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SINCE 1985

REPORT



# ANALYSIS OF THE GoM REPORT ON ONLINE GAMING & LATEST LEGISLATIVE

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DEVELOPMENTS IMPACTING GST  
ON ONLINE GAMING



## Broad Framework

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## Executive Summary

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The issue of applicability of GST on online gaming sector has been a matter of significant debate amongst the members of GST Council, with detailed deliberations on the valuation mechanism and the GST rate applicable. The Group of Ministers (GoM) formed to examine GST for online gaming, casino etc. submitted its first report recommending tax at the rate of 28% on full value of the contest entry amount. The issue has since been deliberated in the GST Council and the GoM has submitted its second report, the contents of which are not available in public domain.

The past jurisprudence has consistently treated online gaming as games of skill distinct from betting and gambling. The recent developments (amendment to MeitY's intermediary guidelines and amendments to Income Tax Act, 1961 via Finance Act, 2023) for the online gaming industry have further substantiated this difference and have recognised the immense potential of the online gaming industry.

The Hon'ble Finance Minister, Nirmala Sitharaman recently made a statement wherein she exuded confidence that stability, transparency, and clarity in taxation policy will boost investment in the online gaming sector.

Further, recently, the Hon'ble Karnataka High Court in *Gameskraft* matter has held that online games of skill do not amount to betting and gambling, and consequently quashed a show cause notice demanding GST at 28% on contest entry amount. While holding so, the Court observed that merely because games are played online and for stakes does not make it betting and gambling. It further followed the jurisprudence laid down by Hon'ble Supreme Court and various High Courts and held that online games of skill whether played with or without stakes do not amount to betting and gambling.

In light of the above recent developments, the GST Council should consider the latest legal and regulatory developments in relation to online gaming and request GoM to revisit the position based on the same. GST Council may provide a distinct treatment to online gaming different from lottery, betting and gambling as recognized in latest legal developments and as recognised by Government of India under the IT Act and IT Rules.

The GST Council and the revenue department will benefit from the clarity emerging on 'permissible online real money game' that will be certified and

recognized under the IT Rules. As a corollary, online games recognized as 'permissible online real money game' in terms of MeitY's intermediary guidelines will be excluded from gambling, betting or wagering.

India adopting a taxation regime in tandem with global best practices will establish a balance between the interests of the industry and the revenue augmentation of the Government. This will help in achieving the broad agreement that mechanism of valuation should be simple and easy to calculate, in conformity with law, and at the same time aid in the progressive growth of the industry.

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# 1. Background of Deliberations in GST Council Meetings

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The GST ushered in a new era of cooperative federalism in tax matters between State and Central governments. The GST Council is the key decision-making body that has been entrusted with the function of addressing significant issues pertaining to Goods and Service Tax (GST) faced by industries across the country.

The formulation of the taxation policies of the online gaming industry has been one such contentious issue that the GST Council has been deliberating over in recent times. The Finance Minister, Nirmala Sitharaman in May 2023 iterated that the taxation regime and regulation policy required a lot more calibration, and the discussions regarding the same are being actively carried out by the GST Council to closely understand factors like the consumption rate, employment potential, amongst other things, in arriving at a coherent taxation policy, adding that the sector could attract investors once the certainty arrives, through the establishment of transparent and clear taxation policies. The statement of the Finance Minister comes in the wake of the online gaming industry eagerly awaiting the deliberations of the GST Council on the taxation regime in the 50<sup>th</sup> GST Council Meeting which is scheduled to be held in June, 2023, as the 49<sup>th</sup> GST Council Meeting held on 18 February, 2023 did not take up the GoM report on online gaming.

The GST Council had constituted the GoM on Casinos, Race courses and Online Gaming (GoM) to analyse the issues faced by online gaming sector vide Office Memorandum dated 24 May, 2021, and was thereafter reconstituted on 10 February, 2022 with Chief Minister of Meghalaya as Convener of the GoM. The GoM was primarily constituted to examine, discuss and suggest any changes to be introduced in the legal regime of valuation services provided by casinos, race courses and online gaming. The GoM submitted its report in the 47<sup>th</sup> meeting of the GST Council. The GoM in its report intended to bring in uniformity in the rates and valuation while understanding the method of functioning of online gaming, horse racing and casino, as these were different activities. The findings, analysis, and implications of the GoM on the online gaming industry report submitted in June, 2022 shall be enumerated in Chapter 3.

The issues in relation to gaming have been seized by the GST Council since 2018. GST Council had various deliberations based on representations received

from the online gaming industry on international best practices. The GST Council discussions on gaming is summarized as under:

GST Council Meeting	Observations
21 June, 2019: 35 <sup>th</sup> GST Council Meeting	The GST Council noted that multiple representations from Associations had been received on issues pertaining to the rate and valuation of Casinos, Horse Racing, Online Gaming and Betting which the Group of Ministers on Lottery had stated would be directed to the Fitment/ Law Committee and then presented before the GST Council.
20 September, 2019: 37 <sup>th</sup> Council Meeting	Fitment committee recommendation has been deferred. It was decided that the issue may be examined and decided in the GoM on lottery.  The Fitment committee had discussed the value of supply may be fixed as Gross Gaming Revenue (GGR) which is internationally prevalent. Tax rate to be suitably decided or the rate applicable be clarified. Gross Gaming Revenue (GGR) is the amount wagered minus the winnings returned to users (Stakes minus winnings), implications of gray market and other allied issues. "
October 5, 12, 2020: 42 <sup>nd</sup> GST Council Meeting	A Group of Ministers (GoM) should be formed to discuss and analyze taxation in casinos and lotteries.
31 December, 2021 46 <sup>th</sup> GST Council Meeting	Ministers expressed the Governments' conflicted notions about the dilemma faced by political executives between revenue augmentation vs the interests of the industry.
28, 29 June, 2022: 47 <sup>th</sup> GST Council Meeting	The consequences of imposition of higher rate of tax such as complexity of tracking and higher instances of tax evasion were discussed where ministers and representatives of various States put forth their views on the implications of the recommendations of the GoM report. The following observations were <i>inter alia</i> presented on the suggestions of the GoM report on online gaming indicating that the issues addressed needed re-examination in the interest of the industry: <ul style="list-style-type: none"> <li>· The imposition of higher rate of tax might encourage users to access the online platform through a virtual private network (VPN) and it would be impossible to detect the location of the user since the location of the user would appear to be outside the taxable territory, thereby avoiding the imposition of tax.</li> <li>· The rate of tax must be such that the possibility of evasion would be minimized.</li> <li>· The service providers should be mandated to track the location of the user of their platform by tracking the payments made by the user on the online platform.</li> </ul>

GST Council Meeting	Observations
	<ul style="list-style-type: none"><li>· Casinos, horse racing and online gaming could not be clubbed together as each activity was totally different.</li><li>· Proper inputs, more meetings with the stakeholders and more information on the table was needed for the GST Council to decide on the issues contended by the GoM.</li></ul>

A recommendation was made in the 47<sup>th</sup> meeting of the GST Council to re-examine the issues analysed in the report based on the inputs rendered by the States, following which the GoM submitted its second report to the GST Council in December 2022 which is currently being evaluated and deliberated upon by the GST Council and is yet to be made available in the public domain.

Meanwhile, the Government of India has announced new rules for online gaming under the IT Act of 2000, providing clear legal status to the online gaming industry distinct from gambling, betting, wagering & lottery. The fears expressed in various discussions of the GST Council meeting need to be considered, as the issues relating to significant impact on the online gaming sector, pushing of customers towards gray market operators, significantly hampering the progress made by industry till date and reversing the efforts undertaken by Ministry of Electronics and Information Technology (MeitY).



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## 2. Key Developments since the last GST Council Meeting

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### Background of legislation of Gaming laws

Hon'ble Prime Minister of India, Shri Narendra Modi, in his speech, shared his vision for India to be a global gaming hub expected to be worth INR 3 lakh crore (400 billion USD approximately) in the next two years. Further, the Union Finance Minister, Smt. Nirmala Sitharaman, in Budget 2022-23 indicated the importance of the mobile gaming industry in India and announced formation of an Animation, Visual, Gaming and Comics (AVGC) promotion task force to make India a global hub for game development and gaming services. AVGC taskforce recommended for a vision document and national framework to be formulated for online skill gaming that protects interests of the users at large and ensures structured growth of the industry, fill regulatory void and cross legal hurdles. The AVGC task force also identifies tax uncertainty due to GST as a major issue for attracting investments and FDI.

Further, the Union Government constituted an inter-ministerial task force to work on the national level regulatory framework for the online gaming industry and identify a nodal ministry.

On December 23, 2022, the Government of India (Allocation of Business) (Three Hundred and Seventieth Amendment) Rule, 2022 was notified which amended the rules to include matters relating to online gaming under the Ministry of Electronics and Information Technology (MeitY). This directly put the gaming sector under the regulatory umbrella of MeitY for any further regulations. Immediately thereafter, the draft Information Technology (Intermediary Guidelines and Digital Media Ethics Code) Amendment Rules, 2023 were notified for public consultation.

Upon consulting with the public and making further changes to the draft amendment, the Information Technology (Intermediary Guidelines and Digital Media Ethics Code) Amendment Rules, 2023 ("**IT Intermediary Amendment Rule**") were introduced in April 2023.

### Information Technology (Intermediary Guidelines and Digital Media Ethics Code) Amendment Rules, 2023

The IT Intermediary Amendment Rules have introduced an enabling regulatory regime for online gaming intermediaries. The said rules define an online game,



an online gaming intermediary and permissible online real money games and provide a framework for operation of permissible online real money games by online gaming intermediaries. Some major changes that have been brought about through these rules are the introduction of self-regulation mechanism for the online gaming intermediaries, KYC and due-diligence requirements.

The IT Intermediary Amendment Rules provides that the ministry shall designate multiple online gaming self-regulatory bodies (“**SRB**”) that shall provide memberships to any online gaming intermediaries that want to operate in the country subject to such intermediaries being compliant with applicable law and offering permissible online real money games. The SRBs are bestowed with the responsibility of ensuring that the online gaming intermediaries are organising permissible online real money games i.e. games which are not in the nature of gambling, betting and wagering and are in compliance with the due-diligence requirements specified under the same. One of the due diligence to be complied by the online gaming intermediary as per IT rules is that it shall not host or publish any information that is gambling in nature. This has been a positive step in the pursuit of promotion of the online gaming sector in India. The said developments have shed light on a very positive outlook by the Central Government with respect to the regulation and promotion of gaming industry and an attempt to increase the ease of business for the industry.

### **Digital India Act**

The Central Government is set to future proof the digital legislations by introducing Digital India Act, 2023, which will replace the Information Technology Act, 2000 on account of the transformed internet landscape today, with significant internet penetration, multiple intermediaries operating across the internet and complex forms of user harms.

The Digital India Act specifically identifies that there can be various types of intermediaries, which include gaming intermediaries that shall be governed under the same.

