

## VILE PARLE (EAST) CPE STUDY CIRCLE

Welcome all the members

**Subject** : Important judicial pronouncements explaining basic concepts and fundamentals of service tax

**Date** : 20<sup>th</sup> December, 2009 (Sunday)

**Venue** : PTVA's Institute of Management, M.L. Dahanukar College, Vile Parle (East), Mumbai – 400 057.

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## Scope of Presentation

- Focus is on judicial pronouncements explaining:
  - Basic concepts
  - Basic principles
- Specific service related judicial pronouncements are not covered except for :
  - Information Technology Services
  - Renting of immovable property
  - Construction services
- Judicial pronouncements on procedural aspects are not covered.

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## Jurisprudence under Other Legislation - Relevance

- Service tax is an evolving legislation .
- In absence of elaborate jurisprudence history, reliance on jurisprudence evolved under:
  - Excise law
    - Both are indirect tax
    - Both are value added tax
    - Both are administered by excise authorities
    - Service tax law drafted on the lines of excise law
    - Input tax credit mechanism (cenvat) is common
    - Some provisions of excise are applicable to service tax.
  - Sales tax / VAT law
    - Both are indirect tax
    - Both are value added tax
    - Generally both are mutually exclusive levy
  - Income tax law
    - Both are central government levy
    - Both are fiscal statutes
    - Rights and obligations of tax payers and tax authorities are similar

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## Constitutional Validity

- Service tax is levied by central government under residuary entry 97 of list I (Union List).
- Tax can be levied under residuary entry 97 on the items not appearing in state list (List II) or concurrent list (List III).
- Constitutional challenge may arise when subject matter of service tax levy appear to fall in list II or list III.
- Advertising Club v. CBEC 2001 (131) ELT 35 (Mad.)
  - It is tax on the advertising services and not on advertisement.
  - Constitutional validity upheld.
- All India Federation of Tax Practitioners v. UOI (2007)(7) STR 625 (SC) / Chartered Accountants Assosiation v. UOI (2001) 115 Taxman 543 (Guj HC)
  - It is tax on professional services not on profession.
  - It does not tantamount to discrimination.
  - Constitutional validity upheld.

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## Constitutional Validity

- **Dr. V Shanmughavel v. CCE (2001) 131 ELT 14 (Mad. HC)**
  - It is tax on professional services not on profession.
  - Reasonable classification is not discrimination.
  - Constitutional validity upheld.
- **Kerala Colour Lab Association v. UOI (2003) 156 ELT 17**
  - It is not tax on material but on photography services
  - Constitutional validity upheld.
- **Tamil Nadu Kalyana Mandapam Association v. UOI (2004) 167 ELT (SC)**
  - It is not tax on immovable property.
  - It is tax on services provided by mandap keeper.
  - Constitutional validity upheld.
- **Home Solutions Retail India Ltd. v. UOI [2009 TIOL 196 HC- DEL].**
  - It was pleaded that service tax on renting amounts to taxation on property.
  - Court did not opine on constitutional validity.

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## Person Liable to Pay / Bear Service Tax

- **Allahabad High Court in the case of Thermal Contractors Association v. Director, Rajya Vidyut Utpadan Nigam Ltd. [2006] 5 STT 329 has confirmed the following basic propositions:**
  - Service tax is service provider's obligation.
  - If contract permits, service tax can be passed on to the customer / client by separately charging it in bill or invoice.
  - If contract does not permit, service tax is to be borne by service provider.
- **Implications:**
  - Service provider is liable to pay tax whether or not recovered from the customer.
  - where service provider doesn't charge service tax separately, bill amount is supposed to be inclusive of service tax.
  - service tax department has recourse to service provider only for recovering service tax.
  - service tax department does not have recourse to service recipient for tax recovery (exception of Rule 2(1)(d) and Section 66A of the Act).

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### **Self Service – Not Taxable**

- **Existence of two parties is a pre requisite for providing services.**
- **Precot Mills Ltd. V. CCE 2006 (2) STR 495 (Tri. – BANG) / Indian Oil Corporation Ltd. V. CCE Patna 2007 (8) STR 527 (Tri. Kolkatta)**
  - **Services rendered by one unit of legal entity to its other unit.**
  - **All units are part of same corporate legal entity.**
  - **No client principal relationship exists.**
  - **It is a self service and hence no service tax is leviable.**
- **Magus Constructions Pvt. Ltd. v. UOI 2008 (11) STR 225 (Gauhati HC).**
  - **Developer constructs the property on his own account.**
  - **Allottee is a purchaser and not a service recipient.**
  - **In absence of service recipient, no service tax is leviable.**
- **In a stay petition in case of Pala Marketing Co-Operative Society Ltd [2007-TIOL-1124-CESTAT-Banglore], it was held that:**
  - **Where two entities are carrying on business jointly.**
  - **When they are sharing Profit & Loss.**
  - **They Can not be said to have rendered service to each other.**

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### **Self Service – Not Taxable**

- **Services rendered to a joint venture by its member amounts to service to the self. It is not liable to service tax:**
  - **CCE Vs Sundaram Finance Ltd 2007 (7) STR 55 (Tri-Chennai).**
  - **Maini Precision Private Limited 2006 (1) STR 230.**
- **Mutuality concept upheld by Kolkatta High Court in:**
  - **Dalhousie Institute – 180 ELT 18**
  - **Saturday Club Ltd. – 180 ELT 457**
- **Mutuality concept diluted after 01.05.2006 on insertion of explanation to section 65 wherein services rendered by unincorporated association / body of persons to its member is deemed to be services.**

