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Taxability of Corporate Guarantees under GST Laws: Analysis of the Recent Gujarat High Court Decision in Torrent Power Ltd. v Union of India

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The issue of taxability of corporate guarantees issued by a holding company to a financial institution for the benefit of its subsidiary company emerged as one of the most contentious issues in the Goods and Services Tax (GST) regime pursuant to the introduction of the levy in 2023. The controversy centers on a fundamental question: when a holding company furnishes a corporate guarantee, without charging any fee from its subsidiary company, to a bank to enable its subsidiary to secure credit facilities, does such activity constitute a taxable "supply of services" under the Central Goods and Services Tax Act, 2017 (CGST Act)?

The issue gained legislative dimension when the GST Council, in its 52nd meeting held on 7 October 2023, recommended the insertion of Rule 28(2) in the Central Goods and Services Tax Rules, 2017 (CGST Rules), which prescribed a deemed valuation of 1 percent per annum of the guaranteed amount for corporate guarantees extended between related persons (Rule 28(2)). This rule was introduced vide Notification No. 52/2023 dated 26 October 2023. Subsequently the Central Board of Indirect Taxes and Customs (CBIC) issued clarificatory Circulars dated 27 October 2023 and 11 July 2024 (CBIC Circulars) to operationalize the levy.

The Revenue proceeded to issue show cause notices even for periods pre-dating the introduction of Rule 28(2), seeking to recover GST on corporate guarantees furnished by holding companies.

The constitutional validity of Rule 28(2) of the CGST Rules, Section 15(4) of the CGST Act and the CBIC Circulars were challenged before various High Courts and a challenge is presently also pending before Delhi High Court in a group of petitions.[1]

The Hon'ble Bombay High Court (Nagpur Bench) in M/s. D.P. Jain & Co. Infrastructure Private Limited v Union of India, [2026] 186 taxmann.com 392 (Bombay) [2] held in favour of the taxpayer. The Court while placing reliance on the Supreme Court's decision in Edelweiss Financial Services Ltd[3], which was rendered in the Service Tax regime, observed that a corporate guarantee executed without consideration is outside the scope of taxable supply and struck down the demand based on Rule 28(2).

Recently, the Hon'ble Gujarat High Court delivered its judgment on 14 August 2026 in a batch of thirteen writ petitions led by Torrent Power Ltd. v Union of India & Others[4] (Torrent Power Decision). In this article, the authors have encapsulated their analysis of the decision and have also suggested a way forward for the taxpayers.

A. Key Observations of the Hon'ble Gujarat High Court in Torrent Power Decision:

A.1 The Hon'ble Gujarat High Court has rendered a comprehensive judgment addressing multiple facets of the controversy. The following are the critical observations made by the Court on each issue:

[1] See Sterlite Power Transmission Ltd & Ors v Union of India & Ors, W.P. (C) no. 17559/2024.
[2] Judgment dated 6 May 2026.
[3] [2023] 149 taxmann.com 76 (SC).
[4] R/Special Civil Application No. 12175 of 2024

A.2 Whether corporate guarantee constitutes "*supply*" under Section 7 of the CGST Act:

a. The petitioners argued that corporate guarantees do not constitute "*supply*" under Section 7 of the CGST Act for several reasons: (i) furnishing a corporate guarantee involves no activity or service rendered and it is merely a contingent promise to pay at a future date which may or may not materialize; (ii) the guarantee is a contingent contract under Section 31 of the Indian Contract Act, 1872, where nothing is 'provided' unless and until the guarantee is invoked; (iii) Schedule I to the CGST Act does not deem "*consideration*" into existence as it only deems certain supplies made without consideration to be taxable supplies thereby, presupposing an existing supply; and (iv) in the absence of any express deeming provision (unlike Section 7(1)(aa) which was enacted to tax transactions between a person and its members), corporate guarantees cannot be treated as supplies merely by implication.

