier is primary	The liability of the surety is secondary and the primary liability us on the Debtor. The debtor making a default renders the surety liable for repayment.
Act	The indemnifier does not necessarily act at the request of the debtor.	The surety acts on the request of the principal debtor.
Existence of debt/ Duty	The indemnifier undertakes an indemnity based on the happening of a contingent event i.e., the happening of a loss.	There is an existing debt or duty, which is guaranteed by the surety.
Right to sue	The indemnifier cannot sue third-parties in his own name unless the promise (indemnified) relinquishes his right in favour of the promisor (indemnifier).	The surety has the right to file suit against the Principal debtor upon discharge of the debt or duty.
Number of agreements	There is only one agreement i.e., the agreement between indemnifier and indemnity holder.	There are three agreements i.e., agreement between the creditor and principal debtor, the creditor and surety and surety and principal debtor

"Whether a contract is one of guarantee or of indemnity is a question of construction in each case"

[3] Section 127 of the Indian Contract Act, 1872 (Act No. 9 of 1872)
[4] State Bank of India v. Mula Sahakari Sakhar Karkhana AIR 2007 SC 2361

3. CORPORATE GUARANTEE

3.1. After establishing the distinction between the fundamental nature of a Contract of Indemnity and Guarantee, let us understand the concept of corporate guarantee.

3.2. A Corporate Guarantee is a guarantee in which any corporation agrees to be responsible for the financial obligations of, or the performance of, contractual obligations by the principal debtor to the creditor, in the event the principal debtor fails to discharge his obligation to the Creditor. These transactions usually include inter- group Corporate guarantees, which are given to facilitate a smoother financial functioning to the 'Related' or 'Associated' persons.

3.3. Corporate Guarantees without consideration are quite generic transaction among companies wherein holding or parent companies issues corporate guarantee to various Banks or other Financial Institutions as a collateral security for the credit facilities availed by its subsidiaries. Also, corporate guarantee, is unsecured, which means it is not secured by or tied to any specific asset of the surety. Corporate guarantee to related parties without consideration are based on the business needs and for group synergy.

Corporate Guarantee and Personal Guarantee

3.4. Corporate Guarantee is different from Personal Guarantee in the sense that Personal Guarantee is a promise made by an individual being in a capacity of an executive or partner of a business which has taken any debt and the promisor assumes a personal responsibility of repayment upon default by the business. For example, as per the banking practices the banks require collateral security for providing financial assistance which may generally takes the form of a personal guarantee taken from a director/ partner of such Borrower Company/ firm.

Corporate Guarantee and Bank Guarantee

3.5. A Bank Guarantee is also similar to personal guarantee but, the only difference is that there, is a Promise/ commitment given by a bank to a third party in this case. The bank assures the third party that in event of any non-performance by the bank's customer, the bank will honour the claim against the guarantee. A bank guarantee is a legally

enforceable contract and constitutes of three parties. The banker is the guarantor who assures the third party (beneficiary) to pay him a certain sum of money on behalf of his customer, in case the customer fails to fulfil his commitment to the beneficiary. However, a bank guarantee is also inherently different from a corporate guarantee. A bank guarantee is a surety that the bank will pay off the debts in case the business entity is unable to do so. For this, banks run risk assessments to ensure that the guaranteed sum can be retrieved, and bank may also require a security in the shape of cash or capital assets. However, corporate guarantee, apart from the fact that no fee is charged, corporate guarantees are issued without any security or underlying assets. For the purpose of income tax, this difference has been established by various cases. Few of the cases are discussed below:

Glenmark Pharmaceuticals Ltd vs. Addl. CIT[5]

- Corporate guarantees are issued in order to safeguard and support the financial health of their Associate enterprises or to facilitate smoother functioning of the enterprise. However, the bank provides bank guarantees as a part of their general course of business and charge the consideration accordingly.
- Bank guarantees are reliable and infallible instruments of security and a failure in honouring the guarantee is treated as a deficiency of services under the banking law. Although, Guarantor is bound by contract law and has the right to sue in case of corporate guarantees, these are not infallible.
- Thus, there is a fundamental difference in the functional approach of both types of guarantees.

