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LEGAL IMPLICATIONS OF RECENT ISSUES IN THE HOSPITALITY SECTOR IN INDIA

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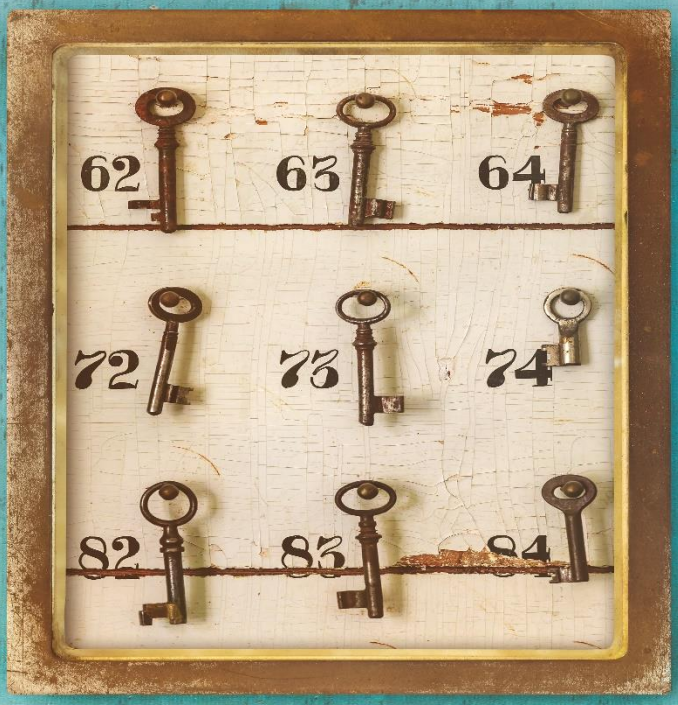

FOREWORD

Set against the backdrop of one of the most difficult periods in the hospitality sector, ELP's booklet is an attempt to address certain legal issues which the industry has been facing during the pandemic.

We have chosen a few recent issues and incidents which occurred in the industry and have analyzed these from a legal perspective. Some of these issues include the duties of independent directors of ailing hotel companies and the rights of hotel employees for unpaid wages.

We have also included an article on a guest's 'right to be forgotten' i.e. have their personal data deleted or removed from the hotel's database.

With the hospitality sector facing multiple headwinds, every opportunity of tax optimization is a boon. To this end, ELP's tax team has authored an article which has outlined some of the key tax optimization and mitigating strategies, that can be adopted by the industry to optimize tax costs.

Our team of hospitality specialists has endeavored to simplify and present these issues in a commercially attuned and reader friendly manner.

We hope this makes for some interesting reading. We value every reader's opinion and welcome your feedback.

Warm regards

ELP's Hospitality Team

01

Duties of Directors of Ailing Hotel Companies

Overview

This article has been written against the backdrop of the recent resignations tendered by the Independent Directors of a hospitality chain. The article discusses certain Sections of the Companies Act which offer regulatory guidance to Independent Directors. It also covers the level of protection offered to Independent Directors under Section 149(12) of the Companies Act and Regulation 25(5) of SEBI's LODR Regulations.

Asian Hotels (West) Limited (**Owner**) was recently in the news on account of suspension of operations of Hyatt Regency, Mumbai. Apropos such suspension, the Owner has been beset by several challenges, one of which is the resignations tendered by the independent directors of the Owner. The independent directors have cited the financial crunch faced by the Owner and alleged non-compliances of applicable laws by the Owner. It was also contended that the Chairperson and other directors of the Owner failed to convene a meeting of the board of directors to discuss the financial condition of the Owner. This incident, coupled with the financial constraints faced by several hotel companies across the country, begets the question as to what duties directors have in such circumstances.

With the enactment of the Companies Act, 2013 (**Companies Act**), the duties of directors were codified. Section 166(2) of the Companies Act requires a director of a company to "*act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of environment*." While the erstwhile jurisprudence only contemplated fiduciary duties of a director towards the company, the Companies Act has now extended the duties to not just the company but also the company's employees and shareholders, the community and for the protection of environment. This provision has significantly broadened the scope of duties of directors.

