

INTRODUCTION

1.1 NEED FOR A TAX ON SERVICES

Service tax is a “tax of the future”. As per General Agreement on Trade and Tariffs (GATT), Excise & Customs tariffs have been coming down and in the ensuing years have to come down further. The shortfall in revenue necessitated exploring new avenues of taxation. Thus service tax was born. Secondly, services contribute to approximately 50% of the GDP. Government's argument hence, is substantial revenue should come from the service sector. Thus the tax on goods (excise duty) has to be complemented with the tax on services. The Government's plan is to introduce service tax on all services and exempt a few.

1.2 GENESIS OF SERVICE TAX IN INDIA

The imposition of service tax was in sequel to the Report of the Chelliah Committee on Tax Reforms. On these recommendations Dr. Manmohan Singh, the then Union Finance Minister, in his Budget speech for the year 1994-95 introduced the new concept of Service Tax and stated that “There is no sound reason for exempting services from taxation, when goods are taxed and many countries treat goods and services alike for tax purposes. The Tax Reforms Committee has also recommended imposition of tax on services as a measure for broadening the base of indirect taxes. I, therefore, propose to make a modest effort in this direction by imposing a tax on services of telephones, non-life insurance and stock brokers.” Thus, service tax was imposed on 3 services.

The baton then passed on to successive finance ministers who widened the service tax net in their budgets. It is expected that all services would be in the service tax net except a few exempted services.

Since the introduction of Service Tax in 1994, revenue collected from Service Tax has been increasing slowly but steadily. Service tax collection is primarily from metro areas and bigger towns.

The Directorate General of Service Tax, Mumbai in their website www.servicetax.gov.in have given the vital statistics on service tax which is reproduced under :

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Year	No. of assesseees	Gross Collections (Rs. Crores)	Percentage(%) of growth	No. of Services
1994-1995	3943	410	Base Year	3
1995-1996	4866	846	101	3
1996-1997	13982	1022	24	6
1997-1998	45991	1515	49	18
1998-1999	107479	1787	18	30
1999-2000	115495	2072	16	27
2000-2001	122326	2540	23	26
2001-2002	187577	3305	26	41
2002-2003	232048	4125	25	51
2003-2004	403856	7890	91	58

Trends of revenue indicate that the Service Tax collection is growing at fast rate since its inception.

1.3 CONSTITUTIONAL AUTHORITY

The Government derives its power to levy taxes from the Constitution of India. Elaborate provisions have been made in the Constitution of India to regulate the power of taxation of both the Central Government and the State Governments. Article 265 of the Constitution of India prohibits arbitrary collection of tax. It reads as:

"No tax shall be levied or collected except by authority of law."

Thus the Government may levy a tax on the citizens only under the authority of the Constitution of India. The Constitution, in its Schedule VII, has enumerated the matters on which the Central Government and the State Government can make laws. Such matters are divided into three categories--

- a) List – I : Union List (It contains the matters in respect of which only the Central Government has the power of legislation)
- b) List – II : State List (It contains the matters in respect of which only the State Government has the power of legislation)
- c) List – III : Concurrent List (It contains the matters in respect of which both the Central and the State Governments have power of legislation).

Entries 82 to 92C of List I enumerate the subjects where the Central Government has power to levy taxes. Entries 45 to 63 of List II enumerate the subjects where the State Governments have power to levy taxes.

Entry 92C of the Union List of the Seventh Schedule to the Constitution of India enables the Union to levy "Taxes on Services". Initially there was no specific entry in the Union List for levying service tax. Service tax was levied by the Central Government by drawing power from entry 97 of the Union List. Entry 97 is a 'residuary entry' in List-I, which has been reproduced below:

"97 - Any other matter not enumerated in List II or List III including any tax not mentioned in either of those Lists."

The 'residuary entry' provides wide powers to the Central Government in respect of taxation of the subjects not mentioned in the Lists given by the constitution.

However, as a result of deliberations between the States and the Centre and as per the recommendations of the various expert committees, entry 92C was introduced in the VII Schedule in the Union List vide Constitution (92nd Amendment) Act, 2003 with effect from 07.01.2004. Entry 92C reads as under:

"92C - Taxes on services."

A new Article 268A was inserted in the Constitution which reads as follows:

- "268 (1) Taxes on services shall be levied by the Government of India and such tax shall be collected and appropriated by the Government of India and the State in the manner provided in clause (2).
- (2) The proceeds in any financial year of any such tax levied in accordance with the provisions of clause (1) shall be--
- (a) Collected by the Government of India and the States;
 - (b) Appropriated by the Government of India and the States,
- in accordance with such principles of collection and appropriation as may be formulated by the Parliament by law."

