



**PUNJAB AUTHORITY FOR ADVANCE RULING,  
GOODS AND SERVICES TAX, BHUPINDRA ROAD,  
PATIALA 147001, PUNJAB**

①

**ORDER NO. AAR/GST/PB/001 Dated 28.09.2018**

(Note: An Appeal against this order lies with the Appellate Authority in terms of Section 99 and Section 100 of the CGST Act, 2017 and Section 99 and Section 100 of the PGST Act, 2017 within a period of thirty days from the date of communication of this order.)

Name and Address of the Applicant	:	M/s Louis Dreyfus Company India Private Limited Ground Floor, House No. 378 Model Town, Phase-1 Bhatinda, Punjab 151001
GSTIN of the Applicant	:	03AAACL7361E1ZV
Date of application/ Date of Receipt	:	07-06-2018 / 20-06-2018
Date of Personal Hearing	:	13-08-2018
Present for the Applicant	:	Sh. Abhishek Mishra, C.A. & Sh. AnandAggarwal, C.A.

M/s Louis Dreyfus Company India Private Limited, Ground Floor, House No. 378, Model Town, Phase-1, Bhatinda, 151001(Punjab) hereinafter referred to as 'applicant' had submitted an application for advance ruling in form GSTARA-01 vide his letter dated 07.06.2018 received on 20.06.2018 seeking "to determine the applicability of Goods and Services Tax ("GST") on the differential payment received by a party to the aforesaid Contract from the other party to the Contract is event of "Settlement", "Washout" or "Closure" of Contract by it." In this regard, comments from the concerned officer i.e. Assistant Commissioner of State Taxes, Bathinda has been sought. The concerned officer vide his letter No. 5076 dated 03-08-2018 stated that charges received on account of washed away / cancelled contracts for supply of goods are covered under GST as services as per definition of services u/s 2(102) of the Act *ibid*. The activities relating to use of money are clearly covered under services in view of the above



mentioned definition of services. As per the definition of consideration under the Act as per section 2(31)(b) of the CGST, the charges received on account of forbearance for supply of goods are part of consideration. A personal hearing was held on 13.08.2018 before the Advance Ruling Authorities, Punjab. On 13-08-2018, Sh. Abhishek Mishra & Sh. Anand Aggarwal, Chartered Accountants appeared on behalf of the applicant with regard to advance ruling application and reiterated their submissions made in Annexure-1 & Annexure-2 of their advance ruling application dated 07-06-2018. They stated that the activity of M/s Louis Dreyfus Company India Private Limited, Ground Floor, House No. 378, Model Town, Phase-1, Bhatinda, 151001 (Punjab) of signing forward contracts for sale/purchase of Cotton wherein the contract is closed by settlement without supply of goods would not be covered under the term "Services" as defined under section 2(102) of the CGST Act, 2017, in as much as these above said activity would be covered under the term "Securities" which has been excluded from the scope of "Services". They argued that the legal scope of "Services" would prevail over the scope of "Supply" as defined in section 7 of the CGST Act, 2017. They also stressed that the question raised by them in the present advance ruling application has been clarified by the Government in FAQ on Banking, Insurance and Stock Brokers section which is entered at Sr. No. 36 and 37 and available at the website [www.cbic.gov.in](http://www.cbic.gov.in). They further stated that the activity of M/s Louis Dreyfus Company India Private Limited, Ground Floor, House No. 378, Model Town, Phase-1, Bhatinda, 151001 (Punjab), discussed above would not be covered in the term "activities relating to the use of money ....." mentioned in section 2(102) as the term "Securities" has been specifically excluded from the term "Services" and once a specific exclusion has been made in the definition, it cannot be covered under general inclusion. The question raised by the applicant has been discussed at length. The Chartered Accountants for the applicant have nothing more to submit or add in addition to Annexure-1 & Annexure-2 already submitted with the advance ruling application, which are reproduced as follow:

#### **Annexure 1**

#### **Statement of relevant facts having a bearing on the question(s) on which advance ruling is required**

#### **Background**

1. The Applicant is a Company incorporated under the Indian Companies Act, 1956, and is *inter alia* engaged in the business of purchase and sale of cotton, oil and grains. The Appellant, for the purposes of carrying on its business, is registered under the provisions of the Central Goods and Services Tax Act, 2017 (hereinafter referred to as the 'CGST Act') and State Goods and Services Tax Act, 2017 *vide* Goods and Services Tax Identification No. **03AAACL7361E1ZV**.



### Nature of activity proposed to be undertaken by the Applicant

2. In order to stay competitive in the trading of commodities and to ensure minimal profitability in highly volatile commodities market, the Company enters into customized Contracts which are an ensemble of "Supply" cum "Settlement" Contracts. Such Contracts culminate into and entail performance either by way of actual delivery of goods or settlement by payout of differential sum.
3. The Company enters into Sale and Purchase Contracts of aforesaid nature with its customers and vendors respectively, the salient terms of which are produced hereunder for ease of reference:

