# CASE ALERT

## Chief Commissioner of Central Goods and Services Tax & Ors. vs. M/s Safari Retreats Private Ltd. & Ors. [Order dated 03.10.2024 in Civil Appeal No. 2948 of 2023]

In a significant ruling, the Hon'ble Supreme Court of India addressed the constitutional validity of exceptions under clauses (c) and (d) of Section 17(5) of the Central Goods and Services Tax Act, 2017 ("CGST Act"), which blocks the availment of Input Tax Credit (ITC) on goods and services used for the construction of immovable properties, even if the property is used for business purposes.

The appeal resulted from the construction of a shopping mall by Safari Retreats, which claimed ITC on the goods and services used for the construction. The respondents argued that since the mall was let out for commercial purposes, they should be allowed to claim ITC against the rent received.

The key issues revolved around whether the denial of ITC in such cases was constitutionally valid, particularly under Articles 14, 19(1)(g), and 300A of the Constitution of India, and whether the definition of "plant and machinery" in Section 17 will also apply to "plant or machinery" in Section 17(5)(d) The appellants, the tax authorities, contended that ITC could not be claimed due to the restrictions placed by Section 17(5)(d) and the use of "plant or machinery" in clause (d) should be read as "plant and machinery" as both clauses deal with the construction of immovable property.

The Hon'ble Supreme Court made the following observations:

***(a) Distinction between "Plant or Machinery" and "Plant and Machinery" made consciously***

There is a distinction between "plant and machinery" (used elsewhere in the CGST Act) and "plant or machinery" (under Section 17(5)(d)). Section 17(5)(d) does not exclude all immovable properties from ITC eligibility. ITC is available for the construction of "plant or machinery." The expression "plant or machinery" was deliberately used in clause (d) to distinguish it from "plant and machinery", which is defined in the explanation in Section 17(5). The explanation defining "plant and machinery" excludes land, buildings, and other civil structures from ITC, but Section 17(5)(d), by using "plant or machinery," shows that there could be an immovable property which is "plant" and so offers more leeway, allowing availment of ITC if the construction qualifies as a plant or machinery. Whether a building is a plant, is a question of fact.

***(b) Functionality or essentiality tests must be applied to decide "plant"***

The term "plant" is not defined under the GST laws. The Supreme Court applied the functional test to determine whether a building can be considered a "plant." It held that if a building is constructed to meet special technical requirements crucial for a business, it can qualify as a "plant". If the construction of a building was essential for carrying out the activity of supplying services, such as renting or giving on lease or other transactions in respect of the building or a part thereof, which are covered by clauses (2) and (5) of Schedule II of the CGST Act, the building could be held to be a plant. However, if the building is used for personal use or as a setting for conducting business, ITC will not be available.

***(c) Section 17(5)(c) & (d) and Section 16(4) of CGST Act does not violate Article 14 of the Constitution.***

Section 17(5)(c) and (d) of the CGST Act does not violate Article 14 of the Constitution. Clauses (c) and (d) are entirely different from other cases and only apply to classes of cases involving immovable property and immovable goods and these can constitute a class by themselves to satisfy the test of intelligible differentia. Restrictions on ITC imposed under Section 17(5) are based on reasonable classification and have a rational nexus to the objectives of the CGST Act. ITC is a statutory right and not a fundamental right. Therefore, the legislature is within its power to carve out exceptions to ITC availability. On Section 16(4), the Court observed that its unconstitutionality is not established and The fact that the provisions could have been drafted in a better manner or more articulately is not sufficient to attract arbitrariness.

***(d) There are hardly any similarities between clauses (c) and (d).***

Under clause (c), the chain of credit breaks at the dividing line of 'issuance of completion certificate or after its first occupation' as contained in Clause 5(b) of Schedule II and applies only when the building/unit is sold. Such expression is not there in Clause 2 of Schedule II and hence a chain of credit is not broken on the supply of services in the form of renting or leasing the building or premises if a building qualifies to be a plant under clause (d), subject to other conditions like the use of building for own use.

***(e) Meaning of 'own account'***

The expression 'own account' means: (i) construction is made for personal use and not for providing service, or (ii) construction is to be used as a setting in which business is carried out.

The Hon'ble Court remanded the matter to the Hon'ble High Court to determine whether the shopping mall in question qualifies as a "plant" based on the functionality test.

**W&B Comment :**

This decision has significant implications for industries like real estate, hospitality, and others where buildings are used for taxable supply of services. By recognizing that a building integral to business operations may qualify as a "plant," the Court has opened the door for claiming ITC on GST paid during the construction of such buildings, where the construction directly contributes to service provision, such as leasing or renting. However, there is a dichotomy that will need resolution between the two exceptions to the restrictions under Section 17(5)(d):

1. Other than own account exception (construction for leasing or rental purposes), and
2. Plant or machinery exception (allowing ITC for buildings classified as "plant").

Despite the Court recognizing that constructing immovable property for leasing or licensing falls under the first exception, it still proceeded to examine the second exception related to "plant or machinery" and remanded the matter to the High Court. This creates a grey area. The exception of "Other than own account" is broad enough to exclude all constructions intended for leasing or licensing, which should allow ITC for supplies used in such construction without requiring further tests. Nonetheless, the High Court's decision on the remanded matter will be crucial in clarifying this ambiguity.

The functional test adopted by the Supreme Court also appears subjective. The distinction between a building being a "mere setting" for business and a "means" of carrying out business is subtle. In our opinion, if a building is constructed with the intention of leasing, it should be viewed as the primary asset for the leasing business, making it a "means" for conducting that business and qualifying for ITC. However, in other scenarios, one must assess whether the building has specific technical capabilities that contribute to outward taxable supplies. If such functionality exists, ITC should not be blocked.

The department may raise a point that a building was not initially designed and constructed with some special feature to attract customers but is used for such a purpose. The Apex Court observed that such an argument can only be raised on the case of hotels or cinema theatres and whether or not the immovable property is a plant, is a question of fact.

While the Supreme Court has upheld the constitutional validity of Section 17(5)(c) and 17(5)(d), its acceptance of the argument on the interpretation of “plant or machinery” is a positive development. It signals a more flexible approach to the law, with a potential for buildings like malls to be treated as "plant" and subject to case-by-case analysis using the functional test to determine ITC eligibility.
However, this judgment leaves several open questions. Though the ruling pertains to malls, it is yet to be tested whether the concept of “plant” can extend to other sectors like ports, airports, factories, or warehouses. Judgments where the courts differentiated between ‘plant’ and ‘building’ to decide upon the appropriate rate of depreciation could be of assistance to businesses. Further, clarification is needed on unresolved issues, such as whether ITC for works contract services would be available under Section 17(5)(d) for buildings constructed for leasing.