Further, questions also arise as to which duty would be foremost pursuant to Section 166(2) under a given set of circumstances. Unlike jurisdictions where the company law specifies a hierarchy of duties, the Companies Act does not have any guidance on that. If we were to take the issue that has plagued most hotel companies during this pandemic, employee lay-offs within the permit of applicable laws could have helped most companies stay solvent by cutting down on their operating expenses. By ensuring the solvency of the company, the directors would have been compliant towards their duty to the shareholders of the company. However, they would at the same time be in breach of their duty to the employees of the company. On the other hand, if the board of directors were to act in the best interests of the employees, they would run the risk of the company becoming insolvent in the long run. Accordingly, until there is clarity from the legislature as to the manner in which effective compliance of Section 166(2) can be ensured, it would be important for directors to strike a balance and ensure that the interests of all relevant stakeholders are borne in mind whilst taking any decision.

As regards independent directors of a company, Schedule 5 of the Companies Act offers guidance to such directors in the manner in which they are to conduct themselves. The Schedule also prescribes a wide range of duties, some of which include assisting in protecting the legitimate interests of the company, shareholders and its employees. Further, where they have concerns about the running of the company or a proposed action, independent directors are to ensure that these are addressed by the Board and, to the extent that they are not resolved, insist that their concerns are recorded in the minutes of the Board meeting. However, Section 149(12) of the Companies Act and Regulation 25(5) of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations 2015 do accord some level of protection to independent directors by stipulating that they could be held liable, only in respect of such acts of omission or commission by a company which had occurred with their knowledge, attributable through Board processes, and with their consent or connivance or where they had not acted diligently.

Another aspect that all directors ought to bear in mind is whether the company meets the insolvency test. Under Section 66(2) of the Insolvency and Bankruptcy Code, 2016 (*whose operation was suspended for a year on account of the outbreak of Covid-19*), directors of a company would be

personally liable to make such contribution to the assets of the company if such director or partner knew or ought to have known that the there was no reasonable prospect of avoiding the commencement of a corporate insolvency resolution process in respect of the company and such director or partner did not exercise due diligence in minimizing the potential loss to the creditors of the company. Effectively, personal liability would accrue if a director allows a company to trade or incur debts knowing fully well that the Company was unlikely to meet its liabilities.

What then can the directors of hotel companies do in the present circumstances apart from playing by the book and exercising his/her duties with due and reasonable care, skill and diligence? They could revisit their directors and officers (D&O) liability insurance policies to ascertain the nature of liabilities that would be covered. Like other insurances, D&O policies also come with several exclusions and it would thus be important to get a sense of the level of protection accorded to them. Given the case of the Owner, it would also be important to check the extent to which the policies cover the directors for matters that may relate to issues during their term but arising only post their resignation. The D&O policy should help protect the interests of the directors considerably.

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- *This article has been published in ET Hospitality*

02

Rights of Hotel Employees for Unpaid Wages

Overview

The article discusses the rights of employees against owners and operators of hotels in case of non-payment of wages. In this article, the authors analyze the recent suspension of operations by a prestigious hotel in Mumbai and examine who would be responsible to the employees – would it be the owner or the operator? It also discusses how Labour Courts could react in such circumstances.

Hotel chains are not usually the owners of the hotels they manage but merely their operators. The entities who actually own the property (**Owners**) enter into Hotel Management Agreements (**HMAs**) with these hotel brands to operate their properties for a fee (**Operators**). On paper the employees are the employees of the Owner but at the same time they are entirely under the control and supervision of the Operator.

It is no secret that the hospitality sector, being a contact intensive sector, has been severely impacted as a result of the outbreak of Covid-19. Occupancies have plummeted to all time lows. As a result, all hotels have struggled to make ends meet. The hospitality sector, being one of the hardest hit, has been constrained to reduce staff strength.

Hyatt Regency, Mumbai, recently announced that it was suspending operations temporarily as no funds were allegedly forthcoming from the owner of the hotel. It is reported that the employees of the hotel have filed a case against the Owner and Hyatt, the Operator, before the relevant industrial court. Whilst we do not propose to delve into the merits of this particular case, the incident has brought into the spotlight the job losses occurring in this otherwise profitable industry, and thrown open the debate as to who would be held liable by the courts in case of closure of a hotel and for the payment of unpaid wages.