b. The Court rejected the aforesaid contentions and held that the execution of a corporate guarantee constitutes a "*supply of services*" under Section 7(1)(c) read with Entry 2 of Schedule I. Relying on Sections 126, 127, 140, and 145 of the Indian Contract Act, 1872. The Court reasoned that corporate guarantees involve a tripartite arrangement where the holding company (surety), the subsidiary (principal debtor), and the creditor bank are bound together. Once the guarantor settles the debt, it steps into the shoes of the creditor bank through subrogation under Section 140 establishing the connecting link for treating the arrangement as a supply of service. Further, since the holding company and subsidiary are "*related persons*" under Explanation (a) to Section 15, the supply falls within Schedule I even without consideration. (Paragraphs 32–35 and 39–40)

A.3 Whether furnishing corporate guarantee falls within the ambit of "*business*" under Section 2(17) of the CGST Act:

a. The petitioners contended that furnishing a corporate guarantee is a "*shareholder activity*" undertaken solely by virtue of the holding company's ownership interest in the subsidiary, and not in the course or furtherance of business.

b. The Court rejected this argument, holding that the definition of "*business*" under Section 2(17) is wide and transaction centric. Even if issuing guarantees is not the main business of the holding company, it is "*incidental or ancillary*" to their main trade and commerce, and extending the guarantee is 'business' even though the motive of profit is excluded. (Paragraphs 36–40)

A.4 Whether corporate guarantee falls within Entry 5(e) of Schedule II of the CGST Act:

a. The petitioners argued that Entry 5(e) of Schedule II which treats '*agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act*" as supply of services – does not apply to corporate guarantees. The petitioners contended that the expression "*to do an act*" cannot be read in isolation and must be read in conjunction with "*agreeing to the obligation*" and neither the holding company nor the subsidiary agree to any independent obligation. Guarantee is part of a single, integrated transaction with the bank / financial institution.

b. The Court partially agreed with this interpretation of Entry 5(e) but nevertheless held that a corporate guarantee fall within the ambit of Entry 5(e). The Court analyzed the expression "*obligation*" as: (i) a legal or moral duty to do or not do something; and (ii) a formal, binding agreement or acknowledgment of a liability to pay a certain amount or to do a certain thing for a particular person.

c. The Court observed that an "*obligation in law is a binding legal tie (vinculum juris) that compels one party to perform an act, make a payment, or refrain from doing something for another party*." Applying this meaning, the Court held that the relationship between a holding company and its subsidiary under Section 2(87) of the Companies Act, 2013 constitutes *vinculum juris* i.e. a statutory legal tie. By virtue of this relationship, the holding company is bound by legal duty to do or not do something for its subsidiary.

Therefore, when a subsidiary requests a corporate guarantee and the holding company acknowledges the obligation to provide financial security, this satisfies the expression "*agreeing to an obligation to do an act*" under Entry 5(e) of Schedule II. Consequently, corporate guarantees constitute "supply of services" under Article 5(e) of Schedule II. (Paragraphs 41–46)

A.5 Whether the subsidiary qualifies as "*recipient*" under Section 2(93):

a. The petitioners contended that the subsidiary cannot be the '*recipient*' under Section 2(93) since the guarantee is furnished to the lender bank, not to the subsidiary.

b. The Court rejected this, holding that Section 145 of the Indian Contract Act, 1872 creates an implied promise by the principal debtor (subsidiary) to indemnify the surety (the guarantor holding company), and therefore a contractual link is established to conclude that the supply of services ultimately accrues to and is rendered for the benefit of the subsidiary. The subsidiary thus qualifies as the "*recipient*" under Section 2(93)(c) i.e. "*the person to whom the service is rendered*" (pertaining to scenarios where no consideration is payable). (Paragraphs 47–49)

A.6 Whether corporate guarantee is an "*actionable claim*":

a. The petitioners argued that corporate guarantees are "actionable claims" under Section 3 of the Transfer of Property Act, 1882, and therefore excluded from "supply" under Schedule III. They attempted to link corporate guarantees to the definition of "*debt*" under Article 366(8) of the Constitution and the Insolvency and Bankruptcy Code, 2016.

