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20<sup>TH</sup> SURANA AND SURANA CORPORATE MOOT  
COURT COMPETITION, 2023

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IN THE HON'BLE HIGH COURT OF KARNATAKA||  
AT BENGALURU, KARNATAKA

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WP No.:1001 to 1004 of 2023

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MIDAS ONLINE GAMES INDIA PVT. LTD.

V.

DIRECTORATE GENERAL OF GST INTELLIGENCE DEPARTMENT

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BEFORE SUBMISSION TO HON'BLE CHIEF JUSTICE

AND HIS COMPANION JUSTICES

OF THE HON'BLE HIGH COURT OF KARNATAKA||

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MEMORANDUM ON BEHALF OF THE PETITIONER

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**TABLE OF CONTENTS**

TABLE OF CONTENTS.....	i
LIST OF ABBREVIATION .....	ii
TABLE OF AUTHORITIES .....	iii
STATEMENT OF JURISDICTION .....	v
STATEMENT OF FACTS .....	vii
STATEMENT OF ISSUES .....	viii
SUMMARY OF ISSUES .....	ix
ARGUMENTS ADVANCED .....	10
ISSUE 1 .....	10
ISSUE 2 .....	16
PRAYER.....	24

( ), 20^  
LIST OF ABBREVIATIONS

**LIST OF ABBREVAITION**

IBC	Insolvency and Bankruptcy Code, 2016
CIRP	Corporate Insolvency Resolution Process
GST	Goods and Services
CGST	Central Goods and Service Tax
SCN	Show cause notice
PVT..	Private
Ltd.	Limited

**TABLE OF AUTHORITIES**

**CASE LAWS-**

1. Varun Gumber vs. UT of Chandigarh 2017 Cri. L J 3827
2. Public Gambling Act, 1867, § 2, No. 3, Acts of Parliament, 1867 (India)
3. Dr. R. K. Lakshmanan v. State of Tamil Nadu State of Andhra Pradesh v. K. Satyanarayana, AIR 1968 SC 825
4. State of Bombay v. R.M.D. Chamarbaugwala AIR 1957 SC 699
5. D. Krishna Kumar v. State of Andhra Pradesh, (1988) 3 SCC 609
6. Dr. K.R. Lakshmanan v. State of Tamil Nadu, (1996) 2 SCC 226 Central Goods and Services Tax Act, § 2(52) (2017)
7. Dream 11 (GST AAR Maharashtra), Advance Ruling No. GST-ARA-27/2018-19/B-27, (2019) 2 G.S.T.L. 641 (Mah. A.A.R.) Gurdeep Singh Sachar v. Union of India, (2015) 16 SCC 283 Gaussian Networks PVT.... Ltd. v. Union of India, (2019) 1 SCC 796
8. Dominance Games PVT.... Ltd. v Union of India, (2021) 3 SCC 555
9. Skill Lotto Solutions PVT.... Ltd. vs. Commissioner of Commercial Taxes, Karnataka, (2018) 13 SCC 139
10. Kunnath Pharmaceuticals vs. The State of Kerala, (2014) 4 SCC 108
11. Kerala value added tax act, 2003) Om Prakash vs. State of Uttar Pradesh and Others, (2006) 8 SCC 1
12. Godfrey Phillips India Ltd. vs. State of U.P. and Others, (2005) 2 SCC 515
13. State of Andhra Pradesh vs. K. Satyanarayana and Others, (1968) 1 SCR 825
14. Innoventive Industries Ltd. v. ICICI Bank & Anr, (2017) 1 SCC 407 JK Jute Mill Mazdoor Morcha vs Juggilal Kamalpat Jute Mills Company Ltd., (2018) 10 SCC 641
15. Mobilox Innovations Private Limited v. Kirusa Software Private Limited (2017) 1 SCC 407.
16. K. Kishan v. Vijay Nirman Company PVT.... Ltd., (2018) 6 SCC 534
17. Arbitration and Conciliation Act, 1996
18. Central Goods and Services Tax Act, § 74(9) (2017)
19. M/s Siddhartha Enterprises v. Union of India & Ors, (2018) 90 GST 154 (Uttarakhand).
20. P K Zaveri PVT.... Ltd.. v. Union of India & Anr, 2018 SCC OnLine Del 10485.
21. Arun Kumar Gupta v. Union of India & Ors, 2019 SCC OnLine Bom 22.

**LEGISLATIONS-**

1. Insolvency and Bankruptcy Code, 2016
2. Goods and Service Act, 2016
3. General Clauses Act, 1897, § 3(10) 1897

TABLE OF AUTHORITIES

4. Arbitration and Conciliation Act, 1996
5. Central Goods and Services Tax Act, § 74(9) (2017)
6. The Constitution of India, 1950.

Q, 20^  
STATEMENT OF JURISDICTION

**STATEMENT OF JURISDICTION**

It is most humbly submitted that the Petitioner has approached the honourable High Court of Karnataka under Article 226 of the Constitution of the Union of India. The petitioner most humbly and respectfully submits before the jurisdiction of the present court and accepts that under Article 226, it has the power and authority to preside over the present case to issue instructions, orders, and writs to any person or authority, including the government.