Thus, various regulatory developments have taken place since the last GoM meeting that have been in the form of positive regulatory developments by the Central Government for the gaming sector indicating a clear objective of nurturing and promoting the said sector.

### **Finance Act 2023:**

Prior to the Finance Act, 2023, the Income-tax Act, 1961 (“the IT Act”) did not contain any specific provisions relating to taxation of online gaming. The winnings from online gaming were taxable u/s. 115BB of the IT Act at the rate of

30%. Further, the online gaming companies were required to deduct tax at source u/s. 194B of the Act. Considering the development of the online gaming sector in India and initiatives taken by the MeitY, the Finance Act, 2023 introduced specific provisions (i.e., Section 115BBJ and Section 194BA) for taxability of income arising from online gaming and introduced new taxation methodology. Earlier, online gaming was subject to income tax and TDS under the same provisions for lottery, gambling, betting. Under these new provisions, the “net winnings” from online games shall be subject to tax as well as for deduction of tax at source by the online gaming intermediaries. Further, the term “Online Game”, “Online Gaming Intermediaries” have been defined.



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## 3. Findings and Analysis of GoM Report

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In the wake of various representations of the stakeholders of the industries on the disputed areas of taxation issues, the Group of Ministers (GoM) on Casinos, Race Courses and Online gaming was constituted vide Office Memorandum dated 24.05.2021 following a recommendation of the GST Council to review and assess the issues relating to taxation of Casinos, Race Courses and Online Gaming. On February 10, 2022, the GoM was reconstituted with the Chief Minister of Meghalaya as Convener.

The Terms of Reference for consideration by the GoM were as follows:

- i. To examine the issue of valuation of services provided by Casinos, Race courses and online gaming portals and taxability of certain transaction in a casino, with reference to the current legal provisions and orders of Courts on related matters.
- ii. To examine whether any change is required in the legal provisions to adopt any better means of valuation of these services.
- iii. To examine the administration of such valuation provisions if an alternative means of valuation is recommended.
- iv. To examine the impact on other similarly placed services like lottery.

The GoM submitted its report in May 2022 which was considered by the GST Council in its 47<sup>th</sup> meeting held on 28.06.2022 and 29.06.2022. The following recommendations were made in the GoM report:

- i. GST on activities of casinos, racecourses, online gaming and lottery should be uniform in terms of the rate and valuation.
- ii. No distinction shall be made in the levy of GST on the activities of casinos, race courses, online gaming and lottery on the ground that an activity is a game of skill or a game of chance or both.
- iii. GST shall be levied on activities of casinos, race- courses, online gaming and lottery at the rate of 28%.
- iv. In the case of online gaming, the activities be taxed at the rate of 28% on the full value of the consideration which shall be inclusive of the platform fee and the prize pool contributed by the user irrespective of the distinction made between the games of skill and games of chance.

- v. In the case of race courses, GST to be continued to be levied at the rate of 28% on the full value of bets pooled in the totalisator and placed with the bookmakers.
- vi. In the case of casinos, GST to be levied at the rate of 28% once on purchase of chips/coins (on face value). Thereafter, no further GST shall apply on the value of bets placed in each round of betting including those played with winnings of previous rounds. Further, a mechanism was suggested for taxation of entry fees in case of other services offered by casinos.

In its report, the GoM discussed the need to consider various aspects such as that the mechanism of valuation should be simple and easy to calculate, in conformity with law and at the same time should not render the industry unviable. However, various discussions in the GoM report and conclusions derived basis the same appear to be not aligned with these aspects which were sought to be achieved. The factual and legal aspects of the conclusions drawn is provided below:

### **1. Applicability of Skill Lotto judgment on lotteries to online gaming and consideration of online gaming as actionable claim**

#### *Conclusions drawn in GoM report*

- A. GoM report relies heavily on judgment of the Hon'ble Supreme Court in *Skill Lotto Solutions Pvt. Ltd. Vs. Respondent: Union of India (UOI) and Ors. [2020 (43) G.S.T.L. 289 (S.C.)]* and states that while deciding taxability of issues in case of casinos, online gaming, horse racing, etc., the principles decided in Skill Lotto need to be taken into consideration.
- B. Based on Skill Lotto, the report concludes that online gaming also involves supply of actionable claim and hence, needs to be taxed on full value at 28%.
- C. Any differential tax treatment will result in litigation qua lottery as well.

#### *Factual & legal aspects for consideration*

- D. Bringing parity between lottery and online gaming is not the right approach as the modus operandi and legal status of lottery is different from that of online gaming. The sale of lottery tickets involves supply of actionable claim which is considered goods for GST purposes. Lotteries typically do not entail any separate service charges to be charged from customers which is not the case in online gaming. In online games, the supply by companies is only that of the technology platform for which it receives platform fees. The amount

received towards prize pool is held in a fiduciary capacity by online gaming companies and paid to the winner.

E. Online gaming and lottery/betting/gambling is fundamentally different and cannot be compared. Lottery/betting/gambling are clearly games of chance, and these make it fundamentally different from games of skill. Recently, the Hon'ble Karnataka High Court in *Gameskraft* matter has held that online games of skill being actionable claim do not amount to betting and gambling, and consequently quashed a show cause notice demanding GST at 28% on contest entry amount. It was held that merely because games are played online and for stakes does not make it betting and gambling. The jurisprudence laid down by Hon'ble Supreme Court and various High Courts holding that online games of skill do not amount to betting and gambling has been applied and followed, thereby establishing a distinction between games of skill and games of chance.