b. The Court rejected this, holding that an actionable claim represents a direct, primary right to claim payment, whereas a corporate guarantee creates a secondary, contingent liability that triggers only upon default of the principal debtor. The Court concluded that "*a corporate guarantee cannot be dragged into an actionable claim through definition of 'debt' under Article 366(8) read with IBC code*". (Paragraphs 50–55)

A.7 Validity of Rule 28(2) of the CGST Rules and Section 15(4) of the CGST Act:

a. The petitioners challenged the constitutional validity of Rule 28(2) on several grounds: (i) it is a machinery provision that cannot create the levy itself—the levy must exist in the charging provisions of Sections 7 and 9 of the CGST Act; (ii) the uniform 1 percent deemed valuation is arbitrary and bears no nexus with the actual cost or value of the guarantee; (iii) the expression "*whichever is higher*" takes away the taxpayer's right to pay GST on actual consideration; and (iv) there is discrimination between a personal guarantee by a director (valued at "*Nil*") and a corporate guarantee (valued at 1 percent).

b. The Court upheld the constitutional validity of Rule 28(2) in principle, relying extensively on the Supreme Court's recent decision in *Gameskraft Technologies (P.) Ltd.,* [2026] 186 taxmann.com 1232 (SC). The Court held that Rule 28(2) is traceable to Sections 15(4), 15(5), and 164 of the CGST Act. Section 15(5), which commences with a non-obstante clause, enables the Government, on the recommendations of the GST Council, to prescribe special valuation mechanisms in respect of notified supplies. The Court observed that the GST valuation framework under Section 15 operates through a harmonious combination of ordinary transaction-value principles under Section 15(1) and specialized valuation methodologies under Sections 15(4) and 15(5) for unique or complex commercial supplies. The Court held that specialized valuation methodologies constitute matters of legislative and fiscal policy, and the legislature possesses considerable latitude in devising standards so long as a reasonable nexus exists with the underlying taxable event.

c. Relying on the Supreme Court's view in *Gameskraft Technologies*, the Court further held that once it is established that Rule 28(2) was introduced pursuant to the GST Council's explicit recommendation in its 52nd meeting, the precise statutory channel through which delegated authority was exercised cannot by itself invalidate the Rule. Once substantive statutory requirements stand fulfilled and the Rule is otherwise traceable to statutory rule-making power, procedural arguments lose their force. Consequently, the challenge on the ground that the Rule was introduced without a notification under Section 15(5) was rejected. (Paragraphs 72–74)

d. However, the Court read down the expression "*whichever is higher*" in Rule 28(2) as being arbitrary and violative of Articles 14 and 19(1)(g) of the Constitution. The Court observed that the GST Council itself acknowledged that bank guarantee commission ranges from 0.5% to 3%, and in some cases there may be no commission at all. Therefore, when actual charges are ascertainable (such as 0.25% to 0.3% in some petitioners' cases), imposing a mandatory higher valuation of 1%

is unreasonable and arbitrary.

A.8 Retroactive application of Rule 28(2) of the CGST Rules:

a. The petitioners argued that Rule 28(2), inserted on 26 October 2023, cannot be applied to corporate guarantees furnished prior to this date.

b. The Court accepted this argument and held that the levy of GST on pre-26 October 2023 corporate guarantees under this provision is violative of Articles 14 and 19(1)(g), characterizing such application as "retroactive" (creating new obligations on past transactions) which imposes an unexpected financial burden without any fault on the assessee. However, for guarantees that continue beyond 26 October 2023, the levy is attracted from this date on the outstanding guarantee amount (Paragraphs 111–114).

