

TAXABILITY OF COMPOSITE AND MIXED SUPPLIES UNDER GST IN INDIA: TAKING A LEAF OUT OF SERVICE TAX LAW AND EUROPEAN VAT MODEL

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The provisions related to composite and mixed supply under Indian Goods and Services Tax law have been introduced with a sea of ambiguities. The lack of any guiding principles has made the taxability of such supplies highly complex, as it is difficult to ascertain the nature of supplies involving complex and multi-dimensional contracts. Moreover, some contradictory provisions within the GST framework have made it important to highlight the need of clarifications on the subject by the Central Board of Indirect Taxes and Customs ("CBIC") and the Goods and Services Tax Council. GST law is still in its nascent stage and little research has been undertaken and published since the introduction of the new law. The existing literature on the concept relates to specific cases where various Advance Rulings have been analysed. However, they are merely in the form of a summary of the Rulings along with minor inputs from the authors. The Education Guide on Service Tax, published by the erstwhile Central Board of Excise and Customs in the year 2012, does provide some principles on interpretation for better application of the relevant provisions. The jurisprudence from the European Value Added Tax Model can also be considered relevant in the present context as much of the provisions in the Indian GST law are based on this European VAT model. The present paper is aimed at taking a contributory leap forward, being an analysis of all the applicable principles with regard to the concept along with the challenges and suggestions to make the provisions of composite and mixed supply less ambiguous. The present study is a doctrinal research involving legal principles and provisions. It is an analytical study examining the validity and feasibility of various provisions of law. It contains a critical analysis of the relevant legal provisions and principles.

I. INTRODUCTION

The indirect taxation structure in India has seen a lot of modifications over the past few years. There have been a lot of amendments in taxation at every stage from manufacture to sale for final consumption. The latest entrant in this spree of sea changes is the novel Goods and Services Tax ("GST").

Even though the discussions about the introduction of this integrated tax structure were already initiated in the first decade of the twenty-first century, the initial attempts at laying down a consolidated legislative framework were futile. It was only in the seventeenth year of this century

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that the Indian indirect taxation regime saw the rolling out of this landmark change after crossing all the political and legislative hurdles.

The main purpose behind rolling out GST is to prevent the cascading effects created by levy of multiple taxes at both Central and State level. This integrated tax structure allows set-offs of taxes throughout the value chain. Hence, the popular theory that GST is just a clubbed concept of Value Added Tax and Service Tax, is not quite correct.

Internationally, VAT and GST are considered synonymous to each other. This is so because the VAT structure in other countries cover both goods and services (unlike in India where services were leviable to Service Tax). Keeping that in view, over 150 countries around the world have adopted the VAT/GST structure directly or in different forms. However, the practical aspects and scope of this tax regime differ from nation to nation according to the individual requirements of the countries' economy.

A. COMPOSITE SUPPLY

The expression “composite supply” has been defined as “*a supply made by a taxable person to a recipient consisting of two or more taxable supplies of goods or services or both, or any combination thereof, which are naturally bundled and supplied in conjunction with each other in the ordinary course of business, one of which is a principal supply.*”¹

The expression “principal supply” has been defined as “the supply of goods or services which constitutes the predominant element of a composite supply and to which any other supply forming part of that composite supply is ancillary”.² Further, according to the CGST Act, a composite supply comprising two or more supplies, one of which is a principal supply, shall be treated as a supply of such principal supply.³

A composite supply is a combination of goods or services or both supplied as a composite whole, where some or all of the components of such supply are chargeable at different rates of tax, and one such component is the principal supply. Principal supply must be the one which is at the essence of the whole package of goods or services or their combination thereof. A negative

¹ Central Goods and Services Tax Act (Act No. 12/2017) (India), § 2(30) [hereinafter “CGST Act”].

² *Id.*, § 2(90).

³ *Id.*, § 8(a).

test may be adopted in which all the goods or services other than the principal supply may be negated as not constituting the essence of the package.

The expressions “naturally bundled” and “in conjunction with each other” play a significant role in determining if a supply falls within the definition of a composite supply. Neither expressions have been defined in the GST legislations. There is ambiguity regarding the scope of the concept of principal supply. However, “naturally bundled” may be inferred in the light of “bundled service” under the erstwhile service tax regime. The Education Guide of Central Board of Excise and Customs on Service Tax (“CBEC Guide”) explains the concept of ‘bundled services’.