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## Taxable Event and Rate of Tax

- **Taxable event :**
  - Provision / rendition of the taxable services.
  - Advance receipt for service to be provided.
- **Service tax liability accrues on happening of taxable event.**
- **Schott Glass India Pvt. Ltd. V. CCE (2007) 8 STR 407 (Tri. - AMD) / CCE Bhopal v. Siemens Ltd. 2006 – TIOL – 290 – CESTAT - Del**
  - Services provided prior to the date of service becoming taxable is not liable to tax.
  - Date of invoicing is irrelevant.
  - Date of realization is irrelevant.
- **Art Leasing Ltd. V. CCE (2007) 8 STR 162 (Tri. – BANG)**
  - In case of hire purchase, taxable event occurs upon entering into hire purchase contract.
  - Service tax rate on contract execution date is relevant.
  - Change in tax rate during contract period is of no consequence.
- **Reliance Industries Ltd. V. CCE (2008) 15 STT 28 (Tri. - AMD)**
  - Applicable tax rate is a rate in force on provision of services
  - Billing date, due date or realization date is irrelevant.

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## Introduction of New Service

- **Service brought to tax as “New Services” implies that there was no legislative intent to tax it earlier.**
- **Works contract and trunk projects are taxable only after enactment of Finance Act, 2007 levying tax on “Works Contract”:**
  - Diebold Systems (P) Ltd v. CST(2008) 9 STR 546 (Tri – Chennai)
  - Air Liquid Engineering India Pvt. Ltd. V. CCE (2008) 9 STR 486 (Tri – Bang)
  - Sepco Electric Power Construction Corp. v. CCE (2007) 7 STR 229 (Tri – Del)
  - L&T Ltd. V. CCE (2007) 7 STR 224 (Tri – Ahm)
- **Above stand is not tenable for services which were specifically covered under old category and reclassified under new category.**
  - Credit card services earlier taxable under “banking and financial services” category reclassified under “credit card services” category.
  - Installation of ATM machines earlier taxable under “erection, installation and commissioning services” category reclassified under the category of “ATM operations services.”

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## **Classification of Services – Tax Implications**

- **Tax incidence may vary with classification on account of:**
  - **Effective date of tax liability**
  - **Eligibility for abatement**
  - **Eligibility for composition scheme**
  - **Applicability of exemption notifications**
  - **Implications under export of Service Rules, 2005**
  - **Eligibility to cenvat**
  - **Implications under “reverse charge mechanism”**
  
- **Dr. Lal Path Lab Pvt. Ltd. V. CCE 2007 (8) STR 337 (P&H High Court)**
  - **Service kept specifically out of levy under one category can not be subjected to tax under another category.**
  - **Backdoor taxing is not permissible.**

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## **Interpretation of Term “In Relation to”**

- **Taxable services is defined U/s 65(105) of the Act.**
- **Definition of most of the taxable services uses this phrase.**
- **In the case of Doypack Systems Pvt. Ltd. V. UOI (1988) 36 ELT 201 (SC), Supreme Court held that:**
  - **Use of this expression widens the scope of taxability.**
  - **It embraces the direct, indirect and even remotely connected services.**
- **Following examples can be cited:**
  - **Storage, transport, packing, unpacking in course of cargo handling will be taxable under cargo handling services.**
  - **Ironing after dry cleaning is taxable as dry cleaning services.**
- **Same phrase is used in the definition of “input” and “Input Services” under cenvat credit Rules, 2004.**
- **Term “in relation to” can be interpreted in a manner beneficial to the assessee for Cenvat Credit Mechanism.**

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## **Aspect Theory**

- **Escotel Mobile Communication Ltd. V. UOI (2003) TIOL 132 HC - Kerala - ST**
  - Sale of sim card is exigible to sales tax.
  - Activation charges is in nature of deferred payment for consideration of original sale.
  - It amounts to part of the sale and is liable sales tax.
  - Both sale of sim card and activation are services.
  - It is also liable to service tax.
- **State of Uttar Pradesh v. UOI 130 STC 1 (Supreme Court)**
  - Rentals charged to subscribers for telephone instruments.
  - It is transfer of right to use movable property.
  - It is liable to lease tax under the state law.
  - Such rentals were liable to service tax was irrelevant.
- **Inferences of above judicial pronouncements:**
  - Transaction can have varying aspects.
  - Legislation are competent to levy tax on different aspects of same transactions.
  - Levies were under different statutes.
  - Plea against double taxation rejected .

## **Aspect Theory**

- **Overlapping jurisdiction of state (VAT) and Service Tax (central) is inflicting undue hardship and many cases double taxation.**
- **Aspect theory upheld in Escotel and State of Uttar Pradesh was reviewed by constitution bench of Supreme court in BSNL case.**
- **Supreme Court in Bharat Sanchar Nigam Ltd. Vs Union of India (2006) 2 STR 161 laid down following propositions:**
  - VAT and service tax are mutually exclusive.
  - Aspect theory does not allow to levy VAT on service element and service tax on material element.
  - Total value taxed under both the legislation should not exceed the transaction value.