F. In games of chance, there is no element of competition between users even though many people may be involved together. Rather their success is based on their own good fortune (or fate). One can win regardless of whether the others have more skills or better talent. Importantly, there is no inter-se competition that decides the outcome and hence the element of contest between users is missing. Therefore, the relationship between the lottery operator and the entrant is singular one where the lottery operator offers the entrant a chance to win a large sum of money on a purchase of ticket. It is an individual and discrete relationship with the operator with no relationship between the entrants inter-se. Thus, the model of operation (both in form and substance) of lottery/betting tends to be around the operator, who organizes the event, promotes the event to get enrollment, procures entrants through sales of ticket through a large network of distributors, retains unsold tickets, organizes a draw, distributes the winnings.

G. In the activities of betting and gambling, the participants play against the house, which may also win the entire amount in case the user loses, which is not the case in online gaming.

H. Therefore, any differential tax treatment is only more justified rather than being discriminatory. The issue of taxing lottery, betting and gambling as opposed to other actionable claims was held to be correct in the case of Skill Lotto, wherein the Hon'ble Supreme Court held that these activities (of betting, gambling, lottery) are *res extra commercium*, whereas online gaming activities have been held by multiple courts across the country to be legitimate business activities protected under Article 19(1)(g) of the Constitution of India. Thus, the issue of differential treatment being violative of Article 14 does not arise in the case of online gaming vis-a-vis lottery.

## **2. Impact of past jurisprudence on consideration of online gaming as equivalent to betting, gambling and lotteries; removal of distinction between game of skill and game of chance**

### *Conclusions drawn in GoM report*

A. The GoM report states that online gaming involves betting. It has been further stated that the common thread between all the three activities of gaming, casino and race-courses was betting and gambling. Thus, there was a recommendation to levy uniform taxes on each of the three activities.

B. At the same time, the GoM has recommended that the question of games of skill or chance should not be relevant for GST regime, and that both should be taxed accordingly in the same manner. It has been further recommended that if such a differentiation exists, the same may be aligned.

### *Factual & legal aspects for consideration*

C. Equating online gaming with betting and gambling is incorrect interpretation of the jurisprudence on the issue as also based on the recent judgment of Hon'ble Karnataka High Court in the matter of *Gameskraft*, and the differentiation of online gaming from betting, gambling, wagering in the IT Rules

D. The erstwhile Finance Act, 1994 defined betting and gambling under Section 65B(15) and restricted the definition to a game or a contest whose result may be determined by chance or accident. This distinction between games predominantly involving skill vis-à-vis games of chance was clear and based on the past jurisprudence developed on this issue.

E. The indirect tax jurisprudence has in pre-GST as well as post-GST regime always made a distinction between betting and gambling and online gaming while determining the rate of tax and value of supply. Section 66D of the Finance Act, 1994 provided for a negative list of services that included betting, gambling or lottery. Thus, betting, gambling or lottery was not charged with Service Tax as it was the prerogative of State legislation. While betting and gambling was in the negative list, online gaming was a part of the definition of online information data access or retrieval services (OIDAR) as defined under rule 2(1)(cc) of Service Tax Rules, 1994. Gaming companies have been in existence since more than a decade and have been paying tax to the Central Government under OIDAR. Section 2(17) of the IGST Act includes online gaming as a part of OIDAR under the GST regime, while betting, gambling and lottery are under Schedule III entry 6 of the CGST Act. Even under the Scheme of Classification of Services, online gaming forms part of HSN code 998439 while betting and gambling forms part of HSN Code 999692.

F. As noted above, the legal jurisprudence is settled that online gaming is distinct from gambling, betting or lottery that means only games of chance. Any different interpretation by the tax authorities would result in altering the legal jurisprudence and constitutionally protected status of the legitimate business i.e., online gaming.

G. Courts have consistently held that online gaming predominantly involving skill cannot be considered as betting or gambling.<sup>1</sup>

H. Consistently, Courts have recognized online gaming to be not in the nature of betting/gambling. Thus, considering them as betting/gambling for taxation perspective is not in line with jurisprudence developed on this issue. The Hon'ble Karnataka High Court has recently ruled that games of skill whether played online/offline with or without stakes continue to be games of skill and therefore, do not amount to betting and gambling. Issue of game of skill and chance is relevant even in respect of taxation and the policy adopted to tax lottery/betting /gambling activities is not applicable to tax games of skill. The taxation policy of games of skill needs to be separately evaluated.

I. As discussed in Chapter 2, recently, the Central Government has also recognised the distinction between online gaming and gambling, betting and wagering and has provided for provisions specific to online gaming.

### 3. Taxation on GGR vs on full value

#### *Conclusions drawn in GoM report*

A. The GoM report states that there is no uniform international practice as regards value on which tax needs to be paid in online gaming sector. Further, it is observed that if at all there is any uniformity, it is in that most countries levy multiple taxes on betting and gambling and the cumulative incidence of taxes on them is quite high. They subject these activities to GST, VAT or Sales Tax as well as several kinds of betting, gambling and sweepstakes duty and taxes such as Betting Tax, Stamp Duty [which may be charged on winnings too], Gaming Tax, Pool Betting Duty, Casino Duty, etc.