A consequential amendment to Article 270 of the Constitution was also made to enable Parliament to formulate by law, principles for determining the modalities of levying the service tax by the Central Government and collection of the proceeds thereof by the Central Government and the State Government.

With this amendment in the Constitution, the Central Government has become competent to enact a separate legislation on service tax.

1.4 SERVICE TAX LAW

Service tax was introduced in 1994 but there is no independent statute on service tax as yet. However, following sources provide statutory provisions relating to service tax and can be broadly grouped under the following categories:

1.4.1 Finance Act, 1994: The statutory provisions relating to service tax were first

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promulgated through Chapter V of the Finance Act, 1994. Since then, Chapter V of the Finance Act, 1994 is working as the Act for the service tax provisions. Later, in the year 2003, the Finance Act 2003 inserted Chapter VA relating to advance rulings on service tax in the Finance Act, 1994. In the year 2004, the provisions relating to charging of 'education cess' on the amount of service tax were made applicable through Chapter VI of the Finance (No.2) Act, 2004.

1.4.2 Rules on service tax: Section 94 of Chapter V and section 96 -I of Chapter VA of the Finance Act, 1994 grants power to the Central Government to make rules for carrying out the provisions of these Chapters. Using these powers, the Central Government has issued Services Tax Rules 1994, Service Tax (Advance Rulings) Rules, 2003, CENVAT Credit Rules, 2004, Export of Service Rules, 2005, Service Tax (Registration of Special Category of Persons) Rules, 2005, Service Tax (Determination of Value) Rules, 2006 and Taxation of Services (Provided from Outside India and Received in India) Rules, 2006 which are amended from time to time.

Rules should be read with the statutory provisions contained in the Act. Rules are made for carrying out the provisions of the Act. The rules can never override the Act and cannot be in conflict with the same.

1.4.3 Notifications on service tax: Sections 93 and 94 of Chapter V, and section 96-I of Chapter VA of the Finance Act, 1994 empower the Central Government to issue notifications to exempt any service from service tax and to make rules to implement service tax provisions. Accordingly, notifications on service tax have been issued by the Central Government from time to time. These notifications usually declare date of enforceability of service tax provisions, provide rules relating to service tax, make amendments therein, provide or withdraw exemptions from service tax or deal with any other matter which the Central Government may think would facilitate the governance of service tax matters.

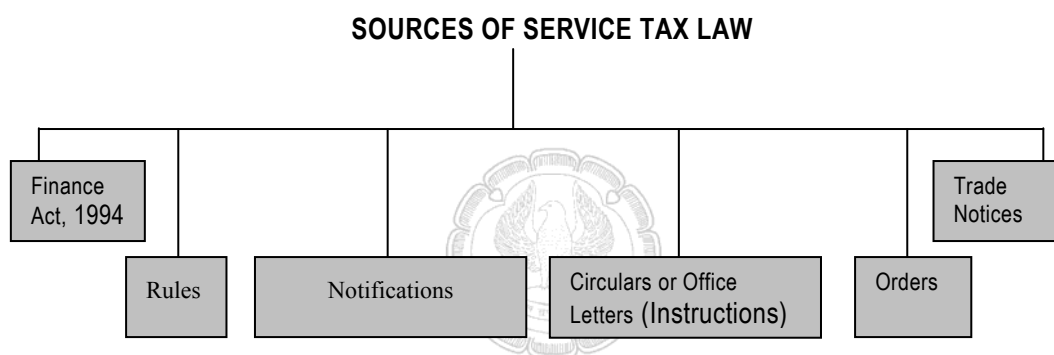
1.4.4 Circulars or Office Letters (Instructions) on service tax: The Central Board of Excise and Customs (CBEC) issues departmental circulars or instruction letters from time to time to explain the scope of taxable services and the scheme of service tax administration etc. These circulars/instructions have to be read with the statutory provisions and notifications on service tax.

The circulars clarify the provisions of the Act and thus, bring out the real intention of the legislature. However, the provisions of any Act of the Parliament cannot be altered or contradicted or changed by the departmental circulars.

1.4.5 Orders on service tax: Orders on service tax may be issued either by the CBEC or by the Central Government. Rule 3 of the Service Tax Rules, 1994, empowers the CBEC to appoint such Central Excise Officers as it thinks fit for exercising the powers under Chapter V of the Finance Act, 1994. Accordingly, orders have been issued by the CBEC, from time to time, to define jurisdiction of Central Excise Officers for the purposes of service tax.

