4 CHAPTER ESSENTIALS OF CLASSIFICATION

4.1 SUPPLY CLASSIFICATION

Supply is not everything. Supply is specific. Supply if finite. Supply is knowable. Transactions in business can be tested to know if each of them fall within classification of supply. Supply is not turnover of business. Income reported is not turnover from supply. Accounting income cannot be assumed to be the result of outward supply, much less, result of taxable outward supply. Payment realization is not proof of supply. Realization of payment can raise suspicion about the possibility of underlying supply but not confirm it be the result of outward supply, much less, taxable outward supply. As a corollary, non-realization of payment is also not proof of absence of supply. And for this reason, any delay or permanent loss in realization of payment is of no consequence as to the taxability of supply, and therefore to the immutability of its recoverability. Admission that payment realized is consideration raises presumption about existence of supply. And burden rests on Payee to establish exclusion or exemption.

It is uncharitable to legislative labour in crafting seven (7) specific definitions to 'supply' along with specific and finite instances where recourse to legal fiction has been restored to, in order to exclude some and include some others, besides additional carve-outs and express exemptions. Such a complex construct of the definition of supply cannot be dismissed by treating 'everything to be supply' or 'all income to be the result of supply'.

Supply is defined in:

(I) section 7(1)(*a*) of CGST Act;

(II) section 7(1)(*aa*) of CGST Act;

(III) section 7(1)(*b*) of CGST Act;

(IV) section 7(1)(*c*) of CGST Act read with four (4) specific entries in Schedule I;

(V) sections 19(3) and 19(6) of CGST Act (see repetition in section 143 of CGST Act);

(VI) section 31(7) of CGST Act; and

(VII) section 35(6) of CGST Act.

<table>
<tr><th colspan="4">Supply</th></tr>
<tr><th>Non-taxable supply</th><th>Excluded supplies</th><th colspan="2">Taxable supplies</th></tr>
<tr><td rowspan="2">Alcohol-ENA, securities-money, 5-petro products and pure agency</td><td rowspan="2">Schedule III* plus (i) services not classifiable (ii) goods cultivated by agriculturists**</td><td>Exempt supplies</td><td>Others</td></tr>
<tr><td>Section 11(1)</td><td>Seven (7) definitions</td></tr>
</table>

** Only while applying any 'treatment' will they not be supply.*

*** Excluding those notified under RCM notification of goods.*

It is important to note that the 'forms' of supply in section 7(1)(*a*) of CGST Act do not apply to 'transactions' treated to be supply in section 7(1)(*aa*) of CGST Act. Even though transactions *inter se* association and its members resembles, say, sale of goods, absence of two parties (due to operation of 'principle of mutuality') takes these transactions out of section 7(1)(*a*) of CGST Act and for this reason, would not be liable to GST. However, the legal fiction in section 7(1)(*aa*) of CGST Act expressly overcomes the absence of essential ingredient (of the existence of two parties) to impute supply by legal fiction in these transactions *inter se* association and its members. Again, legislative humility and wisdom are salutary, in furnishing the missing ingredient to bring a non-exigible transaction into the taxing net. This need for express legislative language points to the specificity of the eight (8) forms of supply in section 7(1)(*a*) of CGST Act. Had it not been for the retrospective introduction of section 7(1)(*aa*) of CGST Act, nothing in unamended section 7(1) of CGST Act could have successfully landed the incidence of GST on transactions involving associations and its members. There is clearly no room of intendment, after all, it is not impossible that the vast expanse of the forms that supply occupies could not possibly accommodate transactions of associations. Specificity touches scope of every one of the forms of supply and the outermost boundary of each of them.

