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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

% *Date of Decision: 18.05.2023*

+ **W.P.(C) 11430/2022**

M/S MCDONALDS INDIA PVT. LTD. Petitioner

Through: Mr Tarun Gulati, Senior
Advocate. with Ms Priyanka
Rathi, Mr Ashwani
Chandrasekaran & Ms
Shubhangi Gupta, Advocates.

versus

**ADDITIONAL COMMISSIONER, CGST
APPEALS - II, DELHI & ANR.** Respondents

Through: Mr Akshay Amritanshu,
Advocate.

CORAM:

HON'BLE MR. JUSTICE VIBHU BAKHRU

HON'BLE MR. JUSTICE AMIT MAHAJAN

VIBHU BAKHRU, J. (Oral)

1. M/s McDonald's India Pvt. Ltd. (hereafter 'the petitioner') has filed the present petition impugning an order dated 14.02.2022 (hereafter '**the impugned order**') passed by the Appellate Authority (Additional Commissioner, CGST Appeals - II, Delhi) rejecting the petitioner's appeal against an Order-in-Original dated 31.08.2020.

2. The petitioner is a company incorporated in India and is a subsidiary of McDonald's Corporation, USA (hereafter '**McDonald's**')

USA’).

3. The petitioner had entered into a service agreement dated 01.01.1996 (hereafter ‘**Service Agreement**’), whereby the petitioner had agreed to perform certain services. The petitioner claims that it is an independent service provider for the services falling within the scope of the Service Agreement. The petitioner is entitled to a consideration on cost plus 10% mark-up basis for the services rendered under the Service Agreement. The petitioner claims that the services rendered by it to McDonald’s USA are ‘zero rated supplies’ under Section 16 of the Integrated Goods and Services Tax Act, 2017 (hereafter ‘**IGST Act**’).

4. The controversy in the present petition relates to the period of April 2018 to March 2019. The appellant claims that during the said period, it had provided services under the said Service Agreement without payment of Integrated Goods and Services Tax (hereafter ‘**IGST**’) and thus, is entitled to refund of tax paid on inputs (hereafter ‘**ITC**’)

5. The petitioner filed an application dated 04.08.2020 for refund of goods and service tax paid on the inputs used for the services rendered to McDonald’s USA, its holding company, under the Service Agreement.

6. Respondent no. 2 issued a Show Cause Notice dated 14.08.2020 proposing to reject the petitioner’s claim for refund of ITC of ₹9,26,34,542/- as claimed by the petitioner.

7. The petitioner responded to the said Show Cause Notice by a letter dated 27.08.2020. The Adjudicating Authority considered the petitioner's application for refund of ITC and rejected the same by the Order-in-Original dated 31.08.2020. The Adjudicating Authority held that the services rendered by the petitioner could not be considered as export of services as the services rendered by the petitioner were intermediary services and therefore, the place of supply of the said service was in India.

8. The petitioner preferred an appeal against the Order-in-Original dated 31.08.2020 before the Appellate Authority. However, the same was rejected as well.

9. The Appellate Authority upheld the decision of the Adjudicating Authority, holding that the services rendered by the petitioner were intermediary services and the place of supply was in India. The Appellate Authority also held that the services included making periodic visits to existing and prospective suppliers on behalf of McDonald's USA and in terms of Section 13(3)(b) of the IGST Act, the supply of such services was located in India as it required the personal presence of the recipient of services or the person acting on its behalf. The Appellate Authority held that the provisions of Sections 13(3)(b), 13(5) and 13(8)(b) of the IGST Act covered the petitioner's case and held that the place of supply of services was in the taxable territory (India) and did not qualify as export of services under Section 2(6) of the IGST Act.

Submissions

10. Mr Gulati, learned senior counsel appearing for the petitioner, submitted that the impugned order passed by the Appellate Authority was beyond the scope of the Show Cause Notice dated 14.08.2020 and further did not arise from the petitioner's appeal against the Order-in-Original dated 31.08.2020 passed by the Adjudicating Authority. He submitted that the impugned order is liable to be set aside on this ground alone.