Under typical HMAs, the employees of the hotels are stated to be the employees of the Owners. However, the power to hire, fire, train, supervise and control these employees, often vests solely with the Operators. Wages are paid by the Operators as they have exclusive control over the operating accounts of the hotels. Owners have very little say in respect of the costs related to hotel employees' wages, benefits and compensation programs whilst finalizing the budgets proposed by the Operators. The responsibility to conduct employee relations in accordance with the prevailing labour laws and best industry practices is that of the Operator. The logical question then arises is whether the Operators could be deemed to be the employers of the hotel staff.

It is, therefore, likely that in case of closure of a hotel, retrenchment of employees or non-payment of wages, the employees could seek redressal jointly against the Owners and Operators. Owners could submit a defence where they say that since they have no control whatsoever over any aspect of the employees' employment, they are not the principal employers but merely acting as contractors supplying employees to the Operators and that the Operators are the principal employers of these employees. In such a scenario, the labour courts could hold both parties jointly responsible for any breach of law, "Unfair Labour Practice" or for payment of the unpaid wages of the employees. Alternately, in cases where the operating fees are paid out by the Operators to themselves from the gross revenue of Hotels before payment of wages to employees, the Courts could be more inclined to hold the Operators responsible for the unpaid wages rather than the Owners who may in such circumstances not receive a share from the gross revenue.

The labour courts could also disregard the agreed priority of payments under the HMAs and the financing documents and require that employee wages and other statutory payments take priority over the operator's fees, owner's share and the lender's dues. Operators and Owners may also be directed to deposit the back wages of workers in court - pending decisions in case of disputes - that are taken to court.

What then can the Operators and Owners do to mitigate their liabilities in such scenarios? A starting point would be to have abundant clarity in the HMAs for eventualities in force majeure situations such as the present pandemic. Owners and Operators can revisit their arrangements and decide how funds

could be apportioned in unprecedented situations and arrive at a mutually agreed strategy keeping the long term interests of the hotel in mind which every Operator acting as an agent is required to do.

Operators could also revisit the extent of their control over employee related matters. Courts in India have usually held the following factors relevant while determining whether an employer-employee relationship exists: (i) responsibility for payment of the salary; (ii) exercise of control and supervision over the work of the employees; (iii) responsibility for selection and appointment of the employees, and (iv) exercise of disciplinary authority over the employees. In view of the above tests, Operators who do not want to take on the responsibility of employees may want to increase the Owners' involvement in all of the above.

It may also be prudent for Operators and Owners to engage in discussions with their insurers and understand the extent to which risks arising on account of non-payment of wages to, or termination of employees, would be covered. Perhaps business interruption insurances could be taken for longer periods so as to be able to cover employee salaries, among other costs, until the business is up and running. Given that the hospitality industry is entirely driven by its workforce, it may possibly be the right time to introduce a reserve for employee related payments. This could be similar to the FF&E reserves that hotels are usually required to maintain and would ensure availability of funds for salaries in cases where the hotels are temporarily non-operational.

Most importantly, we are of the view that both the Operators and the Owners work in tandem while dealing with any unforeseen situation. The reputation and goodwill of hotel chains may require them to absorb some losses in the interest of providing job security for their employees and to retain brand loyalty of their guests. Operators and Owners must work out an equitable method of sharing these losses.

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- *This article has been published in ET Hospitality*

03

Guest Data – Right to be forgotten

Overview

In this article the authors discuss how 'Guest Data' is increasingly becoming a complicated and debated issue in the hospitality sector. More specifically the article deep dives into the concept of 'right to be forgotten' which is an individual's right to have their personal data deleted or removed from the database (where this data is stored and processed by any third party). The article also analyzes the 'right to be forgotten' against the context of GDPR and India's Information Technology (Reasonable security practices and procedures and sensitive personal data or information) Rules, 2011 (IT Rules).

In the past few years, there is no doubt that both hotel owners and operators have realized the value of guest data. The sharing of this guest data between the owner and operator though is increasingly becoming a complicated and strained issue.

Typically, in hotel management contracts, the hotel operators retain the exclusive rights over such data.

