THE AUTHORITY FOR ADVANCE RULING
IN KARNATAKA
GOODS AND SERVICES TAX
VANIJYA THERIGE KARYALAYA, KALIDASA ROAD
GANDHINAGAR, BENGALURU – 560009

Advance Ruling No. KAR ADRG 48/2020
Date : 16-09-2020

Present:

1. Dr. Ravi Prasad M.P.
   Additional Commissioner of Commercial Taxes . . . . Member (State Tax)

2. Sri. Mashhood Ur Rehman Farooqui,
   Joint Commissioner of Central Tax, ... Member (Central Tax)

1.	Name and address of the applicant	M/s Midcon Polymers Pvt. Ltd., #3, 3rdCross, Lalbagh Road, Near Garuda Maruthi Show Room, Bengaluru-560 027.
2.	GSTIN or User ID	292000000413AR6
3.	Date of filing of Form GST ARA-01	09-07-2020
4.	Represented by	Sri. Ramesh Ananthan C A, Authorised Representative
5.	Jurisdictional Authority – Centre	The Principal Commissioner of Central Tax, Bangalore South Commissionerate.
6.	Jurisdictional Authority – State	LGSTO-70, Bengaluru.
7.	Whether the payment of fees discharged and if yes, the amount and CIN	Yes, discharged fee of Rs.5,000/- under CGST Act vide CIN SBIN20062900296270 dated 29.06.2020 & Rs.5,000/- under KGST Act vide CIN SBIN20072900104086 dated 08.07.2020.

ORDER UNDER SECTION 98(4) OF THE CGST ACT, 2017 & UNDER 98(4) OF THE KGST ACT, 2017

1. M/s Midcon Polymers Pvt. Ltd., (called as the 'Applicant' hereinafter), #3, 3rdCross, Lalbagh Road,Near Garuda Maruthi Show Room,Bengaluru-560 027, having User-ID 292000000413AR6 have filed an application for Advance Ruling under Section 97 of CGST Act,2017 & KGST Act, 2017 read with Rule 104 of CGST Rules 2017 & KGST Rules 2017, in form GST ARA-01, discharging the fee of Rs.5,000/- each under the CGST Act and the KGST Act.

2. The Applicant have proposed/ planned for engaging in the business of renting of commercial property on monthly rents and allied business. They intend to enter in to a contractual agreement of renting of immovable property with an Educational Institution in Bangalore. The Contract is on the basis of the reserved

monthly rent of Rs 1.50 lakhs or Annual Rent of Rs 18.00 Lakhs and also refundable caution deposit of Rs 500 Lakhs, which shall be returned without interest on the termination of the tenancy. Further, since the applicant is required as per law to refund the advance caution deposit, the same does not in anyway determines the quantum of rent.

2.1 The Applicant discharge the statutory taxes levied by the BBMP (Bruhut Bengaluru Mahanagar Palike) and also deposits, which is as per the contract. These taxes being paid on the property and such deduction are legal in respect of valuing the actual receipt of rent under the contract.

2.2 The applicant do not have any taxable activity other than the activity of leasing out Immovable Property commercial spaces and hence they are at present claiming exemption since their turnover is less than Rs.20 Lakhs.

2.3 In view of the above, the applicant sought for advance ruling in respect of the following questions:

i. For the purpose of arriving at the value of rental income, whether the applicant can seek deduction of property taxes and other statutory levies.

ii. For the purposes of arriving at total income from rental, whether notional interest on the security deposit should be taken into consideration.

iii. Whether the applicant is entitled for exemption of tax under the general exemption of Rs.20 lakhs.

3. **Admissibility of the application** : The applicant filed the instant application as an unregistered person, in relation to the proposed business of Renting of Immovable Property for commercial purposes and have sought advance ruling in respect of the questions on the issues covered under Section 97(2)(e) of the CGST Act 2017 and hence the application is admitted.