**STATEMENT OF FACTS**

**A. Introductory background-**

1. Midas online Games Pvt. Ltd. is a registered company involved in the business of a range of multiple Games- primarily Games of Skills such as rummy, poker, and the like; fantasy cricket; horse racing; etc. the model of the business is such that it involves two different types of payments to be made by the consumers- (i) admission fee: which constitutes 25% of the total payment and is the direct income of the company; (ii) pooling fee- which aggregates into the monetary prize for winners and will be distributed accordingly, i.e., The company derives no benefit from this segment of the payment.
2. Since the company mainly provides Games of Skills that are classified under service of goods- it paid 18% GST on the income, which was 25% of the total payment processed in addition to direct income taxes.

**B. National Bank of India-**

1. Due to profitable business undertakings and similarly aligned goals, the company had a revenue of 5000 crore INR each financial year. In addition to that, it had incurred liabilities of around 5000 crore INR from the National Bank between July 2017 to August 2022 that were granted with ease due to financially prudent and prompt attitude of clearing dues by the company.
2. Further, upon the orders of NCLT as on 6.10.2022, the NBI filed its claim as a secured creditor under form B for the above said due amount.
3. It is to be noted that the NBI believed that it was the biggest secured and financial creditor and was the creditor for 90% of the company's due. Further, it also believed that the GST Department cannot be a secured creditor.

**C. The GST Department:**

1. The Office of the Director General of GST Intelligence issued show cause notices (SCN) to the company alleging that they were liable to pay 28% of GST rate on the total processed payment by the consumers since the GST Department classified the undertakings of the company as a Game of Chance, and not Skill. Moreover, the department also claimed dues equivalent to 28% tax rate penalty.
2. The department, after hearing replies and pleadings to the SCN, reserved its order on 30.09.2022.

Q, 20^  
STATEMENT OF ISSUES

3. As a response to online and media speculations of insolvency of the company, the GST Department passed orders demanding the dues alleged in the aforementioned SCN, that is Rs. 5000 cr INR by the evening of 5.10.2022.
4. The department further uninitiated recovery proceedings under section 79(1)(c) of the GST Act by directing the NBI to freeze all the bank accounts of the company and thereby, created a 'charge' on the accounts lying in the bank accounts to the tune of INR 6,000 approximately towards the demands raised in the said four orders.
5. Further, upon the orders of NCLT as on 6.10.2022, the department filed its claim as a secured creditor under form B.

**D. Insolvency proceedings:**

1. The company, rightfully, reserved its right to non- payment to its software supplier due to delivery of poor upgradation. However, the said supplier in turn filed an application of insolvency of Midas Online Games Pvt. Ltd. before the National Company Law Tribunal.
2. It is to be noted that the software supplier failed to observe the due process laid down by the law. Nevertheless, the NCLT pronounced its orders admitting the application and declared the company insolvent in addition to initiation of the Corporate Insolvency Resolution Process, appointment of the Interim Resolution Professional (consequently declared as the RP), and ordering of a moratorium as in accordance to section 14 of the Insolvency and Bankruptcy Code.

**E. Pleadings of the Company:**

1. The IRP collated all the claims of the company and conducted a meeting of the committee of creditors. The primary three takeaways from this meeting were that: a) the IRP to be appointed as the RP; b) the claims of the GST Department were unsustainable, especially because the dispute is against the GST laws itself; c) file write petitions before the Karnataka High Court under 74(9) and 73(9) and recovery proceedings initiated on 06.10.2022 under section 79(1)(c) of the GST Act which were in a hurried and desperate manner.
2. The primary two contentions formed in extraction of the writs are as follows:
  - (i) classification of the undertakings by the company and hence consequent valuation of the tax rates due.
  - (ii) validity of status of the GST Department as a secured creditor.



**STATEMENT OF ISSUES**

**ISSUE 1**

WHETHER THE UNDERTAKINGS OF THE COMPNAY SHOULD BE CLASSIFIED AS 'GAME OF CHANCES' OR 'GAME OF SKILL' AND CONSEQUENTLY WHAT TAX RATE IS DUE?

**ISSUE 2**

WHETHER THE GST DEPARTMENT CAN BE TREATED AS SECURED CREDITOR OR MERELY AN OPERATIONAL CREDITOR?

**SUMMARY OF ISSUES**

**ISSUE 1**

Given that the company's online Games are 'Games of Skill', it is not required to pay consideration on the total amount. The petitioners argue that the evidence will demonstrate that the Games played on the Midas platform are Games of Skill rather than Chance. Only the admission fee will be taxed; 100% consideration will not be levied. The petitioners will provide statutes and pertinent cases to demonstrate how Midas paid tax on the total consideration resulting from the platform charge, which was equal to 18% of the 25% they were paid.

**ISSUE 2**

The GST department should only be recognised as a 'operational creditor' in order to collect its obligations rather than a 'secured creditor'. It is respectfully submitted before the honourable high court of Karnataka that, after careful consideration of the arguments, it is clear that the GST department's claims to be a 'secured creditor' lack foundation and that it can only be considered an 'operational creditor'. Such claims are made on two primary grounds: Firstly, the department lacks the necessary security to have a secured interest. The same can be proved by establishing that the department lacks any security interest, and any interest claimed is invalid and cannot be admitted before the court. Secondly, the plaintiff additionally claims that the NCLT's declaration of insolvency as of its order dated 6.10.2022 is unlawful and unenforceable because it did not follow the due process requirements set forth in section 9 of the IBC, which should be read in conjunction with section 8. This will be established if the requirements and consequent lack thereof, primarily absence of notice and due amount under dispute. All of the aforementioned shall be proven by critical analysis of the case along with judgements by various competent courts enumerating on the same.