The contention over access of this data is borne out of the insights that the data would yield. Apart from names, addresses and other demographic data, more personal information relating to health and preferences is also stored. All of this needs to be viewed against the backdrop of increasing threats to privacy and efforts to monetize personal information. With personal data becoming increasingly vulnerable to misuse, customers are naturally demanding due protection. To this end, businesses are implementing systems for data protection to comply with law and meet the expectations of their customers.

Operators now seek the prior consent of guests to store and process their information. While seeking such consent, certain operators offer the 'right to be forgotten' to the guests. The 'right to be forgotten' implies an individual's right to have their personal data deleted or removed from the database where this data is stored and processed by any third party. Such a right would entitle guests to request to have their personal data permanently removed from the database of the hotels.

Hotel operators are bound by the provisions of the General Data Protection Regulation (**GDPR**), which sets out stringent provisions for protection of personal information of European Union (**EU**) subjects (which translates to European hotel guests). The reach of the GDPR extends even beyond the borders of the EU which is why Indian hotel operators must comply.

India, unlike the EU (which follows GDPR Rules) has no specific legislation on personal data protection other than in relation to electronic data under the Information Technology (Reasonable security practices and procedures and sensitive personal data or information) Rules, 2011 (**IT Rules**). The IT Rules do not incorporate the 'right to be forgotten', although it embodies consent requirements for collection, processing and storage. Further, a corporate or any person on its behalf who holds this sensitive personal data or information cannot retain information post the period of time it is required to be retained under law.

The 'right to be forgotten' was incorporated in the Personal Data Protection Bill, 2019 (**PDP Bill**), which was mooted in 2019 and is still pending. However, judicial decisions have dealt with such rights in the recent past. In the Supreme Court's landmark judgment in 2017 (*Justice K S Puttaswamy (Retired) and Another vs. Union of India and Others*) the 'right to privacy' was recognized as an individual's fundamental right being an integral part of both 'life' and 'personal liberty' under Article 21 of the Constitution. In the same judgment, the Supreme Court, while referring to the GDPR, observed that any recognition of the 'right to be forgotten' in India would be subject to certain qualifications. Such qualifications could include: where the information/data is necessary for exercising the right of freedom of expression and information, for compliance with legal obligations, for performance of a task carried out in public interest, on the grounds of public interest in the area of public health, for archiving purposes in the public interest, scientific or historical research purposes or statistical purposes, or for the establishment, exercise or defence of legal claims. Indian High Courts have also expressly recognized the 'right to be forgotten', albeit without a reference to such qualifications.

Although the 'right to be forgotten' is recognized, such a right is not absolute. Hotels in India are legally mandated to retain or record certain information such as the names and addresses of all guests, the

date and time of their arrival and departure and other prescribed particulars. Further, if a crime has been committed, the local police authorities may also require the hotels to produce data in respect of the concerned guests. During the Covid-19 pandemic, hotels have been required to collect and share with local authorities, information pertaining to their guests' health.

Accordingly, hotel operators would need to note that, even though such a right is not expressly provided to guests, they would, under law, be authorized to seek erasure of their data. Further, where such right has been provided, it would be advisable to apprise guests of the qualifications of such rights as prescribed by the Supreme Court and, if relevant, the GPDR. Instead of offering an erasure of all data provided by the guests, hotels could consider retaining basic information such as names, addresses, date and time of their arrival and departure (and additional details as are usually sought by local authorities) for the limited purpose of complying with the relevant laws, and offer erasure of sensitive personal data and information such as guest preferences and satisfaction.

However, hotels may be caught between the asymmetry between GDPR and Indian laws. Given the global nature of the travel and hospitality industry, there is a need for an international convention for data privacy for this sector - which will require its members to adopt and align to appropriate domestic laws for this industry.

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- *This article has been published in ET Hospitality*

04

INTERPLAY OF GST AND THE HOSPITALITY INDUSTRY

Overview

Set against the severe cash flow and financing crunch the industry is facing, this article has outlined some of the key tax optimization and exposure mitigating strategies that can be adopted to optimize tax costs.

During the pandemic, the hospitality industry has struggled with low occupancy rates, steeply decreased revenues (coupled with additional expenditures on maintaining government prescribed SOPs) as well as the pressure to keep business afloat. The Federation of Hotel and Restaurant Associations of India (**FHRAI**) had submitted representations urging immediate support from the government to revive the industry.