Micro Ink Limited v. ACIT[6]

- Bank guarantee is a surety by the bank to pay off any debts or liabilities on account of any loss to a person or entity. For such guarantees, a guarantee fee is charged by the bank even though, such guarantees are backed by deposits.
- But the corporate guarantees are issued without any underlying assets or securities. These guarantees are majorly motivated by business needs.
- Thus, a comparison cannot be drawn in between the two.

[5] TS-329-ITAT-2013(Mum)-TP
[6] Micro Ink Limited v. ACIT (ITA No. 2873/Ahd/10)

Laws Governing Corporate Guarantees

3.6. There are a number of laws in existence which governs/ regulate the contract of corporate guarantee such as:

Companies Act, 2013

- Section 185 enumerated inter- corporate loans which are prohibited to be offered by any company. This provision specifically disallows the companies from providing loans, guarantees and securities in favor of its directors or to any other person in whom the director is interested in. However, the provision makes a few exceptions as following:
  - Any loan made by a holding company to its wholly owned subsidiary company or any guarantee given or security provided by a holding company in respect of any loan made to its wholly owned subsidiary company[7]; or
  - Any guarantee given or security provided by a holding company in respect of loan made by any bank or financial institution to its subsidiary company[8].
- Therefore, the Companies Act, 2013, allows for Inter- Corporate guarantees among related parties subject to the condition that such loans when provided by the holding companies be used by the subsidiary companies for its **principal business activities**.

Foreign Exchange Management (Guarantees) Regulations, 2000

- The essence of any transaction being covered under the Foreign Exchange Management act, 1999 (hereinafter referred as 'FEMA') is that all current account transactions are permitted except those specifically prohibited by law and all capital account transactions are prohibited except those expressly provided by law.
- The capital account transactions alters the assets or liabilities, including contingent liabilities outside India of persons residing in India, or assets or liabilities in India of persons residing outside India. Therefore, any transactions that decrease or increase the assets or liabilities by an Indian resident or even a non-resident, falls under the ambit of FEMA.

[7] Section 185 (3) (c) of the Companies Act, 2013 (Act No. 18 of 2013)
[8] Section 185 (3) (d) of the Companies Act, 2013 (Act No. 18 of 2013)

- Therefore, in order to regulate the guarantees, Foreign Exchange Management (Guarantees) Regulations, 2000 were issued by the Reserve Bank of India (hereinafter referred to as 'RBI') in exercise of the powers conferred upon the under Section 6 (3)(j)(i) read with Section 472 of the FEMA. These regulations have put restrictions on the issue of guarantee by a person resident in India against a debt, obligation or any other liability owed by a person resident in India to a person resident outside India. Therefore, a special permission granted by the RBI is the only mode of legitimizing such transactions.

4. GST ON CORPORATE GUARANTEE WITHOUT CONSIDERATION

Applicable Provisions

4.1. The taxable incident under GST is derived from Section 7 of the Central Goods and Services tax Act, 2017 (hereinafter referred as "the CGST Act"). It provides that GST would be leviable on all the transactions which qualify as 'Supply', as may be applicable, except the supplies which are outside the purview of GST i.e., non-taxable supplies.

4.2. In this regard, clause (a) of Section 7(1) of the CGST Act provides that supply includes all forms of supply of goods or services or both such as sale, barter, exchange, license rental, lease or disposal made or agreed to be made for a consideration by a person in the course or furtherance of business[9].