Further of Schedule II offers alteration (of treatment) but does not declare any transaction to be a supply by itself, when it is otherwise not a supply. In other words, unless a transaction is already determined to be a supply, occurrence of a transaction in Schedule II does not *ipsi dixit* raise any presumption about the transaction to be a supply. That would not be presumption flowing from Schedule II but an assumption. Supply must exist in fact, not assumed to exist. Also, express language in section 7(1A) of CGST Act makes this delineation explicit that supply is not dictated by occurrence of a transaction in Schedule II but the transaction must be one that is otherwise determined to be a supply, and recourse be had to the entries in Schedule II to determine the treatment to apply by alteration, if any, of the classification of object of supply. Government is even empowered to issue a notification under section 7(3) of CGST Act to create exceptions to classification of goods as services or *vice versa*, but not even any such notification will be

authorized to constitute a new classification of supply but only reconstitute the treatment applicable of the object of supply.

There are six (6) exclusions from incidence of GST and are found in:

(I) section 2(52) of CGST Act and 2(102) of CGST Act– money and securities;

(II) section 9(1) of CGST Act– alcohol and ENA;

(III) section 9(2) of CGST Act– 5 petro-products;

(IV) section 7(2)(*a*) of CGST Act read with Schedule III and section 7(2)(b) of CGST Act read with any notification issued;

(V) section 23(1)(*b*) of CGST Act– goods cultivated by agriculturists; and

(VI) rule 33 of CGST Rules– pure agency exclusion.

Exclusion from the incidence of tax is not to be misconstrued as exemption from tax, not even when they are *"treated as"* exempt supplies for the limited purposes of section 17(2) of CGST Act in section 17(3) of CGST Act or in *Explanation 3* to rule 43 of CGST Rules. Exclusion is not synonymous with exemption. Exclusion flows from statutory expression and exemption flows from notification under section 11(1) of CGST Act.

Abatement of taxable value (compared to invoice value) such as rule 32(5) of CGST Rules or Explanation 2-2A to GST tariff notification of taxable services, does not come within this fiction "as" exempt supply since legal fiction cannot be extrapolated to other (seemingly similar) instances unless supported by express statutory language or necessary intendment. Further, there may be some (misplaced) debate that another exclusion from value of taxable supplies in rule 33 could be exempt supply, but such valuation adjustment is only an exclusion from the quantification of tax but not an exclusion from supply. Unless such value abatements and exclusion of reimbursements from the value of taxable supplies are not artificial vivisection of the value of composite supply but affirmation in express statutory provisions that they are not to be included for all intents and purposes of affording any treatment under this law.

Abatement is to write-down the taxable value compared to invoice value. Abatement need not always be a negative adjustment. Although not called abatement, there can be write-up of the taxable value compared to taxable value, say, section 18(6) of CGST Act or section 29(5) of CGST Act. Adjustment of taxable value for computation of tax ought to be taken into consideration much later; involving them at the stage of classification of supply will contaminate the entire exercise.

To omit any transaction (partially or completely) while applying any 'treatment' in this law is not the same as excluding that transaction from the 'turnover' itself. Say, while determining applicability of threshold for registration or composition, none of these adjustments (write-downs

or write-ups) must be omitted although they will be, while applying any 'treatment', such as compliance under section 17(2) of CGST Act or section 44 of CGST Act.

Whether a transaction is supply or not must be examined entirely at the level of transaction and not at the level of the object involved (goods or services) or of its taxability (taxable, exempt or non-taxable) or of its valuation (excluded or included). The answer to the question – is this transaction a supply – will be binary, a 'yes' or a 'no'. The answer will not be connected to how much will be the quantum of this tax. If the transaction is determined to be a supply, then the question of quantification arises. But if the answer is that the transaction is not a supply, then the exercise of classification must stop right there.

4.2 CLASSIFICATION OF NO-SUPPLY

Not everything is supply. Not every payment realized must arise out of supply. Not every income in financial statements will be proof of supply. No-supply is when a transaction is not a supply as defined in GST law. Transactions that fall outside boundaries of definition of 'supply' will be 'no-supply'. There are not a few definitions of supply, but still, supply is not everything. Had Legislature intended that supply should be the entire boundless universe of transactions, the strife evident in crafting complex definitions of supply will be rendered otiose. Transactions that fall outside the definition and referred herein as 'no-supply' transaction, is not only those which fail to be admitted as supply but also those that are listed in schedule III and expressly declared as 'no-supply'.