The need for a GST specific relief for the hospitality sector was a common thread that echoed throughout the industry. Unfortunately, no reliefs were given to the industry on the tax front. Given that the industry is facing multiple headwinds, every opportunity of tax optimization is a boon. To this end, our article has outlined some of the key tax optimization and exposure mitigating strategies/positions, that can be adopted by the industry players to optimize tax costs.

1. Optimum Utilization of Input Tax Credit

A critical aspect of the GST system is the correct availment and utilization of credit as certain credits remain restricted. A thorough analysis of the nature of various expenditures should be carried out to prevent leakage of eligible credit.

For instance, GSTR-3B return for the month of September 2021 is the last chance for availing any pending input tax credit for procurements relating to financial year 2020-21. Once this timeline has elapsed, any GST paid on such procurements will be a hit to P&L and will create further cost pressure on the business.

2. Reversal of Common Input Tax Credit

Section 17(2) of the CGST ACT, 2017 provides for a mechanism for apportionment and reversal of common input tax credit (relating to procurement of services) for reversal of common service credit to the extent of exempt supplies to the total supply. It is common for various hotels/restaurants to undertake such reversal on a periodic basis.

It has been observed that many businesses consider every GST service credit as a common credit and undertake reversal on the entire pool of input services. Factually, there are various service procurements which are directly attributable to taxable outward supplies. A significant opportunity lies in strategizing and identifying procurement of such input services which relate directly to taxable outward supplies and are not subject to any reversal. This in turn reduces the quantum of reversal resulting in direct P&L benefit.

Businesses should undertake the exercise to identify these tax saving opportunities (in form of reduced input tax credit reversal) as the outcome in form of enhanced credits will be a direct P&L benefit.

3. Expansion Strategy

Expansion of business by way of more properties/increasing rooms in an existing property is an organic growth strategy adopted by most hospitality chains. While it is a general rule, ITC on expenses relating to additions to immovable assets are not eligible to GST credit, there are avenues to structure the construction/additions in a manner so as to avail GST credits on eligible procurements. Considering that expansion plans typically entail significant capital outlay, strategizing procurement contracts relating to expansion could lead to sizable cost optimization and benefit to the business.

For instance, vendor contracts for additions to or procurement of movable and immovable assets may be bifurcated and suitably structured to reflect the underlying intent and at the same time can be

optimized for GST credit availment. Similarly, input tax credit on expenses incurred for plant and machinery are available under GST and therefore it is critical to bucket expenses appropriately and create appropriate documentation to avail and substantiate eligibility of such GST credits.

Along with tax optimization, discharging GST liability appropriately is also of utmost importance to avoid any exposures relating to interest and penalty emanating from non-payment/short payment of tax. Following are some of the key aspects that shall require thorough analysis before adopting tax positions:

GST: Key Issues: Hotel and Lodging Sector	
TYPE OF SUPPLY	▪ Hotels supplying accommodation service often supply incidental services to its resident guests, viz. restaurant services, transportation services, sight-seeing, etc. ▪ Hotels to determine if their supply qualifies as independent supply, composite supply or mixed supply under GST because the same will determine the rate of GST applicable. ▪ GST treatment of such supplies will vary depending upon factors such as advertisements by hotel/online travel agents, booking confirmations, invoicing and accounting in the books of account. This has to be determined on a case-to-case basis.
CIGARETTES & AERATED BEVERAGES	▪ Certain products such as cigarettes and aerated beverages are also supplied by hotels. In such cases, evaluating whether the supply shall be treated as a composite or mixed supply is fundamental for discharging tax at appropriate rates. ▪ Supply of aerated beverages and supply of services by the restaurant are treated to be naturally bundled as supplied in conjunction to each other and hence is a composite supply of service classifiable under SAC 996331 chargeable at 18%. ▪ Sale of cigarettes is not treated as naturally bundled together with restaurant services. The services of the restaurant mainly involve serving of food and beverages alone in the normal course. Hence, supply of cigarette products is not a composite supply but a mixed supply chargeable at 28% and compensation cess at the rate applicable to cigarettes. Under GST, a mixed supply will have the tax rate of the item which has the highest rate of tax and thus cigarette will be treated as principal supply and 28% will apply on supply of restaurant services as well. ▪ The view is supported by ruling pronounced by AAR in the case of **Mfar Hotels & Resorts (P.) Ltd. [2020] 120 taxmann.com 442 (AAR –TAMIL NADU) [12-05-2020]**. ▪ In cases where the supply of cigarette products is treated as composite supply and a part of restaurant services, compensation cess shall not be

