

TAX LIABILITY IN BAILMENT UNDER GOODS AND SERVICES TAX REGIME- AN ANALYSIS

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ABSTRACT

Goods and Services Tax ('GST'), which took effect from 1st July 2017 levies tax on all goods and services at the time of taxable event of 'supply'. The term supply as defined in Section 7 of the Central Goods and Service Tax, 2017 ('CGST Act') has a very wide scope and includes almost all the commercial transactions within its ambit barring a few exceptions. Section 7(1) of the CGST Act defines supply to include sale, transfer, barter, exchange, license, rental, lease or disposal or Importation of services for consideration when made in course or furtherance of business. In light of such wide coverage of the term 'supply', it becomes pertinent to analyse the implications of GST on the transactions under the contract of bailment. Section 148 of Indian Contract Act, 1872 provides that bailment is delivery of goods by one person to another for some purpose to be accomplished and upon accomplishment of such purpose, the goods are returned or otherwise disposed of according to the directions of the bailor. Thus, a contract of bailment involves movement of goods from bailor to bailee and *vice versa* (upon completion of the job) and it also involves a 'purpose', which may constitute a service under GST, which the bailee performs on such goods on the instructions of the bailor. Therefore, the implication of GST on such a contract is required to be analysed as to which leg of the transaction / activity is taxable under GST.

Key words: Bailment, Delivery, Supply, Goods and services tax

1. INTRODUCTION

The advent of goods and service tax (GST) has revolutionised the taxation regime in India and has been welcomed as a desirable change. It has introduced the idea of one nation one tax. The introduction of this novel concept of goods and services has its implications on various transactions because of the new taxation regime under the Goods and Services Tax legislation recently introduced in India. Under the new indirect tax regime it is important for ascertaining taxability of the transaction that it should fall in the category of 'supply' defined under Section 7 of Central Goods Services Tax Act, 2017. This has fundamentally altered the taxability of various transactions and requires clarity for the purpose of its implementation.

Bailment is one such transaction that requires some clarity in view of its nature and components involving 'delivery' of goods as well as 'service'. In view of the peculiar nature of the transaction of bailment, the issue of taxability might arise at two stages. One, at the stage of delivery of goods and two, at the stage of providing service. The scope of this paper is limited to ascertaining the liability of tax in case of transaction of bailment. The main aim of this paper is to split and analyse the transaction of 'bailment' for the purpose of levy of Goods and Services Tax ('GST'), since GST is levied on all goods and services at the time of taxable event of 'supply', since 1st July 2017. Therefore, it is pertinent to ascertain whether tax would be levied on the delivery of goods or on the services rendered or on both. Clear understanding of the concept of bailment for the purpose of levy of goods and service tax would require a detailed analysis of the various aspects of bailment in the light of relevant provisions of taxation law.

2. HISTORY OF GOODS AND SERVICES TAX IN INDIA

The concept of goods and services tax was first introduced in the year 2000 by Sh. Atal Bihari Vajpayee, who was the then Prime Minister of India. A committee was constituted for designing the model of GST. After the introduction of this concept, a team for the management of budget as well as for the fiscal responsibility was formulated in 2003. The purpose behind forming this team was to get a recommendation for replacing the existing indirect tax regime by single tax known as goods and services tax. In other words, recommendation was required to introduce comprehensive tax known as GST in place of state level and central level Value Added Tax (VAT). Accordingly, a replacement of all types

of indirect taxes on all goods and services was recommended, except custom duty with the VAT. Prior to the introduction of GST, different types of indirect taxes were being levied separately by the union and the states separately depending upon the transaction under different legislations, leading to legal complexity and multiplicity of taxes.¹ The types of indirect taxes which were being levied by the Central Government have now been subsumed within the GST.²

While voicing the Budget speech for the year 2006-07, P. Chidambaram, the then Finance Minister of India briefed the drive towards Goods and Services Tax. In the beginning, GST was proposed to be introduced from the start of the financial year of 2010 *i.e.* from 1st April 2010 but it took a long time to prepare the structure and roadmap covering various aspects of Goods and Services Tax. Subsequently, after the constant endeavour to introduce GST in India, the Constitution (122nd Amendment) (GST) Bill, 2014 was introduced in the Parliament with an object of harmonising the system of taxation by subsuming all indirect taxes under single tax. On 03rd August 2016, *Rajya Sabha* passed the Bill and later on it was passed by *Lok Sabha* on 08th August, 2016. Subsequently, more than 15 states passed the Bill.

