May 2023

Gameskraft Technologies Private Limited v. Directorate General of Goods and Service Tax Intelligence & Others [WP 19570 of 2022]

Judgement of the Hon'ble High Court of Karnataka dated 11 May 2023

Facts of the Case:

- The aforesaid Writ Petition arose out of a Show Cause Notice dated 23 September 2022, issued by the Directorate General of Goods and Service Tax Intelligence (hereinafter "*the Authority*") to Gameskraft Technologies Private Limited (hereinafter "*Gameskraft*") under Section 74(5) of the Central Goods and Service Tax Act, 2017 (hereinafter "*CGST Act*").
- The Show Cause Notice alleged that Gameskraft had evaded Goods and Service tax (hereinafter "*GST*") by mis-classifying their supply as "services" and not as "actionable claims", which are goods, thereby mis-declaring the taxable value of the supply. The Petitioners in turn, challenged certain other actions taken by the Authority, in connected proceedings.
- The substance of the allegations under the Show Cause Notice was that Gameskraft had not appropriately categorised the supply as an "actionable claim" in the form of 'betting' or 'gambling', as contended by the Authority. The Authority contended that in accordance with Rule 31A of the Central Goods and Service Tax Rules, 2017, Gameskraft should be taxed at 28% on 100% of the face value of the participation fee, and not only on the 10% charge collected by them as the facilitator of the game of Rummy [also known as Gross Gaming Revenue or "Rack", in industry parlance]. In effect, the Authority sought to argue that the entire 'buy-in' amount to play the game of Rummy should be considered the revenue of Gameskraft, and therefore should be taxable as an "actionable claim" like betting, gambling, chargeable to 28% GST.
- The challenge to the Show Cause Notice was primarily on the ground that it was issued without jurisdiction in light of various decisions of the Supreme Court and the High Courts holding that Rummy was not a game in the nature of 'betting' or 'gambling', but a "game of skill". Gameskraft thus, resisted the characterisation of the game of Rummy hosted by it on its platform as 'betting' or 'gambling', and contended that they were not covered by Rule 31A of the Central Goods and Service Tax Rules, 2017 [which invokes 28% GST on the total fee paid for games of betting, gambling, horse racing]. Gameskraft argued that the games hosted by them were 'game(s) of skill' and not a 'game of chance'. Hence, such games could not be considered equal to 'betting' or 'gambling', for the purposes of the CGST Act, and be subject to 28% GST.

Issue before the Karnataka High Court:

- The High Court of Karnataka considered the question whether Rummy for stakes, as hosted by Gameskraft, would amount to a 'game of skill' or a 'game of chance'?

Contention of the Revenue Authority:

- In this context, the Authority took the stand that the game as played on the platform involved two distinct transactions. First, the game of Rummy itself, and second the wager on the outcome of the game. Such an interpretation would mean that while the game of Rummy itself maybe a game of skill, but the wager on the outcome, was in effect an alleged event of gambling on the uncertain outcome of the game. The Authority sought to draw parallels with prize competitions advertised in newspapers where participants would be called upon to predict an uncertain event or to 'forecast', in order to win a prize. In such situations, while it could be possible for certain specialists with access to specific information or data to predict such outcomes to a reasonable degree, a common person would not be able to achieve such a result. Hence, the game in totality should be considered as a game of wager or betting.

Ruling of the Karnataka High Court:

- In its decision, the High Court of Karnataka held that the game of Rummy was a single transaction, and any stakes if placed were done so depending on the knowledge and the confidence of the player on his skill and ability. The Court observed that the game of Rummy was one, where the outcome was not being forecasted or predicted, but rather, one where a person was predominantly using his own skill, to control the outcome of the game. Rummy thus being totally dependent on a skill set and was a "game of skill". It could not be considered to be gambling, irrespective of whether it was being played with stakes or not.
- The High Court culled out the dichotomy between "games of skill" and "games of chance". Focusing on the words "gambling", "game of chance", "game of skill", the High Court applied the principle *of Nomen Juris* [meaning "A technical legal term"]. The High Court held that *"the words should be construed in their legal sense, instead of general parlance. While "gambling" or "game of chance" have been held to involve chance as a predominant element, on the other hand "game of skill" has an exercise of skill which can control the chance. The element of chance cannot be completely overruled in any case but what is to be seen is the predominant element. In a game of rummy, certain amount of skill is required because the fall of the cards has to be memorised and the building up of rummy requires considerable skill in holding and discarding cards.*". Hence, the predominant element in the game was the exercise of "skill", which dwarfed the element of "chance". The High Court held "*when the outcome of a game is dependent substantially or preponderantly on skill, staking on such game does not amount to betting or gambling.*"
- The High Court further interpreting "betting" and "gambling", featuring in Entry 6 of Schedule III of the CGST Act, held, that the same interpretation as Entry 34 of List II of the Seventh Schedule to the Constitution and the Public Gambling Act, 1867 was applicable. Placing reliance on several of decisions of the Supreme Court of India and previous decisions of the High Court of Karnataka and other High Courts in India, the High Court concluded that online/ electronic/ digital games of Rummy are not taxable as 'betting' and 'gambling'. The High Court also held that the term 'business' in terms of section 2 (17) of the CGST Act in itself would not mean that lottery, betting and gambling were the same as "games of skill". Games of skill, while being actionable claims, fall outside the scope of 'supply' within the meaning of the CGST Act, which only applies to the sub-sect of "lottery, betting and gambling" and thus only these three sub sects were subject to tax under GST laws. The terms, "betting" and "gambling", appearing in Entry 6 of Schedule III of the CGST Act does not, and cannot include "games of skill" within their ambit.
- The High Court stringently indicated that the Show Cause Notice was an "*outcome of a vain and futile attempt on the part of the respondents to cherry pick stray sentences from judgments of Supreme Court, [*and other High Courts] *....and try to build up a non-existent case out of nothing which clearly amounts to splitting hairs and clutching at straws which cannot be countenanced and is impermissible in law*".

As a result, the Karnataka High Court quashed the Show Cause Notice issued to Gameskraft and held that the same was void ab-initio and without merit.

Please feel free to address any further questions or request for advice to:

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