THE INDIRECT EDGE

Indirect Tax

Gujarat High Court ruling on applicability of GST on corporate guarantee

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Gujarat HC | Applicability of GST on the supply of corporate guarantee services[1].

The Gujarat High Court in the case of Torrent Power vs. UOI has held that **GST is not applicable** on the provision of **corporate guarantee** prior to the insertion of Rule 28(2) of the CGST Rules, i.e., **prior to 26.10.2023.**

GST is applicable on the provision of corporate guarantee services after the insertion of Rule 28(2) of the CGST Rules, i.e., **after 26.10.2023**. However, **where the actual consideration for the supply of corporate guarantee services is lower than 1% p.a., the actual consideration has to be considered.**

Brief Facts

- In the facts of the case, the holding company had provided corporate guarantees to lenders to who have provided credit/ loan to the subsidiary company.
- The case of the petitioner was that giving a corporate guarantee to a lender for a loan taken by a subsidiary should not be treated as a supply of taxable services under GST.

High Court Ruling

- The activity of providing a corporate guarantee by a holding company to its subsidiary to secure a loan for the subsidiary's commercial activities is incidental to trade, commerce, etc. **Accordingly, it would qualify as a business activity.**
- A corporate guarantee provided by the Holding Company to the subsidiary, and acknowledged by the Holding Company for securing the subsidiary's financial obligations, **would fall within the expression "agreeing to do an obligation to do an act" under Entry 5(e) of Schedule II.**
- The HC observed that even though the subsidiary company is not a party to the corporate guarantee agreement, the service is rendered for the benefit of the subsidiary. Accordingly, the **subsidiary company would be considered the "recipient" of the services** under the corporate guarantee.
- An **actionable claim** represents a direct and primary right to claim a payment or debt. **This cannot be compared with a corporate guarantee,** which arises from a secondary and contingent liability that is triggered upon the default of the principal debtor under a tripartite arrangement.
- The HC examined the specific facts of the case, where shares were pledged. It held that the intent of the pledgor was to secure the loan and allow appropriation of the shares in the event of default by the subsidiary company. **Accordingly, execution of an agreement for pledging of shares along with a corporate guarantee constitutes a supply of service.**
- The Court **disagreed with the judgement in D.P. Jain & Co**. passed by the Nagpur Bench of the Bombay High Court. The Court noted that the said judgement relied upon the Supreme Court's judgement in Edelweiss Financial Services, which was rendered under the Service Tax regime, when the applicable legal provisions were different.
- The High Court upheld the validity of Section 15(4) read with Rule 28(2) of the CGST Rules. **However, the High Court held that fixing the value of a corporate guarantee at 1%, even where the actual consideration is lower than 1%, is unreasonable and arbitrary.**
- **Consequently, the words "whichever is higher" in Rule 28(2) of the CGST Rules**

[1] Torrent Power v. UoI (2026) (Guj. HC)

were struck down. The Court observed that these words do not provide the corporate guarantor with an option to pay GST on the actual consideration, even though actual consideration is an essential factor for making the levy and the Rule workable.

- **Rule 28(2) imposes a retrospective levy of a new tax for a period during which, as per the law, no such levy existed.** Accordingly, imposing GST based on a 1% valuation per annum on corporate guarantees for the period prior to the introduction of Rule 28(2) w.e.f. 26.10.2023 was held to be harsh and unfair to taxpayers. **This appears to indicate that the HC has held that GST itself was not leviable on corporate guarantees prior to 26.10.2023.**
- The High Court has held that **Section 74 of the CGST Act cannot be invoked** in respect of the transaction in question, as the matter involved a disputed interpretation regarding the applicability of Rule 28(2) of the CGST Rules.
- The High Court has also held that **any excess amount of GST deposited, if any, shall be refunded to the petitioners.**

Our Comments

- The judgement is a welcome relief for the corporate guarantees issued prior to October 2023.
- It is interesting to note that the judgement has principally held that issuance of a corporate guarantee is a supply of service. Inspite of such a holding, the HC has struck down the levy of corporate guarantee on the grounds that specific provisions related to valuation in Rule 28(2) of the CGST Rules was introduced after 26.10.2023. The Court has not held that GST on corporate guarantee prior to 26.10.2023 has to be paid by adopting some other reasonable value.
- The judgement will also be welcomed by assessees where where the actual consideration for the supply of corporate guarantee services is lower than 1% p.a.
- The judgement does not provide a general finding on whether the issuance of a corporate guarantee by a holding company for loan facility availed by its subsidiary qualifies as a shareholding activity. Instead, the court has given specific findings based on the share pledge agreement and the facts present case leaving this issue open to litigation.

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