**ARGUMENTS ADVANCED**

**ISSUE 1**

**THE COMPANY IS NOT LIABLE TO PAY CONSIDERATION ON THE ENTIRE AMOUNT SINCE THE GAMES OPERATED BY IT ONLINE ARE ‘GAMES OF SKILL’.**

It is humbly submitted before the honourable High Court of Karnataka that in light of the aforementioned contentions, it is firmly established that the demands of the Department of Goods and Service Tax (GST) are not maintainable under the law and Midas Online Games India Pvt. Ltd. is not required to pay GST on the entire consideration received by it since all the Games operated by it online are only ‘Games of Skill’ and not ‘Games of Chance.’

**1.1 Game of Skill v. Game of Chance**

1.1.1 It is humbly submitted by the counsel for the petitioners that Midas Online Games India PVT... Ltd. is involved in the business of online Games such as card Games like rummy, poker, fantasy cricket, horse racing, lottery among others.

A "**Game of Skill**" is primarily reliant on a person's level of mental or physical competence rather than Chance. A Game of Skill offers players the freedom to test their athletic prowess, which is one of its most important advantages. The participants are encouraged by these Games to become acclimated to a certain set of rules while searching for methods to develop and use new techniques through regular practice. It is untrue to say that Games of Skill do not involve a certain amount of Chance; in fact, they do. Yet, **the success percentage is determined by each person's unique Skills**. Examples of Games of Skill include chess, carrom, **rummy**, horse racing, and **fantasy sports**. Here it is a Game of Skill and not a Game of Chance as clearly stated.

1.1.2 In the case of Varun Gumber vs. UT of Chandigarh 2017<sup>1</sup>, it was stated that

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<sup>1</sup> *Varun Gumber vs. UT of Chandigarh 2017 Cri. L J 3827*

*“Participating in a fantasy league involves the user building a virtual team, which would certainly require considerable Skill, judgment and discretion;*

*(b) The participant has to assess the relative worth of each athlete/sportsperson against that of all other athlete/sports-persons available for selection; and*

*(c) The participant is required to study the rules and regulations and analyze the strengths/weaknesses of the athlete/player.*

*The factors indicated above would affect the results of the Game, thus making it a Game of Skill and excluding it from the ambit of gambling. Further, the Supreme Court dismissed the special leave petition filed by the petitioner against the Punjab & Haryana High Court’s order without any adverse remarks.”*

It can thus be stated that the Game can be considered as a Game of Skill and not a Game of Chance and therefore, the counsel for the petitioner pleads the same.

1.1.3 The definition of "gambling" in the Public Gambling Act, 1867,<sup>2</sup> and other state laws refers to Games of Chance, and not Games of Skill. As the Games offered by the company involve a significant element of Skill, they should not be classified as gambling. This view was supported by the Supreme Court in the case of *Dr. K.R. Lakshmanan v. State of Tamil Nadu (1996)*<sup>3</sup>, where the court held that horse racing, which involves a significant degree of Skill, cannot be considered gambling.

1.1.4 Preponderance of Skill over Chance- The counsel for the petitioner submits that many of the Games that the company offers, such as rummy, poker, and fantasy cricket, involve a significant degree of Skill and strategy on the part of the players, which makes them different from pure Games of Chance. As the Supreme Court has held in the case of *State of Andhra Pradesh v. K. Satyanarayana*<sup>4</sup> (1968), Games that involve a preponderance of Skill over Chance cannot be classified as gambling. It said that held that horse racing was a Game of Skill, and therefore, not gambling. The court held that the Skill involved in picking a winning

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<sup>2</sup> Public Gambling Act, 1867, § 2, No. 3, Acts of Parliament, 1867 (India)

<sup>3</sup> Dr. R. K. Lakshmanan v. State of Tamil Nadu

<sup>4</sup>State of Andhra Pradesh v. K. Satyanarayana, AIR 1968 SC 825

horse was the result of a combination of factors such as the Skill of the jockey, the physical condition of the horse, and the expertise of the trainer.

1.1.5 The same principle was upheld in the case of State of Bombay v. R.M.D. Chamarbaugwala<sup>5</sup> where the Supreme Court held that Games that involve a substantial degree of Skill are not gambling. Similarly, in the case of D. Krishna Kumar v. State of Andhra Pradesh<sup>6</sup> the Supreme Court held that horse racing is a Game of Skill. These judgments provide a strong basis for arguing that the company's Games of Skill should be taxed at a lower rate.

1.1.6 In the case of K.R. Lakshmanan (Dr) v. State of T.N<sup>7</sup>, states that “A Game of Skill, although the element of Chance necessarily cannot be entirely eliminated — is one in which success depends principally upon the superior knowledge, training, attention, experience and adroitness of the player. Golf, chess and even rummy are considered to be Games of Skill. The courts have reasoned that there are few Games, if any, which consist purely of Chance or Skill, and as such a Game of Chance is one in which the element of Chance predominates over the element of Skill, and a Game of Skill is one in which the element of Skill predominates over the element of Chance. It is the dominant element — ‘Skill’ or ‘Chance’ — which determines the character of the Game.”