Thereafter on 8th September, 2016, President gave his assent to “The Constitution (One Hundred and First Amendment) Act, 2016”. Later on the other Bills including the Central Goods and Services Tax (CGST) Bill, Integrated Goods and Services Tax (IGST) Bill, Union Territories (without legislature) Goods and Services Tax (UTGST) Bill and Goods and Services Tax Bill to provide compensation to states was passed on 29th March 2017 by the *Lok Sabha* and the same was passed by the *Rajya Sabha* on 6th April 2017. The Notifications regarding the above mentioned Bills were issued when these Bills became Act with the assent of the President on 12th April 2017. The Goods and Services tax was implemented on 1st July 2017 and accordingly, infrastructure and technology of tax systems and Information Technology systems of trade and industry were updated.³

Goods and Services tax was introduced as a tax to be charged on destination basis. The imposition of tax is on the consumption of goods or services. Because this tax is leviable at every stage where value is added to the goods or services, this indirect tax is levied from the stage of manufacturing up to the consumption stage. There is no doubt that goods and services tax is a tax to be levied at multi stage but the final consumer is the person on whom the burden of the tax finally falls.⁴ With the amalgamation of various indirect taxes under the

single umbrella known as GST, the ill effects of previous indirect tax system including the cascading effect and effect of double taxation are mitigated and a market known as common national market has been created.⁵ Among different ill effects which are removed by the introduction of GST as mentioned before, the main lacunae which is refurbished by GST is removal of cascading effect. The situation of cascading effect arises when the tax is charged on tax. Earlier the tax was not only being charged on the actual product price but also on the tax being charged on the same product in addition to the actual product price. This disadvantage of former indirect tax system was being faced in majority of the transactions taking place during former tax regime.⁶ The complex system of indirect taxation has been simplified to great extent with the help of input tax credit (ITC) mechanism by removing the multiple taxes which were being imposed and by avoiding the situation where tax was being charged on tax.⁷ The biggest advantage from the consumer point of view is that overall tax burden on goods has been reduced which was about 25 to 30 per cent and the system of levying indirect tax becomes transparent and easy to be administered.⁸

3. THE CONTRACT OF BAILMENT AND THE GOODS AND SERVICES TAX

Sections 148–181 under chapter IX of Indian Contract Act, 1872 deal with the concept of bailment. Under the contract of bailment, there is a temporary delivery of possession of goods from one person to another for some purpose. The person who gives the possession of goods under the contract of bailment is known as Bailor and the person taking the possession is known as Bailee. Once the purpose is accomplished, goods are returned or otherwise disposed of according to the directions of the person who delivered the goods.⁹ For the contract of bailment to arise, delivery of goods has to be ‘voluntary’ or there should be voluntary assumption of the possession of goods.

To cover the transaction of bailment under the ambit of being charged with the goods and services tax, the main query to be resolved is that whether the ‘movement’ of goods from the bailor to the bailee constitutes ‘supply’ under the Central the Goods and Services Tax Act or not. To find answer to this query, some important provisions of Central the Goods and Services Tax Act are indispensable to be considered.

Section 9(1) of Central Goods and Services Tax Act

According to section 9 (1) and Section 5 of Central Goods and Services Tax Act, 2017, goods and services tax is to be levied on all the intra-state and inter-state supplies of goods and services respectively except on the alcoholic liquor supplied for human consumption.

Section 20 of the Integrated Goods Services Tax Act

As per Section 20 of the Integrated Goods Services Tax Act and rules made thereunder, the provisions related to ‘scope of supply’ given under Central Goods and Services Tax Act should be applied *mutatis mutandis* to charge integrated tax in the same way as these provisions are applied in the case of central tax.¹⁰

Section 7 of Central Goods and Services Tax Act, 2017- ‘Scope of Supply’

It becomes important to first understand the meaning of supply as per Section 7 of the Central Goods and Service Tax, 2017 (CGST) Act. To cover ‘delivery’ in bailment as ‘supply’ for levying Integrated Central Goods Services Tax, the ‘scope of supply’ in the Central Goods Services Tax Act needs to be understood. The relevant part of Section 7 of the Central Goods Services Tax Act, 2017¹¹ provides-

