

Karnataka High Court Quashes ₹21,000-Cr GST Notice Issued to Gameskraft: A Landmark Victory for the Online Gaming Industry
written by King Stubb & Kasiva | June 2, 2023



Introduction

In a landmark case of [*Gameskraft Technologies Private Limited Vs Directorate General of Goods Services Tax Intelligence*][1], the Karnataka High Court quashed a staggering ₹21,000-crore Goods and Services Tax (GST) notice issued to Gameskraft, an online gaming platform. This ruling has sent ripples of relief throughout the online gaming industry, signaling a pivotal moment in the legal landscape surrounding taxation in the rapidly growing sector. The judgment brings much-needed clarity and protection to online gaming companies, safeguarding their interests and fostering a favourable environment for their continued growth and development.

Background

The Indian online gaming industry has experienced exponential growth in recent years, fuelled by technological advancements, increased smartphone penetration, and a growing user base. However, regulatory challenges have persistently loomed over the sector, often creating uncertainty and ambiguity regarding taxation and compliance obligations. Gameskraft, a leading online gaming platform, faced one such challenge when it received a staggering ₹21,000-crore GST notice from the authorities, casting a shadow of uncertainty over its operations and financial stability.

This legal battle pivoted on the fundamental distinction between skill and chance, as well as the interpretation of rummy as a skill-based or chance-based game. The proceedings centred on the crucial determination of whether the online games hosted on the platform should be classified as games of skill or games of chance, with the latter attracting a higher GST rate of 28 percent, while the former qualifies for a reduced rate of 18 percent.

However, in a resolute and emphatic ruling, Justice S.R. Krishna Kumar decreed the notice to be "illegal, arbitrary, and devoid of jurisdiction." This unequivocal pronouncement underscores the court's unwavering commitment to upholding the principles of fairness, justice, and sound legal reasoning.

Contentions Raised by the Parties

GTPL, the online gaming platform, has been accused by authorities of submitting fake or backdated invoices, which were discovered during a comprehensive forensic examination of the documents. Additionally, it was alleged that GTPL enticed customers to place bets, as once the money was added to their wallets, there was no option for its return. Further, the GST department sought to dispute this viewpoint by asserting its classification of rummy as a game of chance, thereby subjecting it to a higher tax rate. Therefore, the GST department submitted that rummy should be deemed a game of chance, consequently warranting taxation at the higher rate of 28 percent. In response, GTPL presented its argument, asserting that its offerings should be categorized as skill-based gaming activities. Gameskraft persuasively cited precedents that had unequivocally established rummy as a skill-based game and such activities, according to the platform, are subject to an 18 percent GST rate solely on the platform fee. GTPL further explained that it deducted a portion of the offerings from the entry fees paid by players, ranging from 5 to 15 percent of the contest entry amount. The remaining funds were then directed toward the players' prize pool.

Further, Gameskraft firmly contended that the majority of their offerings revolved around the game of rummy, which has consistently been acknowledged as a game predominantly reliant on skill.

Through these contentions, GTPL sought to establish the skill-based nature of its gaming activities, thereby advocating for a lower GST rate applicable to such games. By linking the deductions made from entry fees to the prize pool, GTPL aimed to demonstrate that it operated within the framework of skill-based gaming, fostering an environment where players could utilize their expertise and abilities to compete for prizes.

The Hon'ble Karnataka High Court's Observations

Justice S.R. Krishna Kumar, the sole presiding judge, unequivocally denounced the notice as "illegal, arbitrary, and lacking jurisdiction."

The court's judgment emphasized the distinction between "games of skill" and "games of chance," recognizing that online gaming platforms primarily offer skill-based games, which are not subject to GST under the current tax framework. The ruling strengthens the legal standing of online gaming platforms, affording them protection against exorbitant and unjustified tax demands, thereby fostering an environment conducive to their sustained growth and economic contribution.