## Mutual Exclusivity of Sales Tax and Service Tax

- **Overlapping jurisdiction of state (VAT) and Central (Service Tax) is inflicting undue hardship and causes double taxation.**
  - Sale of software
  - Comprehensive maintenance contract
  - Franchise Agreements
  - Right to use the goods
- **General perception transaction liable to VAT are not liable to service tax . Judiciary followed this proposition in following cases:**
  - LSG Sky Chefs (India) Pvt. Ltd. [2009 TIOL 1125 CESTAT BANG]
  - Idea Mobile Communication Ltd. [2006 (4) STR 132 Tri. – BANG]
  - ASL Motors Pvt. Ltd. [2008 TIOL 114 CESTAT – Kolkatta]
  - Thermax Ltd. [2007 TIOL 1466 CESTAT – Mumbai]
  - GERB Vibration Control Systems [2007 (7) STR 403 – Tri. BANG]
  - Adlabs [2006 (2) STR 121 Tri. – BANG]
  - Shilpa Colour Lab [2007 (5) STR 423 Tri. – BANG]

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## Mutual Exclusivity of Sales Tax and Service Tax

- **No express provision in any of the Acts providing for mutual exclusivity of VAT and service tax.**
- **Propositions laid down in above referred pronouncements can not be treated as sacrosanct.**
- **Imagic Creative Pvt. Ltd. V. CCT (2008) 9 STR 337 (SC)**
  - Imagic created concept and designed advertising material.
  - Printed advertising material was sold to customer.
  - Separate break up for service element and material was given.
  - Sales tax charged on material and service tax charged on concept and design charges.
  - Sales tax authority levied sales tax on entire contract value including the design and concept charges as same went into the creation of product which was sold.
  - Supreme Court held that it is composite contract for sales and services. It is not an indivisible contract.
  - Sales tax, therefore, would not be payable on entire contract but only on material component.

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## Software - Is it Goods or Service?

- VAT laws treat software as goods.
  - State governments levy Sales tax / VAT on sale of software.
  - Custom Act treats software as goods and 0% duty is prescribed on all software.
  - Excise Laws levies duty on canned / packaged software while exemption is given to customized software.
  - Supreme Court in Tata Consultancy Service case [137:STC:620] observed that tangible and intangible property capable of following is a goods:
    - Abstraction
    - Consumption and use
    - Transmission
    - Transfer
    - Delivery
    - Storage
    - Possession
- Software has all above attributes and hence goods.

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## Software - Is it Goods or Service?

- Further observations of Supreme Court in TCS case:
  - Intellectual property once put on media becomes goods liable to sales tax.
  - No difference between software and music CD / cassette.
  - Buyer pays for IP and not for CD or Disk.
- Verdict of Supreme Court in TCS case :
  - Canned / packaged / off-the-shelf software are goods.
  - No opinion expressed for customized software.
- TRU circular no. D.O. F. No.334/1/2008-TRU dated 29.02.2008 at para no. 4.1.3 indicates that packaged / canned software is goods exegible to excise.
- Madras High Court in case of Infosys Technologies Ltd. (2008 – TIOL – 509 – HC – MAD – CT) held customized software as goods
- Law seems to be fairly settled that software is goods.
- “Information Technology Services” is taxable w.e.f. 16.05.2008.
- Both service tax and VAT authorities claim tax on software.
- Following proposition may be applied to customized software:
  - Copy right resting with developer – “goods” liable to VAT.
  - Copy right resting with customer – “Service” liable to service tax.

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## Cenvat – Basic Concepts

- **CCE V/s. Dai Ichi Karkaria Ltd – 112 ELT 353 (SC)**
  - Cenvat credit validly availed cannot be reversed by tax authorities.
  - Benefit of credit is available without any limitation.
  - Scheme is infeasible.
- **Eicher Motors Ltd Vs UOI 106 ELT 3**
  - Cenvat credit balance is like tax deposit with the government available for future tax liability.
- **Vijay Anandan Road Lines Ltd. Vs CCE 10 STT 95 (Bang. CESTAT).**
  - Cenvat credit balance can be carried forward eternally.
- **CCE Vs Ram Sarup Electricals Ltd 2007 TIOL 640 (Allahabad HC)**
  - Cenvat is set off claim.
  - Cenvat is not a refund claim.
  - Limitation period applies to refund claim and not to set off.
  - Ratio laid down in Dai Ichi Karkaria's Case (SC) relied upon.
  - No time limit for assessee to avail MODVAT.

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## Cenvat – Basic Concepts

- **CCE V/s Engine Values Ltd. [1990] 48 ELT 287-TRI**  
**CIT V/s Vegetable Products Ltd. Vs 88 ITR 192 (SC)**
  - Being a beneficial Rules, CCR should be interpreted liberally.
  - If two interpretation are possible, interpretation favorable to assessee should be preferred.
- **Maschmeijer Aeromatics (I) Ltd Vs CCE 46 ELT 395 (Mad CEGAT)**  
**Aluminum Industries Ltd Vs CCE 1993 (65) ELT 460 (Mad. CEGAT)**
  - Assessee can not be deprived of benefits of Cenvat Scheme for some procedural lapse or defects.
  - Benefit can be denied only in case of malafide intention.
  - Procedural lapse to be ignored where there is substantive compliance.