(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;

According to the above mentioned definition of ‘Supply’, clause (a) of sub section (1) of section 7 clearly provides that the supply includes many transactions including-

1. Sale
2. Transfer
3. Barter
4. Exchange
5. Licence
6. Rental
7. Lease or
8. Disposal

However, the above mentioned transactions will only be covered under the ambit of ‘supply’ if the transaction takes place ‘for consideration’ and ‘in the course or furtherance of business. The meaning of the transactions included in the above mentioned definition are nowhere defined in the provisions of the CGST Act, so dictionary meanings or definitions given in other statutes need to be considered.

Section 4 of the Sale of Goods Act, 1930 defines ‘sale’ as follows -

(1) A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price

The term ‘transfer’ is defined under section 5 of the Transfer of Property Act, 1882 as under -

Transfer of Property means an act by which a living person conveys the property in present or in future:

1. To one or more other living persons, or
2. To himself, or
3. To himself or one or more other living persons, and to transfer such property is to perform such act.

The definition of ‘Exchange’ is given under section 118 of Transfer of Property Act, 1882 as follows-

When two persons mutually transfer the ownership of one thing for the ownership of another, neither thing or both things being money only, the transaction is called an “exchange”.

According to the Cambridge dictionary¹², ‘Barter’ means “To exchange goods for other things rather than for money”.

‘License’ means “An official document that gives you permission to own, do, or use something, usually after you have paid money and/or taken a test”.

‘Rentals’ means “An arrangement to rent something, or the amount of money that you pay to rent something.”

‘Lease’ means “To make a legal agreement by which money is paid in order to use land, a building, a vehicle or a piece of equipment for an agreed period of time”.

‘Disposal’ means “the act of getting rid of something”.

The essence of all these terminologies used in section 7(1) (a) of Central Goods Services Tax Act lies in the ‘transfer of actual control’ on the goods from the owner to the receiver of goods. This transfer of actual control may be permanent or temporary. In case of sale or exchange, where ownership is transferred for consideration in return, in terms of money or goods, it is permanent; while in case of lease or rentals it is temporary in nature where the permission to use the goods for stipulated time as agreed between the parties is given for consideration in return. As a necessary corollary ‘transfer of actual control’ conveys that the receiver must have the power to actually hold and deal with the goods the way he wants.

The definition of ‘supply’ as given under clause (a) of sub section (1) of section 7 has widened its scope by including different kinds of transactions. However, in all these transactions one common feature is the enjoyment of ‘full and effective control’ that gets transferred to the receiver of goods, permanently¹³ or temporarily¹⁴, as the case may be.

Another important aspect to be taken into account for further clarification about the ‘concept of supply’ is the open ended and inclusive definition of ‘supply’ given under section 7 (1) (a) of Central Goods Services Tax Act, 2017. Here the Latin maxim *‘noscitur a sociis’* of Interpretation of Statutes suggests that “the meaning of a word may be known from accompanying words”. This rule of interpretation clarifies the doubt regarding the interpretation of the words used in the provisions of a statute. Any ambiguity in the meaning of the words used in a legislation is to be removed by referring to the rest of the provisions of the statute or the words associated with them. If the words are used in the same context of the phrase, they must be related to each other. In simple words, the judgement of meaning of the word can be made by the company kept by that word.

12th edition of Maxwell’s interpretation of statutes explains this rule as follows-

“When two or more words susceptible of analogous meaning are coupled together, they are understood to be used in their cognate sense. The words take their color from

and are quantified by each other, the meaning of the general words being restricted to a sense analogous to that of the less general.”¹⁵

Therefore, the meaning of the word ‘supply’, under section 7(1) (a) of Central Goods and Services Tax Act, 2017 can be drawn from the colour of other terminologies used in the definition of supply and it cannot be restricted only to those terminologies.

Analysis of the above discussed points leads us to conclude that for a transaction to be included in the definition of ‘supply’, there should be transfer of ‘entire control’ on the goods from one person to another, permanently or temporarily. If the meaning of open ended definition of supply needs to be drawn from the colour of other words used in the definition of ‘supply’, it is to be considered that in all other terms used in the definition ‘actual control’ on the goods passes from the transferor to the transferee on delivery of goods. Therefore where the ‘actual control’ on the goods does not pass from the transferor to the transferee, any other transaction, if not mentioned in the definition will not amount to supply. However, where the actual control on the goods passes from the transferor to the transferee, any other transaction even if not mentioned in the definition will amount to supply.