1.1.7 Thus, the counsel submits there indeed exists the dominance of Skill in the online Games such as rummy, poker, fantasy cricket, and horse racing, which are offered by Midas Online Games. The mere presence of lottery cannot disqualify them from the tax bracket of 18%, pushing them to the category of ‘Game of Chance’ at a tax rate of 28% on the whole consideration.

## **1.2 Tax to be charged only on admission fee and not 100% consideration**

1.2.1 The counsel humbly submits that Section 2(52) of the Central Goods and Services Tax (CGST)<sup>8</sup> Act defines "escrow account" as an account in which a part of the amount from a

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<sup>5</sup> *State of Bombay v. R.M.D. Chamarbaugwala* AIR 1957 SC 699

<sup>6</sup> *D. Krishna Kumar v. State of Andhra Pradesh*, (1988) 3 SCC 609

<sup>7</sup> *Dr. K.R. Lakshmanan v. State of Tamil Nadu*, (1996) 2 SCC 226

<sup>8</sup> *Central Goods and Services Tax Act, § 2(52)* (2017)

transaction is kept aside by the promoter of a scheme, only for the purpose of payment of tax under the provisions of the Goods and Services Tax Act.

1.2.2 The money deposited by the participants to the escrow account qualifies as a transaction in money, since the money has been only deposited and has not yet been used by the participant to play any Game or avail any service of the platform. This amount would remain as that of the participant. Further, it is in the nature of an 'actionable claim'.

1.2.3 Schedule III of the Central Goods and Services Tax Act ('CGST Act') provides that "*actionable claims, other than lottery, betting and gambling*"<sup>9</sup> shall be treated neither as a Supply of Goods nor a Supply of Services. Levy of tax on the money deposited in this account is against the basic principle of the GST law.

1.2.4 In the case of *Dream 11 (GST AAR Maharashtra)*<sup>10</sup>, the Authority for Advance Rulings (AAR) held that the amount collected by the company from the participants as the entry fee and kept in the escrow account cannot be considered as the company's income, as the company only acts as an intermediary between the participants who are playing the Game. The AAR further held that the tax liability of Dream 11 is only on the service fee/commission charged by them for conducting the Game and not on the entire amount collected in the escrow account.

1.2.5 Similarly, in the case of *Gurdeep Singh Sachar v. Union of India*<sup>11</sup>, the Delhi High Court held that the entry fee paid by the participants to play the Game of poker online cannot be considered as the value of taxable service provided by the website. The court observed that the money deposited by the participants in the escrow account was not received by the website as consideration for the service provided, but was only held in trust for the participants, and hence cannot be subjected to service tax. Further, it observed that the amount pooled in the escrow account is an 'actionable claim' as the same is to be distributed amongst the winning members as per the outcome of a Game, and the said actionable claim would fall under Entry 6 of the Schedule III under Section 7(2)<sup>12</sup> of CGST Act.

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<sup>10</sup> *Dream 11 (GST AAR Maharashtra)*, Advance Ruling No. GST-ARA-27/2018-19/B-27, (2019) 2 G.S.T.L. 641 (Mah. A.A.R.)

<sup>11</sup> *Gurdeep Singh Sachar v. Union of India*, (2015) 16 SCC 283

<sup>12</sup> *Central Goods and Services Tax Act*, § 72 (2017)

It was also held that this activity or transaction pertaining to such actionable claim can neither be considered a supply of goods nor supply of services and is thus, clearly exempted from levy of any GST, and as such Rule 31A (3) of CGST Rules<sup>13</sup> is not applicable in the present matter.

1.2.6 In the case of *Gaussian Networks Pvt. Ltd. v. Union of India*<sup>14</sup>, the Gujarat High Court held that online poker was a Game of Skill and not a Game of Chance, and the tax liability was limited to the admission fee only, meaning that if the company can establish that its Games are predominantly Games of Skill, it would be liable to pay tax at the rate of 18% only on the admission fee. Further, the Gujarat High Court in the case of *Dominance Games Pvt. Ltd.. v. Union of India*<sup>15</sup> held that the tax liability on online fantasy gaming should be calculated only on the admission fee charged by the company.

### **1.3 Lottery not a supply of goods and services, thus cannot be taxed**

The counsel humbly submits that the sale of a lottery ticket does not constitute the supply of a tangible good or a service.

1.3.1 In the case of *Skill Lotto Solutions Pvt. Ltd.. vs. Commissioner of Commercial Taxes, Karnataka*<sup>16</sup>, the Karnataka High Court held that lottery tickets cannot be considered as goods or services for the purpose of taxation under the GST regime. The court reasoned that the sale of lottery tickets does not result in the transfer of any tangible or intangible property, nor does it involve the provision of any service.

1.3.2 Similarly, in the case of *Kunnath Pharmaceuticals vs. The State of Kerala*<sup>17</sup>, the Kerala High Court held that lotteries cannot be treated as goods or services for the purpose of taxation under the Kerala Value Added Tax (VAT) Act<sup>18</sup>. The court held that the sale of lottery tickets is not a transaction involving the transfer of property, and is therefore not subject to VAT.