	charged on the outward supply and thus the input tax credit of compensation cess paid at the time of procuring such items becomes a cost in the chain. ▪ Therefore, classification for supply of goods and services is quite essential to discharge appropriate tax. Any incorrect classification will result in short payment of GST thereby exposing business to liability in the form of tax, interest and penalty.
ALCOHOL CONSUMPTION	▪ Supply of alcohol for human consumption is outside the purview of GST, being a non-taxable supply. ▪ However, input tax credit in proportion to such supply of alcohol will be required to be reversed.
ADVANCE RECEIVED/REFUND OF ADVANCE	▪ Hotels often receive advance in terms of the timelines identified in the contract for bookings at a future date. However, the final invoice is issued at the time of check-out after completion of the event. ▪ Advance may be for services exigible to GST at different rates viz. 5%/12%/18%. ▪ Options may be explored by hotels to minimize cashflow on GST payment on advance. ▪ Cases where advance received has to be refunded, the refund amount shall be the net amount after deducting GST in cases where timeline to avail re-credit of GST has elapsed.
CANCELLATION/ NO SHOW CHARGES	▪ Cancellation/no show charges may attract GST at the rate of 18% - being classified as services of 'tolerating an act' - as per a residuary entry of 18% in the absence of a specific entry.
COMPLIMENTARY STAY/FREE MEALS	▪ Complimentary stay (without charging any consideration)/Free Meals if provided to the hotel's own employees/management may be susceptible to the levy of GST, considering that employers and employees are 'related parties' and supply between such 'related parties' is treated as taxable supply under the GST Laws, even though it is made without consideration. In such scenarios, appropriate valuation also becomes important. The view is supported by ruling pronounced by AAR in the case of **Mfar Hotels & Resorts (P.) Ltd. [2020] 120 taxmann.com 442 (AAR –TAMIL NADU) [12-05-2020]**. ▪ Unlike employees of the hotel, auditors and consultants do not qualify as "related persons" of the hotel and thus one needs to analyze whether complimentary services to that class of persons qualify as a supply under GST law.

EXTRA BED/EXTRA PERSON/ UPGRADE CHARGES COLLECTED BY HOTELS	▪ Additional charges are collected by hotels for providing extra bed/ upgrade or accommodating an extra person. ▪ Such additional charge out results in the increase in transaction value of the unit of accommodation. ▪ Applicable GST rates are dependent upon the value of supply (tariff) which is a composite of total charges for the said accommodation including extra bedding, extra upgrade charges etc. ▪ The view is supported by ruling pronounced by AAR in the case of **Jewel Classic Hotels (P.) Ltd. [2021] 124 taxmann.com 38 (AAR – HARYANA) [25-06-2020]**.
ONLINE PLATFORMS	▪ For online platforms (such as makemytrip.com, hotels.com, Airbnb.com) which act as a conduit between the customer and the service provider i.e., hotels or accommodation providers, these will be recognized as electronic commerce operators (**ECOs**) who will have an obligation to collect tax at source (**TCS obligations**) and remit to the government. ▪ Further, such entities may also qualify as Online Information Database Access and Retrieval (**OIDAR**) service providers, and accordingly will have to take registration and remit tax.
CREDIT FOR MAJOR EXPENSES	▪ Credits in relation to major expenses for this industry i.e., works contract service and construction services are restricted and remain a cost in the system. ▪ For instance, lift/elevators, shall not be entitled for input tax credit when used in construction of immovable property since they take the character of building itself. The view is supported by ruling pronounced by AAR in the case of **Jabalpur Hotels (P.) Ltd. [2020] 118 taxmann.com 42 (AAR – MADHYA PRADESH) [08-06-2020].** ▪ Input tax credit of GST paid on supply of wood, board, mica, tapestry, paint, polish and other consumables and on labour supply meant for repair of existing furniture and fixtures will be available to applicant-hotelier in accordance with provisions of section 16 of CGST/RGST Act,2017. **{Rambagh Palace Hotels (P.) Ltd., [2019] 106 taxmann.com 172 (AAR – RAJASTHAN) [30-04-2019].}**
TRAVEL AGENTS	▪ While the concept of pure agent as existing under Service tax, has been continued even under GST, there has been a divergence in the practice being adopted by travel agents while charging their customers and claiming this exclusion. ▪ In some cases, the travel agent only raises an invoice for its agency fees and the service provider (e.g., hotels/airlines) directly raise their invoices on the ultimate customer.