4. DELIVERY OF GOODS UNDER BAILMENT - SUPPLY OR NOT?

In order to examine whether the transaction of bailment is liable to be charged with goods and services tax, it is pertinent to study the concept of bailment, where the actual control on the goods transferred does not pass from the bailor to the bailee. The notion of bailment including the persons involved in this transaction is well defined under section 148 of the Indian Contract Act, 1872 as follows-

A "bailment" is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them. The person delivering the goods is called the "bailor". The person to whom they are delivered is called, the "bailee"... .

In simple words bailment can be understood as an act of delivering goods to a bailee, for a particular purpose, without transfer of ownership. The bailee gets only the temporary

‘possession’ of the goods bailed and is duty bound to either return the goods to the bailor or make such disposition of the goods as directed by the bailor, after the said purpose is accomplished. The purpose of delivery could be for safe custody, repair or personal use. Since the ownership in bailed goods remain with the owner of the goods, no authority is given to the bailee to perform any act against the terms of the contract of bailment unless and until it is directed by the bailor to be performed.

Explanation appended to Section 148 of the Indian Contract Act further clarifies that in order to enter into the contract of bailment, delivery of goods is necessary. But if the goods are already in the possession of the bailee, the act of retaining the goods by the bailee by entering into contract of bailment with the bailor is equally valid and the requirement that the goods must be delivered under contract of bailment is deemed to be fulfilled.

For example-

A customer wants to get his Apple iPhone repaired from Panchkula Apple store. The person at customer service in the store suggested the replacement of screen of the phone. Here, it is the discretion of the customer to get the phone repaired from the store or not. If the customer nods for the same, only then the screen is replaced by customer service. In this example, customer is the bailor of the goods who is giving his goods *i.e.* iPhone to the bailee *i.e.* the person at customer service for some specific purpose *i.e.* for the repairing the screen. The bailee cannot perform any other function on the goods bailed *i.e.* the iPhone until permission for the same is given by the bailor to him.

From this example it is clear that in contract of bailment, the effective or actual control over the goods remains with the bailor. That is why without his direction, no other action can be taken by the bailee on the goods bailed. Bailment as such is nowhere expressed to be included in the definition of supply given under section 7(1)(a) of Central Goods Services Tax Act but considering that the definition of supply is inclusive but not exhaustive in nature, many other terms can be included in the definition of supply. To include any other transaction under the concept of ‘supply’, the essential requirement is ‘permanent or temporary transfer of entire control’ from one person to another. Further, in view of the application of the maxim ‘*noscitur a sociis*’ in interpreting the meaning of ‘supply’ as under Section 7 (1)(a), would require permanent or temporary transfer of actual control from one person to another, which is missing in the context of bailment. According to the maxim, the meaning of a term can be

drawn from the colour of other terms used in the context of the phrase. Likewise the words used in the definition of 'supply' are considered to draw the meaning of the other words. Accordingly, it is interpreted that in all other terms used in the definition of 'supply', actual control over the goods passes from the transferor to the transferee when the goods are passed. Here, under the contract of bailment, goods are transferred temporarily for the accomplishment of some purpose but the entire control on the goods bailed remains with the bailor and not transferred to the transferee *i.e.* the bailee.

In continuation of the above stated example, where the iPhone is given by the customer to the customer service personnel to get the same repaired, the actual control is retained by the customer as the owner of the iPhone. This does not allow any repair work to be carried out without any direction by the customer. Consequently it can be said that the transaction of delivering iPhone is not covered under the definition of 'supply' given under 7(1) (a) of Central Goods Services Tax Act. Hence, goods and services tax will not be charged on the price of the product delivered for 'some purpose' under the contract of bailment.

Levy of Goods and Service Tax for the Services Rendered as per Contract of Bailment

Further, the matter of concern is regarding the levy of goods and services tax in respect of second leg of transaction of bailment, *i.e.*, for the service provided as per the contract. Again in further continuation of the above mentioned example, the screen of iPhone as required is repaired by the bailee *i.e.* the customer service personnel. Here, the bailee provided the services when the screen was repaired by him.