Further, the expression “ordinary course of business” finds no explanation in GST law. According to the CBECE Guide, normal and frequent practices in the particular business area are a significant factor in determining what constitutes “ordinary course of business” for that business area.⁴ These practices, in turn, are to be determined taking into consideration several illustrative indicators.

A works contract and restaurant services are composite supplies as well, in a technical sense.⁵ The reason for this observation is that in a works contract, it is not only the construction service that is being provided by the supplier, but it also involves supply of goods in the form of requisite raw materials, and that both the supplies are generally made in conjunction with each other. Similarly, supply of services by a restaurant owner also includes supply of goods in the form of food that is served as a part of the service. Be that as it may, GST law recognises both of these as a specific supply of services with a prescribed GST and not composite supply.⁶

B. MIXED SUPPLY

The expression “mixed supply” has been defined as “two or more individual supplies of goods or services, or any combination thereof, made in conjunction with each other by a taxable person for a single price, where such supply does not constitute a composite supply”.⁷ For example, if flowers and scents are supplied in conjunction with each other for a single price, and supply of

⁴ CENTRAL BOARD OF EXCISE & CUSTOMS, TAXATION OF SERVICES: AN EDUCATION GUIDE, 127 (2012).

⁵ CENTRAL BOARD OF INDIRECT TAXES & CUSTOMS, GST FLYERS, 26 (Mar. 18, 2020), https://www.cbic.gov.in/resources/htdocs/cbec/gst/51_GST_Flyer_Chapter4.pdf;jsessionid=0C9BC58B6139D1235028765641541E48.

⁶ CGST Act, sch. II.

⁷ *Id.*, § 2(74).

flowers is taxable at the rate of 5%, while supply of scents is taxable at the rate of 12%, the mixed supply of flowers and scents would be taxable at 12%, since it is the higher rate out of the two.

II. ANALYSING THE LEGISLATIVE PROVISIONS

A. COMPOSITE SUPPLY

In order to understand the implications of the concept of composite supply in India, it is important to analyse all the components of the definition of the expression “composite supply” under GST laws.

1. “Naturally Bundled” and “Supplied in Conjunction with each other” in the “Ordinary Course of Business”

The expressions “naturally bundled”, “in conjunction with each other”, and “ordinary course of business” have not been defined anywhere in the GST Act. According to P. Ramanatha Aiyar, “naturally” means “according to nature of things”, and applies therefore to the connection between events according to the original constitution or inherent properties of things.⁸ Further, “bundling” has been defined by him as “a practice of providing more than one product or service at once at an inclusive price”.⁹

For the purpose of interpreting the above-mentioned expressions, reference has to be taken from the CBEC Guide and its analysis of the expression “bundled service” under the erstwhile Service Tax regime. The Guide defines ‘bundled service’ as a “bundle of provision of various services wherein an element of provision of one service is combined with an element or elements of provision of any other service or services”.¹⁰ For instance, consider a supplier of hotel services who offers a breakfast included package. Such a service is provided in the ordinary course of business and hence will be said to be naturally bundled. The essential character in this combined service is the service of providing hotel accommodation and hence the service as a whole would be treated as the service of providing accommodation by the hotel.

Taking another example, a luxurious resort has been booked for a business conclave for a composite package including services like accommodation, breakfast, tea and snacks, fitness room facility, conference room accessibility, swimming pool, etc. It is amply clear that all these services

⁸ P.R. AIYAR, 3 ADVANCED LAW LEXICON (2016).

⁹ P.R. AIYAR, 1 ADVANCED LAW LEXICON (2016).

¹⁰ *Supra* note 4, at 126.

might be charged at different rates of taxation in accordance with their classification. It is impossible to determine any one service which forms an essential character of this bundle of services. However, this type of service falls under the head of convention service as per the Service Tax laws and would have a prescribed rate of taxation.

The CBEC Guide lays down the principle that the expression “ordinary course of business” should be interpreted to mean “the normal or frequent practices followed in the area of business to which the services relate”. The Guide further lays down certain indicators which facilitate the normal and frequent practices that are undertaken in a particular area of business.