Significance and Implications

The Karnataka High Court's ruling carries significant implications for the entire online gaming industry in India. It sets a precedent that clarifies the tax obligations of online gaming platforms, distinguishing them from other forms of gambling or chance-based activities. By recognizing the predominant skill-based nature of online gaming, the judgment paves the way for a more nuanced and tailored regulatory approach in the future. This decision will provide much-needed reassurance to the industry, encouraging innovation and investment while ensuring compliance with applicable tax laws.

Boosting Investor Confidence

The quashing of the huge ₹21,000-crore GST notice against Gameskraft serves as a crucial catalyst in boosting investor confidence within the online gaming sector. The ruling signifies that the judiciary is committed to safeguarding the rights and interests of businesses operating in this domain. With the cloud of uncertainty lifted, potential investors can now consider entering the market with greater confidence, leading to increased funding opportunities for existing companies and paving the way for new entrants to explore the Indian gaming landscape.

Future Regulatory Framework

The Karnataka High Court's judgment brings forth the need for a well-defined and comprehensive regulatory framework specifically tailored to the online gaming industry. By acknowledging the skill-based nature of online games, policymakers have an opportunity to create a balanced and transparent system that accounts for the unique characteristics of the sector. The ruling provides the impetus for proactive discussions among industry stakeholders, policymakers, and legal experts to collaborate on shaping regulations that promote responsible gaming, consumer protection, and sustainable growth within the online gaming ecosystem.

Implications and Industry Outlook

The quashing of the massive ₹21,000 crore GST notice against Gameskraft carries significant implications for the broader online gaming industry in India. It serves as a crucial milestone in establishing a clear and definitive legal framework for taxation purposes, reinforcing the distinction between skill-based and chance-based games. This ruling bolsters investor confidence, encouraging potential stakeholders to consider the industry's growth potential and prompting further innovation and investment in the sector. Moreover, the decision sets the stage for constructive discussions between industry stakeholders, policymakers, and legal experts, leading to comprehensive and tailored regulations that foster responsible gaming practices and protect consumer interests.

Recognition of Rummy as a Skill-based Game

Crucially, the court acknowledged that rummy is primarily a game of skill rather than chance. It emphasized that even if players wagered on the game, it would not be considered gambling but rather a skill-based activity. This recognition applied to both online and offline modes of the game. The court's decision aligns with previous legal interpretations and highlights the importance of understanding the underlying skills required in rummy gameplay. By recognizing rummy as a skill-based game, the court protected Gameskraft from unwarranted taxation and established a precedent for similar cases in the future.

Conclusion

The Karnataka High Court's decision to quash the ₹21,000-crore GST notice issued to Gameskraft has ushered in a new era of legal clarity and protection for the online gaming industry in India. The ruling recognizes the skill-based nature of online gaming. This highlights the significance of upholding a legal position that has been well-established for over six decades: skill-based games cannot be equated with betting and gambling, even if played for stakes. This reaffirmation of legal principles maintains the integrity of the gaming industry and protects its operators from unwarranted tax burdens, ensuring a fair and equitable business environment.

FAQs

Are skill-based games and chance-based games treated differently for tax purposes?

Yes, skill-based games and chance-based games are treated differently for tax purposes. Skill-based games are typically subject to a lower tax rate compared to chance-based games. This distinction recognizes the level of skill and expertise required to succeed in skill-based games, distinguishing them from games primarily reliant on chance or luck.

What happens if a gaming platform is accused of submitting fake or backdated invoices?

If a gaming platform is accused of submitting fake or backdated invoices, it may face legal consequences and potential penalties. The authorities may conduct a thorough investigation, including forensic examination of the documents, to verify the authenticity of the invoices. If found guilty, the platform could face financial penalties, legal action, or regulatory sanctions depending on the severity of the offense.

Can gaming platforms categorize their offerings as skill-based to benefit from a lower tax rate?

Gaming platforms can argue that their offerings qualify as skill-based games to benefit from a lower tax rate. However, this classification typically requires substantiation and evidence to demonstrate the extent of skill involved in the games offered. The platform may need to provide supporting documentation and legal arguments to establish that the majority of the games provided fall under the skill-based category, which can help reduce the tax liability compared to chance-based games.

[1] W.P. No. 19570/2022

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