The act performed by the bailee in the example is falling under the category of services as defined under sub-section (102) of section 2 of Central Goods and Services Tax Act, 2017. The definition of "**services**"¹⁶ is as follows-

“Services mean 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 charge.”

According to the definition, which is again not exhaustive in nature includes anything with some exceptions for which the consideration is charged. In the above mentioned example, consideration *i.e.* the price is being charged by the service provider from the customer for repairing the screen of the iPhone. So, it can be concluded that the same falls under the definition of 'Service'. Hence, goods and services tax is liable to be levied on the services provided by the customer service personnel. The tax is chargeable on the cost of services provided and accordingly, the same after being collected by the service provider from the customer will be deposited to the government.

CONCLUSION

The detailed analysis of the transaction of bailment, in the light of the relevant provisions of various laws and the application of rules of interpretation of statutes, brings forth the clear picture about the levy of goods and services tax on the two distinct and severable parts of the transaction of bailment. The position of law hence brought forth thus becomes clear that firstly, the delivery of goods under bailment does not satisfy the definition of supply under Section 7(1)(a) of the Central Goods and Services Act, 2017, hence outside the ambit of levy of goods and services tax on the price of the product under bailment. Secondly, the liability of the goods and services tax will arise only on the 'services' provided by bailee on the goods bailed.

Therefore, taking the concept of bailment, where goods are delivered but only for specific purpose, is not considered as 'supply'. Whereas the specific purpose for which goods are delivered under the contract of bailment, if accomplished by providing services according to the definition of "services" given under section 2(102) of Central Goods and Services Tax Act, 2017, the transaction of providing services will attract goods and services tax.

References

¹ Prior to CGST Act, 2017, tax would be levied on sale of goods and services in respect of goods separately. However, there was no clear demarcation between the transactions of sale and services. The ambiguity in understanding the nature of transactions of sale and services has been dealt with by the Hon'ble Supreme Court in a catena of cases for deciding on the of levy of corresponding taxes. See *State of Madras v. Gannon*

Dunkerley & Co, AIR (1958) SC 560; *State of H.P. v. Associated Hotels of India Ltd.*, AIR (1972) SC 1131; *Northern India Caterers v. Lt. Governor of Delhi*, AIR (1978) SC 1591.

² Like VAT, Excise duty, Service tax, Octroi/Entry Tax etc.

³ Goods and Service Tax Council (2017). Retrieved from <http://www.gstcouncil.gov.in/about-gst>

⁴ Chapter Nineteen, INPUT TAX CREDIT MECHANISM IN GST, Retrieved from http://www.cbic.gov.in/resources/htdocs-cbec/gst/51_GST_Flyer_Chapter19.pdf

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⁹ The Indian Contract Act, 1872, Section 148- A "bailment" is the delivery of goods by one person to another for some purpose, upon a contract that they shall, when the purpose is accomplished, be returned or otherwise disposed of according to the directions of the person delivering them.

¹⁰ Section 20 of IGST Act - Application of provisions of Central Goods and Services Tax Act, Retrieved from <http://www.aaptaxlaw.com/igst-act/section-20-igst-act-application-of-provisions-of-central-goods-and-services-tax-act.html>

¹¹ The Central Goods and Services Tax Act, 2017, Retrieved from <http://www.cbic.gov.in/resources/htdocs-cbec/gst/cgst-act.pdf>

¹² Cambridge Dictionary retrieved from <https://dictionary.cambridge.org/>

¹³ In the case of sale, exchange or barter, with the transfer of ownership from the seller to the buyer, the effective control over the goods is transferred to the buyer.

¹⁴ In the case of license, the full control over the goods is transferred from licensor (the person giving the license) to the Licensee (the person taking the authority to use the goods).

¹⁵ WHAT IS NOSCITURA A SOCIIS IN INDIAN JUDICIARY?, Retrieved from <https://www.pathlegal.in/What-is-Noscitur-a-Sociis-in-Indian-Judiciary--blog-1229384>

¹⁶ The Central Goods And Services Tax Act, 2017, Retrieved from <http://www.cbic.gov.in/resources/htdocs-cbec/gst/cgst-act.pdf>