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## Cenvat Credit – Meaning of Input Services

- **Coca Cola India Pvt. Ltd. Vs CCE, Pune-III [2009-TIOL-449-HC-Mum-ST]**
- Appellant is manufacturer of concentrate.
  - Appellant incurred expenditure on market research, advertising and sales promotion of aerated beverages.
  - Aerated beverages is final product of bottlers.
  - Appellant claimed input credit of above-referred services.
  - Appellant discharged its excise liability on concentrate from above referred credit availment.
  - Department's contention :
    - Aerated beverage is not a final product of appellant.
    - Input services are not used in or in relation to manufacture of concentrate which is final product of appellant.
  - Appellant's contention :
    - Advertisement on the brand name of soft drink has direct relationship with the manufacture of concentrate.

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## Cenvat Credit – Meaning of Input Services

- Advertisement of aerated water enhances marketability of concentrate.
- Advertisement and brand promotion expenses form part of sales price of concentrate on which excise duty is paid by the appellant.
- Service tax is a value added tax system.
- In order to effective and efficient tax system, all input credits should be allowed.
- Service tax is consumption tax.
- It is to be born by ultimate customer and not by manufacturer or service provider.
- "Business" is a wider term than the "manufacture".
- Business is integrated and continues activity.
- Term "Business" should not be confined / restricted to manufacture of product only.
- Term "Activities in relation to business" covers all activities related to functioning of business.

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## Cenvat Credit – Meaning of Input Services

- Use of term “include” and “such as” makes definition illustrative and not “exhaustive”.
- Word “activities related to business” is wide enough to cover above referred services in the second and inclusive limb of “input service” as defined in Rule 2(l) of CCR, 2004.
- Honorable Bombay High Court accepted above referred contentions of the appellant and allowed the Cenvat credit.
- This judgment has far reaching implications:
  - Input tax credit can be claimed for all items having direct or indirect nexus with business of appellant.
  - Broader concept of relatability of input to the business and not to manufacture.
  - If the cost incurred is included in the final value of the product or services on which tax or duties are paid, Cenvat credit of same can be claimed.
  - Controversy of allowability of Cenvat in respect of post production activities will be diluted.

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## Cenvat Credit – Allowability of Specific Input Services

Sr. No.	Input Service	Allowability Upheld
1)	Mobile phone	Indian Rayon Industries [2006-TIOL-1152-CESTAT-MUM] Circular No.97/8/2007 dt. 23.08.07.
2)	Landline phones in factory	CCE Vs Beekay Engg. & Casting Ltd. 2009-TIOL-1376-CESTAT-Del
3)	Residential telephone of Director / Employees / Partners	ITC Ltd. Vs CCE, Salem 2009-TIOL-439-CESTAT-MAD.
4)	CHA service for export of goods	CCE Vs Adani Pharma Chem Pvt. Ltd. 2008-12-STR-593 (Ahm. Tri.)
5)	Health insurance of Staff / Director	GTC Industries 2008-TIOL-1634-CESTAT-MUM (LB)

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### Cenvat Credit – Allowability of Specific Input Services

Sr. No.	Input Service	Allowability Upheld
6)	Insurance of Plant & Machinery	Finolex Cables Ltd Vs CCE 2009-14-STR-303 (Mum-Tri.)
7)	Security services	C.J. Galetine Products Vs CCE 7 STR 558 (Del-Tri.)
8)	Construction of residential colonies	Victor Gaskets Ltd. 2008-10-STR-369 (Mum.-Tri.)
9)	Staff colonies maintenance	Manikgarh Cement Vs CCE 2008 (9)-STR-554 (Bom.Tri.)
10)	Canteen Services	CCE Vs GTC Industries Ltd. 2008 (12) -STR-468 (Mum.Tri.LB)
11)	Staff Medical Insurance	Millipore India Ltd. Vs CCE (2009) 13 STR 616 (Bangalore - Tri.)
12)	Staff Bus Transportation	CCE Vs Cable Corpn. Of India Ltd. 2008 (12) STR 468 (Bom.-Tri.-LB)

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### Cenvat Credit – Allowability of Specific Input Services

Sr. No.	Input Service	Allowability Upheld
13)	Man Power Supply	Sanghi Industries Ltd Vs CCE 2009 (13) STR 167 (Ahm. Tri.)
14)	Commission of Sales	Metro Shoes Pvt. Ltd. VS CCE 2007 (8) STR 502 (Bom.Tri.)
15)	Advertisement	Kamdhenu Ispat Ltd. Vs CCE 2007 (8) STR 188 (Del. Tri.)
16)	Rent-a-cab Services	C.J. Geletine Products Vs CCE 2007 (7) STR 558 (Del. Tri.)
17)	Loan processing fees	Alluminium Powder Co. Ltd. Vs CCE 2007 (8) STR 353 (Mad. Tri.)
18)	Merger / Takeover expenses	Aditya Birla Nuvo Ltd Vs CCE 2009 (14) STR 304 (Ahm. Tri.)
19)	General Insurance towards fire, machinery breakdown, cash handling, group gratuity, group accident etc.	CCE, Raipur Vs Beekay Engg. & Castings Ltd. 2009-TIOL-1376-CESTAT-Del.)