1.4.6 Trade Notices on service tax: Trade Notices are issued by the Central Excise/Service Tax Commissionerates. These Commissionerates receive various instructions from the Ministry of Finance or Central Board of Excise & Customs for effective implementation and administration of the various provisions of service tax law. The same are circulated among the field officers and the instructions which pertain to trade are communicated to them in the form of trade notices. Trade Associations are supplied with the copies of these trade notices. Individual assesses may also apply for copies of trade notices. The trade notice disseminate the contents of the notifications and circulars/letters/orders, define their jurisdiction; identify the banks in which service tax can be deposited; give clarifications regarding service tax matters, etc.

The various components making service tax law have been represented in the following diagram:



1.5 SELECTIVE VS. COMPREHENSIVE COVERAGE

Depending on the socio-economic compulsions, each country evolved a taxation system on services adopting either a comprehensive approach or a selective approach. In comprehensive approach all services are made taxable and a negative list is given in case some services are to be exempted. In selective approach, selective services are subjected to service tax. While most of the developed countries tax all the services with very few and limited exemptions, most of the developing countries have opted for taxation of select services only. India has adopted a selective approach to taxation of services.

In India, service tax has been levied on specified taxable services and the responsibility of payment of the tax is cast on the service provider (barring few exceptional cases). The service tax is leviable on the gross amount charged by the service provider from the client. System of self assessment of service tax by the assesses has been introduced. Tax returns are expected to be filed half yearly. Central Board of Excise & Customs is the central authority to regulate service tax matters. Directorate of Service Tax at Mumbai oversees the activities at the field level for technical and policy level coordination.

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1.6 ADMINISTRATION OF SERVICE TAX

The Department of Revenue of the Ministry of Finance exercises control in respect of matters relating to all the direct and indirect taxes through two statutory Boards, namely, the Central Board of Direct Taxes (CBDT) and the Central Board of Excise and Customs (CBEC). Matters relating to the levy and collection of all the direct taxes (income tax, wealth tax etc.) are looked after by CBDT, whereas those relating to levy and collection of indirect taxes (customs duties, central excise duties etc.) fall within the purview of CBEC. The two Boards were constituted under the Central Board of Revenue Act, 1963.

The responsibility of administration and collection of service tax has also been vested upon the CBEC ('Board'). The Board administers service tax matters through the Central Excise Zones and each Zone, in turn works through Central Excise Commissionerate falling under its territory. Each zone is headed by a Chief Commissioner of Central Excise, while each Commissionerate is headed by a Commissioner of Central Excise.

The Chief Commissioner of Zone exercises supervision and control over the working of the Commissionerates in the Zone and is mainly responsible for monitoring revenue collection, disposal of pendencies, redressal of grievances of trade, etc. He also ensures coordination among the Commissionerates within the Zone.

1.6.1 Director General (Service Tax): Considering the increasing workload due to the expanding coverage of service tax, it was decided to centralise all the work and entrust the same to a separate unit supervised by a very senior official. Accordingly, the office of Director General (Service Tax) was formed in the year 1997. It is headed by the Director General (Service Tax). The functions and powers of Director General (Service Tax) are as follows:

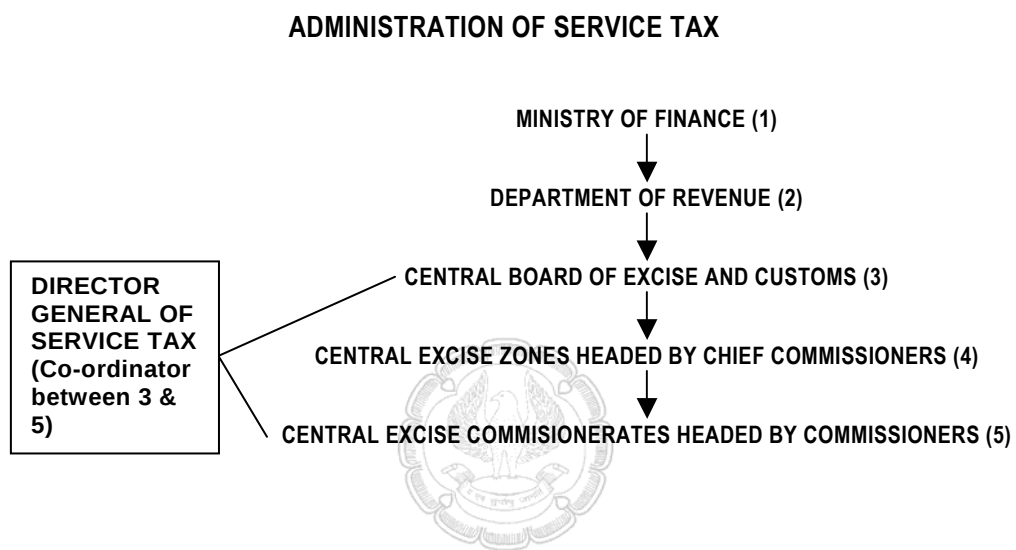
- (1) To ensure that proper establishment and infrastructure has been created under different Central Excise Commissionerates to monitor the collection and assessment of service tax.
- (2) To study the staff requirement at field level for proper and effective implementation of service tax.
- (3) To study as to how the service tax is being implemented in the field and to suggest measures as may be necessary to increase revenue collection or to streamline procedures.
- (4) To undertake study of law and procedures in relation to service tax with a view to simplify the service tax collection and assessment and make suggestions thereon.
- (5) To form a data base regarding the collection of service tax from the date of its inception in 1994 and to monitor the revenue collection from service tax.
- (6) To inspect the service tax cells in the Commissionerate to ensure that they are functioning effectively.
- (7) To undertake any other functions as assigned by the Board from time to time.