4. **Applicant's interpretation of law** : The Applicant submits their interpretation of law that Section 15 of the CGST Act 2017 specifies that the value of supply shall include any taxes etc., However, there is no specific description of value of service whether it includes Property tax paid to the Local Authority and whether the same should be taken into consideration. Further there is no provision to include notional interest under the GST Acts.

PERSONAL HEARING / PROCEEDINGS HELD ON 30.07.2020

5. Sri. Ramesh Ananthan, Advocate & duly authorised representative of the applicant appeared for personal hearing proceedings held on 30.07.2020 & reiterated the facts narrated in their application and also furnished written submissions, in support of their argument, inter alia stating as under:

5.1 The interest free security deposit is free from the levy of GST, for the purpose of the valuation, as the same is taken to act as guarantee against damage to properties and fixtures attached, if any, during the lease period. The said security deposit, is returnable after expiry of lease, has no direct link with supply of Renting of Immovable Property service and therefore cannot be said to be a consideration for leasing of property. The applicant also draws attention to Section 15 of CGST Act 2017 with regard to value of the taxable supply and Section 2 (31) of CGST Act, 2017, with regard to definition of "consideration".

5.2 The applicant, quoting the sections supra contends that the value of supply of services shall be the transaction value, which is the price actually paid or payable for the said services. In the instant case, the annual rent is determined and the security deposit is refundable, which shall carry no interest. As such, the applicant is of the opinion, for the purpose of arriving at the taxable value, that only the rent determined has to be taken up for consideration and not the refundable deposit. Further, since the taxes levied on the immovable property by the local corporation is not related to the service of giving the property on rent, the same cannot form a part and parcel of the taxable value. Further as per the definition of consideration is concerned, as per the proviso, the deposit given in respect of supply of services shall not be considered unless the supplier applies such deposit as consideration for the said supply. Even, as per this provision, deposit or interest will not be treated as consideration under the rental service.

5.3 The applicant further relies on Authority on Advance Ruling in the case of M/s. E-Square Leisure Pvt Ltd [2019 (24) GSTL 125 (AAR-GST)], in the case of M/s. Avadh Infratech Ltd [2016 (45) STR 580 (AAR)] and CESTAT Order in the case of M/s. Ashiana Maintenance Services LLP [2019(24) GSTL 47 (Tri. Del)].

6. DISCUSSION & FINDINGS:

6.1 We have considered the submissions made by the Applicant in their application for advance ruling as well as the issues involved & relevant facts having a bearing on the questions in respect of which advance ruling is sought by the applicant.

6.2 At the outset, we would like to state that the provisions of both the CGST Act, 2017 and the KGST Act, 2017 are the same except for certain provisions. Therefore, unless a mention is specifically made to such dissimilar provisions, a reference to the CGST Act would also mean a reference to the corresponding similar provisions under the KGST Act.

6.3 The applicant sought the advance ruling in respect of the questions at para 2.3 supra, which all are in relation to the proposed renting of immovable property service. We take up one question at a time for discussion.

6.4 (a) The first question is whether the property tax & other statutory levies paid/payable by the applicant be deducted from the rental income for the purpose of arriving at the value of rental income. Section 15(2) of the CGST Act 2017 is relevant to the instant issue and is as appended below:

15 (2) The value of supply shall include—

(a) any taxes, duties, cesses, fees and charges levied under any law for the time being in force other than this Act, the State Goods and Services Tax Act, the Union Territory Goods and Services Tax Act and the Goods and Services Tax (Compensation to States) Act, if charged separately by the supplier;

It could easily be inferred from Section 15(2) supra that any taxes, duties, cesses, fees and charges, levied under any law for the time being in force, shall include in the value of taxable supply. In the instant case the property tax is levied, under the Karnataka Municipalities Act 1964, by the BBMP in Bangalore. Further the only exclusions from the value of the taxable supply are the taxes, duties, cesses, fees and charges levied under the CGST Act 2017, SGST (KGST) Act 2017, UTGST Act 2017 & GST(Compensation to States) Act, subject to the condition that they are charged separately by the supplier.