	▪ In other cases, travel agents raise an invoice for both their agency fee and for the main service (e.g., accommodation service/transportation by air service), and the service provider (hotels/airline) raises its invoice on the agent. ▪ There remains an ambiguity with regards to which is a befitting structure fulfilling legal requirements.
SUPPLY TO SEZ	▪ Services of short-term accommodation, conferencing, banqueting, etc. provided to a SEZ developer or a SEZ unit shall be treated as an inter-State supply. ▪ If event management services, hotel, accommodation services, consumables, etc. are received by an SEZ developer or an SEZ unit for authorized operations, as endorsed by the specified officer of the Zone, the benefit of Zero-rated supply shall be available in such cases to the supplier. ▪ The view is supported by ruling pronounced by AAR in the case of **Carnation Hotels (P.) Ltd. [2019] 110 taxmann.com 196 (AAR - KARNTAKA) [16-09-2019]**. ▪ Hotels being unaware of the SEZ status of the customers may erroneously issue invoices levying improper GST and thus, hotels should ascertain whether the customer qualifies as an SEZ unit/developer at the time of entering into contracts with them/issuance of invoice to correctly collect and discharge GST.
GST TREATMENT OF STANDALONE RESTAURANTS	▪ In order to mitigate the risk of standalone restaurants being perceived as one operating in the premises of the hotel and charged at 18%, one needs to ring fence the restaurant (operationally and physically) from hotel operations. Suitable steps may be prescribed upon analysis of the arrangement to mitigate risk of attracting higher rate of GST. ▪ Further, appropriate transition/structuring may also be required if the restaurant is expected to cater for room service to resident guests. ▪ This could facilitate supplies at a lower rate of 5% by such restaurants. Room service related supplies will need to be structured appropriately. ▪ If the registered person provides accommodation and restaurant services from one premise charging 18% rate of GST and opens a standalone restaurant in another premise, then the rate of GST to be charged shall be 5% with ITC reversal in case of common accounts being maintained. The view is supported by ruling pronounced by AAR in the case of **Hotel Sandesh (P.) Ltd. [2021] 125 taxmann.com 134 (AAR - KARNTAKA) [26-02-2021].**

GST: Key Issues: F & B Sector	
SUPPLY OF SERVICE	▪ Under GST laws, as per the definition for restaurant services, supply of food and drinks by way of or as part of any service or in any other manner whatsoever, is deemed to be a supply of service. ▪ Therefore, the place of supply and the rate of tax shall have to be determined accordingly.
TAKE AWAY SALES	▪ There arises ambiguity as regards take-away sales or drive-in sales and whether these will be seen as "by way of or as part of any service or in any other manner whatsoever", to qualify as a deemed service. ▪ However, the service tariff code prescribed for restaurant services, specifically SAC 996331 is wide in scope and specifically covers "takeaway services, room services and door delivery of food" and it may be said that even take- away sales or drive-in sales would come within its ambit. ▪ The view is supported by ruling pronounced by AAR in the case of **Ananya Goyal [2018 (14) G.S.T.L. 299 (A.A.R. - GST)]**
INPUT TAX CREDIT	▪ Under the GST regime, restaurants are liable to pay GST at the concessional rate of 5%, but with the condition that input tax credits are restricted. ▪ Input tax credits in relation to supply of food and beverages and outdoor catering is restricted unless output supply is also of same category of goods/services. ▪ Hence, except for the hospitality sector itself, for other businesses, credits in relation to such supplies is restricted.
ANTI-PROFITEERING	▪ Certain restaurant operators have received an anti- profiteering notice requiring them to showcase how they have passed on the benefits under GST to the customers. ▪ Considering that this sector services the end customer [B2C], it is expected that this sector will face greater scrutiny from the anti-profiteering authorities, especially since there has been a change in rate applicable which should have had a consequential impact on the price of items supplied.
FREE ITEMS	▪ If there are free items (e.g., toys) provided along with meal, the GST treatment of such a free item becomes an issue to be addressed.