Naysayers of strict interpretation assert that the definition of supply contextually refers to 'goods' and by strict interpretation should not include 'services' as a verb. That is, sale refers to sale of goods and is included in one of forms of supply as defined; how then can professional consultancy services be included in the definition of supply. While supply classification addresses the scope and extent of each transaction falling within the forms of supply, it will suffice to show that if one were to take away 'goods' as being the object of that contract and replace it with 'any service' (professional consultancy services) to find out if definition of supply fails to accommodate it.

Example 134: *License is permission to use, movable or immovable property. Professional opinion on a tax matter is also a license to use the knowhow located in the opinion document. It is a non-transferable license to use the knowhow for the purposes for which the licensee entered into this contract of supply.*

Example 135: *Sale is permanent transfer of property in goods including right of retransfer. Sub-contractors services to main contractor is permanent transfer of the services in the form of the works carried out including right to retransfer the said works to customer.*

Substituting object of contract involving verbal-services (services that are a verb) while applying the ingredients in the definition of relevant 'form' that supply takes in the context, one will be able to find that all professional services are reliably accommodated within supply as defined in the relevant statutory expression(s). The meaning – nature, scope, extent and limits – of each 'form' of supply is deliberated later in the course of examining supply classification.

Adverting to no-supply transactions, each 'form' is, without exception, pregnant with meaning expounded by over 100 years of judicial thought and consideration of various authorities now has the force of law in India. After all, Property law is over 135 years and Contract law over 145 years before introduction of GST law. Some of the newer legislations have the roots in legislations from before Independence and built on English Common Law principles. There are several other substantive legislations that illuminate our understanding of these 'forms' that transactions take. It helps to remind that the publication on GST and Allied Laws exposes the ingredients of each of these transactions to test whether they will be 'no-supply' to escape the incidence of GST even though the underlying financial arrangement may be in the course or furtherance of business.

Example 136: *Assignment is not a supply, even if the object of assignment are goods or services and a rate of tax can be located in either of the GST tariff notifications.*

Example 137: *Coparceners secure absolute title according to their respective share by a Deed of Partition of land (previously owned by HUF). This Partition is actually an exchange (of undivided share for divided share) and as such, exchange is very much a supply. But since the object of partition (land) is excluded from the incidence of tax, there will no tax incidence on this supply.*

Example 138: *Insurer acquires title to wreck after settling claim of Insured, not by some form of sale-by-legal-fiction but by operation of law – subrogation. And this Insurer can even sell and confer lawful title to buyer of wreck. Passing of title by subrogation is not supply.*

To attempt a definition is rash. But to construct a definition similar to the definition of supply in CGST Act could illustrate the possibilities that Legislature has elected to expressly exclude many transactions in business and bring out the deliberate legislative attempt to include a finite number of transactions in business, by crafting the statutory definition(s) of supply with much thought and consideration. Transactions that are not supply (or no-supply) may also be defined in the same manner as section 7(1)(*a*) of CGST Act to expose the exclusions *albeit* in the course or furtherance of business:

"No-supply includes:

(a) all forms of supply of goods or services or both NOT in the course of furtherance of business;

(b) all forms of supply by organizations governed by international agreements and treaty obligations of Republic of India to grant immunity from domestic tax; and

(c) all forms of no-supply of goods or services or both such as partition, transmission, assignment, subrogation, escheat, mortgage, forfeiture or destruction made or agreed to be made for a consideration by a person in the course or furtherance of business."

Further, it is possible that a transaction that is not expressly excluded from Schedule III may still not be a supply, not because it is a 'no-supply' but because it is omitted or unclassified in the Scheme of Classification of Services. Unclassified services are limited to services, because goods have a residual classification (entry 453 of Schedule III and entry 639 of Schedule II from 22 Sept. 2025 to GST tariff notification of goods). Unclassified services are those that cannot be fit into any of the entries in GST tariff notification of services. Supplies (of goods) by agriculturists where they are not notified under RCM notification of goods, remain non-taxable due to operation of exclusion under section 23(1)(*b*) of CGST Act to such Suppliers. Actionable claims, on the other hand, are goods but actionable claims that are not specified in section 2(*102A*) of CGST Act continue to remain goods, but (being non-specified actionable claims) stay excluded from being admitted as supply by Schedule III to CGST Act.