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<sup>13</sup> Central Goods and Services Tax Act, Rule 31A (2017)

<sup>14</sup> *Gaussian Networks Pvt.... Ltd.. v. Union of India*, (2019) 1 SCC 796

<sup>15</sup> *Dominance Games PVT.... Ltd.. v Union of India*, (2021) 3 SCC 555

<sup>16</sup> *Skill Lotto Solutions PVT.... Ltd.. vs. Commissioner of Commercial Taxes, Karnataka*, (2018) 13 SCC 139

<sup>17</sup> *Kunnath Pharmaceuticals vs. The State of Kerala*, (2014) 4 SCC 108

<sup>18</sup> Kerala value added tax act, 2003

#### **1.4 Demand orders for payment of tax arbitrary and egregious**

1.4.1 The counsel for the petitioner argues against the constitutionality of Rule 31(A)<sup>19</sup>, where the department has demanded payment of tax upto 28%, which is discriminatory and arbitrary in nature, as it does not have a clear rationale or basis for setting the GST rate at 18%. In the case of *Om Prakash vs. State of Uttar Pradesh and Others*<sup>20</sup>, the Supreme Court of India held that a tax law that is arbitrary or irrational, and does not have a clear rationale or basis for setting the tax rate, would be unconstitutional

1.4.2 Further, it can also be said that it treats online gaming companies differently from other businesses that provide similar services. In the case of *Godfrey Phillips India Ltd.. vs. State of U.P. and Others*<sup>21</sup>, the Supreme Court of India held that a tax law that is discriminatory in nature and targets specific businesses or individuals without a rational basis for doing so would be unconstitutional.

1.4.3 Moreover, if online Games such as rummy, poker, fantasy cricket, horse racing, or lottery are considered to involve an element of Skill, then levying GST on the entire 100% consideration is outrightly arbitrary and egregious. In the case of *State of Andhra Pradesh vs. K. Satyanarayana and Others*<sup>22</sup>, the Supreme Court of India held that a Game that involves an element of Skill, even if it also involves an element of Chance, cannot be considered gambling.

Therefore, the counsel for the petitioner most humbly submits that the company is not liable to pay compensation on the entire amount, since the Games operated by it online are “Games of Skill”.

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<sup>19</sup> Rule 31A of CGST Act (2017)

<sup>20</sup> *Om Prakash vs. State of Uttar Pradesh and Others*, (2006) 8 SCC 1

<sup>21</sup> *Godfrey Phillips India Ltd.. vs. State of U.P. and Others*, (2005) 2 SCC 515

<sup>22</sup> *State of Andhra Pradesh vs. K. Satyanarayana and Others*, (1968) 1 SCR 825



## ISSUE 2

### **THE GST DEPARTMENT CANNOT BE TREATED AS ‘SECURED CREDITOR’ BUT ONLY AS OPERATIONAL CREDITOR TO RECEIVE ITS DUES.**

It is humbly submitted before the honourable High Court of Karnataka that in light of the aforementioned contentions, it is firmly established that the demands of the GST department to be so called the ‘secured creditor’ has no leg to stand and at best can only be an ‘operational creditor’, and so, has to wait in queue as per the IBC provision of 53 to receive its dues.

#### **2.1 The department does not hold necessary security to have secured interest**

2.1.1 A creditor who has a security interest in the debtor's assets to guarantee payment of the debt is referred to as a "secured creditor." Under Section 5(28) of The Insolvency and Bankruptcy Code, 2016 (IBC)<sup>23</sup>, 'secured creditors' of a company subject to the Corporate Insolvency Resolution Process (CIRP)<sup>24</sup> are those who have a security interest in respect of the assets of the corporate debtor, including a mortgage, charge, hypothecation, or pledge.

2.1.2 However, the GST Department cannot be considered a secured creditor when they create a "charge" over some money in a company's bank account after CIRP<sup>25</sup> has been initiated. The fact that the GST department has created a "charge" over a certain sum of money in the bank against a company that owes them tax payment does not necessarily make them a secured creditor. This is because a "charge" is not the same as a security interest. A charge is a legal claim against property that does not give the creditor the right to take possession of the property. In addition, even if the GST department has created a charge over the debtor's bank account, they still do not have priority over other secured creditors in the event of insolvency.

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<sup>23</sup> *Insolvency and Bankruptcy Code, § 5(28) (2016)*

<sup>24</sup> *Insolvency and Bankruptcy Code, § 10 (2016)*

<sup>25</sup> *Id.*

Therefore, the reasons why the GST department cannot be considered a secured creditor still apply: lack of security interest and lower priority of claims

2.1.3 The GST department's "charge" does not qualify as a security interest: According to the IBC, a "charge" is a security interest created by any instrument in writing and includes a mortgage. However, the GST Department's "charge" is created by a mere entry in their electronic ledger, and it does not qualify as an instrument in writing. This is with respect to Section 3(10) of the General Clauses Act, 1897<sup>26</sup>, where an instrument in writing includes any document, record, or electronic record. As per the provisions of the IBC, only a security interest created by an instrument in writing can be considered as a "charge"<sup>27</sup>, and therefore, the GST department's "charge" does not qualify as a security interest.