11. Next, he submitted that the Adjudicating Authority as well as the Appellate Authority has misconstrued the services rendered by the petitioner in terms of the Service Agreement. He submitted that there was a separate agreement (being a Master License Agreement – hereafter '**the MLA**') between the petitioner and McDonald's USA, whereby the petitioner was granted non-exclusive rights to certain intellectual property of McDonald's USA including the right to sublicense the same with the approval of McDonald's USA. He stated that in terms of the MLA, the petitioner had entered into franchisee agreements with various parties. The petitioner was duly discharging its liability to pay royalty to McDonald's USA under the said agreement. He stated that in terms of the MLA, the petitioner was liable to pay consideration to McDonald's USA. It was contended that the Authorities had confused the MLA with the services provided under the Service Agreement.

12. He referred to the Service Agreement and submitted that the

services rendered by the petitioner under the said agreement were independent services and did not involve any third-party supplier. He also contended that the issue involved in the present case was covered by an earlier decision of this Court in *M/s Ernst and Young Limited v. Additional Commissioner, CGST Appeals-II, Delhi & Anr.*: W.P (C) 8600/2022, decided on 23.03.2023 and *M/s Ohmi Industries Asia Private Limited v. Assistant Commissioner, CGST*: W.P. (C) 6838/2022, decided on 29.03.2023.

Reasons and Conclusion

13. The principal question involved in the present case is whether the petitioner is an intermediary within the meaning of Section 2(13) of the IGST Act in respect of services rendered under the Service Agreement.

14. The petitioner had entered into two agreements with its holding company – McDonald’s, USA. The Recitals of the said agreements provided the context of the agreements. The MLA records that McDonald’s USA had developed and operates a restaurant system (hereafter ‘**McDonald’s System**’). The same includes proprietary rights in valuable trade names, service marks and trademarks including the trade name ‘McDonald’s’ and ‘McDonald’s Hamburgers’, designs and colour schemes for the restaurant buildings, signs, equipment layouts, formulas and specification for certain food products etc.

15. In terms of the MLA, McDonald’s USA had granted a non-exclusive license to the petitioner to adopt and use McDonald’s System in respect of certain intellectual property owned by it. Article 2 of the

MLA, which sets out the scope of the license granted by McDonald's USA to the petitioner, is set out below:

“2. License Grant and Term. Licensor grants to Licensee for the following stated term the non-exclusive right, license and privilege (“License”):

(a) to adopt and use the McDonald's System in Restaurants to be constructed at locations to be mutually agreed upon by the parties hereto in India in accordance with the terms and conditions of this Agreement, and

(b) to advertise to the public that it is a licensee of Licensor, and

(c) to adopt and use, but only in connection with the sale of those food and beverage products which have been designated by McDonald's at the Restaurants, the trade names, trademarks and service marks which McDonald's shall designate, from time to time, to be part of the McDonald's System and

(d) subject to the prior written consent and approval of Licensor, to sublicense to approved individuals or corporate entities (“Franchisee”) the rights conferred on it by this Agreement or to enter into such other arrangements as Licensee deems advisable for the interim operation of any of the Restaurants. Any sublicenses shall contain provisions to the effect that, upon the termination of this Agreement for any reason, the sublicenses shall be deemed to be automatically assigned to Licensor, which hereby accepts such assignment, and Licensor shall be deemed to be substituted for Licensee as Licensor under such sublicenses. Licensee agrees to insert provisions in each of such sublicenses whereby the sublicensee shall acknowledge and agree to such assignment to Licensor.”

16. Pursuant to the license granted by McDonald's USA, in terms of the MLA, the petitioner has entered into Franchise Agreements with various franchisees for operating McDonald's Restaurants. It is stated that the royalties received by the petitioner from the franchisees are

subjected to tax and are not a matter of controversy.

17. The petitioner is liable to pay an initial franchisee fee for each restaurant operated or franchised by it. In addition, it is also liable to pay royalty equal to 5% of the gross sales from the operation of all restaurants on a monthly basis. There is no controversy regarding the payments made by the petitioner to McDonald's USA under the MLA.