#### Sale Contract:

A.	Contract no.	SO/GJ/2016-17/202
B.	TT no.	LDC-GJ-1617-1284
C.	Sale Date	13/10/2017
D.	Contract Generation Date	13/10/2017
E.	Quantity	500 (Five Hundred Only) Fully pressed Bales
F.	<u>Specification</u>	
	1. Growth	Indian raw cotton crop 2016/17 (GJ-V797, Gujarat) in
	2. Station	Fully pressed Bales
	3. Staple Length	Ant station of Gujarat Zone at supplier's option
	4. Micronaire	22 mm
	5. Remarks	4.7 NCL-5.5 NCL
	6. Trash	Pre-Approved Lots
	7. Moisture	13% Max 9% max
G.	Type of sale	Spot
H.	Sample Tendering Period	13/10/2017 to 03/11/2017 at Supplier's option
I.	Last date of Payment	03/11/2017
J.	Price	28400 (rupees Twenty Eight Thousand Four Hundred Only) Indian Rupees/ Candy
K.	Taxes	The Price is exclusive of all applicable taxes like the Goods & Service tax, duties, cesses, local taxes and



		any other indirect taxes. Any additional tax burden, duties and cesses etc. at the time of invoicing shall be borne by the recipient.
L.	Incoterms	Ex-Gin/Warehouse, Gujarat (INCOTERMS 2010)
M.	HSN Code	5201
N.	Payment Terms	Margin Money at 10% value of goods (plus taxes) to be paid by recipient to supplier within 3 working days from the contract generation date. Balance payment as per last date of payment.
O.	Cash Discount	Cash discount for a maximum 15 days at the rate of 15% p.a. prorated for early payment before the last date of payment shall be given to recipient, on total contract value including taxes or received amount whichever is lower
P.	Interest on Margin Money	Not Applicable
Q.	Last Payment/ Carry Terms (Supplier's Exclusive Option and sole discretion)	<p>On any unpaid Outstanding amount inclusive of taxes last date of payment (clause I) carry will be charged prorated as follows:</p> <ol style="list-style-type: none"> <li>1. For rest of India except Punjab, Haryana and Rajasthan @ 15% p.a. for first 15 days delay in payment, @ 18% p.a. for next 30 days &amp; @ 24% p.a. thereafter.</li> <li>2. For Punjab, Haryana and Rajasthan @ 16.8% p.a. for first 15 days delay in payment, 18% p.a. for next 30 days &amp; 24% p.a. thereafter.</li> </ol> <p>In any event, all payment along with applicable late payment and carry charges etc. are to be paid by Recipient in full by 30<sup>th</sup> Nov 2017. Similarly, lifting of such cotton is to be completed by 15<sup>th</sup> Dec 2017, beyond which the supplier shall not carry cotton in its warehouse and exercise the supplier's exclusive right as per clause Q above.</p>
R.	Lifting Terms	Lifting is subject to valid delivery order (DO) issued by the supplier as per general terms and agreement

Clause 3 of the General Terms and Conditions applicable to Cotton Sale Contracts / Agreements ("GTC") –



"In case the Recipient fails to make the balance payment / initial margin / mark to market margin (clause 2 of the GTCs) / Carry Charges (Clause Q of the Contract) as per the time period stipulated in the Contract or as and when demanded by the Supplier as the Contractual terms, or delays approval (clause 4 of the GTCs), Supplier has the exclusive right exercisable as its sole discretion to settle / close the Contract, and debit any loss and charges to Recipient's account."

### **Purchase Contract**

A.	PO generation date	09/12/2017
B.	Trade Date	08/12/2017
B.	TT no.	RS 17-18/0297
C.	Contract no.	PO/PB/2017-18/0043
E.	Quantity	110 (One Hundred Ten Only) Fully pressed Cotton Bales. Bales weight of 165 Kg. each. +/- 3.0% variation in weight allowed
F.	<u>Specification</u> 1. Growth 2. Station 3. Variety 4. Grade 5. Staple 6. Micronaire 7. Strength 8. Trash 9. Moisture	Indian raw cotton crop 2017-18 Crop Year Punjab (PB) All Punjab J-34-RJ-RG Midding 28+ mm Minimum 4.0+ NCL 28 GPT Minimum 4 % (1:1 discount above 4%) 9% (Moisture will be checked on spot (at gin) with moisture meter before approval)
G.	Price	INR 4038 (Rupees Four Thousand Thirty Eight Only) / Maund
H.	Taxes	The Price is exclusive of all applicable taxes like the Goods & Services Tax, duties, cesses, local taxes and any other indirect taxes. Any burden due to any additional tax, duties and cesses etc. imposed due to any reason whatsoever at the time of invoicing shall be borne by the Supplier.
I.	Incoterms	FCA (Free Carrier) Gin/Warehouse(Punjab)



		AS PER INCOTERMS 2010
J.	<i>Delivery Period</i>	09/12/2017 to 19/12/2017
K.	<i>Weight Basis</i>	Bale by bale weighing OR Empty/ Loaded Truck weighing will be carried out at the gin at the Supplier's cost in the presence of the Recipient's representative and/ or appointed controller. The Recipient reserves the right to carry out weighbridge empty/ loaded truck/ container weighment immediately upon receipt either at the Recipient's warehouse or port. Max weight loss of 500 gm per bale (i.e. 27.50 Kg for lot of 55 bales, 45 Kg for lot of 90 bales and 50 Kg for lot of 100 bales) allowed between Pressing weights and empty/loaded weights at time of receipt.
L.	<i>HSN Code</i>	5201
M.	<i>Payment Terms</i>	Payment will be made within 8 days from date of pressing but after lifting of goods by the Recipient from Supplier's designated gin/ warehouse.
N.	<i>Cash Discount</i>	Cash discount of 16.8% per 360 days for max 8 days pro-rated will be deducted by the Recipient for early payment on total Invoice value including taxes, if any. Bank charges, if any, to Recipient's account.