One of the prominent factors for determining what constitutes an ordinary course of business is the “perception of the consumer or the service receiver”. This means that a bundle of services may be recognised as naturally bundled in the ordinary course of business, if a very high number of recipients of those services reasonably expect such services to be supplied as a combined whole. Another significant criterion is that “majority of service providers in a particular area of business provide similar bundle of services”.

These indicators are of utmost significance in order to determine if a supply can be termed as a composite supply or not, in the absence of any other set of guiding principles, and also to some extent explains the concept of a ‘principal supply’ under GST.

2. Principal Supply

It is clear from the definition of composite supply that a “principal supply” must be first ascertained in order to determine the question of taxability of a composite supply. Every composite supply constitutes a principal component on which the taxability of the whole transaction is dependant. The definition of “principal supply” as per the CGST Act has already been reproduced above.

The expression “predominant” is of utmost significance in order to determine the component which forms the principal supply. This process of determination of a predominant element of a composite supply may be complex in cases where the transaction is very technically entwined. In this regard, perception of the recipients of the supply becomes very important.

The perception of the recipient is relevant as it determines the purpose behind a particular supply. The main purpose for which the recipient is receiving the supply should be met, and without the fulfilment of this purpose, the whole supply is rendered meaningless to him. Hence, the predominant element of the supply is the one which is the most important to the recipient. For instance, the supply of service by a restaurant owner is a composite supply as it is characterised by multiple features and activities. However, the supply of service by a restaurant would be rendered purposeless if the most significant component, i.e. provision of food, is absent, even if all other ancillary services are being supplied. Hence, the provision of food largely predominates the supply and is the principal component of the restaurant services.¹¹

There may be a situation when more than one component of the supply possesses an essential character and hence, is equally predominant to any other component of that supply. However, both these components are still predominant over other components of the supply. This situation which is known as the table-top model of composite supply, confronted the Court in the case of *Commissioner for Excise and Customs v. FDR*.¹²

It was held that in such a scenario, “principal supply must be identified with a further re-look at the supplies”. It was further clarified that “unnecessary complexities” be avoided and principal supply may be determined on the reference on the numerical domination. This case, though it pertains to European jurisprudence, has proved to be very helpful in view of the fact that the expression “composite supply” under Indian GST regime does not recognise a situation where there may be more than one principal supply.

B. MIXED SUPPLY

As in the case of composite supply, there are no guiding principles to determine the scope of the components of the definition of expression “mixed supply”, under the GST Act. Hence, reliance, yet again has to be placed on the rule laid down in the CBEC Guide.

The concept may be explained with the help of an example, which has been referred to in the CBEC Guide as well. Consider a building that has to be put on rent by the owner. There are two storeys in the building, one to be rented out for residential purposes, and the other for establishing a printing press. This type of activity is not generally undertaken by a supplier involved in such a

¹¹ *Faaborg-Gelting Linien A/S v. Finanzamt Flensburg*, C-231/94 (1996).

¹² *Commissioner of Excise and Customs v. FDR*, Case No: C/1999/0654 (2000).

business. Hence, keeping in view the principles laid down above, it may be said that these services are not naturally bundled in the ordinary course of business.

As per the abovementioned rule, if a transaction comprises more than one component being supplied as a composite whole, the transaction will be deemed to be a supply of the component that attracts the highest rate of taxation among all the components.

III. TREATMENT OF COMPOSITE AND MIXED SUPPLY IN SERVICE TAX REGIME

The concept of composite and mixed supply is not a novel concept for the Indian tax regime. The concept also found a mention in the previous Service Tax regime. The form and manner of the provision and its implementation were different from what it is in the GST era. However, the basic premise on which the concept stands is similar.

A. COMPOSITE SERVICE IN THE NEGATIVE LIST REGIME

The year 2012 saw a landmark change in the way services were taxed in India. The concept of “negative list” was introduced vide Finance Act of 2012, amending the 1994 Act.¹³ The negative list of services was a list of services which were exempted from Service Tax. This system was different from the pre-2012 period, in the sense that earlier there was a list of services which were taxable. Section 66F of the Finance Act, 2012 provided for classification of composite services under the service tax regime of the negative list.

B. SPECIFIC DESCRIPTION OVER GENERAL DESCRIPTION

Section 66F(2) provided the ‘more specific over general rule’, according to which, if the services that are being provided can be classified under more than one descriptions, the more specific description will prevail over the general description. This is because of the reason that differential treatment could have arisen due to the ad hoc abatement in arriving at the value of taxable service, of certain services, after Notification No 26/2012.