18. In addition to the above, the petitioner has also entered into the Service Agreement with McDonald's USA for performance of certain services. The scope of services to be provided by the petitioner under the Service Agreement is set out in Article 2 of the Service Agreement. The same is reproduced below:

“2. Services - At McDONALD'S direction, McDONALD'S INDIA shall perform the following services on McDONALD's behalf in the Territory:

- A. Conduct research on subjects including consumer attitudes, demographics, marketing and advertising strategy;
- B. Investigate the timing and location of Restaurant openings and other strategic matters;
- C. Conduct interviews, make reference checks, and perform certain other screening services in connection with potential joint venture partners, franchisees and employees necessary to operate McDonald's Restaurants;
- D. Research and develop any necessary or desirable modifications to the McDonald's System including (1) food formulas and specifications for designated food and beverage products, (2) methods of inventory control and quality assurance, (3) equipment layout and design, (4) business practices and procedures, (5) bookkeeping and accounting procedures, and (6) other management, advertising and personal policies:

E. Develop and institute training programs at various local sites designed to give the Covered Entitles expertise in all facets of the McDonald's System:

F. Consult with and make periodic visits to existing and prospective suppliers concerning all matters related to the procurement of supplies for McDonald's Restaurants in the Territory:

G. Perform any other services requested in connection with the introduction of the McDonalds's System to the Territory."

19. It is material to note that the scope of services as mentioned in the Service Agreement, read in isolation, do not entail procurement or facilitating services from third-party suppliers.

20. It is material to note that the Show Cause Notice dated 14.08.2020 issued by respondent no. 2 did not specifically set out any reason in detail for denial of refund of ITC as claimed by the petitioner. The Show Cause Notice merely stated that "*Place of provision appears to be in India. ITC availed appears to be not admissible as per CGST Act*".

21. The Show Cause Notice was in broad terms. However, the petitioner was made aware that the principal question is whether the petitioner is an intermediary in the context of the services rendered by it. The Adjudicating Authority had considered the Service Agreement and highlighted Recitals in the said agreement for the purposes of concluding that the services rendered by the petitioner were in the nature of intermediary services. The Recitals as emphasized by the Adjudicating Authority are underlined and set out below:

“Whereas, McDonald’s will be obligated under the terms of certain agreements to provide certain know-how and business processes and to render certain services to subsidiaries, joint ventures and other commercial entities that participate in the McDonald’s System (the “Covered Entities”), such services to include training and technical assistance in the operation of the McDonald’s System in the Territory;

Whereas, McDonald’s wishes to obtain operating efficiencies and economics in adapting and introducing the McDonald’s System to the Territory by contracting certain services to an Indian based service organization in lieu of furnishing these services from its Oak Brook Headquarters;”

22. The Adjudicating Authority held that the petitioner was performing services on behalf of McDonald’s USA in the backdrop of McDonald’s USA’s obligations. Paragraph 5 of the impugned order reads as under:

“5. On perusal of the above, it appears that the services which should be performed by the McDONALD’S India on behalf of McDONALD’S shows for enhancing chain of McDONALD’S Restaurant/ McDonald’s System and for that part the expenditure part will be reimbursed by McDONALD’s. The service fee which bars upto 10% of Authorized Expenditure will also be provided by McDONALD’s to McDonald’s India. The base of whole agreement is to enhance their McDonald’s System/ Restaurant Service having specialization of its know-how. The know-how term is nothing but a intellectual property right for which franchisee give them franchisee fee and royalty. The input invoices also support it. The ultimate buyer of provided service under agreement is the franchisee who in their turn give them franchisee fee and royalty fee. To support their franchisee the franchisor has developed McDonald’s Systems. The McDonald’s India is doing their business to just support for conduit of McDonald’s Systems, so that their franchise business will enhance and for that part the service fee upto 10% was fixed.”

23. In view of the aforesaid reasoning, the Adjudicating Authority rejected the petitioner’s claim for refund of ITC.

24. Rendering service on behalf of another person does not render

the service provider an intermediary. These issues are covered by the recent decision of this Court in *M/s Ernst and Young Limited v. Additional Commissioner, CGST Appeals-II, Delhi & Anr.* (*supra*) and *M/s Ohmi Industries Asia Private Limited v. Assistant Commissioner, CGST:* (*supra*).