Clause 3 of the General Terms and Conditions applicable to Cotton Purchase Contracts / Agreements ("GTC") –

*"In case of non-delivery or failure to fulfill the contract by Suppliers per Specification (Clause F of the contract), the contract will be settled as per CAI Rules and By-laws.*

*Supplier to give written intimation via Broker or directly to the Recipient if it cannot fulfill the delivery of the contracted quantity (Clause E of the contract) as per Specification (Clause F of the contract).*

*For Settlement/ Non-Delivery, average bale weight of: - 162 Kg. for Gujarat/ Maharashtra/ MP/ Lower Rajasthan and 164 Kg. for Telangana/ Karnataka/ AP/ Punjab/ Haryana/ Upper Rajasthan shall be considered.*



**Statement containing Applicant's interpretation of law and / or facts, as the case may be, in respect of the question(s) on which advance ruling is required**

1. The Applicant has approached the Hon'ble Advance Ruling Authority to determine the applicability of Goods and Services Tax ("GST") on the differential payment received by a Party to the aforesaid Contract from the other Party to the Contract is event of "Settlement", "Washout" or "Closure" of Contract by it.
2. In this regard, GST is applicable on supply of goods or services or both. Section 7(1) of the CGST Act, provides that supply includes all forms of supply (of goods or services or both), made for consideration in course or furtherance of business such as sale, transfer, barter, exchange, license, rental, lease or disposal. Section 7(1) of the CGST Act reads as under:

*"7. (1) For the purposes of this Act, the expression "supply" includes—*

  - (a) all forms of supply of goods or services or both such as sale, transfer, barter, exchange, licence, rental, lease or disposal made or agreed to be made for a consideration by a person in the course or furtherance of business;*
  - (b) import of services for a consideration whether or not in the course or furtherance of business;*
  - (c) the activities specified in Schedule I, made or agreed to be made without a consideration; and*
  - (d) the activities to be treated as supply of goods or supply of services as referred to in Schedule II."*
3. It is apparent that in case of "Settlement", "Washout" or "Closure" of Contract, there is no supply of goods (i.e. Cotton in the instant case) and applicability of GST on supply of goods is as a corollary not triggered.
4. It is, however, important to determine whether any Service is being transacted between Parties to the Contract in event of "Settlement", "Washout" or "Closure" of Contract by either of such Parties to completely rule out the possibility of GST implications in eventuality of "Settlement", "Washout" or "Closure" of Contract. In



*MCX price for forward contracted month/ CAI spot price or mutually agreed price to be used for establishing mark to market differential for mutual settlement."*

4. It is apparent that the intention of the Parties is to effect supply of cotton pursuant to execution of aforesaid Contracts. The Contracts also stipulates well defined methodology for settlement / closure of Contract (generally referred to as "closure" or "washout" of contract), in the event of Supply of goods not being effected by Supplier of cotton or payment not being made by recipient of goods. The "closure" or "washout" of aforesaid Contracts is necessarily a fall out or unequivocal resultant of Contractual terms.
5. In case of supply of cotton effected in terms of Contract, the Recipient of cotton is required to pay sum pre-specified in the Contract against supply of pre-determined quantity of cotton.
6. On the other hand, in case of "closure" or "washout" of aforesaid Contracts, the party to the Contract which opts for such "closure" or "washout" is required to pay to the other party a sum equivalent to difference between the Settlement rate and the rate of cotton at which the supply of the same is agreed upon.
7. The Settlement rate is enshrined in the Contract to be as follows:

Sale Contract – It is discretionary upon the Company to settle / close the Contract at the rate fixed by it. In this regard, the rate at which the Company settles is usually the market rate of cotton prevalent on the Commodities Exchange such as MCX on the day on which such settlement is made.

Purchase Contract – Market rate of cotton prevalent on Commodities Exchange such as MCX on the day on which such settlement is made.

The fixation of rate as per the Contract is binding on the other Party to the Contract without any room for aberration or further deliberation / negotiation. The rate at which the Parties had agreed to settle the Contract in the event of non-delivery of cotton is sacrosanct and any deviation to the same is to be construed as violation of Contractual terms with potential of causing dispute and resultant arbitration proceedings, which is also in-built in the Contracts itself.



this regard, reference is made to serial no 5(e) of Schedule II of the CGST Act, which is reproduced below for ease of reference:

5

*"Agreeing to the obligation to refrain from an act or to tolerate an act or situation or to do an act"*