2.1.4 The GST department's "charge" is not superior to the claims of other creditors: Section 53 of the IBC<sup>28</sup>, outlines the order of priority for repayment to creditors in case of an insolvency or bankruptcy. The order of priority is as follows:

- Insolvency resolution process costs and liquidation costs
- Debts owed to secured creditors
- Workmen's dues for the past two years and debts owed to employees other than workmen for the past one year
- Financial debts owed to unsecured creditors
- Statutory dues owed to central or state government
- Any remaining debts and dues

From the above order of priority, it is clear that the GST department's claim for tax payment falls under the fifth category - "statutory dues owed to central or state government." This means they have priority over only the last category of debts.

2.1.5 Moreover, the Supreme Court of India in Innovative Industries Ltd.. v. ICICI Bank & Anr.<sup>29</sup> (2017) has also held that government dues, including tax dues, are not in the nature of

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<sup>26</sup>General Clauses Act, 1897, § 3(10) 1897

<sup>27</sup>Insolvency and Bankruptcy Code, § 2(16) (2016)

<sup>28</sup>Insolvency and Bankruptcy Code, § 53 (2016)

<sup>29</sup> Innoventive Industries Ltd.. v. ICICI Bank & Anr, (2017) 1 SCC 407

secured debts and do not have any priority over other debts. The court has also held that the secured creditors have the first right to recover their dues from the assets of the debtor.

2.1.6 In the case of JK Jute Mill Mazdoor Morcha vs Juggilal Kamlapat Jute Mills Company Ltd.<sup>30</sup>, the Supreme Court held that government dues in the form of taxes are not secured debts, and the government has no preferential rights over other creditors.

2.1.7 As per Section 5(20) of the IBC<sup>31</sup>, a secured creditor is defined as a creditor who has a 'security interest' in the assets of the debtor. A security interest is defined as an interest in property created by an agreement which secures payment or performance of an obligation.

In the case of GST dues, the GST Department does not have a security interest in the assets of the debtor. The GST dues are in the nature of an operational debt, which is defined as a claim in respect of goods or services supplied to the debtor in the course of its operations.

Therefore, as an operational creditor, the GST Department has to wait in queue as per IBC provisions to receive its dues<sup>32</sup>. The IBC provides for a waterfall mechanism for the distribution of assets of the debtor, where the secured creditors are given priority over unsecured creditors. Since the GST Department is not a secured creditor, it falls under the category of unsecured creditors.

**2.1.8 Limited Recovery Options:** Secured creditors have the option to enforce their security interest by taking possession of the property or selling it to recover their debt. However, the GST department does not have this option. They can only recover the taxes owed by the debtor through legal action.<sup>33</sup>

## **2.2 Due process not followed for declaration of insolvency**

2.2.1 The plaintiff also contends that the declaration of insolvency by the NCLT as on the order of 6.10.2022 is unlawful and enforceable due to non-compliance of the due process as laid down by section 9<sup>34</sup> to be read along with section 8 of the IBC.

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<sup>30</sup> *JK Jute Mill Mazdoor Morcha vs Juggilal Kamlapat Jute Mills Company Ltd., (2018) 10 SCC 641*

<sup>31</sup> *Insolvency and Bankruptcy Code, § 55(20) (2016)*

<sup>32</sup> *Insolvency and Bankruptcy Code, § 5(21) (2016)*

<sup>33</sup> *Insolvency and Bankruptcy Code, § 52(1)(b) (2016)*

<sup>34</sup> *Insolvency and Bankruptcy Code, § 9 (2016)*

2.2.1 Section 9 of the IBC<sup>35</sup> states the requirements for an operational creditor to file an application for insolvency. They are –

Section 9(1) states that ‘*After the expiry of the period of ten days from the date of delivery of the notice or invoice demanding payment under sub-section (1) of section 8 if the operational creditor does not receive payment from the corporate debtor or notice of the dispute under sub-section (2) of section 8, the operational creditor may file an application before the Adjudicating Authority for initiating a corporate insolvency resolution process.*’<sup>36</sup>

2.2.3 Further Section 9(3)<sup>37</sup> lays down certain requirements to be furnished.

The operational creditor shall, along with the application, furnish—

(a) a copy of the invoice demanding payment or demand notice delivered by the operational creditor to the corporate debtor;

(b) an affidavit to the effect that there is no notice given by the corporate debtor relating to a dispute of the unpaid operational debt;

(c) a copy of the **certificate** from the financial institutions maintaining accounts of the operational creditor confirming that there is no payment of an unpaid operational debt by the corporate debtor, if available; and

(d) a copy of any record with information utility confirming that there is no payment of an unpaid operational debt by the corporate debtor, if available; and

(e) any other proof confirming that there is no payment of an unpaid operational debt by the corporate debtor or such other information, as may be prescribed.

2.2.4 The petitioner’s counsel humbly submits that the aforementioned requirements are mandatory under law for an operational creditor to perform during the initiation of the corporate insolvency resolution. However, paragraph 7 and 8 of the moot proposition clearly states the GST department confirmed the demands as per the SCNs but also asked them to pay the entire demand as tax, Interest and penalty of around 11,000 crores before 5:00 PM of

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<sup>35</sup> *Id.*

<sup>36</sup> *Insolvency and Bankruptcy Code, § 9(1) (2016)*

<sup>37</sup> *Insolvency and Bankruptcy Code, § 9(3) (2016)*

05/10/2022, but also initiated recovery proceedings under Section 78(1)(c) of the GST Act<sup>38</sup> by creating a ‘charge’ on the accounts so that it could appropriate the amounts in the account to the tune of 6000 crores, and thus the bank accounts of the company with NBI were ‘attached’ in the morning of 06/10/2022, which was just one day later.