Supply (but not taxable)			**No supply** *(transactions not within definition of 'supply')*
Non-taxable supply	**Excluded supplies***	**Exempt supplies**	
Alcohol-ENA, securities-money, 5-petro products and pure agency	*Schedule III * plus (i) services not classifiable (ii) goods cultivated by agriculturists *****	*Section 11(1)*	

** Only while applying any 'treatment' will they not be supply.*

*** Excluding those notified under RCM notification of goods.*

It is remarkable that the expression 'supply' itself has had to be employed while describing certain transactions in Schedule III while declaring that they will NOT be 'treated' as supply. Transactions listed in Schedule III will be supply, except that when any 'treatment' is to be applied to them, and in those occasions, they will not be admitted to being a supply.

Example 139: *Section 22 of CGST Act is not a treatment; turnover of Schedule III transactions cannot be excluded from 'aggregate turnover' while examining requirement of registration. But rule 42 of CGST Rules is a treatment; for reversal of credit of Schedule III transactions will not be included as 'exempt supply' (unless expressed in legal fiction).*

Article 50(*c*) of the Constitution of India enjoins upon the Republic of India to *"foster respect for international law and treaty obligations"*. And where such agreements or obligations proscribe any incidence of domestic tax on such organizations, even without any exclusion (Schedule III to CGST Act) or exemption (section 11(1) of CGST Act), transactions 'by' such organizations are *ab initio* excluded. And this is another supervening form of no-supply. Circular 83/2/2019-GST dated 1 Jan 2019 affirms this position of law.

4.3 OBJECT CLASSIFICATION

Articles delivered need not be the 'object' of supply. And 'name' (of document) does not dictate the 'form' (of supply). The object of supply must be discerned by considering the (*i*) contract involving supply and (*ii*) express language as to the object of supply in that contract or (*iii*) (in the absence of express contract) intention of Parties about the object of supply. In earlier tax regime, intention of Parties had to make way for dominant object (that gave the name 'dominant object test') but was eventually unsuccessful in locating the object of contract, as noted in the catena of decisions in the context of 'works contract tax'. An attempt at offering a comprehensive list of these decisions has been made in para 3.7.2 of publication entitled GST and Allied Laws (2nd Edn.).

Example 140: *Fabrication and sale of rolling shutters was works contract involving sale of metal (MS) and service of fabrication under earlier tax (VAT-ST) regime. Sale of fabricated rolling shutters was (and still is) sale of goods.*

Example 141: *Printing of copyright (provided by customer) material was works contract (and currently job work of services), even where job-worker provided paper, ink, machinery and labour.*

Object of supply is traceable to the contract for supply, express or implied. It is important to note that all eight (8) forms of supply in section 7(1)(*a*) of CGST Act are one or other form of 'enforceable contract'; and as a valid contract, whose object must either be goods or services. All other definitions of supply are an illustrative sub-set of supply with legal fiction to include or exclude specific use-cases. It is for this reason that a deep understanding of Contract Act would be highly advisable (imperative even) to locate the object of supply. There is not a single transaction of supply, that can be shown not to arise out of a valid contract. Even when the legal fiction of 'distinct persons' is entertained, transactions *inter se* distinct persons would still

have to be admitted to be operating under a contract (capacity to contract of each distinct person assumed by legal fiction). And not even schedule I declares a no-supply to be transformed into a supply. In fact, schedule I upholds the requirement of all ingredients for a valid contract, by furnishing the ingredient of consideration, in cases where consideration is missing when distinct persons (or related persons) are transacting with each other.

Object of a contract is that which is the subject matter of *consensus ad idem*. When all parties are equal and they enter into a bargain, then the object is that which is bargained for and stated to be the object. But when unequals enter a bargain, then the object is that which the one with the lesser understanding recognizes to be the object of their contract.