25. However, if it is found that McDonald's USA is obliged to perform certain services to third parties and the petitioner is facilitating or arranging such services from third-party suppliers; the services performed by the petitioner may fall within the scope of intermediary services. However, it is essential that the principal service, the supplier of such services, and the service purchaser are identified to ascertain whether the services performed by the petitioner are those of a facilitator or one that arranges such services. The Order-in-Original has not analysed the services rendered by the petitioner on the aforesaid anvil.

26. The impugned order appears to be proceeded on a somewhat different basis. The Appellate Authority has held that the petitioner was acting as a mediator between prospective joint ventures and franchisees, where the main supplies were made by McDonald's USA and ancillary supplies were provided by the petitioner.

27. We find no basis for the Appellate Authority to have concluded that the petitioner acts as a mediator between joint ventures/ franchisees and McDonald's USA. The Appellate Authority has not considered that the MLA, which entitles the petitioner to enter into sub-licenses with

franchisees, is a separate agreement. Further, certain observations made in the impugned order also indicates that the Appellate Authority has proceeded on the basis that providing services on behalf of another party amounts to acting as an intermediary.

28. According to the Appellate Authority, the place of services supplied by the petitioner is in India, under Sections 13(3)(b) and 13(5) of the IGST Act. However, this was not the subject matter of controversy that had travelled to the Appellate Authority. There is no such allegation in the Show Cause Notice dated 14.08.2020 – which, as the Order-in-Original dated 31.08.2020 indicates, was preceded by a pre-consultation – or the Order-in-Original. We find merit in the contention that no such additional grounds for rejecting the petitioner’s claim for refund could be raised *suo motu* by the Appellate Authority, in an appeal preferred by the petitioner. The impugned order is liable to be set aside on this ground alone.

29. Having stated the above, we also consider it apposite to briefly examine whether the provisions of Section 13(3)(b) and Section 13(5) of the IGST Act are applicable in the present case. The said provisions are reproduced below:

“13. Place of supply of services where location of supplier or location of recipient is outside India.–

xxx

xxx

xxx

(3) The place of supply of the following services shall be the location where the services are actually performed, namely: –

(a) xxx

xxx

xxx

- (b) services supplied to an individual, represented either as the recipient of services or a person acting on behalf of the recipient, which require the physical presence of the recipient or the person acting on his behalf, with the supplier for the supply of services.

xxx

xxx

xxx

(5) The place of supply of services supplied by way of admission to, or organisation of a cultural, artistic, sporting, scientific, educational or entertainment event, or a celebration, conference, fair, exhibition or similar events, and of services ancillary to such admission or organisation, shall be the place where the event is actually held.”

30. Section 13(3)(b) of the IGST Act is applicable in respect of services where the physical presence of the service recipient or its representative in India is necessary. The Appellate Authority had reasoned that since the petitioner is required to “*consult with and make periodic visits to existing and prospective suppliers concerning all matters related to procurement of supplies*” on behalf of McDonald’s USA, Section 13(3)(b) of the IGST Act was applicable. In order to examine whether Section 13(3)(b) of the IGST Act is applicable, it is necessary to identify the service provider and the service recipient. In the present case, under the Service Agreement, the service recipient is McDonald’s USA and the petitioner is the service provider. The supply of services by the petitioner to McDonald’s USA does not require the physical presence of McDonald’s USA. We are unable to follow as to why the physical presence of the service recipient, that is, McDonald’s USA, in India is necessary for receiving the services rendered by the petitioner or any third-party supplier. Section 13(3)(b) of the IGST Act

contemplates the location of service, whereby the presence of a service recipient is necessarily to be in India.

31. Section 13(5) of the IGST Act contemplates the supply of services by way of admission to, or organisation of a cultural, artistic, sporting, scientific, educational or entertainment event. It also contemplates admission to, or organisation of a celebration, conference, fair, exhibition or similar events. Conducting interviews, making reference checks or performing any screening services in connection with potential joint venture partners, franchisees or employees has no connection with the services as contemplated under Section 13(5) of the IGST Act.

32. In view of the above, we consider it apposite to set aside the impugned order as well as the order passed by the Adjudicating Authority and remand the matter to the Adjudicating Authority to consider the petitioner's case afresh in light of the observations made in this order.

33. The petition is disposed of in the aforesaid terms.

VIBHU BAKHRU, J

AMIT MAHAJAN, J

MAY 18, 2023
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