B. Further, the GoM report states that a country may choose to apply GST/VAT on service element leaving aside the prize pool from the scope of GST/VAT,

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1. *Federation of Indian Fantasy Sports v. The State of Karnataka [W.P.No.22371/2021]*; *Varun Gumber Vs. Union Territory of Chandigarh, 2017 Cri LJ 3827*; *Gurdeep Singh Sachar Vs. Union of India & Ors., 2019-VIL-283-BOM*; *Ravinder Singh Chaudhary v. Union of India & ors., 2020(4) RLW 3322 (Raj)*; *Saahil Nalwaya v. State of Rajasthan and Ors., Civil Writ Petition No. 2026 of 2021.*

but may simultaneously impose betting tax, which may again be on gross gaming revenue or on the full bet value. In addition, in varying prevailing practices, countries opt to impose pool tax, gaming tax, stamp duty, casino tax, local duties and other taxes. Besides this, certain countries impose flat tax on winning amounts (in addition to tax on incomes). Such taxes cascade on each other and the cumulative incidence of tax on betting and gambling is quite high.

C. It has also been observed that the global regime also suggests that these industries survive even with higher taxation.

#### *Factual & legal aspects for consideration*

D. Countries globally are adopting progressive tax practices which has been enumerated in detail in a report published by us which provided a detailed overview of the taxation regime followed by leading countries in the world where it was concluded that:

a. International practices indicate unilateral progression towards the GGR model even wherever it is currently levied on total amount, which is only in a very few countries;

b. Most of the mature and developed nations have capped the tax rates between 15-20% on GGR as it results in the highest revenue generation for their respective economies; Even where additional duties are levied on online games of skill, they are mostly based on GGR and after addition of the levies, the total tax burden mostly is less than 28% of GGR;

c. Markets like United Kingdom and France which earlier used to tax the entire amount including the prize pool and contribution have now shifted to taxing only the GGR due to business shifting to black markets, loss of revenue and non-compliance with the licensing and regulatory system.

E. The GoM report's conclusion that higher taxes are prevailing in international jurisdiction appears to be contrary to the factual on-ground scenario.

#### **4. Levying of tax on platform fee vis-à-vis wider implications on other sectors**

##### *Conclusions drawn in GoM report*

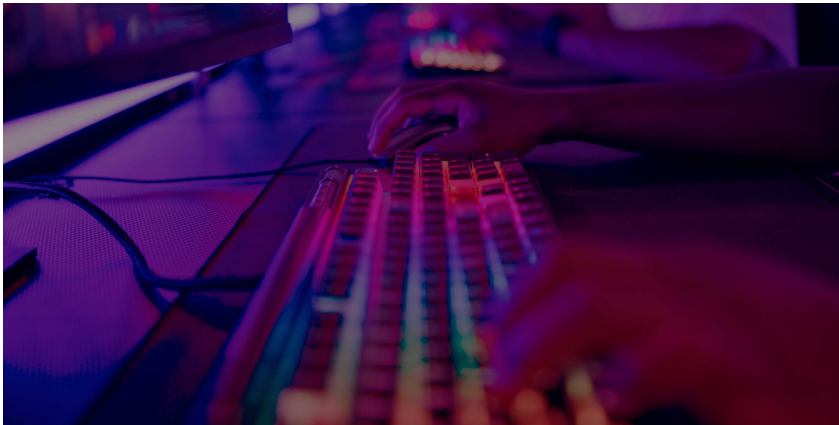
A. The GoM report states that applying GST only on platform fee for online gaming, GGR for casino etc. on the ground that tax should only be levied on the consideration accruing to service provider leaving the prize pool out will have wider implication for other services such as manpower supply agencies, and e-commerce service providers like Ola, Uber.



*Factual & legal aspects for consideration*

B. The form of the transaction and nature of supply is completely different in manpower supply services and e-commerce operators compared to online gaming. In manpower supply, the contractor engages into contract with employees / labourers and further supplies manpower services to its customers. All the aspects relating to employee provident fund, employee turnover, etc. is the responsibility of the manpower supplier and hence, the question of taxing him on commission vis-à-vis entire income does not arise. If such a service provider is merely a commission agent, then the tax arises only on commission income.

Online gaming companies only provide the service of technology platforms for which they charge platform fees and pay taxes. Thus, the above activities are not comparable to online gaming, which has also been pointed out by Hon'ble Finance Minister of Goa in GoM report, wherein it has been stated that such a comparison is like comparing apples with oranges.



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## 4. Comparative Analysis: Legal Status and Business Models of Lottery Vs. Online Gaming

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The GoM report finds its basis in two Supreme Court decisions pertaining to indirect tax implications on lottery. The two Supreme Court decisions mentioned above are the decisions in the matter of *Sunrise Associates vs. Govt. of NCT of Delhi and Ors.* reported at AIR 2006 SC 1908 (hereinafter referred to as ‘Sunrise Associates Case’) and *Skill Lotto Solutions Pvt. Ltd. vs. Union of India and Ors.* reported at AIR 2021 SC 366 (hereinafter referred to as ‘Skill Lotto Case’). Sunrise Associates decide upon the classification of lottery as actionable claim, and Skill Lotto is on the issue of GST and valuation of actionable claim of lottery. Since both the judgments are highly relied upon by the GoM in their report in relation to online gaming, it is pertinent to discuss these judgments.

The taxability of lottery as sale of ‘goods’ has always been a questionable issue till it got settled in 2006 by the Constitution bench of the Hon’ble Supreme Court in *Sunrise Associates Case*. Three separate decisions including the decision of the Hon’ble Supreme Court in the case of *H. Anraj vs. Government of Tamil Nadu* reported at AIR 1986 SC 63 (hereinafter referred to as ‘H. Anraj Case’) were referred before the Hon’ble Constitutional bench for reconsideration. All three decisions referred to had affirmed the decision of *H. Anraj Case* with respect to the tax liability on sale of lottery tickets. The Hon’ble Court in *H. Anraj Case* regarded lottery tickets as dealer’s merchandise, and considered sale of lottery as transfer of a right to participate in draw by State as a promoter which will amount to transfer of property and therefore, liable to sales tax as sale of goods.