4.3. In view of the aforementioned definition of 'supply', it is ascertainable that any transaction/activity would qualify as 'Supply' under clause (a) of Section 7(1) of the CGST Act, upon satisfaction of the below-mentioned conditions:

a. the transaction/activity is made or agreed to be made for consideration; and

b. the transaction/activity is carried out in the course or furtherance of business

4.4. Further, Section 7(1) (c) of the CGST Act provides that the activities specified in Schedule I, made or agreed to be made without a consideration will be covered within the scope of the term 'supply'. Section 7(2)(a) of CGST Act stated that activities mentioned under Schedule III of the act shall neither be treated as supply of Goods nor supply of services.

4.5. Schedule I states activities to be treated as supply even if made without consideration which includes:

"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:

[9] Section7 (1)(a) of CGST Act, 2017 (Act No. 12 of 2017)

Provided that gifts not exceeding fifty thousand rupees in value in a financial year by an employer to an employee shall not be treated as supply of goods or services or both"

4.6. According to Schedule III, the activities or transactions which shall be treated neither as a supply of goods nor a supply of services include:

"6. Actionable claims, other than lottery, betting and gambling."

Analysis

Corporate Guarantees under Service Tax regime

4.7. Before analysing the taxability of issuance of corporate guarantee without consideration under GST regime, it is important to understand first the implications under service tax regime.

4.8. Section 66B of the Finance Act, 1994 (hereinafter referred as the 'Finance Act') was the charging section according to which service tax levied at the rate of 14% on the value of all services, other than those specified in the negative list, provided or agreed to be provided in the taxable territory by one person to another and collected in such manner as may be prescribed.

4.9. However, as per the definition of service under Section 65B (44) of the Finance Act, 1994, for any transaction to qualify as a service, following ingredients must be satisfied cumulatively:

(a) There must be an activity.

(b) Such activity must be carried out by one person for another person.

(c) Such activity must be carried out for consideration.

4.10. On the basis of the forgoing discussion, it can be said service tax was applicable only on provision of a service, and there is provision of a service only if one person is performing any activity for another person for a consideration. If any of the elements, i.e., receipt of consideration or obligation for performance of activity is missing, there cannot be provision of a service. Accordingly, in such a case, liability for payment of service tax would not arise.

4.11. Accordingly, in case of issuance of corporate guarantees to banks on behalf of the related parties, the first and second conditions (activity and activity from one person to another), as required under Section 65B(44) of the Act, stand satisfied. However, the third condition (i.e. the said activity must be carried out for a consideration), does not stand fulfilled. Accordingly, the said activity would not tantamount to be service under Section 65B(44) of the Finance Act.

4.12. Reference can be placed on the position taken by the Hon'ble CESTAT Chandigarh in the case of ***M/s DLF Cyber City Developers Limited vs CST, Delhi-IV (Appeal No. ST/60753/2017)***. It was observed as follows:

"It is an admitted fact that the appellant-assessee has not received any consideration from either from the financial institutions or from their associates for providing corporate guarantee, in that circumstances, no service tax is payable by the appellant-assessee. Moreover, the demand raised in the show cause notices are on the basis of assumption and presumption presuming that their associates have received the loan facilities from the financial institution at lower rate, therefore, the differential amount of interest is consideration, but there is no such evidence produced by the revenue on that behalf. In that circumstances, we hold that the appellant-assessee are not liable to pay any service tax on corporate guarantee provided by the appellant assessee to various banks/financial institutions on behalf of their holding company/associate enterprises for their loan or over draft facility under Banking and Financial Institutions after or before 01.07.2012."

(emphasis supplied)

4.13. Further, it is pertinent to note that Rule 3 of the erstwhile Valuation Rules under Service Tax, which provides for adaptation of the value of similar service by the same service provider, has application only in cases where value of a service is not ascertainable. Therefore, in the case where no consideration is provided by the service recipient, the said Rule 3 will have no application.

4.14. Reliance for this view can be placed upon the recent case of ***Magarpatta Township Development & Construction Co Ltd Versus Commissioner Of Central Excise, Pune-III, 2013 (7) TMI 669 - CESTAT Mumbai*** wherein the Hon'ble Tribunal observed that there is no deeming provision in the service tax law providing for addition of notional amounts to the value/ price charged.