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## **Simultaneous Claim of Abatement and Cenvat**

- Service provider is not entitled to claim abatement when he has claimed cenvat.
- Simultaneous claim of abatement and cenvat may lead to loss of abatement benefit.
- Department rejected abatement claim where nominal cenvat credit was claimed through inadvertence.
- Now following judicial precedents are available for service providers to defend abatement claim.
  - B.G. Shirke Construction Technology Pvt. Ltd. V. CCE, Pune – III [2008 TIOL 1798 CESTAT Mum]
  - M/s. Pujan Builders v. CCE, Vadodara – II [2009 TIOL 57 CESTAT AHM]
- Above referred stay petitions were decided in favour of service provider on following ground:
  - Reversal of credit tantamount to non availment of cenvat.
  - Such reversal of cenvat credit availed would entitle service provider to avail abatement.

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## **Export of Services – Place of Usage**

- **ABS India Ltd. Vs CST [2008-TIOL-2102-CESTAT, Bangalore]**  
**Blue Star Vs CCE [2008-TIOL-716-CESTAT, Bangalore]**
  - So long as recipient of service is located outside India, it can not be said tat service is delivered in India or used in India.
  - Relevant factor for determining place of “usage” is location of service receiver and not place of performance.
  - Place of usage is a place where benefit of service accrued.
- CBEC Circular No.111/2009-ST dated 24.02.2009 accepted the ratio laid down in above referred decisions.
- In recent stay petition in case of Microsoft Corp (I) Pvt. Ltd. Vs CCE [2009-TIOL-1325-CESTAT-Delhi], Tribunal held that:
  - If ultimate consumer of services are located in India, then services are consumed in India.
  - Service tax is destination based consumption tax.
  - If service is consumed in India, export benefit can not be granted.

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## Export of Services – Place of Usage

- Decisions in case of ABS India Ltd and Blue Star are contrary to law laid down by Supreme Court in case of All India Federation of Tax Practitioners.
- CBEC Circular No. 111/2009-ST dated 24.02.2009 runs contrary to above-referred decision of Supreme Court.
- No case made out to show that irreparable injury or undue hardship will be cause to petitioner if full waiver is not granted.
- Pre-deposit of Rs.70 Crore was ordered.
- Microsoft order an interim order for limited purpose of pre-deposit.
- Such orders can not be treated as having binding precedence.
  - Empire Industries Case 20 ELT 179 (SC).
- View taken by the tribunal in the case of ABS India Ltd and Blue Star seems to be better view.
- ABS India Ltd and Blue Star cases will have better precedence value then that of Microsoft.
- Honorable Delhi High Court rejected Microsoft's SLP.

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## Import of Services

- Services received from Non-Resident during period July 1994 to 16.08.2002
  - In absence of express authorization, service recipient is not liable to service tax.
  - This was upheld in:
    - ❖ Cadbury India Ltd Vs CCE 188 ELT 166 (Bom)
    - ❖ Bajaj Auto Ltd Vs CCE 178 ELT 474 (Bom)
- Services provided by Non-Resident in India during 16.08.2002 to 31.12.2004
  - Rule 2(1)(d)(iv) inserted requiring service recipient to pay tax under reverse charge mechanism.
  - Notification No. 36/2004-ST notifying above Rule was notified on 31.12.2004.
  - In absence of enabling notification, Rule 2(1)(d)(iv) was invalid and non-operative till 31.12.2004.
  - No tax liability on service recipient under this rule till 31.12.2004.

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## Import of Services

- This contention upheld in:
  - ❖ Aditya Cement Vs CCE [2007-TIOL-236-CESTAT-Del].
  - ❖ Ispat Industries Ltd. VS CCE [9 STT 291 Mum-CESTAT].
- Services performed and consumed outside India during 16.06.2005 to 17.04.2006:
  - Under explanation to 65(105) such service made liable to tax.
  - It levies tax on services rendered out of Indian territories.
  - Constitutional validity of above provision was challenged.
  - Stay granted by Madras High Court in case of Tamilnadu Spinning Mills Association Vs UOI [2006-TIOL-67-HC-Mad-ST].
- Services rendered outside India by Non-Resident and received by Resident Indian during the period prior to 18.04.2006.
  - Department was collecting tax on services rendered and/or performed outside India on the basis of:
    - (i) Rule 2(1)(d)(iv) effective from 16.08.2002
    - (ii) Explanation to Section 65(105) w.e.f. 16.06.2005.

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## Import of Services

- Bombay High Court in the case of Indian National Ship Owners' Association Vs UOI [2008-TIOL-633-HC-MUM-ST] held:
  - ❖ Before enactment of Section 66A (period prior to 18.04.2006), government lacks authority to levy service tax on Indian residents receiving services outside India.
  - ❖ Following contentions of appellant was accepted by Court:
    - ✓ Article 256 of the constitution lays down that "No tax shall be levied or collected except by authority of law".
    - ✓ Act makes service provider liable to tax.
    - ✓ Rule 2(1)(d)(iv) makes service recipient liable to tax.
    - ✓ Rule can not override the Act.
    - ✓ Rule 2(1)(d) is, therefore, clearly invalid.
    - ✓ Explanation 65(105) seeks to levy tax on services rendered outside India.
    - ✓ This leads to taxation of services performed outside the territorial jurisdiction of government of India.
- Honorable Supreme Court rejected department's SLP.