(b) Further Section 15(1) of the CGST Act 2017, with regard to value of the supply, stipulates as under:

"the value of supply of goods or services or both shall be the transaction value, which is the price actually paid or payable for the said supply of goods or services or both where the supplier and the recipient of the supply are not related and the price is the sole consideration of the supply".

It is observed that in the instant case, the supplier (applicant) and the recipient are not related; price is the sole consideration of the supply and monthly rent is the price payable. Thus the monthly rent is the transaction value and the same would be the value of supply of the impugned service of RIS.

In view of the above, we conclude that the property tax is not deductable from the value of taxable supply of "Renting of Immovable Property" service.

6.5 The second question is whether notional interest on the security deposit should be taken into consideration for the purposes of arriving at total income from rental. In this regard we examine relevant clauses of the draft rental agreement furnished by the applicant, which are as under:

2. The lessee shall pay a monthly rent of Rs. 1,50,000/- (Rupees One Lakh Fifty Thousand only) plus applicable taxes, subject to deduction of tax as may be applicable.

3. The lessee shall pay to the lessor, an interest free refundable security deposit of Rs. 5,00,00,000/-(Rupees Five Crore Only) which will be returned to lessee upon vacation of scheduled property.

5. The lessor shall bear and pay the property taxes and cess as applicable to the concerned authorities in regard to the scheduled property.

6.6 This question involves two parts, one being whether the security deposit so collected need to be considered as consideration towards supply of the service and the other being whether the notional interest earned on such security deposit becomes part of value of supply or not.

The security deposit so collected by the applicant shall not be considered as payment made for supply of RIS service unless the applicant applies such deposit as consideration for the said supply, in terms of proviso to Section 2(31)(b) of the CGST Act, 2017. In the instant case the security deposit, is taken as a guarantee against damage to property, is an interest free refundable deposit which will be returned to the lessee at the expiration of the lease period and hence shall not be considered as consideration for the supply of RIS service. However, at the expiry of the lease tenure, if the entire deposit or part of it is withheld and not paid back, as a charge against damages etc., then at that stage such amounts not refunded will be liable to GST.

6.7 The second issue is the notional interest earned out of security deposit. In the instant case, the applicant proposed to collect security deposit of Rs.5 Crore. It is an undisputed fact that the applicant gets interest out of the security deposit. The applicant relied upon certain case laws which are relevant to the Finance Act 1994 and also the ruling of the Authority for Advance Ruling, Maharashtra, in respect of M/s E-square Leisure Pvt. Ltd., wherein it is held that GST is not applicable on security deposit and hence not answered the instant issue of notional interest.

6.8 We observe that in addition to the case laws relied upon by the applicant there are several other orders of CESTAT on the issue of notional interest.

i. M/s K. Raheja Corp Ltd Vs CCE, Pune-III [2015-TIOL-100-CESTAT-MUM]

ii. M/s. Pheonix International Ltd. [Final Order No. 72654/2018 dated 20.11.2018] [Tri.-Allahabad]

iii. M/s. Murli Realtors Pvt Ltd. [2015 (37) STR 618 (Tri.- Mumbai)].

6.9 It is observed, on examination of the case laws supra, that the order of Hon'ble Supreme Court in the case of Commissioner v. I.S.P.L. Industries Ltd. — 2003 (154) E.L.T. 3 (S.C.) has been followed in all the cases. The Apex Court in the said case, which is a similar case & is related to notional interest on security deposits in relation to goods, held that ***notional interest on advances taken by the assesse from the buyers cannot be added to the assessable value of the goods cleared, unless there is evidence to show that the interest free deposit taken has influenced the price.*** Therefore to decide the instant issue two things are required to be considered i.e. whether the notional interest on security deposit

is in relation to the supply of RIS and whether the said notional interest influences the value of the supply i.e. the monthly rent.