4.15. In nutshell, under service tax regime, the department argues it to be an activity carried out by parent company towards subsidiary companies equating it with the bank

guarantees issued by banks for securing the payments. However, as dealt by judicial forums, a service without a consideration cannot be made leviable to service tax. It has also been observed that there is no provision in the scheme of valuation of service wherein notional amount can be deemed as a consideration for the purpose of arriving at value for payment of service tax. There is no deeming fiction or notional concept in the Act or the rules framed thereunder which provides for deeming any notional value as the value of the service for the purpose of discharging service tax liability thereon.

Service Tax Regime: "No Consideration – No Service – No levy"

Corporate Guarantees under GST regime

4.16. When it comes to supply without consideration, clause (c) of Section 7(1) of the CGST Act provides that the activities specified in Schedule I, made or agreed to be made without a consideration will be covered within the scope of the term 'supply' which include 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.

4.17. In nutshell, the definition of supply covers Schedule I which deems certain activities without consideration also as supply and it includes supply of goods/services between related persons made in the course or furtherance of business. Accordingly, it cannot be said that corporate guarantees are issued without consideration and not leviable to GST due to the aforesaid entry in Schedule I. The said entry under Schedule I under CGST Act is designed by legal fiction on the principle that relationship itself is consideration. Thus, it appears that corporate guarantees, being a transaction between related person without consideration, will be deemed as supply under Schedule I and will be taxable under GST.

4.18. However, let us analyse whether issuance of corporate guarantee is a supply of services *per se*.

[10] State Bank of India v. Mula Sahakari Sakhar Karkhana AIR 2007 SC 2361

4.19. At this juncture, reference can be made to provisions of transfer pricing under Income Tax since taxability of corporate guarantee has been a bone of contention under Income tax as well.

Corporate Guarantee under Income Tax

- Chapter X of the Income Tax Act, 1961 lays down the provisions that govern transfer pricing in India. Section 92B provides that any income arising out of an international transaction entered by a taxpayer with its associated enterprise, shall be computed taking into regard arm's length price. Therefore, cases wherein any commission for Corporate Guarantees are received, from overseas, or vice versa, a question usually comes whether the provisions of Income taxes get attracted.
- The assesses have taken various arguments before the courts which *inter alia* includes that issuance of corporate guarantee without consideration does not qualify to be international transaction since it is not a provision of services
- Reference here can be made to the decision of ***Micro Ink***[11] wherein ITAT observed as follows:

> *40. ..... Let us now compare this kind of a guarantee with a corporate guarantee. The guarantees are issued without any security or underlying assets. When these guarantees are invoked, there is no occasion for the guarantor to seek recourse to any assets of the guaranteed entity for recovering payment of defaulted guarantees. The guarantees are not based on the credit assessment of the entity, in respect of which the guarantees are issued, but are based on the business needs of the entity in question. Even in a situation in which the group entity is sure that the beneficiary of guarantee has no financial means to reimburse it for the defaulted guarantee amounts, when invoked, the group entity will issue the guarantee nevertheless because these are compulsions of his group synergy rather than the assurance that his future obligations will be met. We see no meeting ground in these two types of guarantees, so far their economic triggers and business considerations are concerned, and just because these instruments share a common surname, i.e. 'guarantee', these instruments cannot be said to be belong to the same economic genus. Of course, there can be situations in which there may be economic similarities, in this respect, may be present, but these are more of an exception than the rule. In general, therefore, bank guarantees are not comparable with corporate guarantees.*
>
> *41. ..... As a plain look at the details of corporate guarantees would show, these guarantees were issued to various banks in respect of the credit facilities availed by the subsidiaries from these banks. The guarantees were prima facie in the nature of shareholder activity as it was to provide, or compensate for lack of, core strength for raising the finances from banks. No material, indicating to the contrary, is brought on record in this case. Going by the OECD Guidance also, **it is not really possible to hold that the corporate guarantees issued by the assessee were in the nature of***

