[2026] 189 taxmann.com 552 (Article)©

Date of Publishing: August 18, 2026

The Levy Stays, but the 1% Goes Gujarat HC Reshapes the Corporate Guarantee GST Framework

CA PARAG MEHTA

Partner - Indirect Tax, N.A. Shah Associates LLP

CA JATIN SAVALIYA

Manager- Indirect Tax, N.A.Shah Associates LLP

Torrent Power Ltd. v. Union of India [2026] 189 taxmann.com 490 (Gujarat) with 12 connected petitions, Gujarat High Court, dated 14 August 2026

The Verdict at a Glance

On 14 August 2026, the Gujarat High Court decided thirteen writ petitions together, led by Torrent Power Limited. The 148-page judgment settles much of what had remained unsettled about GST on corporate guarantees.

The Court decided partly for the Revenue and partly for the taxpayer, with the larger relief going to the taxpayer. The Court held that a corporate guarantee between related persons is taxable, even when no fee is charged. But it also held that where a fee is charged, GST must be paid on that fee and not on a flat 1%. And no tax can be demanded for any period before 26 October 2023.

Every group company that has given a guarantee, and every adviser or consultant holding a notice on this issue, needs to read the judgment with a calculator.

How the dispute started

In its 52nd meeting on 7 October 2023, the GST Council noted a practical problem. There was no clear benchmark for the fee or commission that should apply to a corporate guarantee. Officers could not value it and taxpayers could not either. Bank guarantee commission in the market ran anywhere between 0.5% and 3%.

So, the Council went shopping in the Income-tax Rules. It came back with 1% (the safe harbour rate under Rule 10TD) and fixed it as the minimum acceptable value, ignoring the small detail that under Rule 10TD, the 1% rate is optional.

This became Rule 28(2) of the CGST Rules, inserted with effect from 26 October 2023. The value of a corporate guarantee between related persons was deemed to be 1% of the amount guaranteed, or the actual consideration, whichever is higher. The words “per annum” were added later, by a notification of 10 July 2024, with effect from 26 October 2023. Two circulars followed, dated 27 October 2023 and 11 July 2024. The first also said that a personal guarantee given by a director is to be valued at Nil.

DGGI then went to work. Notices travelled across the country, many of them reaching guarantees signed years before GST existed. What began as a valuation problem soon became a nationwide litigation problem, with writ petitions landing before one High Court after another.

What the Bombay High Court had said

A significant judicial development came on 6 May 2026 from the Nagpur Bench of the Bombay High Court in D P Jain & Co. *Infrastructure (P.) Ltd. v. Union of India* [2026] 186 taxmann.com 392/110 GSTL 40 (Bombay). The guarantee deeds in that case expressly recorded that the company had neither received nor would receive any fee or commission for furnishing the corporate guarantees.

The Court applied the Supreme Court's order in Commissioner of *CGST and Central Excise v. Edelweiss Financial Services Ltd.* [2023] 149 taxmann.com 76/73 GSTL 4 (SC) and held that if there is no consideration, there is no service, and therefore no GST. It did not strike down Rule 28(2). It simply said the rule cannot be used when there is no taxable supply to begin with. The notice and summons were quashed.

Why the Gujarat High Court disagreed

The Gujarat High Court expressly disagreed with the view taken by the Bombay High Court in D P Jain & Co. *Infrastructure (P.) Ltd. (supra)*. Its reasoning is short and worth understanding.

GST ordinarily requires consideration. However, Section 7(1)(*c*), read with Entry 2 of Schedule I, creates a specific exception for supplies between related persons: such supplies are taxable even when made without consideration. A holding company and its subsidiary are related persons. Therefore, the absence of a fee, by itself, does not take a corporate guarantee outside the GST net.

The Court also distinguished Edelweiss, which arose under the erstwhile service tax regime. Under Section 65B(44) of the Finance Act, 1994, consideration formed part of the statutory definition of "service". GST, however, deliberately removed consideration as an indispensable requirement in specified related-party transactions. Accordingly, the Court held that the principle laid down under the erstwhile regime could not simply be transplanted into GST.

The Court rejected the taxpayers' other arguments as well. A guarantee is not an actionable claim under the Transfer of Property Act, and therefore does not fall within the exclusion under Schedule III. The income-tax concept of 'shareholder activity', relied upon from Micro Ink, was held to have no application under GST.

One finding on the facts deserves note. Torrent Power's guarantee was accompanied by a pledge of shares executed at the same time. The Court read the two documents together as a single transaction, holding that the substance of an arrangement is drawn from its terms and not from the label each document carries

When does the tax become payable

This question mattered because Rule 28(2) prescribes the 1% valuation on a "per annum" basis. If furnishing a corporate guarantee is a one-time act, how can GST arise year after year?

The Court gave a two-part answer. First, a corporate guarantee is not a "continuous supply of services" under Section 2(33), since that provision contemplates periodic payment obligations, which are absent where the guarantee is furnished without consideration. Second, the time of supply is governed by Section 13(2)(*c*) - the date on which the recipient records the service in its books of account.

Thus, where the guarantee continues against an outstanding loan, the recipient's accounting entry becomes relevant in determining the time of supply and, consequently, the year-wise GST liability.

This deserves attention. The holding company's GST liability may therefore depend on how the subsidiary records this transaction in its books.

The main relief: pay GST on the fee you actually charged

Rule 28(2) said the value is 1% of the guarantee amount, or the actual fee, whichever is higher. The word “higher” was the real grievance. A company charging 0.3% still had to pay GST on 1%. In these very petitions, the fees actually charged ranged between 0.25% and 0.3%.

