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Service tax on renting of immovable properties – A way forward

Recently the Hon'ble Delhi High Court in a landmark judgment dated 18 April 2009 in the matter of **Home Solution Retail India Ltd and Others vs. Union of India and others** wherein it is held that *mere renting* of immovable property for furtherance of business or commerce by itself cannot be regarded as a taxable service and held that not exigible to charge service tax in terms of the Section 65 (105) (zzzz) of Finance Act, 1994 and opined on legality, validity and vires of Notification No. 24/2007-ST dated 22/05/2007 and Circular No. 98/1/2008-ST dated 04/01/2008 for interpretation on service tax on renting of immovable properties in terms of Section 65 (90a) and Section 65 (105) (zzzz) of the Finance Act, 1994 as amended by the Finance Act, 2007.

Before discussing way forward of this judgment, let's take a note of brief background of chargeability of service tax on renting of the immovable properties, basis of appeals in writ petitions and highlights of this judgment.

<u>Brief background of chargeability of service tax on renting of the immovable properties:</u>

The Finance Act of 2007 has introduced Section 65 (105) (zzzz) levying Service tax with effect from 01/06/2007 on the services provided or to be provided to any person, by any other person, in relation to renting of immovable property for use in the course or furtherance of business or commerce.

Further the Notification No. 24/2007-ST dated 22/05/2007 exempts property tax levied by the local bodies from the gross value of rent for the purpose of chargeability of service tax and the Circular No. 98/1/2008-ST dated 04/01/2008 clarifies that the "right to use immovable property is leviable to service tax under the renting of immovable property service".

<u>Ground of Appeals in writ Petitions on chargeability of service tax on renting of the immovable properties:</u>

- Merely allowing use of land or building does not amount to provision of a service.

- The grant of lease or license tantamount to transfer of rights and does not amount to a provision of service rendered by one to another since the lessor is not a service provider but a transferor of rights in the immovable property which the lessor makes in favor of

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the lessee or the licensee, who is the transferee of such rights and enjoys such rights during the tenure of lease or the license in terms of contract signed by the parties.

- Levy of Service tax on renting of Immovable Property amounts to levy of tax on land/ buildings where in The Central Government does not have the right to levy tax on land / buildings as the same falls within the State List (List II 49) of the Constitution of India.

Interim Stay granted by following High Courts from collection of service tax in terms of Section 65 (105) (zzzz) of the Finance Act, 1994 as amended by the Finance Act, 2007:

- Bombay High Court - W.P No. 1263 of 2007 - Stay Order dated 30.07.2008

- Andhra Pradesh High Court – W.P. No. 6572 of 2008 - Stay Order dated 27.03.2008

- Gujarat High Court – Special Civil Application No. 5269 of 2008 - Stay Order dated 28.03.2008

- Delhi High Court – W.P.(C) No. 1659 of 2008 - Stay Order dated 03.03.2008

- Madras High Court – W.P. No. 30276 of 2007 - Stay Order dated 09.10.2007

Then the Union of India filed a transfer petition in the Hon'ble Supreme Court of India for transferring the service tax petitions to the Supreme Court. The Hon'ble Supreme Court accordingly transferred the case to the Delhi High Court.

Highlights of the Hon'ble Delhi High Court's judgment:

- Service in relation to renting of immovable property means a service which is distinct and different from *mere renting* of immovable property itself

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- The transaction of renting of immovable property by itself is not taxable in terms of Section 65 (105) (zzzz) of the Finance Act

- Service tax is Value Added Tax and hence only the ‘”value added” is liable to be taxed by way of service tax

- The Act of renting of immovable property by itself does not provide any value addition to any person

- In the case of lease, the right of possession is transferred whereas in the case of license, there is a transfer of permissive possession. Such transfer of right cannot be considered as service; and

- The Hon’ble court has not given judgment on validity of Section 65 (105) (zzzz) of the Finance Act but quashed or set aside the operative part of the subject notification and circular which entails levy of service tax on renting of immovable property

<u>Open Issues:</u>

- Future obligation on service provider i.e. landlord/ lessor, etc. to charge service tax on renting of immovable properties in terms of Section 65 (105) (zzzz) of the Finance Act
- Is there any possibility to claim refund of service tax already paid on renting of immovable properties

<u>Way Forward:</u>

To decide future obligation on service provider i.e. landlord/ lessor, etc., to charge service tax on renting of immovable properties in terms of Section 65 (105) (zzzz) of the Finance Act, we have to first analyze validity of chargeability of service tax on renting of immovable properties in a given scenario.

Prima facie, as decided by the Hon’ble Delhi High Court, it seems that *mere renting of immovable property by itself cannot be regarded as a service* but if there is some other service

provided in relation to renting of immovable property then such other service would be covered by Section 65 (105) (zzzz) of the Finance Act, 1994.

Hence, we may draw a concluding line on recent judgment of the Hon'ble Delhi High Court that service tax is not leviable on:

- *Mere renting* of the immovable property
- Transactions involving transfer of rights, in some form or other in immovable property like Lease agreements, Leave and License agreements, etc.

<u>Refund of service tax already paid on renting of immovable properties:</u>

Further refund of service tax already paid on renting of immovable properties may be dealt in following manner:

- If the service tax has already been paid but not collected from the recipient of service, refund claim can be made within one year from the relevant date under Section 11B of the Central Excise Act, 1944

- If the service tax has already been paid and collected from the recipient of service, the recipient of service may claim the refund provided that he can substantiate that he has not passed the burden of tax to any other person.

Now question arise what happens to refund for a period prior to one year from the relevant date in terms of the Section 11B of the Central Excise Act, 1944. This issue is subjective and depend upon legal interpretation of levy being illegal or unconstitutional so as give right to claim refund either with in specified period of one year in terms of Section 11B of the Central Excise Act, 1944 or filing a suit or writ petition to claim refund for extended period of limitation.

In this regard, following judgments are of substantial relevance to decide a levy being illegal or unconstitutional:

- COLLECTOR OF CUSTOMS, BOMBAY Vs. SANGLI BANK LTD. 1997(93) ELT 3 (S.C.)

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- ASSISTANT COLLR. OF CUS Vs. ANAM ELECTRICAL MANUFACTURING CO 1997 (90) E.L.T. 260 (S.C.)
- MAFATLAL INDUSTRIES Vs. U.O.I. 1997 (89) E.L.T. 247 (S.C.)

Conclusion:

Hence, it may be safely concluded in view of recent judgment of the Hon'ble Delhi High Court and relevant provisions of the Finance Act that service tax is not leviable on *mere renting* of the immovable property and on transactions involving transfer of rights, in some form or other in immovable property like Lease agreements, Leave and License agreements, etc.

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