Supreme Court back curbs on online gaming

Mains: *GS-III – Economy*

Why in News?

Recently, the SC has upheld the constitutional validity of the Centre's retrospective 28% GST levy on online gaming companies and affirmed the validity of State laws prohibiting real-money gaming platforms.

What did the Court have to decide?

State laws prohibiting online betting and wagering

- **Background –** In 2021, Tamil Nadu and Karnataka enacted legislation criminalising betting on games played in cyberspace and prescribing penalties, including imprisonment.
- **High Court Rulings –** After the Madras and Karnataka High Courts struck down these enactments.
- **Supreme Court Appeal –** The respective State governments approached the Supreme Court,
    - Betting and gambling fall under their legislative powers (Entry 34, List II, Seventh Schedule).
- They further contended that the restrictions were necessary to address addiction and other social harms associated with online betting.

Applicability of the GST regime to online gaming involving money stakes

- **High Court Rulings –** The appeals arose from decisions of the Bombay and Karnataka High Courts, which held that
    - Online gaming transactions did not constitute actionable claims under the GST law and
    - Consequently, quashed tax proceedings initiated against gaming companies.
- **Supreme Court Appeal** - The **Union Government** challenged these rulings, arguing that:
    - Online gaming with money stakes should be treated as a taxable supply.
    - GST applies to the full value of stakes, not just platform fees.

Why was the GST levy upheld?

- **Background –** The dispute over the GST liability of online gaming platforms stemmed from amendments approved by the GST Council in August 2023.

- **GST Council's Clarification –** The Council clarified that all online games involving bets or wagers must pay GST.
- Applies irrespective of whether they were predominantly games of skill or games of chance, would attract GST at 28%.
- It is charged on the entire amount staked by players, not just the platform commission.
- **Tax Demands by DGGI –** The Directorate General of GST Intelligence (DGGI) issued a series of tax demand notices to gaming companies.
- The notices sought to levy GST to both
    - Post-amendment period (after Oct 2023).
    - Pre-amendment period, treating the clarification as retrospective, resulting in tax demands running into several lakh crore rupees.
- **Gaming Companies Arguments –** GST could be levied only on the consideration retained by the platform and not on the entire value of bets or contest entry fees contributed by users.
    - Taxing the full-face value of stakes was commercially unviable
    - Failed to account for the long-recognised distinction between games of skill and games of chance.
- **Supreme Court's Reasoning –** The Court held that online gaming platforms involving money stakes were distinct from conventional skill-based competitions.
- **Nature of online gaming –** Platforms encourage repeated play with discounts and bonuses, making them akin to wagering systems.
- **Distinction Irrelevant –** The Court held that, for GST purposes, the distinction between games of skill and games of chance becomes irrelevant once money is staked on an uncertain outcome.
- **Legal basis** – The Central Goods and Services Tax Act, 2017 (CGST Act), already includes actionable claims relating to lottery, betting, and gambling within the tax net.
- The Court concluded that Parliament was competent to levy GST on online gaming involving money stakes.
- **Amendments of 2023 –** Industry argued that the 2023 changes created a new tax.
- The court rejected this, holding that the amendments were only clarificatory and standardising.
- This means they can operate retrospectively, covering revenues even before October 2023.

Why did the Court uphold State curbs on real-money gaming?

- **Betting & Gambling as Res Extra Commercium –** The Court observed that "betting" and "gambling" are res extra commercium (activities outside legitimate commerce).
- Therefore, they fall outside the protection ordinarily available to trade and business activities.
- **Games of Skill vs Money Stakes –** It held that while games of skill may be constitutionally protected, the introduction of money stakes imparts the character of wagering to the activity, bringing it within the States' legislative competence.
- **Fantasy Sports Argument Rejected –** The Bench was not persuaded by the contention that fantasy sports are predominantly skill-based.
- It noted that even sophisticated predictive models are unable to forecast sporting

outcomes with certainty.

Fantasy sports *- These are digital games where you act as the manager of a virtual team composed of real-life professional athletes.*

Your team competes against others based on the actual, statistical performance of those players in real-world matches, earning, or losing points depending on how well they play.

- **Smartphones as Virtual Gambling Houses –** The Court observed that the widespread availability of smartphones & digital payment gateways had effectively turned every mobile phone into a virtual "gambling house".
- **States' Legislative Powers –** States can impose restrictions under:
  - Entry 34, List II - Betting and Gambling.
  - Entry 1, List II - Public order.
- This gives States constitutional authority to ban or regulate real-money gaming.

What are the implications?

- **Impact of the 2025 Online Gaming Act –** The Promotion and Regulation of Online Gaming Act, 2025 (2025 Act) which prohibited all forms of online real-money gaming,
- The government cited national security concerns, including the alleged use of digital wallets and cryptocurrencies for money laundering and illicit fund transfers.
- **Exceptions** – However, it carved out exceptions for e-sports, educational games, and social gaming.
- The industry had effectively come to a standstill following the enactment of the 2025 law, which could make recovery of the tax demands difficult.
- **GST Recovery Challenges –** The Supreme Court upheld 28% GST on full stakes, but
- Many companies have either shifted their operations outside India or pivoted to sectors such as social gaming and fintech.
- The GST demands are several times higher than the revenues these companies have ever earned and are simply beyond their ability to pay.
- The likely outcome is insolvency proceedings across the sector.
- **Legislative Competence Debate –** The Court reaffirmed that betting and gambling are State subjects under Entry 34, List II.
- This raises questions about Parliament's authority to enact the 2025 Act under Entry 52, Union List (regulation of industries in public interest).
- Future litigation may test whether the Union can justify its competence to regulate online gaming.

Reference

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