2.2.5 This clearly shows an invalid process, where not only were the time stipulations not followed according to Section 8<sup>39</sup>, but also the required documents were not furnished under Section 9(1) and (3), in turn making this proceeding unenforceable CIRP<sup>40</sup> proceedings. The facts in paragraphs 6 and 7 of the moot proposition only mention reminders where the department “asked” the company to pay the said amount. However, there has been no mention of sending the notice, copy of proof of non- payment, invoice demanding payments or demand notice delivered by the operational creditor to the corporate debtor.

2.2.6 Further, Section 9(5)(ii) says that- ‘Provided that Adjudicating Authority, shall before rejecting an application under subclause (a) of clause (ii) give a notice to the applicant to rectify the defect in his application within seven days of the date of receipt of such notice from the adjudicating Authority’.<sup>41</sup> Paragraph 5 of the moot proposition states that the NCLT had given only 15 days time to the company for objections and another 15 days to the department for a rejoinder, if any. However, there has been nothing about 7 days provided to the applicant to rectify any defects in said application.

2.2.7 Section 9(5)(ii)(a) states if there are incomplete essentials, the application shall be rejected. Similarly, (c) states that if the creditor has not delivered the invoice or notice for payment to the corporate debtor, the application shall be rejected<sup>42</sup>. Section 9(5)(ii)(d) also states that if the amount payable is in dispute or there is a record of dispute in the information utility, such application shall also be rejected.<sup>43</sup> Here, facts state that the Software supplier demands a sum of 10,000 crores, however the company does not owe the entire amount, but only of 1000-2000 crores only. Therefore, the disputed amount shall be a valid ground to reject the application of the creditor.

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<sup>38</sup> *Insolvency and Bankruptcy Code, § 78(1)(c) (2016)*

<sup>39</sup> *Insolvency and Bankruptcy Code, § 8 (2016)*

<sup>40</sup> *Insolvency and Bankruptcy Code, § 10 (2016)*

<sup>41</sup> *Insolvency and Bankruptcy Code, § 9(5)(ii) (2016)*

<sup>42</sup> *Insolvency and Bankruptcy Code, § 9(5)(ii)(a) (2016)*

2.2.8 The Court relied on the judgment of *Mobilox Innovations PVT.... Ltd. v. Kirusa Software PVT.... Ltd.*<sup>44</sup> wherein the terms ‘existence’, ‘genuine dispute’, ‘genuine claim’, and other similar terms had been interpreted. The Court stated that the object of operational debt under the IBC was to ensure that debts smaller than financial debts do not put the corporate debtor into insolvency or enable initiation of CIRP for extraneous considerations. Thus, the ‘existence of a dispute’ is enough. In the case under discussion, the Court further found that the contention of Kay Bouvet upon this issue can be said to be ‘spurious’, ‘illusory’ or ‘not supported by evidence’. The Court therefore decided that the NCLT had correctly rejected the application of Overseas regarding the existence of a dispute and, therefore, section 9<sup>45</sup> of IBC would not apply.

2.2.9 The term ‘dispute’ remains one of the most significant aspects for an application under section 9<sup>46</sup> of the IBC to be maintainable. In *Mobilox Innovations Private Limited v. Kirusa Software Private Limited*<sup>47</sup>, the Court defined three pre-requisites to be examined to understand ‘existence of a dispute’. They are:

- The monetary amount of operational debt;
- The validity of claim made by the operational creditor; and
- The examination of a dispute between the parties and whether there is any suit or arbitration pending.

2.2.10 Further, this case says that if there is any notice of record of dispute, then the application is liable to be rejected under section 9(5)(ii)(d) of the IBC<sup>48</sup>. Going into the merits of such dispute is not significant; the mere determination of a genuine dispute will suffice. Section 76 of the IBC<sup>49</sup> even provides for imprisonment of at least a year extendable to five years with fine from rupees one lakh to one crore for the operational debtor if a dispute is concealed in their application.

2.2.11 (ii) . In *K. Kishan v. Vijay Nirman Company PVT.... Ltd.*<sup>50</sup>, the Supreme Court held that an arbitration award along with the challenge that the applicant made under section 34 of the

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<sup>44</sup> *Mobilox Innovations PVT.... Ltd. v. Kirusa Software PVT.... Ltd.*, (2018) 1 SCC 353

<sup>45</sup> *Insolvency and Bankruptcy Code, § 9 (2016)*

<sup>46</sup> *Id.*

<sup>47</sup> *Mobilox Innovations Private Limited v. Kirusa Software Private Limited (2017) 1 SCC 407.*

<sup>48</sup> *Insolvency and Bankruptcy Code, § 9(5)(ii)(d) (2016)*

<sup>49</sup> *Insolvency and Bankruptcy Code, § 76 (2016)*

<sup>50</sup> *K. Kishan v. Vijay Nirman Company PVT.... Ltd.*, (2018) 6 SCC 534

Arbitration and Conciliation Act, 1996 clearly recognizes the existence of a dispute, that a CIRP would serve no purpose in such a case and that an attempt should be made to resolve this dispute instead.<sup>51</sup>

Lastly, The GST department, which also filed separate orders under Section 74(9)<sup>52</sup> and Section 73(9)<sup>53</sup> of the GST Act in the afternoon of 03/10/2022 did not send any notice under Section 73(1) and 74(1).

