TAX ALERT

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Sterlite Power Transmission Limited & Ors. vs. Union Of India & Ors. [TS-1014-HC(DEL)-2026-GST]

Delhi High Court partly allows a batch of writ petitions, and upholds the Goods and Services Tax ("GST") levy on corporate guarantees furnished by holding/group companies for borrowings of related entities, holding that "a corporate guarantee furnished by a holding/group company to a banking company or financial institution, for the borrowings of a related person, is a supply of services under Section 7(1)(c) read with Entry 2 of Schedule I of the Central goods and Services Tax Act, 2017 ("Act of 2017"), even where no consideration is charged."

Facts of the case:

The question of law in the subject batch of petitions was to whether the issuance of a corporate guarantee by a holding/parent company in favour of a financial institution, in respect of the financial obligations of its subsidiary/group company, constitutes a '*supply and/or supply of service*' under Sections 7 and 9 of the Central Goods and Services Tax Act, 2017 ("**Act of 2017**"), consequently making it a taxable event attracting the imposition of Goods and Services Tax ("**GST**") at the rate of 1% under Rule 28(2) of the Central Goods and Services Tax Rules, 2017 ("**Rules of 2017**").

Petitioners therein also challenged Notification No.52/2023-Central Tax dated 26.10.20233 ("**Notification of 2023**") and the Circular No.204/16/2023-GST dated 27.10.2023 ("**Circular of 2023**"), *vide* which sub-rule 2 was inserted into Rule 28, prescribing deemed value of 1% for the supply of services by way of providing corporate guarantee to any banking company or financial institution on behalf of a related person. The applicability and interpretation of the said provision came to be clarified further *vide* Circular of 2023.

In addition, the Petitioners also challenged validity of Notification No.12/2024 dated 10.07.2024 ("**Notification of 2024**"), incorporating the following expressions, "*located in India*" and "*per annum*", into sub-rule 2 of Rule 28 of the Rules of 2017 along with the proviso thereto. A challenge also stands raised towards the Circular No.225/19/2024-GST dated 11.07.2024 ("**Circular of 2024**"), *vide* which the applicability of Rule 28(2) was clarified.

Questions of law framed by the High Court:

Hon'ble High Court framed below questions of law:

a) Whether a corporate guarantee furnished by a holding or group company to a banking company or financial institution, for the borrowings of a related person and without consideration, constitutes a supply of services, under Section 7(1)(c) read with Entry 2 of Schedule I of the Act of 2017 and if so, who is its recipient?

b) Whether such a corporate guarantee stands excluded from the levy either as an 'actionable claim' or as a 'security' as per Section 7(2)(a) read with Entry 6 of Schedule III and Section 2(102) of the Act of 2017?

c) Whether the deemed valuation under Rule 28(2) of the Rules of 2017, as inserted by Notification of 2023 and amended by Notification of 2024, is *intra vires* the Act of 2017 and consistent with Articles 14, 19(1)(g), 246A and 265 of the Constitution?

d) When does the supply take place, and what follows therefrom for guarantees executed before 01.07.2017, guarantees executed between 01.07.2017 and 25.10.2023, and the retrospective operation of IN-2024?

e) Whether Circular of 2023 and Circular of 2024 are *ultra vires* Section 168 of the Act of 2017 or otherwise unsustainable?

Hon'ble High Court held that:

Corporate guarantee furnished by a holding/group company to a banking company or financial institution, for the borrowings of a related person, is a supply of services under Section 7(1)(c) read with Entry 2 of Schedule I of the Act of 2017, even where no consideration is charged. The service lies in the assumption of the risk of the related person's default, and the resulting extension of the guarantor's creditworthiness to it. The recipient of the said service is the related person/subsidiary on whose behalf the guarantee is furnished, under Section 2(93)(c) of the Act of 2017.

Court also held that corporate guarantee is not excluded from the levy, either as an actionable claim under Entry 6 of Schedule III, or as a security under Section 2(102) of the Act of 2017. 123.

Insofar as the valuation is concerned, Court held that Rule 28(2) of the Rules of 2017, as amended by Notification of 2024, is *intra vires* Sections 15 and 164 of the Act of 2017, and is not beyond Article 246A or Article 265 of the Constitution of India. However, insofar as it makes the deemed value of 1% per annum a fixed minimum which cannot be displaced, it is arbitrary and violative of Article 14 of the Constitution of India. Therefore, Rule 28(2) is read down to this extent. Thus, the deemed value shall give way to a lower open market value, where the supplier establishes such value on cogent and verifiable material. However, the consideration agreed between the related persons, or the absence of any consideration, shall not by itself constitute such material. The proviso to Rule 28(2) was held valid.

High Court also held that the supply of a corporate guarantee takes place when it is executed, and again upon each renewal, extension of tenure or enhancement of the guaranteed amount, the value of which is to be determined with reference to the period of renewal or extension, or the amount of enhancement, as the case may be. Court held that corporate guarantee is not a continuous supply of services under Section 2(33) of the Act of 2017. While the tax is to be computed on execution for the entire tenure of the guarantee, the Respondents were held to be at liberty to collect the same in annual instalments over such tenure.

As regards the period to which the levy extends, guarantees executed before 01.07.2017, which have not been renewed, extended or enhanced thereafter, are held not liable to GST. Guarantees executed between 01.07.2017 and 25.10.2023 are held liable to GST; however, they shall be valued under the Rules then in force, without recourse to Rule 28(2), and without applying the figure of 1% through Rule 31. High Court held that Rule 28(2) will apply only to guarantees executed, renewed, extended or enhanced on or after 26.10.2023, and does not apply to a guarantee executed earlier merely because it continues to exist thereafter. Accordingly, the retrospective operation of Notification of 2024 is held as valid. Further, Circulars challenged are held as not *ultra vires.*

VA Comments:

High Court decided against the Petitioners and held that that the taxable activity and the service lies in the guarantor assuming the risk of default by the related person and extending its creditworthiness to facilitate the latter's borrowing. It rejected assessee's contention that such guarantees are excluded from GST either as actionable claims under Entry 6 of Schedule III or as securities u/s 2(102) of the CGST Act.

However, relief is given to the Petitioners on the valuation mechanism under Rule 28(2) of the CGST Rules by reading down the provision as arbitrary and violative of Article 14 insofar as it makes the deemed value of 1% per annum a fixed minimum which cannot be displaced. We can say that the ruling avoids a complete exemption for no-commission guarantees while curbing aggressive, mechanical tax demands based on a rigid 1% floor. Companies seeking a valuation below 1% per annum bear the evidentiary burden of establishing a lower open market value.

Relief is also given to the Petitioners on the time of supply as the High Court clarified that a corporate guarantee is not a continuous supply of services within the meaning of Section 2(33) of the CGST Rules, and the supply takes place upon execution of the guarantee and again upon each renewal, extension of tenure or enhancement of the guaranteed amount, with the value for each subsequent event to be determined with reference to the period of renewal or extension or the amount of enhancement, as the case may be.

On the retrospective levy, High Court further holds that guarantees executed before the introduction of GST and neither renewed, extended nor enhanced thereafter are not liable to GST, but at the same time, guarantees executed between July 1, 2017 and October 25, 2023 are taxable under the valuation rules applicable during that period, without recourse to Rule 28(2) or importing its 1% valuation through Rule 31. Further, emphasises that Rule 28(2), effective from October 26, 2023, applies only to guarantees executed, renewed, extended or enhanced on or after that date, and the mere continued existence of a guarantee executed earlier does not constitute a fresh supply or attract the new valuation mechanism.

For any clarifications, please write to:

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