[11] Micro Ink vs ACIT [(2016) 176 TTJ 8 (Ahd)]

'provision for service' and not a shareholder activity which are mutually exclusive in nature. In the light of these discussions, we are of the considered view, and are fully supported by the OECD Guidance in this, that the issuance of corporate guarantees, in the nature of quasi-capital or shareholder activity- as is the uncontroverted position on the facts of this case, does not amount to a service in which respect of which arm's length adjustment can be done.

44. As for the words 'provision for services" appearing in Section 92B, and connotations thereof, our humble understanding is that this expression, in its natural connotations, is restricted to services rendered and it does not extend to the benefits of activities per se. ……

(Emphasis supplied)

- Similar lines of argument have been taken in various decisions under Income Tax. However, some of the decisions are in line with decision of Micro Ink (discussed supra) and some have held corporate guarantee without consideration to be international transactions.

4.20. Basis above decisions under Income Tax, an argument can be taken under GST that issuance of corporate guarantee to related parties without consideration does not qualify as supply of services since Corporate guarantee is entirely entrepreneurial in the sense and it is issued for maximization of gains for the recipient entity and thus the group as a whole. A guarantor does not arrange financing for the debtor, but merely executes a financial instrument in its favour. These guarantees do not cost anything to the guarantors. Lastly, it can also be said to be a mode of ownership contribution, since it is generally given to compensates for the inadequacies in the financial position of the borrower and it can be said to be in the form of quasi-capital as well.

4.21. Thus, a view is possible that there is no service activity undertaken and the company issues the same in its capacity as a shareholder to protect its investment in securities. However, the department will definitely be disputing the above arguments.

4.22. Also, to determine the taxability of Corporate Guarantee, reliance can also be placed on Circular No. 34/8/2018-GST dated 01.03.2018 wherein, it is provided that services provided by Central or State Government to any business entity including PSUs by way of guaranteeing the loan taken from financial institutions against consideration shall be taxable. Hence, the aforementioned circular supports the view that transaction of guaranteeing loan with consideration qualifies as supply and therefore, is leviable to GST.

A view is possible that issuance of corporate guarantee does not qualify as supply of services

Corporate Guarantees as actionable claim

4.23. However, the next interesting argument could be whether issuance of corporate guarantee can be said as supply of actionable claim and therefore it should be outside the ambit of supply as per Schedule III of CGST Act.

4.24. Schedule III of the CGST Act under Clause 6 mentions that actionable claims are not to be considered either as a supply of goods or services.

4.25. Section 3 of the Transfer of Property Act, 1882 defines actionable claim to mean claim to any debt, other than a debt secured by mortgage of immovable property or by hypothecation or pledge of movable property, or to any beneficial interest in movable property not in the possession, either actual or constructive, of the claimant, which the civil courts recognise as affording grounds for relief, whether such debt or beneficial interest be existent, accruing, conditional or contingent.

4.26. From the above, it can be seen that actionable claims are primarily claims that arise with respect to unsecured debts or a beneficial interest in movable property, regardless of whether such debt or beneficial interest be existent, accruing, conditional or contingent.

4.27. In the case of **Sunrise Associates vs. Govt. of NCT of Delhi & Ors.**[13], the Supreme Court held that,

"an actionable claim is of course as its nomenclature suggests, only a claim. A claim might connote a demand, but in the context of the definition it is a right, albeit an incorporeal one. Every claim is not an actionable claim. It must be a claim either to a debt or to a beneficial interest in movable property. The beneficial interest is not the movable property itself, and may be existent, accruing, conditional or contingent. The

[12] State Bank of India v. Mula Sahakari Sakhar Karkhana AIR 2007 SC 2361
[13] Sunrise Associates v. Govt. of NCT of Delhi & Ors. 2006 (5) SCC 603

movable property, in which such beneficial interest is claimed, must not be in the possession of the claimant. An actionable claim is therefore an incorporeal right."