5. Schedule II of the CGST Act provides for specific transactions on which GST applies. In other words, Schedule II is an exhaustive compendium of transactions on which GST applicability is re-emphasized by inclusion in the said Schedule. GST would have applied on such transactions invariably even in absence of Schedule II if such transactions qualified as supply of goods and/ or services. Hence, Schedule II of the GST Act is merely clarificatory in nature and in no manner tends to expand the ambit of transactions on which GST applies under the GST laws.
  6. In the above backdrop, Serial No 5(e) of Schedule II should be construed to mean that GST liability arises in the eventualities enlisted below as the same would be deemed to be supply of "services" under the GST law:
    - agreeing to the obligation to refrain from an act;
    - agreeing to the obligation to tolerate an act or situation
    - agreeing to the obligation to do an act
  7. It is noteworthy that the aforesaid Entry in Schedule II is a combination of two activities on part of the deemed supplier of services, which are as follows:
    - An overt act to agree to the obligation
    - An activity which follows the agreement to the obligation i.e. to actually refrain from an act or to actually tolerate an act or situation
- A combination of aforesaid two acts would result into rendering of "Service" in terms of Serial No. 5(e) of the Schedule II read with Section 7 of the CGST Act.
8. In the present factual matrix, neither of the aforesaid two acts take place as the payment of differential amount is a fall out of the contractual terms and can at best be termed as financial settlement of claim arising from non-performance of Contract by one of Parties to such Contract. At the time of settlement, the "agreeing" to "obligation" does not arise of free will or discretion of the other party



but is imposed on such party to follow in terms of the Contractual terms. In other words, there is nothing left to agree on the part of the Party which opts to "Washout" the Contract as payment of differential sum is an obligation which devolves on it due to the terms of the Contract which mandate payment of a sum pre-decided in the Contract for supply of Cotton.

9. There is no discretion vested on the other Party to the Contract as it is bound by the Contractual terms to accept the Settlement and the payment of differential sum thereof. The second pre-requisite act of either "refrain from an act" or actually "tolerate an act or situation or to do an act" is not fulfilled in the instant case as both the Parties to the Contract are bound by Contractual terms to settle the Contract financially. None of the Parties to the Contract perform an "act" or tolerate the same either in lieu of the transaction involving financial settlement. In simple words, the Party which faces the proposition of the other Party to "Washout" the Contract cannot do anything but accept the exclusive fall out of "Wash out" of Contract i.e. to accept the payment for settling the non-delivery financially. If either of the Parties do not follow the financial settlement as per the terms of the Contract, arbitration entails. In this regard, it would be too far-fetched to state that the Party which faces the "Washout" tolerated such act of the other Party to the Contract by not opting for arbitration and hence rendered a "Service" in terms of the GST Act. Not taking a legal recourse envisaged by the Contract cannot be termed as "Service" as the same cannot qualify as "refraining from an act" or "to tolerate an act or situation".
10. In this regard, reference may be made to Para 6.7.1 of the Education Guide issued by Central Board of Excise and Customs in respect of earlier Service Tax regime governed by Chapter V of Finance Act, 1994 wherein a similar entry existed in the list of Services termed as "Declared Services":

*"6.7.1 Would non-compete agreements be considered a provision of service?"*

*Yes. By virtue of a non-compete agreement one party agrees, for consideration, not to compete with the other in any specified products, services, geographical location or in any other manner. Such **action** on the part of one person is also an activity for consideration and will be covered by the declared services."*

11. The above explanation of "agreeing to an obligation to refrain from an act or to tolerate an act or situation or to do an act" by way of an example is apt as in such case one of the Parties agrees, out of his free will and discretion, to enter into a



non-compete agreement and also takes an "action" by not competing with the other Party to the Contract. Both the said ingredients of "agreeing to an obligation" and "to refrain from and act or to tolerate an act or situation or to do an act" are being fulfilled and hence qualification of such "actions" in unison qualify as "Service" in terms of erstwhile Service tax law governed by Chapter V of the Finance Act, 1994. On the other hand, in the present factual matrix, neither following the exclusive mandate of the Contract is "agreeing to an obligation" nor not opting to take legal recourse i.e. to arbitrate can qualify as "refrain from and act or to tolerate an act or situation or to do an act".

12. In light of the above argument, it emerges that payment of differential sum by the Party to the Contract for effecting "Washout" of the Contract can at best be construed as financial settlement and not a consideration for "Service" and hence should not entail any GST implications.
13. On the other hand, notwithstanding the above, reference is made to definition of "goods" and "services" under the GST law.

Section 2(52) of the CGST Act

*"goods" means every kind of movable property **other than money and securities** but includes actionable claim, growing crops, grass and things attached to or forming part of the land which are agreed to be severed before supply or under a contract of supply"*

In terms of above, 'goods' means every kind of movable property and includes actionable claims, growing crops, grass and other things which are to be severed before supply. However, "Securities" and "Money" is specifically excluded from the definition of goods.

14. Further, Section 2(102) of the CGST Act defines 'services', reads as follows:

*"services" means anything other than goods, money and securities but includes activities relating to the use of money or its conversion by cash or by any other mode, from one form, currency or denomination, to another form, currency or denomination for which a separate consideration is charged"*

Section 2(102) defined services as 'anything other than goods, money and securities'.



15. "Securities" has been defined in Section 2(101) of the CGST Act to read as under:

*"Securities shall have the same meaning as assigned to it in clause (h) of Section 2 of the Securities Contracts (Regulation) Act, 1956."*

16. The definition of 'securities' as given in clause (h) of Section 2 of the Securities Contracts (Regulation) Act, 1956 ("SCRA") is as follows:

*"(h) "securities include-*

*(i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;*

***(ia) derivative;***

*(ib) units or any other instrument issued by any collective investment scheme to the investors in such schemes;*

*(ic) security receipt as defined in clause (zg) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;*

*(id) units or any other such instrument issued to the investors under any mutual fund scheme;*

*(ii) Government securities;*

*(iia) such other instruments as may be declared by the Central Government to be securities; and*

*(iib) rights or interest in securities."*

From the above, it appears that 'securities' include derivative, amongst other things.