¹³ Finance Act, 1994, Act No. 32/1994 (India), § 66B.

Ad hoc abatement was available only to the services specified in the Notification, and not to all the services. The differential treatment could have also only arisen for some of the services where the tax was payable by service recipient and not by the provider.¹⁴

For example, *pandal* and *shamiana* services are provided along with catering services in conjunction with each other. Here, *pandal* and *shamiana* service as a separate description was subject to Service Tax. Similarly, the catering services were also subject to tax and were entitled to abatement. Further, when these services were provided as a combination, there was abatement too. Hence, the combination of these services was a specific description, and these services when provided individually, fell under their respective general descriptions. As a consequence, the concept of bundled service was not applicable to such a combination of services, as there was a specific description, and also neither of the two services formed an essential character of the combination.

C. INPUT SERVICES NOT INCLUDED IN MAIN SERVICE

It is clear from a bare perusal of Section 66F(1) that the main service shall not include, within its fold, a service which is required to provide the main service. Such a service is referred to as an input service in order to facilitate the provision of the main service.

As a corollary to this provision, it is followed that such an input service will have its own classification and hence, will be considered as a separate service in itself. In this regard, the Central Board of Excise and Customs published some clarifications.¹⁵ It is important to note that these clarifications were released prior to the adoption of the new negative list regime. Hence, it can be said that this concept was prevalent even in the old service tax regime, prior to 2012.

In the above-mentioned clarificatory notification, the Central Board of Excise and Customs clarified that services provided by architects and consulting engineers cannot be classified as a works contract service, as this category of services was classified under a specific description under the Finance Act, 1994.¹⁶

¹⁴ D. Shah, *Bundled Services under Negative Service Tax Regime*, [2013] 33 taxmann.com 301 (2013).

¹⁵ Central Board of Excise and Customs, Circular No. 138/07/2011-ST (May 6, 2011).

¹⁶ *Id.*, ¶ 2(ii).

CBEC issued the clarification in order to answer the representations made before it regarding the classification of services of architect and consulting engineers as a works contract, since these services are required to provide works contract services. The purpose of the representations was to ensure that these services can be entitled to exemption from Service Tax, since works contract services of construction of bridges, roads, dams, etc. were also exempt. However, CBEC was of the opposite view. When description of a sub-clause is available for classification, the same cannot be classified under any sub-clause which is general in nature.¹⁷

D. BUNDLED SERVICE

It was only in cases where it became impossible to categorize a service under Section 66F(2), that Section 66F(3) came into picture. Both the sub-clauses of clause (3) helped in determining the taxability of a bundle of service. The first clause provided that when various elements of services are naturally bundled in the ordinary course of business, it shall be treated as a provision of a single service which gives it an essential characteristic. According to a CBEC document, a service which provides economic value to the service recipient will be considered as essential service for the purpose of classification.¹⁸

The definition of taxable services was provided for under Section 65(105) of the Finance Act, 1994. CBEC had clarified that a single composite service can be provided by the supplier of such service either by bundling various services together or by disaggregation of an individual supply into different bits.¹⁹

It was important to determine whether a component of supply was ancillary to the main supply or it could be classified as a separate service in itself. A composite service was classified on the basis of a particular component of the service that formed the essential character of the transaction as a whole.

The classification of a service was dependant on the fact that it provides any economic value to the person to whom the service is being provided. It is important to note that the courts had devised some principles in order to determine the essential characteristic of products. These principles can be used in order to determine the essential character of a transaction.

¹⁷ Shah, *supra* note 14.

¹⁸ Central Board of Excise and Customs, Letter No. DOF. 334/1/2008-TRU (Feb. 29, 2008).

¹⁹ *Id.*

In the case of *Xerox India*,²⁰ the Supreme Court held that the cost of component of the products is a factor in determining its essential characteristics. The Hon'ble Court, in this case, was dealing with a classification-dispute for the classification of multi-purpose printing machines.

The question was whether it is to be classified under heading 8479.89 or heading 8471.60. The features of the machine included all the functions of printing, copying, scanning and faxing. In the opinion of the Hon'ble Court, the function of printing gave the machine its essential character and hence it was the principal function of the machine, since more than 70% of the cost and the total components of the machine were dedicated for performing the function of printing.