Example 142: *Object of a dental implant procedure is healthcare service (Patient's understanding being less than that of the Orthodontist) which is the reason for them coming together into this contract.*

Example 143: *Job-worker delivers finished goods to customer, but the object of contract is not supply of those goods but of those services.*

Example 144: *Quality control report prepared based on products produced by Consumer Goods Company is not supply of goods (products) by Company to Quality Reviewer, but supply of testing service of goods by carrying out specified non-destructive testing methods.*

Example 145: *Export of prototype of microchip is not supply of goods, but supply of R&D services where the microchip is the form in which the research is delivered.*

Example 146: *Sale of EV battery with SIM card to turn-off power supply in case of payment default, is supply of service (battery-on-rent) and not supply of goods (sale of battery).*

GST law, however, mandates that classification of (*i*) goods MUST be based on Rules of Interpretation applicable to Customs Tariff Act and (*ii*) services be based on guidance contained in Explanatory Notes to Scheme of Classification of Services. In order to determine which of the application reference legislations must be examined, determining the object of contract is *sine qua non*. Any misunderstanding about the object of contract will be fatal to the classification exercise undertaken.

4.4 ACCOUNTING CLASSIFICATION

Rules of accounting lay down a methodology of classification of 'heads of account' that make up the 'chart of accounts'. And it is this chart of accounts that appear in schedules to financial statements. The methodology for naming the chart of accounts, does not guide classification of taxable supplies in GST. In fact, accounting classification is unreliable as a guide to classification of

supply or its object for GST purposes. Whether the incidence tax is to be discharged on forward charge basis or reverse charge basis, classification of taxable supplies is agnostic of the classification adopted for arriving at the chart of accounts.

Example 147: *Transportation charges (under operating expenditure) does not affirm inward supply of GTA services.*

Example 148: *Cost of R&D expenses capitalized in books of accounts affirms enduring nature of its benefits and that these inward supplies are "used in the course or furtherance of business" of taxable person.*

Accounting treatment or disclosure of a financial transaction in books of accounts contains an interpretation of that underlying transaction. When tax treatment is applied by taxpayer based on the accounting treatment, say, capitalization of machinery purchased treated as 'capital goods' for GST purposes, is an interpretation of the earlier interpretation. Now, when a demand is raised disputing the reversal of this credit under rule 43, would be an interpretation or an interpretation arising from an earlier interpretation of the underlying financial transaction. This should indicate the remoteness of any evidentiary value that financial statements can have to support any treatment for GST purposes. As such, classification of taxable supplies will not flow from the treatment or disclosure in financial statements.

'Triple interpretation' refers to concept where a financial transaction of purchase or sale of any article is interpreted as to whether the same must be accounted as revenue expenditure or capital expenditure. This is an interpretation in the financial books of the underlying financial transaction. GST treatment adopted in self-assessment by taxpayer of the underlying financial transaction appearing in financial statements is an interpretation of an earlier interpretation. Now, when a demand for GST is raised by canvassing an alternate tax treatment to that adopted in self-assessment will be new interpretation of the taxpayer's interpretation based on the earlier interpretation in the financial statements, of the underlying financial transaction. With this distance between original financial transaction and the eventual tax treatment canvassed, not only is the reliability suspect but the relevance itself is unfathomable. Nothing further needs to be said about such interpretation forthcoming from third-party documents such as 26AS, GSTR7, etc. for purposes of dictating the primary classification of supply or the object of supply.

4.5 DECLARATION OF GOODS

Legislative history involving tax on goods, whether Sales Tax or Central Excise, concludes with the immutable twin-test of the object of contract to be goods, that is, they are declared to be "movable and marketable" and over