17. As per in clause (ac) of the Section 2 of the SCRA, 'derivative' includes:

*"a security derived from a debt instrument, share, loan, whether secured or unsecured, risk instrument or contract for differences or any other form of security;*

*(a) a contract which derives its value from the prices, or index of prices, of underlying securities;]*

*(b) **commodity derivatives;** and*



- (c) such other instruments as may be declared by the Central Government to be derivatives;]"

18. The term "commodity derivatives" is defined as Section 2(bc) of SCRA, to read as follows:

*"commodity derivative means a contract —*

- (i) ***for the delivery of such goods, as may be notified by the Central Government in the Official Gazette, and which is not a ready delivery contract; or***
- (ii) *for differences, which derives its value from prices or indices of prices of such underlying goods or activities, services, rights, interests and events, as may be notified by the Central Government, in consultation with the Board, but does not include securities as referred to in sub-clauses (A) and (B) of clause (ac);]"*

19. In this regard, reference is made to Entry No. 59 of Notification No. S.O. 3068(E) dated 27 September 2016 issued under Section 2(bc) of the SCRA which includes Cotton as follows:

*"Cotton Complex (including Kapas, fibre, loose, half pressed, full pressed, yarn, pods, cloth)*

20. Further, reference is made to Section 2(ea) of the SCRA which defines "Ready Delivery Contract" to mean as under:

*"ready delivery contract" means a contract which provides for the delivery of goods and the payment of a price therefor, either immediately, or within such period not exceeding eleven days after the date of the contract and subject to such conditions as the Central Government may, by notification in the Official Gazette, specify in respect of any goods, the period under such contract not being capable of extension by the mutual consent of the parties thereto or otherwise:*

***Provided that where any such contract is performed either wholly or in part:***



- (I) ***by realization of any sum of money being the difference between the contract rate and the settlement rate or clearing rate or the rate of any offsetting contract; or***
- (II) ***by any other means whatsoever, and as a result of which the actual tendering of the goods covered by the contract or payment of the full price therefor is dispensed with, then such contract shall not be deemed to be a ready delivery contract; ]***

21. On a conjoint reading of the above provisions of SCRA, it emerges that Contract entered into for supply of cotton should qualify as "Commodity Derivative" in the scenario where Contract is settled financially pursuant to which physical delivery of Cotton does not take place.
22. It is apparent that "Commodity Derivatives" are included in the definition of "Derivatives" and in turn the same is included in the definition of "Securities". "Securities" are specifically excluded from the definition of "goods" and "services".
23. This is supported by Frequently Asked Questions ("FAQ") no. 36 & 37 issued by GST authorities. The relevant extract if said FAQ is reproduced hereunder for easy of reference:

S.no.	Question	Answer
36	Would 'future contracts' be chargeable to GST?	<p><i>Future contracts are in the nature of financial derivatives, the price of which is dependent on the value of underlying stocks or index of stocks or certain approved currencies and the settlement happens normally by way of net settlement with no actual delivery.</i></p> <p><b><i>Since future contracts are in the nature of derivatives these qualify as 'securities' as defined in Section 2(101) of the CGST Act, 2017. As securities are neither 'goods' nor 'services' as defined in the CGST</i></b></p>



		<p><b>Act, 2017, future contracts are not chargeable to GST.</b> But where the future contracts have a delivery option and the settlement of contract takes place by way of actual delivery of underlying commodity/currency, then such forward contracts would be treated as normal supply of goods and liable to GST.</p> <p>Further, if some service charges or service fees or documentation fees or broking charges or such like fees or charges are charged, the same would be a consideration for supply of service and chargeable to GST</p>
37	<p>Would forward contracts in commodities or currencies be within the ambit of definition of 'supply'?</p>	<p>A forward contract is an agreement, executed, to purchase or sell a predetermined amount of a commodity or currency at a pre-determined future date at a pre-determined price.</p> <p>The settlement could be by way of actual delivery of underlying commodity/currency or by way of net settlement of differential of the forward rate over the prevailing market rate on the settlement date.</p> <p>Where the settlement takes place by way of actual delivery of underlying commodity / currency, then such forward contracts would be treated as normal supply of goods and liable to GST.</p> <p><b>Where the settlement takes place by way of net settlement of differential of the forward rate over the</b></p>



		<p><b>prevailing market rate on the settlement date, the same would be falling within the purview of 'securities' as defined in Section 2(101) of the CGST Act, 2017. As securities are neither 'goods' nor 'services' as defined in the CGST Act, 2017, future contracts are not chargeable to GST.</b></p> <p><i>However, if some service charges or service fees or documentation fees or broking charges or such like fees or charges are charged, the same would be a consideration for supply of service and chargeable to GST.</i></p>
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Accordingly, the differential payment made for financially settling the Contract for supply of Cotton can be said to have been made against transaction in "Securities", which cannot entail GST implications as GST is applicable only on the supply of "goods" or services" or both, which is not the case herein.