The Hon'ble Supreme Court, in the case of *Bakelite Hylam Ltd.*,²¹ devised the principle of 'functionality of the product', in order to determine the classification of a product. The Court examined the issue of classification of laminated sheet constituting only 30% plastic by weight and the rest of the weight of the sheet being occupied by paper. The Court held that plastic constituted the essential characteristic of the laminated sheet as its strength, rigidity and resistance would depend on the quality of the plastic used. Therefore, the product merits classification as plastic.

E. COMPARISON WITH THE GST REGIME

Sub-clauses (a) and (b), provided in Section 66F (3), were essentially the same concepts which have been defined under the GST law as composite and mixed supply respectively. It is significant to note here that the treatment under Section 66F (2) is similar to what has been accorded to works contract and restaurant services under the GST laws.²² Since there is a prescribed rate of taxation for supply of these two categories of services, a 'principal supply' is not required to be determined, even though these services are in the nature of a composite supply as defined under GST laws. Also, the rule of specific description over general description has been provided for interpretation of classification of services under the GST laws as well.

²⁰ *Xerox India Ltd. v. CC*, 2010 (14) SCC430.

²¹ *Collector of Central Excise v. Bakelite Hylam Ltd.*, 1997 (10) SCC 350.

²² CGST Act, sch. II.

IV. COMPARISON WITH RELEVANT PRINCIPLES OF EUROPEAN JURISPRUDENCE

The European Value Added Tax model has in the last two years proved to be one of the most significant resources to facilitate the interpretation of ambiguous and unclarified concepts under the Indian GST model. The principles from the foreign model have helped GST practitioners across the country in figuring out the object and purpose behind incorporation of certain principles in the Indian model. Same can be said for the provision of composite and mixed supply.

The concept of composite and mixed supply under Indian GST model can be compared to the provisions of ‘single supplies’ and ‘multiple supplies’ under the European model. It is significant to note here that one of the basic differences between the two models is that while the GST legislation in India itself lays down the concept of composite and mixed supply, in Europe the concept of single supplies and multiple supplies has been laid down by the judiciary over a long span of time and not by statutory provisions.²³

A. THE LANDMARK RULING OF THE EUROPEAN COURT OF JUSTICE

The concept of single and multiple supplies was elaborated upon by the European Court of Justice in the case of *Card Protection Plan Ltd.*,²⁴ wherein some principles for determination of different elements of a supply were laid down. In this case, Card Protection Plan Ltd. (“CPP”), was engaged in the business of providing insurance services. These insurance services were to insure the loss incurred by the policy holder due to any fraud or misuse of his credit card. The case of CPP was that since ‘insurance services’ were exempted from VAT, the services provided by it should also not be subjected to VAT.

The major hindrance in smooth acceptance of the claim of CPP was that it was the contention of the department that CPP was mainly a card handling service provider and provided insurance services in addition to this card handling service. Hence, the issue before the Bench was to determine the nature of services that were being provided by CPP. It was held that the services provided by CPP were of the nature of ‘insurance services’. The principles laid down by the Court, which formed the very basis of the European jurisprudence on the concept, were:

²³ *Card Protection Plan Ltd v. Comm’r, Customs & Excise*, C-349/96 (1999).

²⁴ *Id.*

- In all cases of supply of a service, the supply should be considered as “distinct and independent supply”.
- A supply which constitutes a “single economic service” from an “economic point of view” must never be split artificially.
- An examination of the essential character of the transaction is necessary to decide whether a supply constitutes multiple distinct “principal services” or a “single service”.
- When one component of a supply constitutes a principal service and the other component(s) are merely ancillary services.
- An ancillary service is not an end in itself. It is merely a means to an end for better enjoyment of the principal service.²⁵

B. THE PRINCIPLES

The abovementioned ruling of the European Court of Justice is a landmark in laying down the principle of bundled and split supplies. The finding that each supply is “distinct” and “independent” in itself has helped a great deal in determining the flawless treatment of various supplies under VAT. There are additional problems that may arise with respect to this concept as the transactions can get highly complex with the evolving market demands. In order to determine the taxability of such complex supplies, there are specific certainty principles that have been evolved by the European courts and may also be relevant in the Indian context when the need arises. These principles are similar to the principles discussed above in reference to the CBEC Guide. These principles have been discussed in the following paragraphs.