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## Binding Effect of the Notifications

- Government is empowered to issue exemption notification U/s. 93 of the Act.
- Government is empowered to issue notification framing rules U/s. 94 of the Act.
- Notifications, validly issued, are binding on assessee.
- Supreme Court in the case of *Laghu Udyog Bharati v. Union of India* (2002 – TIOL – 182 - SC – ST) laid down the following propositions:
  - Rules can be framed to carry out the purpose of the Act.
  - Rules can not be in conflict with the provisions of the Act.
  - Notification can not increase the liability / obligations casted on the assessee by the law.
  - Notification can not abrogate the rights bestowed on assessee by the Act.
- Rule / Notification, not in consonance with above referred judicial pronouncement, are bad in law.

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## Binding Effect of Circulars

- Circulars are meant to clarify the law and not to lay down a law.
  - *Advertising Pvt. Ltd. V/s. Union of India* 2001 (131) ELT (Mad)
- Circulars issued by the Board would be binding on all officers and persons employed in execution of the Act.
  - *Navnitlal C. Zaveri v. K. K. Sen*, AAC [1965] 56 ITR 198 (SC)
- Even if the directions contained in a circular issued by the board deviate from the provisions of the Act, they are binding on the officers.
  - *Ellerman Lines Ltd. V. CIT* [1971] 82 ITR 913 (SC)
  - *UOI v. Azadi Bachao Andolan*, (2003) 263 ITR 706
  - *CCE v. Usha Martin Industries*, (1997) 7 SCC 47;
  - *Ranadey Micronutrients v. CCE*, (1996) 10 SCC 387;
  - *CCE v. Jayant Dalal (P.) Ltd.*, (1997) 10 SCC 402;
  - *CCE v. Kores (India) Ltd.*, (1997) 10 SCC 338;
  - *Paper Products Ltd. v. CCE*, (1999) 7 SCC 84
  - *Dabur India Ltd. v. CCE*, (2003) 157 E.L.T. 129.
  - *K.P. Varghese v. ITO* [1981] 131 ITR 597 (SC)
  - *UOI V/s. Arviva Industries (India) Limited* 2007 (209) ELT 5 (SC)

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## Binding Effect of Circulars

- Circulars issued by the department are normally meant to be followed and accepted by the authorities.
  - CWT v. Vasudeo V. Dempo [1992] 196 ITR 216 (SC)
- Beneficial circular has to be applied retrospectively while an oppressive circular has to be applied prospectively and that when the circular is against the assessee, they have a right to claim the enforcement of the same prospectively.
  - CCE V. Mysore Electricals Ind. Limited 2006 (204) ELT 517 (SC).
  - Suchitra Components Limited V. CCE 2007(208) ELT 321 (SC).
- Cardinal principles on binding effects of the circular laid down by Supreme Court - Customs v. Indian Oil Corporation (2004) 3 SCC 488.
  - Circular is not binding on a court or an assessee
  - Till circular remains in operation, the revenue is bound by it.
  - Revenue can not be allowed to plead that it is not valid nor that it is contrary to the terms of the statute.

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## Binding Effect of Circulars

- Despite the decision of this court, the department can not be permitted to take a stand contrary to the instructions issued by the Board.
- show-cause notice / demand contrary to the existing circulars of the Board are ab initio bad.
- Constitution bench (4 members) of Supreme Court in the case of CCE Bolpur v. M/s. Ratan Melting & Wire Industries (2008 – TIOL –194 – SC – CX – CB) have taken following view:
  - Board Circular not to prevail over Supreme Court
  - circular which is contrary to the statutory provisions has really no existence in law
  - It is for the Court to declare what the particular provision of statute says and not for the Executive
- Above judgment differs from that of constitution 5 member's bench of supreme court in the case of Dhiren Chemical Industries (2002 – TIOL – 83 – SC – CX). This may again lead to never ending litigation.

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## Refund – Limitation Period

- **Commissioner of Central Excise v. Doaba Company Sugar Mills (1988) 37 ELT 478 (SC)**
  - Limitation period is to be viewed very strictly.
  - Even in genuine cases, authorities do not have powers to relax the same.
- **Brite Neon Signs v. CCE 149 ELT 330 Delhi Tribunal**
  - Limitation period was viewed very strictly.
- **India Cements Ltd. v. CCE (1989) 25 ECR 477 (SC)**
  - Limitation period does not apply to tax paid under protest.
  - Letter saying that amount is paid under protest is a sufficient compliance to circumvent limitation period.
- **Konark Industries Ltd. V. CCE 2002 (144) ELT 454 Kolkatta Tribunal**
  - Limitation period does not apply to pre-deposit of tax pending appeal.
  - Pre-deposit amount refund is not hit by doctrine of unjust enrichment.

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## Refund – Unjust Enrichment

- **Mafatlal Industries Ltd. v. UOI 89 ELT 247 (SC)**
  - Claim of refund can succeed only if petitioner establishes that he has not passed on burden of duty to another person.
  - Were the burden of duty has been passed on, the claimant can not say that he has suffered any real loss.
  - Person who has ultimately borne the duty can claim the refund.
  - If such person does not come forward, state is entitled to retain such amount.
  - If petitioner contend that the Act under which tax was levied is unconstitutional, refund application can not be made under said Act. It has to be made either by way of suit or by way of writ petition.
- **CST v. Standard Chartered Bank [(2008) 10 STR 6 (Kar)]**
  - Excess service tax paid could not be recovered from customers.
  - Claim for refund of excess paid was made by service provider.
  - Principal of unjust enrichment would not apply.
  - It is just money which service provider paid in excess.