The Directorate of Service Tax coordinates between the CBEC and Central Excise Commissionerates. It also monitors the collection and the assessment of service tax. It

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compiles the service tax revenue reports received from various Central Excise Commissionerates and monitors the performances of the Commissionerates. It scrutinises the correspondences received from field formations and service providers and replies to the clarifications sought for, wherever possible. In cases where the doubts/clarification sought involves policy matter, the Directorate apprises the Board for issuing clarification/instruction.

The administrative machinery of the service tax law can be understood with the help of the following diagram:



1.7 SERVICE TAX PROCEDURES

Service tax procedures include registration, maintenance of books and records, payment of service tax, availment and utilization of CENVAT credit, filing of service tax returns, self assessment, provisional assessment and recovery of service tax, interest and penalties, rectification of mistakes, revision of assessment order, appeals, search and seizure, advance rulings, refund etc.

1.8 ROLE OF A CHARTERED ACCOUNTANT

As the gamut of service tax expands there would be a great need for professionals to advice and assist the assessees. A chartered accountant with his training and experience is well-equipped to position himself in the new role as an advisor and facilitator for due compliance of service tax law. The nature of services would be:

1.8.1 Advisory services : With the selective coverage of service tax on certain specified services a great deal of professional acumen would be required to interpret and understand the law and advise the applicability of service tax *qua* an activity or service. A chartered accountant would be able to fill this void.

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1.8.2 Procedural compliance: The service tax law envisages registration, payment of tax, filing returns and assessments involving interface with the excise department. A chartered accountant with his experience and expertise would be the best person to assist the assessee in all the above functions and ensure compliance.

1.8.3 Personal representation: As per the service tax law read with the Central Excise Act and Rules, a chartered accountant is allowed to appear before the assessment authority, Commissioner (Appeals) (first appeal) and Tribunal (second appeal). Here too with his experience and expertise a chartered accountant would be well positioned to represent his clients in these fora.

1.8.4 Certification and audit: With the widening of tax base there will be a phenomenal growth in the number of service tax assessees. In the ensuing years the department would have to evolve a mechanism where there is management by exception i.e. generally accept all the returns as correct and pick and choose those returns which need detailed scrutiny. In this mechanism a chartered accountant could be of great assistance. Service tax returns and financial statements could be certified by the chartered accountant from the perspective of service tax similar to an audit under section 44AB of the Income-tax Act.

1.8.5 Onerous task to keep pace : The service tax like excise is administered more by way of trade notices issued by various Commissionerates. A chartered accountant will have to keep himself abreast of the latest notifications and trade notices in addition to the changes in law so as to meet the client expectations. Thus, in order to render good value added services in the area of service tax a chartered accountant has an onerous task to keep pace with the latest in the legal front.

Self-examination questions

1. Which committee recommended the introduction of service tax?
2. Who has the power to levy service tax – Union or States? Discuss.
3. From which Entry of the Union List of the Constitution, does the authority to levy service tax arise?
4. Under which Act, does the service tax is levied?
5. Which were the first three services to be brought under the service tax net?
6. Write a note on administration of service tax.
7. What do you mean by selective and comprehensive coverage of services for the purpose of service tax? Which system is being adopted in India?
8. Write briefly about the role of a chartered accountant in the field of service tax consultancy.
9. Describe the various sources that provide statutory provisions relating to service tax.
10. Discuss the functions and powers of Director General (Service Tax).