### **Discussion and Findings:**

We have carefully gone through the case details submitted by the party along with annexures and the relevant legal provisions required to answer the questions raised by the applicant. The question which had been posed by the applicant in Sr. No. 14 of Form GST ARA-01, in the context of activity of sale/purchase of Cotton by the applicant, was: *"To determine the applicability of GST on the differential payment received by a party to the aforesaid contract from the other party to the contract is (in) event of "settlement", "washout" or "closure" of contract by it."*

2. To answer this question, we would first like to go through the legal structure under the CGST Act, 2017 (which should be hereinafter read to also mean Punjab GST Act, 2017, the provisions in both Acts being similar) imposing the tax. The charging Section i.e. Section 9 reads as follows: "1) .....there shall be levied a tax called the central goods and services tax on all intra-State supplies of goods or services or both, except on the supply of alcoholic liquor for human consumption, on the value determined under section 15 and at such rates, not exceeding twenty per cent., as may be notified by the Government on the recommendations of the Council and collected in such manner as may be prescribed and shall be paid by the taxable person"



Further, the scope of supply has been laid down in Section 7 of the CGST Act, 2017. Relevant portion of which reads as under:-

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*"7 (1) For the purposes of this Act, the expression "supply" includes – all forms of supply of goods or services or both such as sale, transfer, barter, exchange, licence, rental, lease or disposal made or agreed to be made for a consideration by a person in the course or furtherance of business;*

.....

.....

*(d) the activities to be treated as supply of goods or supply of services as referred to in Schedule II.*

....."

Further, the para 5(e) of Schedule II referred to in Section 7(1)(d) reads as follows:

*"5. Supply of services The following shall be treated as supply of services, namely:— (e) agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act; ..."*

3. Regarding whether the question of the applicant can be treated as supply of goods, it is seen that the contention of the applicant is that in case of "Settlement", "Washout" or "Closure" of Contract, there is no supply of goods, therefore GST on supply of goods is not applicable. This would be required to be tested against the expressions "sale, transfer, barter, exchange, licence, rental, lease or disposal" mentioned in Section 7(1)(a) to see whether the situation of closure of the contract as per agreed terms, would be covered under these. While it is clear that this activity is not a sale transfer, barter, exchange, licence, rental or lease, it is also apparent that the situation of closure of contract which was related to supply of goods, would also not be covered under the term disposal. The term disposal carries a connotation that the goods physically leave the possession of the supplier, which is not the situation in the present case. Therefore, we reach the conclusion that the scenario of closure of contract by the applicant or its other contracting party would not amount to supply of goods and therefore, no goods and service tax would be applicable as far as supply of goods is concerned.

4. Now, it needs to be seen whether the activity of closure of contract by the applicant or the other contracting party would fall under the scope of the term 'service' or under the scope of the term 'supply' under GST law. It is clear that once an activity does not fall under scope of the term 'service', it becomes immaterial whether it falls under scope of the term 'supply' for deciding questions of applicability of tax on services under Section 9. The Section 2 (102) of CGST Act, 2017 defines 'Services' as under-

*"Services means anything other than goods, money and securities but includes activities relating to the use of money or its conversion by cash or by any other mode, from one form, currency or denomination, to another form, currency or denomination for which a*



*separate consideration is charged*". The applicant claims that his activity of closure of contract by way of settlement is covered under the term 'securities' which have been specifically excluded from the definition of 'Services' under CGST Act, 2017, a situation which would entail no taxation. This claim of the applicant requires examination under legal provisions.

**4.1** The Section 2 (101) of CGST Act, 2017 defines 'Securities' as "*Securities shall have the same meaning as assigned to it in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956);*". The definition of 'Securities' as given in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956) (SCRA) is as follows:

*"(h) securities include-*

*(i).....*

*(ia) derivative;*

*....."*

From the above definition of 'securities', it is clear that securities include derivative.

**4.2** Further, Section 2 (ac) of SCRA defines 'derivative' as:

*"derivative"— includes*

*(A) .....*

*(B) .....*

*(C) commodity derivatives; and*

*(D) ....."*

The term "commodity derivatives" is defined as Section 2 (bc) of SCRA, to read as follows:

*"commodity derivative means a contract –*

*(i) for delivery of such goods, as may be notified by the Central Government in the Official Gazette, and which is not a ready delivery contract; or*

*(ii) ....."*

The Central Government has notified 'Cotton complex (including Kapas, fibre, loose, half-pressed, full-pressed, yarn, pods, cloth)' in commodity derivatives vide Entry No. 59 of Notification No. S.O. 3068 (E) dated 27.09.2016 for the purposes of clause (bc) of section 2 of the said Act. Further, to decide whether the activity of closure of contract being examined in the present case is covered under 'ready delivery contract', we need to refer to Section 2 (ea) of SCRA which defines 'ready delivery contract' as:

*"ready delivery contract means a contract which provides for the delivery of goods and the payment of a price therefore, either immediately, or within such period not exceeding eleven days after the date of contract and subject to such conditions as the Central Government may, by notification in the Official*



Gazette, specify in respect of any goods, the period under such contract not being capable of extension by the mutual consent of the parties thereto or otherwise:

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*Provided that where any such contract is performed either wholly or in part:*

- (i) by realization of any sum of money being the difference between the contract rate and the settlement rate or clearing rate or the rate of any offsetting contract; or*
- (ii) by any other means whatsoever, and as a result of which the actual tendering of goods covered by the contract or payment of the full price therefor is dispensed with, then such contract shall not be deemed to be a ready delivery contract."*

**4.3** While examining legal provisions to understand the meaning of the Term 'securities' under the SCRA, it becomes important to understand Section 18A of SCRA which lays down that:

*"18A. Notwithstanding anything contained in any other law for the time being in force, contracts in derivative shall be legal and valid if such contracts are—*

- (a) traded on a recognised stock exchange;*
- (b) settled on the clearing house of the recognised stock exchange, in accordance with the rules and bye-laws of such stock exchange.*
- (c) between such parties and on such terms as the Central Government may, by notification in the Official Gazette, specify"*

**4.4** The applicant has not laid any information which points to the transactions regarding sale/ purchase of cotton and closure of such contracts being traded on recognised stock exchange or being settled on the clearing house of the recognised stock exchange or the contracting parties and the terms being notified by the Central Government. Therefore, on harmonious reading of above provisions of SCRA, especially in view of the said Section 18A, it emerges that the term securities which covers commodity derivatives refers to only those contracts which are traded or settled in recognised stock exchange, unless the contracts are notified by the Central Government. By this measure, the claim of the applicant that the closure of purchase/sale of cotton contract by way of settlement between him and the other contracting party in terms of the contract, would be covered under the term 'securities' in the definition of 'services' in Section 2(102) of the CGST Act, 2017 and hence would not entail tax on services, does not seem to be valid.

**5.** Therefore, while it is forthcoming that legal provisions discussed above do not exclude the closure of purchase/sale of cotton contract by way of settlement between applicant and the other contracting party in terms of the contract from scope of services, and the applicant would therefore be liable to the provisions of Section 9 of the CGST Act, 2017,



it is also noteworthy that executive instructions by way of answers to Frequently Asked Questions (FAQs) published under the FAQs on Financial Service on the Central Board of Indirect Taxes and Customs (CBIC) website [www.cbic.gov.in](http://www.cbic.gov.in) include settlement under forward contracts within the purview of 'securities' as defined in Section 2(101) of the CGST Act, 2017. The extract of the relevant FAQ No. 37 is reproduced below:

37.	Would forward contracts in commodities or currencies be within the ambit of definition of 'supply'?	<p>A forward contract is an agreement, executed, to purchase or sell a pre- determined amount of a commodity or currency at a pre-determined future date at a pre-determined price. The settlement could be by way of actual delivery of underlying commodity/currency or by way of net settlement of differential of the forward rate over the prevailing market rate on the settlement date.</p> <p>Where the settlement takes place by way of actual delivery of underlying commodity/currency, then such forward contracts would be treated as normal supply of goods and liable to GST.</p> <p><b>Where the settlement takes place by way of net settlement of differential of the forward rate over the prevailing market rate on the settlement date</b>, the same would be falling within the purview of 'securities' as defined in Section 2(101) of the CGST Act, 2017. As securities are neither 'goods' nor 'services' as defined in the CGST Act, 2017, future contracts are not chargeable to GST. However, if some service charges or service fees or documentation fees or broking charges or such like fees or charges are charged, the same would be a consideration for supply of service and chargeable to GST.</p>
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Therefore, it is evident that intention of the Government, evident from the answer to the above FAQ, is not to tax settlements under forward contracts where settlement takes place by way of net settlement of differential of the forward rate over the prevailing market rate on the settlement date. Therefore, we feel that if the executive instruction interprets legal provisions in a manner which provides relief to a taxpayer and publishes these on its website, such relief should flow to the taxpayer.

6. However, once such an executive decision passes on relief to a taxpayer, it is natural that the relief must be to the extent mentioned in such executive decision. In the answer to FAQ No. 37 it had been inter-alia specified that *"Where the settlement takes place by way of net settlement of differential of the forward rate over the prevailing market rate on the settlement date, the same would be falling within the purview of 'securities' as defined in Section 2(101) of the CGST Act, 2017. As securities are neither 'goods' nor 'services' as defined in the CGST Act, 2017, future contracts are not chargeable to GST."* But in para 7 of Annexure – I to the Advance Ruling Application filed by the applicant



wherein he had described the nature of activities in respect of which advance ruling had been sought, settlement rate has been described in the contract as follows:

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*"Sale Contract – It is discretionary upon the Company to settle/ close the Contract at the rate fixed by it. In this regard, the rate at which the company settles is usually the market rate of cotton prevalent on the Commodities Exchange such as MCX on the day on which such settlement is made."*

*Purchase Contract- Market rate of cotton prevalent on Commodities Exchange such as MCX on the day on which such settlement is made".*

7. It is seen that the settlement rate described by the applicant in sale contract is at variance from the settlement considered to be falling within the purview of securities as defined in Section 2(101) of the CGST Act, 2017 in the answer to FAQ No. 37. In the answer to FAQ No. 37, the settlement was described as differential of the forward rate over the prevailing market rate on the settlement date, while in the sale contract of the applicant, he has discretion to settle/ close the Contract at the rate fixed by him which may vary from sale price of cotton on commodity market on the day of settlement. The terms of purchase contract mentioned by the applicant are however in line with the settlement envisaged in answer to FAQ No. 37. Therefore, it follows that the purchase contracts entered between the applicant and the other contracting party where settlement is made without supply of goods on the above terms, the activity would be covered under the term 'securities' and therefore would not entail tax.