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## Penalty – Important Judgments

- **UOI v. Dharmendra Textile Processors [2008 TIOL 192 SC CX LB]**
  - Penalty U/s. 11AC of Excise Act applies only when escaped duty was result of conscious act, wrong doing, fraud, collusion etc.
  - If above pre-requisites are present, section 11AC is applicable resulting into:
    - Mandatory penalty
    - Penalty quantified in the Act is leviable.
    - Authority do not have any power to reduce or waive penalty.
  - Payment of duty before show cause notice does not absolve assessee from the vigor of mandatory penalty.
- **Revenue misconstrued above judicial pronouncement as under:**
  - For every short / non-payment of duty, penalty is mandatory.
  - Penalty, like an interest, is an automatic consequence of non-payment or short payment of duty.

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## Penalty – Important Judgments

- **Revenue started levying penalty mechanically in almost all cases of short payment / non-payment of duty / tax.**
- **Supreme Court in case of UOI v. Rajasthan Spinning and Weaving Mills [2009 TIOL 63 Sc EX] explained the correct law laid down in Dharmendra Textile Processor's case:**
  - Conscious act, wrong doing, fraud, collusion etc. is still a pre-requisite for levy of penalty.
  - Penalty is not an automatic consequence of short payment / non-payment.
- **CCEC v. Shri. Ram Alluminium Pvt. Ltd. [2009-TIOL-HC-MUM-CE]**
  - No jurisdiction with authorities to impose penalty lesser than amount stipulated in the Act.
  - If the penalty is otherwise leviable under the Act, payment before issue of show cause notice is of no avail to assessee.

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## Renting of Immovable Property – Whether liable to Tax?

- Writ petitions were filed in various High Courts challenging levy on renting mainly on the following grounds:
  - Tax sought to be levied on “services in relation to renting of property” and not on “renting of property”.
  - Renting is a property transaction transferring occupancy rights and is not a service transaction.
  - Property taxation is a state subject. Central Government is constitutionally incompetent to levy a tax on property.
  - Service tax is a value added tax. In case of pure leasing / renting of premises, there is no value addition.
  - Notification No.24/2007 dt. 22.05.2007 and Circular No.98/1/2008 – ST dt. 04.01.2008 is ultra vires.
- Government moved Supreme Court for transferring various writs before High Courts to Supreme Court for final verdict.
- Supreme Court delegated these cases to Delhi High Court.
- Delhi High Court decided bunch of 23 writ petitions filled by various petitioners. [Home Solutions Retail India Limited and Others v. Union of India [2009 – TIOL – 196 – HC- DEL – ST].

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## Renting of Immovable Property – Whether liable to Tax?

- Court decided the writ in favour of petitioners on following grounds:
  - Service tax is a tax on value addition provided by a service provider. Renting does not entail any value addition and hence can not be regarded as service liable to tax.
  - Section 65(105)(zzzz) does not entail that the renting itself constitute a taxable service exigible to service tax.
- High Court stated that only services in relation to renting such as air conditioning service provided along with the renting of immovable property would fall within section 65(105)(zzzz).
- Issue will now arise how to value and tax such incidental services?
- High court did not examine the alternative plea as to the legislative competence of the Parliament in the context of Entry 49 of List II of the Constitution of India to levy service tax on renting of property.
- Whether this judgment is applicable to whole of India?
  - This is not a judicial pronouncement of Supreme Court
  - Applicability of same on all India basis is debatable issue.

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## **Renting of Immovable Property – Whether liable to Tax?**

- **Decision applies to properties located in Delhi.**
- **Implications on properties located outside Delhi.**
  - **Writ issued by the Court can not run beyond its jurisdiction**
  - **It is not clear whether it applies to the properties owned / occupied by the petitioners outside Delhi.**
  - **It has binding effect in territorial jurisdictions of High Courts on whose behalf writ is decided by Delhi High Court under delegated powers.**
  - **It may have persuasive value but may not be binding in the jurisdictions of other High Courts.**
- **Following judicial pronouncements are worth noting in this regard:**
  - **CIT v. Thana Electric Supply Ltd. (1994) 206 ITR 727 (Bom HC)**
  - **Consolidated Pneumatic Tool Co. (I) Ltd. v. CIT (1994) 209 ITR 277 (Bom HC DB)**
  - **CIT v. Highway Construction 1999 (105) ELT 14 (Gau HC DB)**
  - **Taylor Instrument Co. v. CIT – 232 ITR 771 (Del HC DB)**
  - **CIT v. Ved Prakash (1989) 178 ITR 232 (P & H HC)**
- **Government has filed SLP in Supreme Court against this decision.**
- **CBEC issued circular for recovery of tax.**

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## **Sale of Flats / Units – Is it liable to Service Tax?**

- **Prevalent and general view:**
  - **Builder sales immovable property.**
  - **No service tax on sale of flats / units.**
- **Sale of completed / constructed flats are not liable to service tax.**
- **Applicability of service tax on under construction flats is a subject matter of litigation and controversy.**
- **In case of sale of under construction flats, issue is raised whether builder constructs the flats:**
  - **On his own account as a property seller: or**
  - **Constructs on behalf of allottees as service provider.**
- **Honorable Supreme Court in case of K Raheja Development Corporation vs. State of Karnataka (AIR 2005 SC 2350) in the context of works contract tax:**
  - **Agreements to sale made before completion of construction.**
  - **Builder constructs flats for prospective customers.**
  - **Builder does not construct property for himself.**