The Court held this arbitrary. The GST Council itself had recorded a market range of 0.5% to 3%. The 1% figure came from Rule 10TD of the Income-tax Rules, where it is only an option available to the taxpayer. Rule 28(2), however, gave no such choice.

The Court then relied on the Supreme Court’s decision in *Wipro Limited*, where customs rules deemed 1% of the FOB value to be the value attributable to handling charges. The Supreme Court held that a deemed value cannot be forced on an assessee when the real value is known and available. The same principle applies here.

On the other hand, the Revenue argued that a flat rate avoids litigation. The Court rejected this argument on the basis of *Coal India v. Saroj Kumar Mishra* AIR 2007 SC 1706, holding that the possibility of litigation cannot take away a person’s legal right.

The Court did not strike down Rule 28(2), nor did it disturb the 1% figure. It only read down the words “whichever is higher”. The effect is simple:

- If a fee is charged: GST is payable on the actual fee, even if it is below 1%.
- If no fee is charged: the deemed value of 1% per annum continues to apply.

In short, 1% is not a mandatory floor where an actual fee has been charged.

No tax for the period before 26 October 2023

One of the issues before the Court was the applicability of GST to corporate guarantees furnished between 2012 and 2023. Many of these guarantees had been signed before GST came into existence. Rule 28(2) came into force only on 26 October 2023, yet the department had applied it to earlier years.

The Court held that taxing these earlier periods would be unduly harsh and unfair. Companies plan their affairs based on the law as it stands. A guarantee may run for many years, and applying a new rule retrospectively imposes a cost that was never anticipated. The Court held that this violates Articles 14 and 19(1)(*g*). It also held that collecting tax for those years would amount to unjust enrichment, as the department had no authority to levy it at all.

One caution: The protection is period-specific, not document-specific. A guarantee signed in 2015 is protected only up to 25 October 2023. If the guarantee remained in force thereafter, GST applies from 26 October 2023 onwards.

Section 74 cannot be used for this dispute

This finding deserves separate attention, and its use goes well beyond corporate guarantees.

Most of the notices in this batch were issued under Section 74, which applies only where tax is unpaid because of fraud, wilful misstatement or suppression of facts. It allows the department to go back five years and imposes a penalty equal to the tax. Section 73, the ordinary provision, is far less severe.

The Court found no basis for invoking it. The guarantees were on record and nothing had been hidden. Several were signed before GST even came into force. The real dispute was about the interpretation of the law, not about hidden facts. Explanation 2 to Section 74 says suppression means failing to declare something a person was required to declare. Nothing of that kind had happened. The Court described the department’s action as arbitrary and indicative of non-application of mind.

On the other hand, the department argued that the taxpayers should approach the appellate authority instead of coming to the High Court. The Court refused, holding that where a notice is issued without jurisdiction in the first place, an appeal is no real remedy. The orders and show cause notices under Section 74 were accordingly quashed.

This principle extends far beyond corporate guarantees, as Section 74 cannot become a shortcut to the five-year limitation period where the dispute is simply about the interpretation of law.

What companies should do now

- Separate every demand into the period before and after 26 October 2023 and contest the earlier period.
- For the period from 26 October 2023 onwards, recompute the liability on the fee actually charged and work out the consequential refund or adjustment.
- Where a fee below 1% is charged, build the supporting file with bank quotes, comparable commission rates, transfer-pricing benchmarks and other relevant commercial evidence. After the reading down of "whichever is higher", the actual fee becomes the taxable value, making the commercial basis for that fee important.
- Where no fee is charged, the 1% per annum deemed value continues to apply. Whether it should be computed on the guarantee amount sanctioned or the balance actually outstanding is worth examining, and the Court's time-of-supply reasoning arguably supports the latter.
- Where the recipient is entitled to full input tax credit, the proviso to Rule 28(2) is to be examined, as the invoice value is deemed to be the open market value and the transaction may consequently be revenue-neutral for the group.
- Challenge every Section 74 notice on this issue.
- Watch for fresh CBIC clarifications, as the Court has set aside the existing Circulars to the extent, they conflict with its judgment and permitted the Revenue to issue fresh Circulars or Administrative Instructions accordingly.

What is still open

The judgment settles the core issues, but four important questions remain open.

- First, the two High Courts now hold opposite views. The Bombay High Court held that a guarantee without a fee is not taxable, while Gujarat High Court has held that consideration is not required between related parties. Companies outside both States must therefore decide which view to follow until the Supreme Court settles the issue.
- Second, the judgment itself leaves a tension. The Court holds that a guarantee is not a continuous supply and that the benefit arises on execution yet permits tax to be collected year after year. How a one-time supply creates recurring tax liability remains open.
- Third, there is a valuation question. The rule refers to 1% of the guarantee amount, while the Court's time-of-supply reasoning looks to the loan outstanding each year. On a ₹100 crore guarantee against a ₹20 crore outstanding loan, this could materially change the tax liability.
- Finally, the actual-fee approach may encourage token fees, which could invite scrutiny particularly where the same company has adopted 1% as the arm's-length rate for income-tax purposes.

The bottom line: The levy survives, but the 1% floor does not. The period before 26 October 2023 is protected, Section 74 cannot be invoked to stretch a mere interpretational dispute into a five-year demand, and genuine fees will now speak for themselves. The corporate guarantee battle has entered its next phase, not over whether GST applies, but over how much is actually taxable.