While revisiting the said decisions, including the decision in the case of *H. Anraj*, the Hon’ble Supreme Court in *Sunrise Associates Case* held that the right to participate in the draw is a part of the composite right of chance to win. It was held that there is no value of mere right to participate, and the consideration is paid for the chance to win. The Court further observed that, even if the right to participate is considered as a separate right, transfer of right is not construed as sale of goods. Transfer of right would be of beneficial interest in movable property not in possession of the vendor and therefore, will be construed as actionable claim. Thus, the Court held that sale of lottery ticket would not amount to sale of goods but at the highest a transfer of an actionable claim. Accordingly, Hon’ble Court overruled the decision in *H. Anraj Case* and held that lottery shall qualify as actionable claim.

In the pre-GST regime, actionable claims were categorically excluded from the scope of the term 'goods' for the purposes of levy of sales tax. Later, in GST regime with the introduction of the Central Goods and Services Tax Act, 2017 (hereinafter referred to as '**the CGST Act**') the term 'goods' as defined under Section 2(52) thereof specifically includes actionable claims. However, vide Para 6 of Schedule III of the CGST Act, actionable claims other than lottery, betting and gambling were considered as activities which shall neither be treated as supply or goods nor as supply of services and thus, not chargeable to GST. Since actionable claim of lottery is considered as supply of goods within the CGST Act and excluded from Schedule III, it became chargeable to GST. Further, the valuation for such supply of actionable claim of lottery was also provided in Rule 31A thereof. In view of the said background, a Writ Petition was filed before the Hon'ble Supreme Court in *Skill Lotto* Case wherein out of other questions of law, the following two questions were raised, which are relevant in relation to legal position on games of skill:

- a. Whether the proposition of law that lottery is an actionable claim, as laid down by the Court in the judgment *Sunrise Associates* Case, an *obiter dicta* and not declaration of law?

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- b. Whether exclusion of lottery, betting and gambling from Item No.6 Schedule III of Central Goods and Services Tax Act, 2017 is hostile discrimination and violative of Article 14 of the Constitution of India?

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With respect to the first question, the Hon'ble Supreme Court held that the Constitutional bench in *Sunrise Associates* Case has laid down that lottery is an actionable claim as proposition of law and therefore, the said observation cannot be said to be *obiter dicta*.

With respect to the second question, the Court held that there was a rationale to tax only actionable claims for lottery, betting and gambling as all three have been held to be *res extra commercium* and thus there is no hostile discrimination.

The GoM in its report while discussing the rate of tax, and valuation method for online gaming has relied upon by the afore-discussed case laws and recommended that tax at the rate of 28% shall be levied on the supply of online gaming and such 28% rate shall be levied on the face value i.e., on 100% of the entry fees which includes money towards prize pool as well. Considering the above discussion, it becomes essential to compare and analyze the difference between lottery and online gaming and whether lottery is different from online gaming and the aspects that need to be taken into consideration, and whether a straitjacket formula can be applied on both activities.

It is pertinent to note that lottery is a distinct activity from online gaming, in that in case of lottery, the activity is fully based on chance. The entrants to a lottery merely purchase and hold ticket(s) till results are announced, to determine the winner. No additional set of skills are required by the entrants to participate and win in the activity of lottery winning. Experience, knowledge, preparation, and usage of data analysis, etc., which are fundamental to online games of skill, are not applicable in case of lottery. Lottery involves a single supply by the operator to the entrant and no *inter se* competition between the entrants.

Online gaming, on the other side, involves two distinct components – one being supply of platform services by the online gaming companies to the users and second being *inter se* competition between the users contesting against each other involve skill and judgment. The operator only provides a platform for the users to participate and compete against each other. Winning and losing are the result of the efforts undertaken by users who compete based on their skills, experience, statistical understanding, expertise.

The judgment of the Hon'ble Supreme Court can be said to be applicable on the facts of lottery where there was a single supply of lottery tickets by the operator to the entrant. Whereas the same cannot be said in respect of online games of skill where there is supply of platform services as also inter-se competition amongst users. It is settled law by the Hon'ble Supreme Court that the form of the transaction cannot be ignored except if it has no correlation with the actual transaction in contemplation. In online gaming, the deposits of the users do not form part of the supply by the platform and, hence, cannot form part of the value of the supply made by the online gaming companies. Therefore, the applicability of the judgments on lottery cannot be applied to online gaming.

Based on the above discussion, it can be seen that there are significant differences between lottery and online gaming. As discussed in the previous chapters, in various decisions, Courts have time and again held that online games of skill are permissible business and recognized in terms of Article 19(1) (g) of the Constitution as legitimate businesses, whereas lottery has been held to be *res extra commercium*. Even in the recent matter of *Gameskraft*, in the context of online rummy played with / without stakes, the Hon'ble Karnataka High Court has held that such games shall qualify as games of skill not amounting to betting and gambling. These are therefore not *res extra commercium* (i.e., not beyond commerce). While holding so, the Hon'ble Court observed that the department's reliance on Hon'ble Supreme Court's judgment in *M/s Sivani's* case was incorrect, and that the judgment nowhere said that games of skill amount to gambling.