A.9 Determination of time of supply:

a. The petitioners contended that time of supply cannot be determined under Section 13 since corporate guarantees are contingent in nature. The Court held that time of supply is to be determined under Section 13(2)(c) i.e. the date on which the recipient shows receipt of services in its books of accounts. This is a "continuing, recurring accounting obligation" and the outstanding debt reflected in the subsidiary's books for each financial year triggers valuation under Rule 28(2) of the CGST Rules. (Paragraph 64)

B. The Decision of Hon'ble Bombay High Court (Nagpur) Bench and its Significance:

B.1 The Hon'ble Bombay High Court (Nagpur Bench) in M/s. D.P. Jain & Co. Infrastructure Private Limited v Union of India dealt with a challenge by an infrastructure company engaged in the construction of national and state highways. The petitioner had executed three corporate guarantees in favour of State Bank of India and Bank of Maharashtra to enable its subsidiary companies to obtain term loans for highway construction projects. Critically, all three guarantee deeds contained specific clauses declaring that the petitioner had not received and shall not receive any security, fee, commission, or any other consideration from the borrower for providing the guarantee. The petitioner challenged the show cause notices and the constitutional validity of Rule 28(2) of the CGST Rules and the related CBIC Circulars.

B.2 The Bombay High Court, while upholding the constitutional validity of Rule 28(2) and the CBIC Circulars, took a fundamentally different view on the taxability of corporate guarantees executed without consideration. The Court relied heavily on the Supreme Court's decision in Commissioner of CGST & Central Excise v Edelweiss Financial Services Ltd., wherein the Apex Court had held that corporate guarantees given without consideration are not taxable under the erstwhile service tax regime. The Bombay High Court applied this principle to the GST regime and held that for an activity to be taxable, there must be not only a provider of service but also a flow of consideration for the rendering of such service. In the absence of consideration, taxability does not arise. The Court further observed that corporate guarantee is in the nature of a contingent contract which becomes enforceable only at the instance of the bank in the event of default, and since no consideration flowed for the guarantees in question, the show cause notice and summons issued against the petitioner were quashed and set aside.

B.3 The significance of the Bombay High Court decision lies in its diametrically opposite conclusion to the Gujarat High Court's approach. While the Gujarat High Court has held that the deeming fiction under Section 7(1)(c) read with Schedule I specifically brings supplies between related persons without consideration within the tax net thereby distinguishing the service tax regime from the GST regime, the Bombay High Court has applied the *Edelweiss* principle without engaging with this distinction.

C. Concluding Thoughts – Balancing Revenue interests and Business Realities:

C.1 The High Court's view upholding the levy of GST on the issue of a corporate guarantee creates a practical dilemma for businesses in sectors whose output is not liable to GST, such as companies in the power generation business. Taxing a corporate guarantee under GST laws may adversely impact business operations since corporate guarantees are a routine commercial arrangement that enable subsidiaries (especially newly incorporated subsidiaries or SPVs) to access credit facilities. Imposing

GST on such arrangements increases the cost of financing and places Indian businesses at a disadvantage vis-à-vis jurisdictions that do not tax such intra-group support.

C.2 The Hon'ble Gujarat High Court's decision may also result in significantly increasing valuation related litigation.

- The reading down of the phrase "*whichever is higher*" fundamentally alters the valuation methodology for the taxpayers. Businesses are no longer compelled to accept the flat 1 percent deemed valuation. Instead, they can assign a reasonable value (arm's length price) to their 'act of granting guarantee to the financial institution' and deposit GST on such value.

- It is likely that the taxable value ascribed by the taxpayer to the 'act of issuing guarantee to the financial institution' will become a contentious issue with the GST authorities resulting in further litigation.

C.3 The final word on the taxability of corporate guarantees under GST laws will undoubtedly come from the Hon'ble Supreme Court given the conflicting views expressed by the Gujarat High Court and the Bombay High Court (Nagpur Bench) and a challenge before the Hon'ble Supreme Court can be expected soon. Until then, the Hon'ble Gujarat High Court's decision with its nuanced observations serves as the most authoritative and comprehensive judicial pronouncement on the subject.

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