4.28. At the outset, it is to be noted that corporate guarantee is not beneficial interest in any movable property which is not in possession.

4.29. Let us analyse whether it can be said to be claim to any unsecured debt.

4.30. The meaning of debt can be derived from the ***Law Lexicon*** as*: "a sum of* ***money due*** *under an express or implied agreement; amount due or payable from one person to another in return for money, services, goods or other obligations*."

4.31. In the **Black's law dictionary**, *"a debt is a sum of money due by contract. It is most frequently due by a certain and express agreement, which fixes the amount, independent of extrinsic circumstances. But it is not essential that the contract should be express, or that it should fix the precise amount to be paid."*

4.32. **The most essential feature of debt is that it should for a certain sum of money. Therefore, it has to be an ascertained sum of money that is payable in present or future, due to an existing obligation[14]. Thus, the liability may be conditional or contingent**. An accruing debt is a debt which is not yet actually payable, but is represented by an existing obligation. A few examples of actionable claims are money standing to Credit in a Provident Fund[15], arrears of land, book debts[16], Promissory Note[17] etc. For our purpose, it is necessary to understand a contingent debt, therefore a few example of contingent debt are right to Future Maintenance[18], a letter of credit[19], future rents[20], an amount due under a policy of insurance[21] etc.

4.33. Further, the Supreme court highlighted that Exim Scrips[22] (*M/s Yasha Overseas v. Commissioner of Sales Tax)* and REP licenses[23] (*Vikas Sales Corportion vs. Commissioner of Commercial tax)* **have an intrinsic value and are not convertible/redeemed in money.** Further, such instruments provide a person with an intangible right. However, a claim of unsecured debt has to be a certain sum of money. Thus, these Scrips/Licenses are not actionable claims and are in fact goods. Therefore,

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[14] Commissioner of Wealth-Tax v. Standard Mills Co. Ltd 1963 50 ITR 267 Bom.
[15] Official Trustee v. Chippendale, AIR 1944 Cal 335.
[16] Jugal Kishore v. Raw Cotton Co. Ltd., AIR 1955 SC 376.
[17] Amir Hasan v. Mohammad Nazir Hasan, AIR 1932 All 345
[18] Allimunnisa v. Abdul Aziz, AIR 1936 Pat 527
[19] Jospeh Pyke and Sons (Liverpool) Ltd. v. Kedarnath , (1959) A.C. 328
[20] Poothekka Nachiar v. Annamalai Chetty, (1926) Mad. W.N. 774, 98 I.C. 263, (1926) A.M 1173
[21] Varjivandas v. Maganlal, (1937) 36 Bom. L.R 439, (1937) A.B. 382, 170 I.C. 850
[22] M/s Yasha Overseas v. Commissioner of Sales Tax & Ors. 2008 (8) SCC 681
[23] Vikas Sales Corportion v. Commissioner of Commercial tax AIR 1996 S 2082

it is noteworthy to distinguish between the meaning and scope of a claim of unsecured debt and goods.

4.34. Therefore, it is concluded that a debt is only a money debt which shall be received in cash either in present or in future, and if such an amount is not receivable in cash, then it will not be a debt.

4.35. Accordingly, basis above discussion, it can be argued that corporate guarantee gives rise to an unsecured contingent debt and this debt can be claimed by Banks from parent company in case subsidiaries fails to pay. Hence, it can be contended that corporate guarantee qualifies as actionable claim.

4.36. However, question is whether issuance of corporate guarantee is supply of actionable claim. Let us try to understand the concept of supply of actionable claim through some illustrations.

- Bank provides loan to Company A against interest. Bank ABC gets a right to claim this amount from M/s XYZ, hence, this loan can be said to be an actionable claim. Now, Bank ABC intends to transfer this loan or right to claim the specified amount and this transfer of loan or right to claim loan is a supply of actionable claim.
- House rents: The right to collect the rent arrears can qualify as an actionable claim, but there is an element of service in the form of renting services by landowner as well.