Such online games are excluded from the scope of lottery, betting or gambling and considered as neither supply of goods nor supply of services, in terms of Schedule III of the CGST Act. In such a case, no taxation shall arise. The present legal position needs to be aligned with the proposed taxation, which if based on GGR will be aligned basis the present practice of taxation on platform fees, i.e., service charges charged by platforms.



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## 5. Implications of the Information Technology Rules on GST

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Prior to the notification of the Information Technology (Intermediary Guidelines and Digital Media Ethics Code) Amendment Rules 2023, there was ambiguity with respect to determination of a game of skill and game of chance. Further, the exact service and consideration being provided by the online games provider was questioned time and again with skepticism being that the entire service being provided by an online games provider is an actionable claim.

This skepticism is reflected in the GoM report. The GoM report states that GST on activities of casinos, racecourses, online gaming and lottery should be uniform and should be full value. This position is a conundrum to the very nature of the activities being discussed as betting and gambling is banned in India and anything in the nature of betting and gambling cannot be put on the same pedestal as normal commerce activities. Further, each activity discussed has a differential modus operandi which negates the presumption that valuation and taxation of each activity can be done uniformly which has already been discussed in the previous chapters.

The notification of the Information Technology (Intermediary Guidelines and Digital Media Ethics Code) Amendment Rules 2023 has brought about a regimen shift by (a) providing legitimacy to online skill based real money games that are defined as “permissible online real money games” under the said amendment rules and (b) by identifying the online gaming providers as “online gaming intermediaries” that are merely providing platform services the customer while facilitating the games to be contested amongst the users. The introduction of the IT Intermediary Amendment Rules, 2023 is pivotal to the discussion because it specifies that a permissible online real money game is different from wagering and betting and codifies the distinction between games of skill and games of chance as well as settles the debate on the true nature of services being provided by online games providers. It has been made clear that unlike the business model followed in lottery, as was discussed in skill lotto judgement, the online gaming intermediaries merely provide a platform to the users for contesting games and charge their service fees for the same just like any other intermediary. The law surrounding permissible online real money gaming is very clear now and there is no longer any ambiguity surrounding the legality and the services being provided.

In this context, it is important that the GST Council considers the recent legislative developments to ensure that the GST position is aligned with the established jurisprudence and central legislations on the said matter.



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## 6. Services Vs. Goods

### Argument for Online Gaming

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The GoM report stipulates that the issues raised in respect of lottery, racecourse, gambling, betting, and online gaming are intertwined. Further, the GoM report observed that the intention is evidently to impose GST on actionable claim by extensively relying on the judgement of *Skill Lotto Solutions Private Ltd v Union of India*. However, as discussed above, the said judgement pertains to lottery, which is an actionable claim and taxed as goods by excluding them from Schedule III, whereas the nature of supply of online gaming is merely a supply of service.

The online gaming industry started and continues as a technology enabler for users to compete against each other in contests. The fundamental premise of the industry is that they are *technology service providers* that provide a marketplace for users to compete in contests against each other. The platform provides for the following which can only be classified as supply of services:

- a. The platforms facilitate the contests by providing a stable technology platform.
- b. Cash management of users deposits through independent trustee accounts as a service provided to ensure comfort for individual users about their money and for easy settlement. This amount is never the 'money' of the platform and is always constituted as a prize pool for users in the games.

The online gaming industry merely charges platform fees to the users for providing platform services. Right from the beginning, the companies registered themselves for service tax under IT/ITeS category and discharged tax on their platform fee. This was not an artificial construct but represented the service actually provided by the platform. Online gaming is classified under HSN Code 998439, and the GST is levied at 18% on the platform fee/Gross Gaming Revenue (GGR). Lotteries are classified under HSN Code 999694 and Gambling & betting activities are classified under HSN Code 999692, and the GST is levied at 28% on the face value of the lottery ticket and total bet value, respectively.

It is imperative to understand that the nature of supply of online gaming is only a service. It involves two distinct components. First, is a supply of platform services by the online gaming companies to the users and the second is the



inter-se competition between the users contesting against each other involving skill and judgment.

It is pertinent to note that prize pool contribution by the users is not a consideration for any supply made by the online gaming operators to the users and hence has no nexus with the taxable event of supply of platform services provided by the operator. There is no supplier-recipient relationship between any parties qua the prize pool contribution. Therefore, GST is not payable on such prize pool contribution by the operator.

In this regard, it is relevant to refer to the judgment of Hon'ble Supreme Court in the case of **State of Rajasthan vs Rajasthan Chemists Association** [2006 (202) E.L.T. 217 (S.C.)]. Relevant extract of the judgment is provided below:

*“28. The question of tax on sale of goods may be examined in the said background. **The subject of tax being sale, measure of tax for the purpose of quantification must retain nexus with ‘sale’ which is subject of tax. As noticed above, tax on sale of goods, is tax on vendor in respect of his sales and is substantially a tax on sale price. The vendor or buyer cannot be taxed de hors the subject of tax that is sale by the vendor or purchase by the buyer.** The four essential ingredients of any transaction of sale of goods include the price of the goods sold, therefore, in any taxing event of sale, which become subject matter of tax price component of such sale, is an essential part of the taxing event. Therefore, the question does arise whether a particular taxing event of sale could be subjected to tax at the prescribed rate to be measured with such price which is not the component of the transaction of sale, which has attracted the sales tax.*

*40. These cases give a clear picture that Entry 54 in List II of Seventh Schedule empowers the State Legislature to impose and collect taxes on sale of goods. **The measure to which tax rate is to be applied must have a nexus to taxable event of sale and not divorced from it.***