6.10. The security deposit is taken invariably in all cases and it is a general practice that wherever the quantum of deposit is higher the rent charged is less and *vice-versa*. The applicant is collecting the security deposit as their property is being leased. Had the property has not been leased, the applicant would not have been collected the security deposit. Thus there is a nexus between security deposit taken and the rent charged beyond doubt.

6.11 The security deposit is collected normally equivalent to 6 months or 12 months rent. Also it is a known fact that the higher the security deposit lower the monthly rent amount. In the instant case, an amount of Rs.5 Crore is proposed to be collected as security deposit and a monthly rent of Rs.1.5 Lacs. However the applicant has not furnished adequate date / information so as to decide whether actually the notional interest influences the monthly rental amount or not.

6.12 Section 2(31)(b) of the CGST Act 2017 stipulates that "consideration" in relation to supply of goods or services or both includes *the monetary value of an act or forbearance, in respect of, in response to, or for the inducement of, the supply of goods or services or both, whether by the recipient or by any other person but shall not include any subsidy given by the Central Government or a State Government.* In the instant case the notional interest that the applicant earns is in respect of supply of RIS service, though is not by the recipient of the service but from other person.

6.13 In view of the above, we conclude that the notional interest has to be considered as part of value of supply of service, if and only if the said notional interest influences the value of supply i.e. value of RIS service / monthly rent and is leviable to GST along with monthly rent at the rate applicable to monthly rent.

7. The last question pertains to whether the applicant is entitled for exemption of tax under the general exemption of Rs.20 lakhs. Section 2 (112) of CGST Act, 2017 defines total turnover in State or Union Territory as aggregate value of all taxable supplies (**excluding the value of inward supplies on which tax is payable by a person on reverse charge basis**) and exempt supplies made within a State or Union territory by a taxable person, exports of goods or services or both and inter-State supplies of goods or services or both made from the State or Union territory by the said taxable person but excludes central tax, State tax, Union territory tax, integrated tax and cess. We find that the interest free security deposit does not come under the purview of supply as per Section 7 of CGST Act, 2017 since it is not a consideration as discussed above. However, the notional interest on security deposit becomes part of consideration along with monthly rent, if it influences the value of the supply. Therefore, in view of the submission made by the applicant that they have no other business besides what they have submitted to this Authority, we find that they are entitled for the general exemption for registration purpose, subject to the condition that their annual total turnover

which includes monthly rent and notional interest, if it influences the value of supply, does not exceed the threshold limit.

8. In view of the foregoing, we pass the following

RULING

1. The applicant can't deduct the property taxes and other statutory levies for the purpose of arriving at the value of rental income.

2. The notional interest on the security deposit shall be taken into consideration, for the purposes of arriving at total income from rental, only if it influences the value supply of RIS service i.e. monthly rent.

3. The applicant is entitled for exemption of tax under the general exemption of Rs.20 lakhs, subject to the condition that their annual turnover, which includes monthly rent and notional interest, if it influences the value of supply, does not exceed the threshold limit

16.09.2020

(Dr.Ravi Prasad.M.P.)
Member MEMBER
Karnataka Advance Ruling Authority
Bengaluru - 560 009

(Mashhood Ur Rehman Farooqui)
Member MEMBER
Karnataka Advance Ruling Authority
Bengaluru - 560 009

Place : Bengaluru

Date : 16-09-2020

To,

The Applicant

Copy to :

The Principal Chief Commissioner of Central Tax, Bangalore Zone, Karnataka.

The Commissioner of Commercial Taxes, Karnataka, Bengaluru.

The Principal Commissioner of Central Tax, Bangalore South Commissionerate, Bengaluru.

The Asst. Commissioner, LGSTO-70, Bengaluru

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