4.37. Hence, there can be different possibilities, wherein after supply of goods or services, recipient or supplier have an actionable claim. But the transaction itself may not be of supply of actionable claim rather it could be of supply of goods or services. Similar to the above illustrations, it can be said that issuance of Corporate Guarantee involves provisioning of assurance services and this transaction is resulting into actionable claim in the hands of Bank or Financial Institutions. In other words, the activity of granting of a corporate guarantee shall not amount to a claim of unsecured debt; however, upon default by the Principal debtor, the surety becomes liable to pay the amount due to the creditor. This amount which is due in money shall qualify as an actionable claim. Hence, GST is payable on issuance of corporate guarantee which qualifies as assurance services.

4.38. Alternatively, a view could be possible that the above illustrations are different due to the fact that in case of corporate guarantee, there is no underlying supply of goods or services except supply of actionable claim i.e., corporate guarantee. In other words, there are no assurance services *per se* and the transaction only involves supply of

actionable claim. Further, even if there is an element of service involved in the transaction, it is not a different supply itself. The service elements involved in the transaction is part of the transaction which predominantly relates to actionable claim.

4.39. However, the above arguments will definitely be disputed by department.

Corporate Guarantee is an actionable claim. However, issuance of corporate guarantee may not qualify as supply of actionable claim.

Valuation of Corporate Guarantees

4.40. The first question which can arise is whether commission charged by the banks for issuing bank guarantee to unrelated parties can be taken as the basis for discharging GST liability As discussed earlier, bank guarantees are not comparable with corporate guarantees. Hence, the commission charged by Banks for corporate guarantee may not be taken for valuation.

4.41. Rule 28 deals with valuation of supplies between related or distinct person. Rule 28 provides for open market value or value of supplies of like kind and quality. Otherwise, Rule 30 or Rule 31 can be resorted. The open market value or value of supplies of like kind and quality is not available in case of corporate guarantees. Hence, Rule 30/31 can be applied.

4.42. Rule 31 provides that where the value of supply of goods or services or both cannot be determined under rules 27 to 30, the same shall be determined using reasonable means consistent with the principles and the general provisions of section 15 and the provisions of this Chapter. Further, it explicitly provides that in the case of supply of services, the supplier may opt for this rule, ignoring rule 30.

4.43. The issue pertaining to the corporate guarantee commission between the related parties, have been raised to determine arm's length price in 'transfer pricing' matters under Income tax. In this regard, reference is made to the cases under the Income Tax Act on this subject.

[24] State Bank of India v. Mula Sahakari Sakhar Karkhana AIR 2007 SC 2361

4.44. In the case of ***The Commissioner of Income Tax vs Everest Kanto Cylinders Ltd. reported at [2015 (5) TMI 395 - BOMBAY HIGH COURT].*** the assessee computed corporate guarantee commission @ 0.5% of the loan amount. The department rejected and argued that the corporate guarantee commission shall be determined by considering the commission rates charged by banks for giving bank guarantee. The High Court observed that the bank guarantees are different from the corporate guarantees and rejected the contentions of department. The rate of guarantee commission @ 0.5% of the loan amount was accepted.

4.45. Further, CBDT has also issued Safe Harbor Rules which provides that in case of corporate guarantee provided to wholly owned subsidiary, the commission or fees will be at the rate of 1% per annum on the amount guaranteed.

4.46. Alternatively, taxpayers can take commission or fees as per the valuation done by registered valuer.

4.47. Hence, as per the discussion, a reasonable value consistent with Safe Harbor Rules and judicial precedents can be taken for valuing supply of service by way of issuance of corporate guarantee service. However, the same should be justifiable before the department.

Commission charged by bank not comparable. A reasonable value could be taken for payment of GST.