*49. Another distinguishing feature to be kept in mind is that centre point of legislation under Entry 54 of List II of Seventh Schedule is ‘sale’ in contrast with central point of legislation under Entry 84 of List I of Eighth Schedule i.e. ‘Goods manufactured or produced’. While basic nexus of levy in the former is “sale of specified goods”, in the latter it is “goods manufactured or produced in India”.*

*50. **Every transaction of sale is independent and can be subject to levy of tax and the components and the measure which can make the tax levy effective must have nexus with the taxable event.”***

Further, in the context of valuation for the purpose of levy of service tax, it has been held by Hon'ble Supreme Court in **Union of India vs Intercontinental Consultants and Technocrats Pvt. Ltd.** [2018 (10) G.S.T.L. 401 (S.C.)] that the valuation of taxable service cannot be anything more or less than the consideration paid as *quid pro quo* for rendering such a service. Relevant extract of the judgment is provided below:

*“24. In this hue, the expression ‘such’ occurring in Section 67 of the Act assumes importance. In other words, valuation of taxable services for charging service tax, the authorities are to find what is the gross amount charged for providing ‘such’ taxable services. As a fortiori, any other amount which is calculated not for providing such taxable service cannot a part of that valuation as that amount is not calculated for providing such ‘taxable service’. That according to us is the plain meaning which is to be attached to Section 67 (unamended, i.e., prior to May 1, 2006) or after its amendment, with effect from, May 1, 2006. Once this interpretation is to be given to Section 67, it hardly needs to be emphasised that Rule 5 of the Rules went much beyond the mandate of Section 67. We, therefore, find that High Court was right in interpreting Sections 66 and 67 to say that in the valuation of taxable service, the value of taxable service shall be the gross amount charged by the service provider ‘for such service’ and the valuation of tax service cannot be anything more or less than the consideration paid as quid pro qua for rendering such a service.”*

In the above case laws, it is further explained that for any amount to be taxable as a consideration for a taxable supply, the amount should have a nexus to taxable event and should not be divorced from it. In the instant case, the taxable event is supply of platform service by the online skill gaming platform operators. The consideration for the said supply is the platform fees collected by the operators.

Prize pool contribution is not a consideration for any supply made by the online gaming operators to the users and hence has no nexus with the taxable event triggered by the operator. Where there is no relationship between the taxable event and the measure on which the tax is imposed, such tax imposition would be ultra-vires and hence, avoidable.

In the present transaction, the service of the operator is limited to providing platform services and imposition of tax should be limited to the consideration received in pursuance of the same. Thus, prize pool contribution is not a consideration for any supply by platforms. GST, if any, is payable on platform charges collected by the service providers as the supply of the technology platform is the supply of service.



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## 7. RECOMMENDATIONS

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The online gaming industry has been in existence in the country for more than a decade now, with multiple judicial precedents addressing their legality, valuation and taxation issues and other areas of dispute founded on various principles. Recently, MeitY has introduced amendments to the Central rules i.e., Information Technology (Intermediary Guidelines and Digital Media Ethics Code) Rules, 2021 where Self-Regulatory Bodies (SRB's) recognised by the Government of India are empowered to approve the functioning of online real money games, differentiating such gaming activities from wagering i.e. betting and gambling and providing recognition to online gaming intermediaries. The certification of 'permissible online real money game' under the Information Technology Act and Information Technology Rules provides a clear and distinct legal status.

The introduction of the new provisions of Income Tax Act, 1961 via Finance Act, 2023 dealing specifically with the online gaming industry has brought much relief to the entire industry as well as the users of the online platform. Separate provisions of Section 115BBJ & 194BA is a clear sign of separate status of online gaming w.r.t to lottery, gambling & betting. These amendments, with the removal of the threshold of Rs 10,000 for deduction of TDS and with taxable event as a withdrawal or end of Financial Year ensure that there is no revenue leakage from taxation on prize pool.

The online gaming industry now awaits the final decision of the GST Council on the GST rates and value of supply. In May 2023, during media interaction, the Hon'ble Finance Minister, Nirmala Sitharaman stated that the GST Council is currently deliberating on the taxation policy and exuded confidence that stability, transparency, and clarity in taxation policy will boost investment in the sector.

The following aspects may be considered while arriving at a solution which is progressive for the online gaming industry and beneficial for the Government to implement:

- In light of the above recent developments, the GST Council may consider the latest developments in the legal field in relation to online gaming.
  - The GoM report is to re-examined in light of the new developments.
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- Taxability of the activity of online gaming involving games of skill may be decided considering the jurisprudence developed since 1950s, wherein these games have been recognized as games of skills and distinct from lottery, betting, gambling and wagering.
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- While applying the principle of nomen-juris, the phrase gambling and betting, even for the purpose of GST shall be construed in the legal sense which has been held to involve chance as a predominant element.
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- For the purpose of GST as well, the jurisprudence of distinction between constitutionally protected activities i.e. games of skill and res extra commercium activities i.e. gambling & betting shall be adhered to. The Supreme Court as well as various High Courts have laid down the preponderance test to determine whether a format is a game of skill or game of chance. In order to determine the applicability of GST i.e on Platform Fee (GGR) or on Total amount under the GST law, it has to be factually established whether the online gaming format is a game of skill or game of chance i.e wagering on an outcome. This distinction would be derived from the certification of online games by the Self-Regulatory Body to be recognised by the Government of India.
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- Permissible Online Real Money Games under IT rules to be continued to be taxed on Gross Gaming Revenue
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