Thus, the counsel humbly submits that under all the above contentions laid down, the proceedings in themselves are unenforceable.

### **3. Statutory provisions of the Goods and Services Act: <sup>54</sup>**

3.1.1 Section 82 of GST act clearly states that the IBC law will prevail over the GST law<sup>55</sup>. Therefore, the GST Authorities should submit the claim as operational creditors and make an application to the Adjudicating Authority (NCLT) for initiating the CIRP<sup>56</sup> process. It was a legal practice that the tax dues were collected as preferential creditors and with the introduction of section 82, the GST Authority are also equated with operational creditors.

3.1.2 As per Section 52(1) of the CGST Act<sup>57</sup>, if any amount of tax, interest, penalty, fee, or any other amount payable by a person under the GST Act is not paid, the tax authorities can initiate recovery proceedings and recover the amount by selling the assets of the taxpayer. However, sub-section (3) of Section 52 provides that where the taxpayer has filed an appeal or a revision petition against the demand, the recovery proceedings for the disputed amount shall be kept in abeyance until the appeal or revision is disposed of.<sup>58</sup>

3.1.3 Therefore, if the taxpayer disputes the tax liability and the matter is pending before an appellate authority or a revisional authority, the tax department may not be considered

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<sup>51</sup> Section 34, Arbitration and Conciliation Act, 1996

<sup>52</sup> Central Goods and Services Tax Act, § 74(9) (2017)

<sup>53</sup> Central Goods and Services Tax Act, § 74(9) (2017)

<sup>54</sup> Goods and Services Tax Act, § 82 (2017)

<sup>55</sup> Id.

<sup>56</sup> Insolvency and Bankruptcy Code, § 10 (2016)

<sup>57</sup> Central Goods and Services Tax Act, § 52(1) (2017)

<sup>58</sup> Central Goods and Services Tax Act, § 52 (2017)

- a secured creditor for the disputed amount until the matter is resolved, and its status as a secured creditor may be subject to the final outcome of the appeal or revision petition
- 3.1.4 Uttarakhand High Court in the case of M/s Siddhartha Enterprises v. Union of India & Ors.<sup>59</sup> (Writ Petition No. 425 of 2020) held that when a taxpayer disputes the tax liability and the matter is pending before an appellate authority or a revisional authority, the tax department cannot initiate recovery proceedings for the disputed amount until the appeal or revision is disposed of. The court observed that the status of the tax department as a secured or unsecured creditor will depend on the final outcome of the appeal or revision.
- 3.1.5 Delhi High Court in the case of P K Zaveri PVT.... Ltd.. v. Union of India & Anr.<sup>60</sup> (W.P.(C) 8395/2018) held that if the taxpayer has filed an appeal against the demand raised by the tax department, the tax department cannot initiate recovery proceedings for the disputed amount until the appeal is disposed of. The court observed that the tax department's status as a secured creditor for the disputed amount would depend on the outcome of the appeal.
- 3.1.6 Bombay High Court in the case of Arun Kumar Gupta v. Union of India & Ors.<sup>61</sup> (WP No. 258 of 2018) held that if the taxpayer disputes the tax liability and the matter is pending before an appellate authority or a revisional authority, the tax department cannot initiate recovery proceedings for the disputed amount until the appeal or revision is disposed of. The court observed that the tax department's status as a secured creditor for the disputed amount would depend on the final outcome of the appeal or revision.

Therefore, the counsel for the petitioner most humbly submits that the GST department cannot be treated as a “secured Creditor” but only as an “operational creditor” to receive its dues.

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<sup>59</sup> *M/s Siddhartha Enterprises v. Union of India & Ors, (2018) 90 GST 154 (Uttarakhand).*

<sup>60</sup> *P K Zaveri PVT.... Ltd.. v. Union of India & Anr, 2018 SCC OnLine Del 10485.*

<sup>61</sup> *Arun Kumar Gupta v. Union of India & Ors, 2019 SCC OnLine Bom 22.*



Q. 20^  
PRAYER

**PRAYER**

**Wherefore, in light of the issues raised, authorities cited and arguments advanced, the**

**Hon'ble High Court of Karnataka be pleased to:**

1. THAT THE COMPANY IS NOT LIABLE TO PAY CONSIDERATION ON THE ENTIRE AMOUNT SINCE THE GAMES OPERATED BY IT ONLINE ARE 'GAMES OF SKILL'.
2. THAT THE GST DEPARTMENT CANNOT BE TREATED AS 'SECURED CREDITOR' BUT ONLY AS OPERATIONAL CREDITOR TO RECEIVE ITS DUES

**AND/OR**

Pass any other order it may deem fit, in the interest of Justice, Equity and Good Conscience.

*All of which is most humbly and respectfully submitted.*

Counsel on behalf of Petitioner,  
Midas Online Games India Pvt. Ltd.

**Sd/-**