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### **Sale of Flats / Units – Is it liable to Service Tax?**

- Builder is executing work on behalf prospective customers.
- Falls under definition of Works Contract liable to Sales Tax under Karnataka Sales Tax Laws.
- DGST's Circular F No.V/DGST/22/AUD/MISC/10/2004 dated 16.02.2006 suggests:
  - Levy of service tax on sale of under construction flats / units.
  - No levy of service tax on flats / units sold after completion.
- Mahakaushal Builders Welfare Association Vs. Superintendent of Custom & Excise [2006] 5STT 341 (MP):
  - Above referred DGST circular was challenged in writ petition.
  - Hon. High Court rejected the writ petition treating it as premature on following grounds:
    - ❖ No assessment yet made on petitioner.
    - ❖ No demand is served on the petitioner.
    - ❖ No liability is raised on petitioner.
  - Merits / demerits have not been considered by High Court.

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### **Sale of Flats / Units – Is it liable to Service Tax?**

- Circular F No. 332/35/2006-TRU dt. 01.08.2006 - builders / developers not liable to service tax in respect of construction work on his own.
- Allababad High Court in writ matter of Assotech Realty Private Limited Vs State of UP [2007 (7) STR 129] held :
  - Right / title / interest in construction remains with builder.
  - Property passes to allottees after registration of sale deed
  - Property passes to allottees after full payment of consideration.
  - Payment schedule would not alter real nature of transaction.
  - Construction is not undertaken on behalf of allottees.
  - Sale of flat is not liable to Works contract tax.
- Supreme Court set aside the above referred order on technical ground of non-maintainability of writ.
- Supreme Court did not deliberate on the issue whether Assotech was doing construction on his own account or on behalf of allottees.

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## Sale of Flats / Units – Is it liable to Service Tax?

- “Works Contract Services” category w.e.f. 01.06.2007 covers:
  - Specified composite contracts chargeable to VAT / Sales Tax.
  - Construction of commercial, industrial and residential complex.
- Circular No.12T of 2007 dated 07.02.2007 of Commissioner of Sales Tax, Maharashtra State, Mumbai clarifies :
  - Agreement entered into before completion of construction, it amounts to works contract.
  - Agreement entered after completion of construction, it does not amount to works contract.
- Circular No. F/B1/16/2007-TRU dated 27.05.2007:
  - Para No.9.2 states that contracts which are treated as works contract for the purpose of VAT / Sales Tax shall also be treated as works contract for service tax levy.
- Advance ruling authority in case of Harekrishna Developers (Ruling No.AAR/03(ST)/2008 dt. 07.04.2008) held that sale of under construction flat is liable to service tax.

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## Sale of Flats / Units – Is it liable to Service Tax?

- Gauhati High Court in writ matter of Magus Construction Private Limited [(2008)] 15 STT9] held:
  - Contract is for purchase and sale of property.
  - Contract is not for carrying constructions on behalf of allottees.
  - Stamp duty is levied treating it a property transaction.
  - Until sale deed is executed, the title / interest / ownership and possession of flat remains with builder.
  - Circular No. 332/35/2006-TRU dated 01.08.2006 is binding on department.
  - Developer / builder is not liable to service tax.
- Supreme court, while hearing special leave petition of Larsen & Toubro Limited (2008-TIOL-186-SC-CT) on works contracts tax, has referred K. Raheja’s case to larger bench for re-consideration.
- Circular No. 108/02/2009 – ST dated 29.01.2009 – CBEC has accepted the position that sale of flats are not liable to service tax
- Decision of larger bench in case of review of K. Raheja case may bring finality on applicability of VAT and service tax on sale of flats.

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## **Words of Caution**

- **Views expressed are the personal views of faculty based on his interpretation of law.**
- **Application of various provisions and its implications will vary on facts of the case and law prevailing on relevant time.**
- **Participants are advised to be cautious while using the contents of this presentation.**
- **This educational meeting is arranged with a clear understanding that neither Faculty nor Vile Parle Study Circle will be responsible for any error, omission, commission and result of any action taken by participant or anyone on the basis of this presentation.**

**THANK YOU**

### **Definition – Input Services [Rule 2(l) of CCR]**

- **Used by a provider of taxable service for providing an output service; or**
- Used by manufacturer**
  - **whether directly or indirectly**
  - **in or in relation to manufacture of final products**
  - **clearance of final products up to the place of removal**
- And**
  - **include services used in relation to:**
    - ❖ **Setting up premises of provider of output service or an office relating to such premises.**
    - ❖ **Modernization of premises of provider of output service or an office relating to such premises.**
    - ❖ **Renovation or repairs of a premises of provider of output service or an office relating to such premises**
    - ❖ **Advertisement or sales promotion.**
    - ❖ **Market research**
    - ❖ **Storage up to the place of removal**
    - ❖ **Procurement of inputs**

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### **Definition – Input Services [Rule 2(l) of CCR]**

- ❖ **Activities relating to business, such as:**
  - ◆ **Accounting**
  - ◆ **Auditing**
  - ◆ **Financing**
  - ◆ **Recruitment and quality control**
  - ◆ **Coaching and training**
  - ◆ **Computer networking**
  - ◆ **Credit rating**
  - ◆ **Share registry**
  - ◆ **Security**
  - ◆ **Inward transportation of inputs or capital goods**
  - ◆ **Outward transportation upto the place of removal**

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