1. Point of View of the Consumer

The perception of the person who is consuming the supply is a very important factor in determining whether it is a single supply or a multiple supply. This principle has been coined as “from the point of view of a typical consumer”.²⁶

The purpose of receiving a supply for a customer is to fulfil a specific aim. This aim may be a sole aim or may be manifold. It can be assumed that if the consumer has only one aim to receive the supply and the other components of the supply are merely the means to achieve that aim, the supply can be said to be naturally bundled. Accordingly, the supply would be in the nature of a

²⁵ Commissioner of Customs & Excise v. Madgett & Baldwin, C-308/96 & C-94/97(1998).

²⁶ Everything Everywhere Ltd. v. HMRC, C-276/09 (2010).

composite supply. It is clear that the aim of the consumer here would be derived out of the “principal supply” as defined by the CGST Act.

On the contrary, if the consumer has multiple aims to derive from a supply, the supply would be artificially bundled as each component of the supply would be a distinct and independent supply. Since there is no natural bundling, the supply would not be a composite supply, and hence it would be a mixed supply.

2. Principle of Economic Reality

The next important principle is that of “economic reality”. This simply means to determine that component of a transaction, around which the whole transaction revolves. A taxable person finds ways to reduce his tax liability to the maximum extent possible. Hence, efforts shall be made to look at the transaction with an economical perspective.

This principle helps in identification of economic substance while taking into consideration all the business scenarios. Hence, it is similar to the concept of determining the economic nature of the supply as discussed in the previous chapter. The principle works on the basis of examining the inter-relation between the components of the supply, if the supply consists of multiple components. This examination would include factors like mandatory nature of a component, the price fixation, and the distinct and independent existence and value of each component.

In short, the principle of economic reality ascertains the object and purpose of the supply from an economic perspective. Hence, if the components are integral to the main supply from an economic aspect, the supply may be said to be a composite supply.²⁷ In the same way, if the economic reality of the transaction indicates that the consumer had manifold aims in his mind, supply will be characterized as a mixed supply.

3. Aims versus Means

The abovementioned ruling in *Card Protection Plan Ltd.* also laid down the principle of “aims v. means” when it discussed that the difference between aims and means lies in the fact that while former demarcates the purpose of the whole transaction, the latter is not a principal service and merely an ancillary service. As discussed above, the difference between both is that an ancillary service is just a means to fulfil that purpose, i.e. principal service, more effectively. The Court laid

²⁷ *LevobVerzekeringen BV and OV Bank NV v. Staatssecretaris van Financiën*, C-41/04 (2005).

down the principle that, when there is a determinable principal component in the supply transaction along with other ancillary components, the transaction is deemed as a single supply of that principal component. It is clearly inferable from this explanation that this concept is the same as the concept of composite supply in Indian GST model, where the whole supply is considered to be a supply of the principal supply.

It is amply clear from the above discussion that a transaction which consists of various distinct components, may either be characterised as a single supply or a multiple supply. The taxability will take a completely different path in both the cases after the determination of the nature of supply. Further, it is also significant to note that the principles of erstwhile Service Tax regime in India, the CBEC Guide and the GST Flyers on Composite and Mixed Supply, collectively constitute a very limited set of principles for determining the complex vires of the nature of a supply. Hence, the relevance of these principles of European jurisprudence becomes all the more important for interpreting the provisions of the Indian GST regime.

4. The “Integral, Ancillary or Incidental” Principle

The Integral, Ancillary or Incidental (“IAI”) Identification principle is similar to the principle of “aims vs. means” discussed above. It is clear from the discussion in the preceding paragraphs that if there are multiple parts of a supply, where there is only one essential part and the remaining parts are merely IAI to the essential part, the supply may be termed as a composite supply. In other words, it is fair to say that, even if the part which is IAI is distinct and independent enough to become an individual supply, they can only be ancillary and deeply entwined with the principal supply.

In view of the above, it may be said that a component which is IAI to the main supply, is not an end in itself but a means for better enjoyment of the end. Further, such a component has its own significance, but is not significant enough in the particular composite supply under consideration as compared to the “predominant element”. Moreover, the IAI component constitutes a marginal co-existent of the entire value of the composite supply.