8. However, in sales contracts entered between the applicant and the other contracting party, where settlement is made without supply of goods on the above terms in as far as the applicant considers a discretionary price other than the market price of cotton on the day of settlement, these would not be covered under the term 'securities' and would therefore become subject to section 9 and section 7 of the CGST Act, 2017. In the schedule II to Section 7, inter-alia, *agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act is to be treated as supply of services.*

9. In the present case, there is clearly an agreement between the contracting parties to refrain from bringing in arbitration, which is also built in the contract, if the contract is settled by payment of agreed amount of monies. Therefore, this activity can clearly be considered as supply of service by 'agreeing to the obligation to refrain from an act', and would therefore be subject to applicable tax. The present activity is also a toleration of the act of not providing the other party to the contract, the agreed quantity of goods at agreed prices at the agreed date, on payment of agreed amount of monies to settle the contract. Therefore, this would be liable for consideration as supply of service by way of agreeing to the obligation to tolerate an act or a situation. It is also clear that the applicant and the other contracting party are agreeing to the obligation of doing an act



viz. settling the contract by payment of agreed amount of monies if goods are not delivered in terms of the contract, and therefore this activity of theirs, by this measure too, is to be treated as supply of services and liable to taxation under provisions of CGST Act, 2017.

Therefore, it is seen that the activity of closure of the sale contract of cotton by either of the contracting parties by way of settlement considering a price different from the market price of cotton on the day of settlement would be a supply of service under each of the three limbs i.e. agreeing to the obligation to refrain from an act, agreeing to the obligation to tolerate an act or a situation, or agreeing to the obligation to do an act, mentioned in para 5(e) of Schedule II to Section 7 of the CGST Act, 2017.

9. The comments of the jurisdictional officer sent vide letter No. 5076/CCI dated 3.8.2018 on the Advance Ruling filed by the applicant were to the effect that since the activity of closing contracts by way of settlement was covered under the term 'use of money' in the definition of Services under Section 2(102), and for which a consideration was also being received, it was a service and liable to taxation. The jurisdictional officer also relied upon an Advance Ruling passed by the Maharashtra Authority for Advance Ruling in support of his view. Perusal of the definition of Service in Section 2(102) shows that the specific inclusions which follow the specific exclusions, have to be read completely and not in piecemeal. We feel that the words 'use of money' cannot be read in isolation as has been done by the jurisdictional officer while interpretation of the legal definition of Services. The Advance Ruling passed by the Maharashtra Authority for Advance Ruling was on completely different facts and had nothing in common with the specific question raised by the applicant. Therefore, we feel that the comments of the jurisdictional officer do not address the questions raised by the applicant in the present Advance Ruling application and therefore are not relevant while deciding the present application.

10. In view of the above discussion and Findings we pronounce the following Advance Ruling on the question *"To determine the applicability of GST on the differential payment received by a party to the aforesaid contract from the other party to the contract in event of "settlement", "washout" or "closure" of contract by it."* posed by M/s Louis Dreyfus Company India Pvt. Ltd in the context of purchase/ sale contracts of cotton, and specified in their Application dated 7.6.2018 under provisions of Section 98(4) of the CGST Act, 2017:

#### **Advance Ruling**

- (i) In forward contracts in cotton sales, being settled by M/s Louis Dreyfus Company India Pvt. Ltd. with the other party to the contract by way of payment of the differential of forward rate and prevailing market rate on the settlement date, the same would be falling within the purview of 'securities' as defined in Section 2(101) of the CGST Act, 2017 and would therefore not be chargeable to GST.



- (12)
- (ii) In forward contracts in cotton sales, being settled by M/s Louis Dreyfus Company India Pvt. Ltd. with the other party to the contract by way of payment of the differential of forward rate and rate fixed by the applicant using his discretion, such rate being different than the market price of cotton on the date of settlement, the same would not be falling within the purview of 'securities' as defined in Section 2(101) of the CGST Act, 2017 and would therefore be chargeable to GST.
- (iii) In the forward contracts in cotton purchase being settled by M/s Louis Dreyfus Company India Pvt. Ltd. with the other party to the contract by way of payment of the differential of forward rate and prevailing market rate on the settlement date, the same would be falling within the purview of 'securities' as defined in Section 2(101) of the CGST Act, 2017 and would therefore not be chargeable to GST.

*(Note: It may be noted that this Advance Ruling is based on the contract conditions conveyed by the applicant in his Advance Ruling Application and may not be applicable to contracts with differing conditions)*

*B. Bhinder*  
Navdeep Bhinder  
Member, SGST  
*28/9/2018*

*G.S. Bains*  
G.S. Bains  
Member, CGST  
*28.9.2018*

No. AAR/Punjab/18/246-51

Dated: 01/10/18

To

M/s Louis Dreyfus Company India Private Limited,  
Ground Floor, House No. 378,  
Model Town, Phase-1, Bhatinda, 151001 (Punjab)  
GSTIN :03AAACL7361E1ZV

Copy to:

1. The Special Secretary, Goods and Service Tax Council, 5<sup>th</sup> floor, Tower-II, JeevanBharti Bldg., Connaught Place, New Delhi w.r.t. F. No. 193/Advance Ruling/ GSTC/2017 dated 01.05.2018.
2. The Commissioner of State Taxes, Punjab.
3. The Commissioner, CGST, Ludhiana, GST Bhawan, Rishi Nagar, Ludhiana
4. The Assistant Commissioner of State Taxes, Bathinda.
5. The Assistant Commissioner CGST Division-I and II Bhatinda, MR Complex, Model Town, Phase II, Bhatinda

*Revised*  
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