which someone exercises proprietary rights. Development of jurisprudence in Central Excise, introduced "marketability" as a test to exclude non-marketable articles from being admitted within the understanding of "goods". In other words, articles that are non-marketable could not have been intended to be manufactured, and therefore, where an article is non-marketable (for any reason), would not be excisable. While things stood thus in Central Excise, definition of "goods" in Sale of Goods Act does not expressly exclude non-marketable articles where it covers *"every kind of movable property"*. Proof of marketability must be obtained from trade. But there are certain goods, whose proof of marketability is taken over by allied laws. For instance, goods sold in pre-packaged condition where (*i*) package is presented in standard weight or measure (*ii*) package of approved weight or measure and (*iii*) package bears statutory labelling of all specifications including guidance on duration of storage to be fit-for-purpose. It is not permissible for manufacturer to claim article produced to be 'marketable goods' but not be in compliance with allied laws and *vice versa*. Goods compliant with allied laws asserting their marketability cannot be treated as 'service' unless their pre-package is tampered at the point of supply (immediately prior to) or supplied with the condition that they must be tampered. For instance, can of beverage is opened and served in a cup or bag of chips are served out of the pre-package. Whether these instances remain supply of goods or not, will be dependent of circumstance of the given supply (discussed later), but the marketability of goods taken over and determined affirmatively by allied laws cannot be denied for purposes of GST law. Articles that are not subject to compliance with any allied laws (LM Act) or affirmed under allied laws (FSS Act) to be non-marketable (for that they are unfit for sale, but lacking sufficient shelf-life to be admitted as marketable goods though still fit for consumption or use), proof of marketability falls on taxpayer to establish based on wisdom of trade or domain understanding.

Example 149: *Articles sold in pre-package with MRP label must be presumed to be marketable.*

Example 150: *Steam (not subject to LM Act compliance) cannot be presumed (but be tested) for its marketability.*

Example 151: *Hot meals (subject to FSS Act compliance) must be presumed to be non-marketable.*

Example 152: *Unpainted motorcar is evidently non-marketable (even if classified under same HSN as a completed article).*

Example 153: *Completely built unit of a motorcar without any fuel must be presumed to be marketable.*

As long as the 'article' is movable and someone exercise proprietary rights over it, then that article is goods. Debris in a construction site, is movable

and the owner of the building under construction (or being demolished) will be liable as the proprietor. Wild animals are movable, but no one enjoy proprietary rights over them, though States are obliged by law to protect and conserve wildlife. Goods, in general, were every kind of movable property but, movable and marketable articles included in Central Excise (by a poorly but purposefully worded explanation in section 2(*d*) of Central Excise Act in the definition of *"excisable goods" that "goods"* (notice change of reference from excisable goods to goods *simplicitor*) *includes any article, material or substance which is capable of being bought and sold for a consideration and such goods shall be deemed to be marketable"* from 10 May 2008 *vide* section 78 Finance Act, 2008). Concept of shelf-life is necessary to establish transferability. Article involved in trade that lacks transferability cannot be admitted to being the object of contract, but the means by which another object is performed under that contract. Marketable' refers to be capability, not of the person, but of the article to be carried to the market. Market is not a fixed place. Market is any place where (potential) Buyer and Seller meet to transact. Market may even be at the site of consumption by Buyer or *vice versa* where Buyer comes to site of production and consumes right there.

Example 154: *Ready-mix concrete is carried to site of consumption, although Buyer (paying for it) may be located in a different city.*

Example 155: *Customer takes motorcar to Service Centre to purchase new tyres (and fitment).*

Marketability is proof of shelf-life, not just by any stray observation but with such regularity that those involved in that trade admit it of having shelf-life. After all, marketability is to be capable of being carried to a market. And without shelf-life the article will be transient and suffer from being incapable of reaching the market where it will be accepted for trade.

Example 156: *Molten iron is non-marketable for lack of viable technology to conduct them to a customer; molten iron is not goods.*

Example 157: *Steam is marketable, by conducting through insulated pipes from place of production to site of use; steam is goods.*

Example 158: *Livestock are movable property (goods).*

Example 159: *Harvested honey is movable property (goods).*

Example 160: *Migrating birds are movable but not property (goods).*

Although there is no such explanation in section 2(*52*) of CGST Act to introduce "marketability" as a superadded factor in the definition of "goods", but non-marketable articles (*i*) cannot be the object of a contract for supply of goods and (*ii*) will not find a suitable GST tariff classification when they are non-marketable. Non-marketable is not one stray instance where the