C. COMPARISON BETWEEN EUROPEAN PRINCIPLES AND SECTION 8 UNDER CGST ACT

The significance of the tests laid down by the ruling discussed above cannot be emphasized enough. However, in case the abovementioned principles do not help, some more principles have

been formulated in this regard over the last few years. One difference between the European model and GST has already been mentioned above that while the former has a set of judicial guidelines, the latter has a legislative framework.

1. Single Supply vs. Composite Supply

On a comparison between both the concepts, it may be inferred that there are two alternatives to determine whether a supply is a single supply under the European VAT model. First, the supply consists of a principal supply and one or more ancillary supplies, or second, the elements are closely linked. If either of the two tests is satisfied, the supply will be considered as a single supply.

On the other hand, section 2(30) of the CGST Act lays down two conditions which are to be satisfied mandatorily for a supply to be considered as a composite supply. These two conditions are: 1) principal supply must be naturally bundled with non-dominant supplies; and 2) supplies shall be made in conjunction with each other.

From the above-mentioned principles and provisions, a comparison may be drawn between both the models. The two models differ in the principles for determination of composite supply or single supply, as the case may be. While the European model provides a two-way entry into the applicability of the principle by providing two alternatives, the Indian model lays down a dual test and both the conditions need to be complied with. In any case, it may be said that a single supply under the European model and a composite supply under the Indian model are similar concepts.

2. Multiple Supply vs. Mixed Supply

As already discussed above, two or more elements, if taken together, do not constitute single supply, they are multiple supplies. Further, the concept and definition of mixed supply has also been analysed above.

The line of distinction between the two concepts is very thin. However, the determination of nature of supply may well be different in both the models. The basic difference between the two is easily inferable. While in multiple supplies, all the components are distinct and are taxable individually, in mixed supply, the supply is considered the supply of those goods or services which attract the highest rate of taxation.

At this point, a brief discussion about the expressions “single price” and “in conjunction with” used in the expression “mixed supply” is required. It may be noted that exclusion of these two expressions from the definition of mixed supply would render the whole concept purposeless. These two expressions prevent a taxable person from making a composite supply, as the supply can be manipulated in a composite supply according to the taxability, while in a mixed supply, taxability is determined on the basis of the highest rate.

The above problem may be understood with the help of an illustration. Consider two goods, A, taxable at the rate of 12%, and B, taxable at the rate of 18%. Now, if the supplier makes a composite supply of these products at a single price, he may be able to manipulate the supply in a way to make the principal supply. In that case the composite supply of A and B would be taxable at 12%. Further, in case it is proved by the department that the two supplies are separate supplies, both may be taxable at their respective rates.

However, in the abovementioned illustration, if the supply is made as a mixed supply, it will be taxable to GST at the rate of 18%, being the higher of the two rates. Hence, the supplier might be able to manipulate the supply in order to reduce his tax liability, if the essential expressions from the definition of “mixed supply”, as discussed above are excluded.

D. THE CONCEPT OF SPLITTING OF A SUPPLY

At the outset, it is important to be clear about the proposition that the concept of splitting of supply is only possible in a mixed supply. In the Indian context, this proposition becomes more apparent as a mixed supply is characterised by higher side of tax liability even if all but one components of the supply are individually taxable at a lower rate. It is to be noted that no such provision of taxing the supply at the higher rate exists in the European VAT model.

1. Splitting of a Composite Supply

Though the very concept of composite supply makes it impossible to split it, there may be scenarios which do allow for such a splitting. The splitting in cases of composite supply has to be done rationally, with the determination of value of each component. The CBEC Guide and GST Flyers on Composite and Mixed Supply have recognised this kind of splitting to a limited extent.

The example of supply of service by a hotel which has been booked for a business conference, as discussed in the CBEC Guide, and as elucidated in the introductory chapter above, is followed

by explaining a particular situation where, “it will be fully justifiable for the hotel to charge individually for the services as long as there is no attempt to offload the value of one service on to another service that is chargeable at a concessional rate”.²⁸

Further, there may be a possibility that supply of service of car-servicing may be split into two components, i.e. service provided by the supplier, and the goods supplied by the supplier in the form of spare parts. This possible situation can occur only when the value of goods and the value of services can be identified individually.²⁹ Hence, the above two official publications bear evidence to the fact that a contract of composite supply may be a divisible supply in some specified circumstances.