	▪ If GST becomes separately applicable to such free supplies, then it requires determination as to on what value should GST be levied.
SALE OF BOUGHT-OUT PRODUCTS	▪ Sale of bought out products cannot be classified as restaurant services as an important element of service (preparation/customer order) is missing in the said transaction and the said arrangement will be treated as the sale of goods. ▪ Hence, the GST liability on sale of bought out products needs to be discharged at GST rate applicable to those individual goods/products. ▪ The view is supported by ruling pronounced by AAR in the case of **Manoj Mittal [2021] 126 taxmann.com 48 (AAR - WEST BENGAL) [22-03-2021] and M/s Square One Homemade Treats [2019-TIOL-440-AAR-GST] [30-09-2019].**

In Conclusion

While GST regulations do not provide any specific benefit to the Hospitality sector, strategizing business transactions within the contours of regulatory embargo can go a long way in optimizing the GST cost of the business and in mitigating undue exposures emanating from unintended tax non-payments/short payments.

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AWARDS & ACHIEVEMENTS

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INDIA BUSINESS LAW JOURNAL AWARD WINNING LAW FIRM 2020 **Law Firm of the Year for:** ▪ Taxation ▪ International Trade INDIA BUSINESS LAW JOURNAL Deals of the Year 2016 DEALMAKER **Mergers & Acquisition Deal of the Year** for India leg of global joint venture between, Johnson Controls Inc., Hitachi, Ltd. and Hitachi Appliances, Inc., for air conditioning business	IFLR 1000 RECOMMENDED FIRM 2020 **Highly Recommended for:** ▪ Infrastructure ▪ Technology and telecommunications ▪ Transport ▪ Banking ▪ Capital Markets ▪ M&A ▪ Private Equity ▪ Project Finance	TOP RANKED Chambers GLOBAL 2020 Economic Laws Practice **Top Tier Firm in India for:** ▪ Tax ▪ WTO/ International Trade **Ranked for:** ▪ Competition & Antitrust ▪ Projects, Infrastructure & Energy ▪ Banking & Finance ▪ Private Equity ▪ Corporate & M&A ▪ Dispute Resolution **Spotlight Table:** International Cross Border Capabilities	The Legal 500 ASIA PACIFIC TOP TIER 2021 **Top Tier Firm in India for:** ▪ Dispute Resolution ▪ Projects and Energy ▪ Tax ▪ WTO/ International Trade ▪ Antitrust & Competition ▪ Corporate and M&A **Highly Recommended for:** ▪ Banking and Finance ▪ Capital Markets ▪ Investment Funds ▪ Real Estate and Construction ▪ TMT

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GAR 100 2020 **One of the world's top specialist arbitration firms, and amongst the only two firms in India that have been recognized and recommended for arbitration expertise.** **Asian Legal Business** ALB **Tier 1 Firm for M&A in India**	asialaw CLIENT SERVICE EXCELLENCE **Ranked as the Best Banking & Finance Team in India**	asialaw PROFILES Economic Laws Practice asialaw PROFILES OUTSTANDING 2020		
	Top Law Firm in India by Forbes Legal Powerlist Forbes Present LEGAL POWERLIST 2020 in association with legitquest ENLISTED AS THE TOP LAW FIRM (ABOVE 10 YEARS EXP.)	**Outstanding Firm** for Tax **Highly Recommended for:** ▪ Competition & Antitrust ▪ Dispute Resolution ▪ Energy & Natural Resources ▪ IT, Telco & Media ▪ Banking & Finance ▪ Projects & Infrastructure	**Recommended for:** ▪ Private Equity ▪ Capital Markets ▪ Corporate/M&A	**Notable for:** ▪ Construction & Real Estate ▪ Financial Services Regulatory ▪ Restructuring & Insolvency

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