Here, it is also important to refer to the expression “for a single price” as used in the definition of mixed supply. The definition of composite supply does not make it mandatory for the supply to be made at a single price. Hence, it may be said that pricing is not a factor to determine composite supply. This indicates that the above-mentioned proposition of splitting the composite supply if the value of each component is distinguishable, will be true for all composite supplies. However, this cannot be the case, as this would bring out the biggest loophole in the provision of composite supply.

Hence, the only viable way to interpret the above-mentioned propositions of hotel service and service of car-servicing without contradicting the very basis of section 2(30), is to consider the possibility of having divisible contracts in a composite supply in reference to particular services and not as an absolute concept.

2. Splitting of a Mixed Supply

Prima facie, since a mixed supply consists of components which are not naturally bundled, it must be easier to consider splitting a mixed supply. The concept of splitting rationally on the basis of value of each component, as discussed in the case of a composite supply, becomes further less complex since mixed supply already consists of components which are easily distinguishable from each other. However, different methods for valuation of the components may be used. The Valuation Rules under section 15(4) provide for methods such as “open market value” of each component, “proportionate value” of each component and “discount formulation”.

²⁸ *Supra* note 4, at 127.

²⁹ Central Board of Indirect Taxes and Customs, Circular No. 47/21/2018-GST (June 8, 2018).

V. CONCLUDING REMARKS: CHALLENGES AND SUGGESTIONS

The concept of composite and mixed supply under the Indian GST regime has so far proven to be one-of-a-kind provision. Though it is similar to various principles applicable to the European VAT model and those which were present even in the erstwhile indirect tax regime in India, it has still proved to be unique.

If the principles pertaining to composite and mixed supply are not clarified, it may lead to a plethora of litigation and issues might arise in taxability and rate application. As the transactions are becoming complex day by day, a humungous task lies before the Authorities for Advance Rulings and the Appellate Authorities for Advance Rulings.

The most significant shortcoming of the GST framework in India is the lack of guiding principles. As seen from the discussion above, the GST law does not have answers to many questions, for which reliance has to be placed on principles laid down by the CBEC Guide and the European VAT model. This only leads to misinterpretations and assumptions, as the provisions which are ambiguous in nature have to be interpreted in reference to these principles which may or may not be fit to clearly understand the intention of the legislature behind incorporating a particular provision. Lack of guiding principles has also increased litigation significantly, especially with regards to composite and mixed supply, since it affects the taxability and rate of taxation of supplies.

Another difficulty in the framework of composite and mixed supply is its interplay with the treatment of job work under GST. There were a lot of ambiguities as to the difference between the definition of “composite supply” and “job work” in the initial days after the introduction of GST in India. According to the GST Guidance Note for Textiles Sector,³⁰ (“the Guidance Note”) this difference has to be ascertained by understanding the distinction between the expressions “naturally bundled” and “unnaturally bundled”.

None of the expressions have been defined in the GST framework. The Guidance Note observes that “the recipient of the supply has no option to decide whether he wishes to receive the various elements of the supply being provided as a bundled supply”. This means that if a

³⁰ CENTRAL BOARD OF INDIRECT TAXES & CUSTOMS, GST GUIDANCE NOTE FOR TEXTILES SECTOR (2017).

recipient has an option to refuse to receive an element of the supply, the supply cannot be termed as a composite supply. “Job work” comes into picture when the job worker, i.e. the supplier works upon the goods belonging to the principal, i.e. the recipient. However, the position becomes ambiguous when the job worker supplies some goods as part of the supply of job work. It is yet to be clarified whether such a supply would still be considered as a job work or not.

The next challenge involved in the concept of composite and mixed supply is that of divisible and indivisible contracts. The concept of splitting of composite as well as mixed supply has been discussed in this paper. The question remains that since a mixed supply has to be made for a “single price”, can the supply take place independently, but still qualify as a mixed supply.

It may be concluded from a perusal of the above, that there is still a lot which is required to be done to avoid litigation in this regard. Though the CBIC and the Council have been highly vigilant to clarify all the ambiguities with respect to composite and mixed supply, there is still a long way to go.

As the Indian economy moves forward into a new era of becoming the world’s fastest growing economy, the transactions will become much more complex and the market will become more diverse. With this, the concept of composite and mixed supply would need further clarifications and would be required to be developed further.